Volume Title: The Postwar Residential Mortgage Market

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Volume Publisher: Princeton University Press

Volume ISBN: 0-870-14106-6

Volume URL: http://www.nber.org/books/klam61-1

Publication Date: 1961

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Chapter URL: http://www.nber.org/chapters/c2340

Chapter pages in book: (p. 49 - 73)

CHAPTER 3

Elements in the Changing Postwar Mortgage Market

THE changed structure of mortgage debt and markets, surveyed in Chapter 2, resulted from the interplay of numerous economic, financial, and sociopolitical forces. The purpose of this chapter is to select and describe the main elements of these forces at work during the post-World War II decade. Their dynamic nature is reflected in the record of annual and quarterly changes in the flow of funds into the various sectors of the mortgage market. That record is analyzed in Chapter 5 after the basic subject of mortgage yields is explored in Chapter 4.

During most of the 1946–1956 period, the major elements, both private and federal, influencing residential mortgage market developments tended to be expansionary. During a part of the decade, however, restraining influences, also both private and public in character, acted to limit the flow of funds into mortgage markets.

In an appraisal of the major influential elements at work, the decade breaks down roughly into two equal time periods. The major turning point in the mortgage market as in other sectors of the capital market occurred in March 1951, when the Federal Reserve and Treasury reached an "accord" resulting in the withdrawal in principle of Federal Reserve support of the market for federal obligations. Several months earlier, with the outbreak of hostilities in Korea, steps had been taken by the government to limit the volume of new construction and the flow of mortgage funds, culminating in the issuance of Regulation X on real estate credit under the Defense Production Act of 1950.[1] The restraints placed by federal action on both the supply of mortgage credit and the demand for it brought to an end a unique five-year period during which, with limited exceptions, unrestrained expansionary forces had resulted in the availability of an ample supply of funds to meet large and rising demands for mortgages. While the flow of mortgage funds in the second half of the decade was substantially greater than in the first half, there was not again such an extended period of high tide in mortgage funds.

Expansionary Influences at Work, 1946–1950

With the end of World War II the stage was set for a rapid expansion in mortgage market activity, which continued almost without abatement

[1] Public Law 774, 81st Congress, approved September 8, 1950.

through 1950. Demands for mortgage credit to finance construction and real estate transactions were great; financial institutions were actively seeking new investment outlets; federal actions with respect to general fiscal and credit policies, as well as specific mortgage and housing programs, were expansionary; and mortgage yields were relatively attractive to both lenders and borrowers.

DEMAND FOR MORTGAGE CREDIT

At the war's end, the nation's needs for additional real estate facilities were acute following wartime restrictions superimposed upon the sharply reduced activity during the depressed 1930's. Families separated or dislocated during the war and requiring new accommodations, rapid demobilization of the armed forces, sharply rising marriage and birth rates, and heavy migration of population placed mounting pressure on limited housing facilities. Of the 33.5 million married couples in the United States shortly after the war's end, 3 million or nearly 9 per cent were sharing living quarters, many more in number and proportion than before the war. Uncounted other families were living in temporary, makeshift accommodations. Demands for new and improved living quarters were backed by high and rising incomes and a growing accumulation of liquid assets.

Demands for mortgage funds to finance construction and acquisition of nonresidential properties were also large, but the needs were not so pressing as those for residential facilities. A large part of nonresidential construction and transfer activity was financed from internal sources and through other sectors of the capital market, particularly the corporate bond market. Moreover, in efforts to conserve scarce materials and manpower for construction of housing, especially for veterans, federal restrictions were placed on the construction of nonresidential facilities. The restrictions remained in effect for little more than a year during the short-lived Veterans Emergency Housing Program (see the discussion of federal mortgage programs and policies, below).

LIQUIDITY OF FINANCIAL INSTITUTIONS

The flow of mortgage funds to finance production of new structures and acquisition of existing real estate in the immediate postwar years was limited more by the lack of available or newly constructed accommodations than by the supply of mortgage credit. Financial institutions found themselves in an unusually liquid position with investment portfolios heavily weighted with large holdings of U.S. government obligations.

They amounted at the end of 1945 to well over one-half of all assets held by the four main groups of financial institutions, compared with less than one-tenth for mortgages.[2] In volume of government securities held, commercial banks ranked first, followed by life insurance companies and mutual savings banks; savings and loan associations, specialized mortgage lenders, ranked last in absolute amount and also in ratio to total assets.

TABLE 10

Net Sale of Federal Government Securities and Net Acquisition of Mortgages by Four Main Types of Financial Institutions, 1946–1956 (dollars in billions)

	1946–1950			*1951–1956*		
	Net Sale Government Securities (1)	Net Acquisition of Mortgages (2)	Ratio (1) to (2) (3)	Net Sale Government Securities (1)	Net Acquisition of Mortgages (2)	Ratio (1) to (2) (3)
Selected financial institutions	36.4	30.8	118.2	12.6	59.3	21.2
Savings and loan associations	0.9	8.2	12.2	1.3	22.0	−5.9
Life insurance companies	7.1	9.5	75.8	5.9	16.9	34.9
Commercial banks	28.6	8.9	321.3	5.4	9.0	60.0
Mutual savings banks	−0.1	4.1	−2.4	2.6	11.4	22.8

SOURCE: Data from various issues of the *Federal Reserve Bulletin.*

These financial institutions were anxious to convert their large holdings of riskless but low-yielding assets into investments yielding higher returns. Moreover, outlets for the flow of new savings were needed to replace the purchase of government securities that had dominated the wartime capital markets. The Federal Reserve policy of supporting government bond prices at par made possible the sale of such securities readily and without penalty. As a result, sales of Treasury obligations proceeded rapidly during the period of support, providing a large reservoir of funds to meet private capital demands.

The $36 billion acquired from sale of government securities by financial institutions during the first five postwar years exceeded their total net acquisition of mortgages (Table 10). The large volume of funds was supplemented by an almost equally large net savings inflow of $33 billion. For commercial banks and life insurance companies the sale of

[2] Based on data from various issues of the *Federal Reserve Bulletin.*

governments provided the major source of investment funds; for mutual savings banks and savings and loan associations savings inflows were the major source. Variations in the pattern of investment behavior among the four types of financial institutions (Table 10) were the outcome of a number of important factors, legal and organizational as well as financial (discussed later in Chapter 5, the section on mortgage flows relative to other capital market flows). Briefly, while only commercial banks showed net acquisition of mortgages less than net sale of government securities through 1950, a large but unmeasurable amount of commercial bank funds flowed into construction and interim financing loans. Thus, the unusual liquidity of commercial banks permitted a larger volume of permanent financing by other institutions than might otherwise have been possible.

FEDERAL MORTGAGE PROGRAMS AND POLICIES

In a setting of ready availability of investment funds from financial institutions, the federal government took a series of steps successively liberalizing both its VA and FHA mortgage guaranty and insurance programs. In addition, several bold new housing and mortgage underwriting programs were inaugurated, and expanded secondary mortgage market facilities were provided. These actions, in conjunction with the federal policy of supporting government bond prices at par, created a financial climate in which mortgage loans were especially inviting to financial institutions in comparison with other capital market investments.

That the federal government has come to play a unique and strategic role in housing and mortgage markets is widely recognized. In no other sector of the private capital market—or of the entire nonfarm economy, for that matter—is there such broad federal participation as there is in mortgage markets. A study of postwar mortgage finance would be incomplete, therefore, without an analysis of major federal actions taken in the area since the end of the war. Legislative or administrative details, however, that are adequately provided in several cited sources, are not given here.

The guns of World War II had scarcely been silenced when the federal government took the first of several direct actions to stimulate the flow of funds into the mortgage sector of the capital market. At the end of 1945, the Servicemen's Readjustment Act of 1944[3] was amended to make VA-guaranteed loans more acceptable to both lenders and borrowers, as well as builders. Principally, the amendments provided for (1) an increase in

[3] P.L. 346, 78th Congress, approved June 22, 1944.

the maximum amount of government guarantee from $2,000 to $4,000, (2) an extension of maximum maturities from twenty to twenty-five years, and (3) a change in the basis of property appraisal from "reasonable normal value" to simply "reasonable value." In addition, the act authorized supervised lenders to extend VA-guaranteed loans to eligible veterans without prior approval by the Veterans Administration.[4]

In efforts to further stimulate production of housing and extension of mortgage credit for veterans, the Veterans Emergency Housing Program was put into effect in May 1946, restoring wartime construction controls and renewing liberal wartime FHA mortgage insurance provisions under Title VI of the National Housing Act.[5] Under the reactivated FHA mortgage program, property appraisals were based on the concept of "necessary current cost" rather than "value," and maximum insurable loan amounts were raised on both owner occupied and rental properties. Twice extended beyond its original expiration date, the program was finally allowed to expire on April 30, 1948. Four months later, however, with the enactment of the Housing Act of 1948, the FHA "emergency" program was reactivated until March 31, 1949, for new rental housing only (section 608 of the National Housing Act). That program was further liberalized by authorization of higher maximum insurable mortgage amounts.[6]

The Housing Act of 1948 was based on the theory that production of housing could be increased by stimulating both the demand for mortgage funds and their supply. The act, therefore, in addition to reactivating part of the FHA Title VI program, liberalized prewar terms of the permanent FHA mortgage insurance program under Title II by authorizing increases in maximum insurable loan amounts, loan-to-value ratios, and maturities. It provided, further, for special new programs of mortgage insurance and, perhaps most important in stimulating the flow of FHA and VA mortgage funds, it increased the ability of the Federal National Mortgage Association (FNMA) to purchase federally underwritten mortgages.[7]

Activities of FNMA, and government actions taken to influence them, have played a key role in the postwar mortgage market, almost entirely

[4] P.L. 268, 79th Congress, approved December 28, 1944.

[5] See Miles L. Colean, *The Impact of Government on Real Estate Finance in the United States*, New York, National Bureau of Economic Research, 1950, p. 106, for a discussion of the Veterans' Emergency Housing Program.

[6] The Veterans Emergency Housing Act proved a dismal failure and most of its provisions were discontinued by mid-1947.

[7] A more detailed description of the provisions of this act pertaining to FHA mortgage insurance may be found in the Federal Housing Administration's *Fifteenth Annual Report*, December 31, 1948, pp. 1–4. A summary of all major provisions of the act is given by Colean, *op. cit.*, pp. 124–125.

an expansive one during the first half of the decade. The first major action in that direction was taken on July 1, 1948 (one month before passage of the Housing Act of 1948) when this federally sponsored secondary mortgage market facility was completely reorganized under a new charter. The result was a greatly enlarged capacity to purchase mortgages, authority to purchase VA as well as FHA loans and to issue advance commitments to purchase them.[8] The new charter was intended to stimulate the flow of VA loans, which had been declining from its high 1947 level, partly as a result of the widening spread between rising interest rates on U.S. government and other securities and the fixed 4 per cent rate on VA loans (see Chart 6 and Chap. 5, pp. 113–114). The intended stimulus was largely nullified, however, by the restrictive provision permitting the Association to purchase only one-fourth of the dollar amount of FHA and VA loans originated by a lender. The provision was liberalized one month later in the Housing Act of 1948 to permit purchase up to one-half of the eligible mortgages originated by a lender. Little more than one year later, liberalization reached its peak with statutory authority to purchase all eligible VA loans originated by a lender.

The steady extension of FNMA's purchasing authority, the continuation of its authority to make advance commitments to purchase mortgages, and its administrative policy of purchasing all mortgages at par brought the Association a steadily increasing mortgage portfolio and placed the statutory limit on its holdings under constant pressure. The willingness of Congress to increase the limit steadily, however, maintained FNMA as an effective support to the mortgage market throughout the first half of the postwar decade. In a period of little more than nine months, through April 1950, maximum permitted mortgage holdings were increased three times—to $1.5 billion, to $2.5 billion, and to $2.75 billion. About two years later, in July 1952, a final increase to $3.75 billion was authorized.

The last increase came well after Congress had recognized that FNMA had become a prime generator of mortgage funds and had attempted to limit the drain on the Treasury in the Housing Act of 1950 by rescinding the Association's authority to make advance commitments.[9] The need to increase further FNMA's purchasing authority two years later arose from

[8] P.L. 864, 80th Congress, enacted July 1, 1948. Under its original charter granted in February 1938, FNMA was authorized to purchase only FHA loans and had a maximum borrowing authority of $220 million (increased to $840 million by the July 1 Act). For a time the Reconstruction Finance Corporation (RFC) Mortgage Company was authorized to purchase VA loans (August, 1946–June, 1947) but little use was made of this facility. From June 30, 1947, when RFC was terminated, until July 1, 1948, no federally sponsored secondary market facility existed for VA loans.

[9] P.L. 475, 81st Congress, enacted April 20, 1950.

the continued large volume of mortgage purchases made under earlier outstanding commitments (see the section of Chapter 7 dealing with the Federal National Mortgage Association).

The Housing act of 1950 was the final major piece of federal legislation to influence mortgage markets in the first half of the postwar decade. On balance, the act tended to stimulate further mortgage market activity by making VA and FHA mortgages more attractive to both lenders and borrowers.[10] VA guarantees were increased from 50 per cent and a ceiling of $4,000 to 60 per cent and a ceiling of $7,500, with the maximum maturity extended from twenty-five to thirty years. The Veterans Administration, furthermore, was given new authority to make direct mortgage loans on terms equal to those on its guaranteed loans in areas where the latter were not available from private lenders.

The authority of the Federal Housing Administration was also expanded by the Housing Act of 1950 to include two new mortgage insurance programs with liberal terms, one for small houses in rural communities and outlying areas and another for cooperative housing projects.[11]

Mortgage Markets in a Changing Setting, 1951–1956

The economic, financial, and sociopolitical setting in which mortgage markets functioned changed abruptly following the outbreak of war in Korea. While it underwent further change in later years of the post-World War II decade, the pre-Korea scene was already history. Federal programs and policies were no longer directed towards unqualified stimulation of activity. The almost unlimited liquidity enjoyed by financial institutions through the earlier price support of government securities —which for the individual lending institution made them almost interchangeable with cash—was sharply reduced by changes in federal monetary and fiscal policies. Demands for residential building and real estate, though less urgent than in earlier postwar years, continued generally strong through the second half of the decade and for a time were under

[10] The only nonliberalizing provision included in this act, in addition to the rescinding of FNMA's advance commitment authority, was the withdrawal of authority for the VA to guarantee small second mortgage loans in conjunction with FHA-insured first mortgage loans.

[11] Less than one year before passage of the Housing Act of 1950, another special purpose program was born when FHA was authorized to insure mortgages on very liberal terms for rental housing built on or near military installations (under a new Title VIII added to the National Housing Act by P.L. 211, 81st Congress, approved August 8, 1949). In 1949, also, the authority of FHA to insure mortgages on new rental housing (under the liberal section 608 program), due to expire on March 31, 1949, was extended on four different occasions and finally allowed to expire on March 1, 1950. FHA was actually authorized to continue issuing commitments under that program on applications for insurance submitted on or before March 1, 1950.

direct restraint by federal actions. Demands for industrial facilities, for consumer goods, and for municipal improvements were also large during much of the period after 1950.

In that framework, total demands on private capital and credit markets at times exceeded the available supply of funds, including commercial bank credit. As a consequence, during periods when interest rates and yields were rising because of competition for limited funds, the attractiveness to investors of federally underwritten mortgages having inflexible interest rates waned in favor of conventional mortgages and other capital market securities with completely flexible rates (see Chapter 4 for discussion of mortgage yields and Chapter 5 for analysis of shifting mortgage flows).

MORTGAGE MARKETS UNDER RESTRAINT, 1951–1953

For approximately three years after the beginning of Korean hostilities, mortgage markets were under some federal restraint, either directly by restrictive policies or indirectly by credit and monetary actions. Later, with the lifting of direct federal government restrictions, mortgage markets operated in an atmosphere alternating between credit ease and restraint, influenced by general credit and monetary policies, private capital market conditions, and the re-establishment of most of the pre-Korean federal mortgage terms and practices. In that new environment, further structural changes in mortgage markets occurred as lender reactions varied; borrowers adjusted to or withdrew from the market, and mortgage underwriting terms were alternately tightened and relaxed.

Early Post-Korean Restrictions

The Korean war started at a time when rising economic and financial activity in the United States had already reached unusually high levels. Demands for real estate and construction had expanded to the point where they were straining the nation's productive capacity and resulting in rapid increases in prices, wages, and costs. By mid-1950, even though production of building materials and construction employment were at record levels, shortages of materials and labor and consequent disorganization of markets were common. In this setting, broad restrictive actions were taken by the federal government to dampen inflationary pressures and to conserve resources necessary to the successful prosecution of the war. In construction and real estate markets, terms on which mortgage credit could be made available were restricted and nonessential construction and the use of materials were limited.

Within one month after the start of Korean hostilities, in response to direct requests of the President, the Federal Housing and Veterans Administrations took restricted terms on which they would insure and guarantee mortgage credit, and the Federal Home Loan Bank system adopted restrictive measures for member savings and loan associations. Though fairly mild, they were the first restrictive actions taken by those agencies in nearly twenty years of federal intervention in real estate and mortgage markets. The most important were increase by 5 percentage points of downpayments required on FHA and VA loans, setting construction costs prevailing on July 11, 1950 as the maximum for appraisal purposes, and reduction from $16,000 to $14,000 of the maximum FHA insurable loan on one-family houses.[12]

Measures directly limiting nonessential construction, use of materials, and limiting price increases followed in a short time. Administered by newly created or reconstituted defense agencies—National Production Authority, Office of Price Stabilization, and Wage Stabilization Board—the measures were carried out through direct prohibition of certain types of construction, requirement of authorization for other types, priorities on basic and scarce materials for nondefense uses, and regulation of prices and wages in the construction industry. The techniques of operation, frequently changed, became stabilized by mid-1951 under the Controlled Materials Plan which allocated to users the three basic metals—steel, copper, and aluminum. Supplementary "M" or limitation orders were also directed towards the reduction of nonessential production.[13]

Selective Regulation of Real Estate Credit

Federal actions restricting nonessential construction use of materials were authorized by the Defense Production Act of 1950. For mortgage markets, an added—perhaps heightened—significance of the Act lay in presidential authority to regulate nonguaranteed or noninsured real estate credit. Under Executive Order No. 10161, that authority was

[12] Other actions included requirements for higher downpayments in FHA Title I modernization and repair loans, for narrowing of allowable uses of VA direct loan funds, and for application of VA gratuity payments to the reduction of mortgage loan principal. Formerly the gratuity payment to veterans of 4 per cent of the guaranteed portion of a loan up to $160 could be used for any payments due on a purchased house. Its original purpose was to provide one year's interest on the guaranteed portion of a veteran's mortgage loan. The gratuity was discontinued as of September 1, 1953, by P.L. 149, enacted July 27, 1953.

[13] For a review of post-Korean restrictions on real estate credit and construction see two articles in the *Federal Reserve Bulletin:* "Construction Activity and Mortgage Credit," August 1950, pp. 936–937; and "Residential Real Estate Under Controls," August 1951, pp. 908–912.

delegated to the Board of Governors of the Federal Reserve System, with the stipulation that the Board "obtain the concurrence of the Housing and Home Finance Administrator with respect to provisions relating to real estate construction credit involving residential property before prescribing, changing or suspending any real estate construction credit regulation pursuant to the authority of the Defense Production Act of 1950."

Accordingly, Regulation X, the first selective control ever applied to real estate credit, was issued by the Board of Governors (effective October 12, 1950) with the concurrence of the Housing and Home Finance Administrator. Simultaneously, restrictions conforming to Regulation X were placed on FHA-insured and VA-guaranteed mortgage credit on new one- and two-family dwellings. On January 12, 1951, Regulation X was broadened to include new multifamily units and nonresidential commercial structures (office buildings, warehouses, stores, banks, hotels, motels, garages, restaurants).[14] The regulation did not restrict credit granted on existing properties, except FHA and VA loans, where it applied to both existing and new properties.

Regulation X and accompanying FHA and VA regulations were designed to reduce the demand for real estate credit, and thereby the volume of new construction and real estate transactions, by restricting the terms on which mortgage loans could be made (see Table 11). Minimum downpayments and rates of amortization together with maximum maturities were prescribed. The underlying formula allowed for a schedule of downpayments according to prices of houses. Longer maximum maturities, though not on a graduated basis, were permitted on loans secured by lower-priced houses, but no maximum maturities were specified on multifamily properties. All loans on nonresidential construction subject to Regulation X conformed to existing lending practices and administrative practicability—a maximum of 50 per cent of the value of the property and a maturity up to twenty-five years.[15]

Successive modifications of terms prescribed by Regulation X followed, either by administrative or legislative authority.[16] In each case, changes

[14] *Real Estate Credit, Regulation X,* as amended effective February 15, 1951, Board of Governors of the Federal Reserve System, p. 6.

[15] Board of Governors of the Federal Reserve System, *The Regulation of Real Estate Credit Under the Defense Production Act of 1950,* prepared at the request of the Office of Defense History, Bureau of the Budget, Executive Office of the President (mimeographed), February 24, 1953, p. 11.

[16] Amendments No. 1, No. 6, and No. 11 to Regulation X described in *Federal Reserve Bulletin,* March 1951, p. 271, September 1951, p. 1132, and June 1952, pp. 650–651. See also the Defense Housing and Community Facilities and Services Act of 1951.

TABLE 11

Terms of Mortgage Lending Under Regulation X
(conventional and FHA-insured mortgages)

	1- TO 4-FAMILY PROPERTIES						MULTIFAMILY PROPERTIES			
	Oct. 12, 1950 to *Sept. 1, 1951*		*Sept. 1, 1951* to *June 11, 1952*		*June 11, 1952* to *Sept. 16, 1952*		*Jan. 12, 1951* to *June 11, 1952*		*June 11, 1952* to *Sept. 16, 1952*	
TRANSACTION PRICE PER FAMILY UNIT	Maximum Loan Amount	Loan-to-Value Ratio	Maximum Loan Amount	Loan-to-Value Ratio	Maximum Loan Amount	Loan-to-Value Ratio	Maximum Loan Amount	Loan-to-Value Ratio	Maximum Loan Amount	Loan-to-Value Ratio
$5,000	$4,500	90.0	$4,500	90.0	$4,750	95.0	$4,150	83.0	$4,500	90.0
8,000	6,450	80.6	6,800	85.0	7,050	88.1	6,340	79.2	6,850	85.6
10,000	7,700	77.0	8,500	85.0	8,550	85.5	7,400	74.0	7,950	79.5
12,000	8,900	74.2	9,600	80.0	9,650	80.4	8,460	70.5	9,030	75.2
14,000	10,100	72.1	10,400	74.3	10,750	76.8	9,520	68.0	10,110	72.2
16,000	10,900	68.1	11,000	68.8	11,750	73.4	10,250	64.1	11,150	69.7
18,000	11,300	62.8	11,400	63.3	12,650	70.3	10,650	59.2	12,150	67.5
20,000	11,700	58.5	11,800	59.0	13,550	67.8	11,050	55.2	13,150	65.8
22,000	11,900	54.1	12,000	54.5	14,250	64.8	11,450	52.0	13,890	63.1
25,000	12,500	50.0	12,500	50.0	15,000	60.0	12,500	50.0	15,000	60.0
Over 25,000	—	50.0	—	50.0	—	60.0	—	50.0	—	60.0

SOURCE: *The Regulation of Real Estate Credit Under the Defense Production Act of 1950*, prepared at the request of the Office of Defense History, Bureau of the Budget, Executive Office of the President, February 24, 1953, Table 1, p. 119.

Maximum loan maturities permitted on one- to four-family properties from October 12, 1950 to September 1, 1951 were twenty-five years up to $7,000 value and twenty years for all other properties. Liberalization of terms on September 1, 1951 provided for twenty-five year maturities up to $11,000 value and twenty years for higher-priced properties. No maximum maturities were specified for loans on multifamily properties.

On loans for new construction of nonresidential properties, terms under Regulation X for all dates were a maximum loan of 50 per cent of value and maximum maturity of twenty-five years.

Terms on VA-guaranteed mortgages generally provided for loan-to-value ratios 5 percentage points higher in the lower and upper price ranges, and 10 percentage points higher in the middle price range. Maximum maturities permitted were the same as for FHA and conventional loans. Terms for VA loans were in accord with the general authorization in the Defense Production Act for preferential treatment of veterans' loan applications.

relaxed terms because of special needs associated with housing in defense areas or because of recognized inequities in various price and income groups. Finally, on September 16, 1952, just short of two years after they were first imposed, came suspension of credit restrictions under Regulation X and most of those under FHA and VA regulations in accordance with provisions of the Defense Production Amendments of 1952. The act of June 30, 1952 (the expiration date of Regulation X) extended for one year the Regulation's authority and provided further for a "period of residential credit control relaxation," during which downpayment requirements could not exceed 5 per cent of the transaction price. The period was to begin after three consecutive months with housing starts below a seasonally adjusted annual rate of 1.2 million. Production of housing having remained below that number during June, July, and August, 1952, the Board of Governors of the Federal Reserve System suspended Regulation X as of September 16, 1952.

Accompanying the suspension of Regulation X, restrictions on terms of FHA and VA loans were removed except for the requirements of a minimum downpayment of 5 per cent, a maximum maturity of twenty-five years, and a maximum FHA loan amount of $14,000 on one-family houses.[17] By April 1953, with the further abatement of inflationary pressures, all remaining credit restrictions were revoked, and statutory terms of mortgage lending were restored to the levels before October 12, 1950.

Program of Voluntary Credit Restraint

During most of the Regulation X period, a general voluntary credit restraint program, encompassing extension of real estate credit, was also in effect. General authority "to encourage financing institutions to enter into voluntary agreements and programs to restrain credit" was included in the Defense Production Act of 1950 and delegated by the President to the Board of Governors of the Federal Reserve System. In announcing the new program, the Board requested all institutions to extend credit in ways that would "help maintain and increase the strength of the domestic economy through the restraint of inflationary tendencies and at the same time to help finance the defense program and the essential needs of agriculture, industry and commerce."[18]

[17] The restrictions applied chiefly to VA loans, which before the credit regulations could be made with no downpayment and for as long as thirty years. Now for VA-guaranteed loans on houses priced between $7,000 to $8,400, a 4 per cent downpayment was required. On houses priced below $7,000, no downpayment on loans was required but closing costs up to 4 per cent of the price had to be paid in cash.

[18] "Program for Voluntary Credit Restraint," *Federal Reserve Bulletin*, March 1951, p. 263.

One standard proposed by the Board to cooperating institutions was to screen loan applications not only for credit-worthiness but also by criteria of purpose and uses of loans. As a general criterion for sound lending, the Board's view was that each loan should "commensurately increase or maintain production, processing and distribution of essential goods and services."[19]

The program was implemented by the National Voluntary Credit Restraint Committee, including representatives of commercial banks, life insurance companies, mutual savings banks, savings and loan associations, and investment banking firms. The national committee coordinated the work of a system of committees, among them, regional committees composed of representatives of participating financing institutions in divergent geographic areas. For the guidance of the regional committees in dealing with inquiries of financial institutions about particular applications for credit, the national committee issued a statement of principles and various bulletins on recommendations developed for specific types of credit.[20]

For real estate credit, recommendations were limited to transactions outside the scope of Regulation X—chiefly loans on existing properties and sale-leaseback arrangements on commercial and industrial properties. Recommendations followed a general principle of the national committee, that the function of the program was not "to make the transfer of real estate impossible or impracticable, but rather to reduce inflationary pressures by limiting the amount of additional credit created in the process of real estate transfer."[21] Financial institutions were urged to limit real estate loans to keep total mortgage debt outstanding on any property within the larger of two amounts, two-thirds of its value or the limits imposed by Regulation X on such new construction.[22] Application of the principles of the program was strongly recommended also to certain kinds of property leasing. The committee urged recognition of the fact that leasing arrangements, when used in connection with existing construction of all types and with new construction of commercial or industrial buildings, were sometimes used as substitutes for mortgage financing. Some examples of such leasing arrangements cited by the committee were

[19] *Ibid.*, p. 264.

[20] *Monetary Policy and the Management of the Public Debt, Their Role in Achieving Price Stability and High-Level Employment*, replies to questions and other material for the use of the subcommittee on general credit control and debt management, Joint Committee on the Economic Report, 82nd Congress, Part I, p. 433.

[21] Bulletin No. 4 of the Voluntary Credit Restraint Committee, "Loans on Real Estate," *Federal Reserve Bulletin*, July 1951, pp. 752–753.

[22] *Monetary Policy and the Management of the Public Debt*, p. 436.

"sale-leaseback arrangements, long-term leases which may be renewed for a nominal rental, and leases in which the lessee has the right to have rental payments applied to the purchase price in a subsequent exercise of an option to buy the leased property."[23]

The voluntary credit restraint program was suspended May 12, 1952 (four months before the suspension of Regulation X) by the Board of Governors in accordance with a recommendation of the national committee.[24] Legal authority for the program was repealed June 30 with the enactment of the Defense Production Act Amendments of 1952, which provided "that no voluntary program or agreement for the control of credit shall be approved or carried out. . . ."[25]

Some indication of the impact of selective real estate credit regulations on the flow of funds into various mortgage sectors is given in Chapter 5, pp. 126–128. The delayed decline in mortgage flows into new construction indicate the time lags in effectuating the post-Korean restrictions. They resulted partly from the unusually large volume of mortgage commitments outstanding and were in part the usual lags associated with real estate activity (see Chapter 7, pp. 175–176). The subsequent decline in mortgage lending, moreover, must be attributed largely to the concurrent operation of a restrictive monetary policy and only in part to selective credit regulations. Though the direct impact of real estate credit controls is not measurable, there can probably be little doubt that, among those in operation, the voluntary credit restraint program was the least effective. The real estate credit area covered by the program—conventional mortgage loans on existing houses—expanded steadily during the period of voluntary credit restraint, while other types of real estate credit declined. In part this may have reflected the voluntary nature of the program and in part the fact that, with all other areas of residential real estate credit under legal restraint, the one nonlegally regulated area was stimulated.

While the voluntary credit restraint program appears to have been ineffective in real estate markets, there is no way to determine whether the extension of conventional mortgage credit on existing houses would have been even greater in its absence. The question remains also whether general monetary restraints would have been so effective in the absence of the selective regulation of real estate credit through Regulation X and associated FHA and VA regulations.

[23] Bulletin No. 4, *Federal Reserve Bulletin*, January 1952, p. 24.

[24] "Suspension of Program for Voluntary Credit Restraint," *Federal Reserve Bulletin*, May 1952, p. 501.

[25] *Federal Reserve Bulletin*, July 1952, p. 772.

Monetary and Debt Management Policies and Liquidity of Financial Institutions

A turning point in postwar capital market developments was the change in federal monetary and debt-management policies, set forth in the joint announcement (March 4, 1951) by the Secretary of the Treasury and the Chairman of the Board of Governors of the Federal Reserve System. Both authorities had "reached full accord with respect to debt-management and monetary policies to be pursued in furthering their common purpose to assure the successful financing of the Government's requirements and, at the same time, to minimize monetization of the public debt."[26] The agreement resulted in the withdrawal of inflexible Federal Reserve support of the government securities market, and thus for the first time in the postwar period permitted market forces to determine prices and yields of those securities.

Concurrently, the Treasury announced a new offering of long-term nonmarketable bonds bearing a 2¾ per cent coupon in exchange for outstanding 2½ per cent Treasury bonds of 1967–1972. One intention of the action was to discourage long-term investors from liquidating their holdings of government securities. In that new market framework, mortgage lenders could no longer look to their government securities portfolio as a ready source of funds for acquisition of mortgages. Indeed, for some months after the announcements of the accord and new Treasury offering, lenders were unwilling to sell their government securities at the reduced prices then prevailing. Hence funds available for new mortgage financing shrank as the large volume of mortgage commitments made earlier absorbed such funds available from other sources.

As demands for credit and capital continued to press upon the supply of savings during the two years following the accord, monetary and debt-management policies were directed towards the restraint of bank credit expansion and minimizing of debt monetization. By early 1953, the Federal Reserve had raised the discount rate to 2 per cent from the early 1951 low of 1¾ per cent, and the Treasury had issued a new long-term bond bearing a 3¼ per cent rate. In the face of generally rising interest rates and yields, federally underwritten mortgages with less flexible rates became unattractive to investors with alternative uses of funds. In May 1953, maximum interest rates on FHA and VA loans were increased to 4½ per cent, a level more in line with returns on competitive investments.

Some indication of the reduced liquidity of financial institutions in

[26] *Federal Reserve Bulletin*, March 1951, p. 267.

the years following the "accord" is given in Table 10. Though the main types of financial institutions still owned a large volume of U.S. government bonds at the time of the accord—some $87 billion—they disposed of less than $13 billion between 1951 and 1956. This was only about one-third of the net amount sold in the first half of the postwar decade. It was, moreover, only about one-fifth of the net acquisition of mortgages in the second half, 1951–1956. In that period, therefore, in contrast to the preceding five years, it was the net inflow of savings for all types of financial intermediaries that provided the major source of funds for mortgage investment. Among the major types of financial institutions, there were marked differences in liquidity and investment behavior, just as there were in the first half of the postwar decade. The analysis of these differences will be taken up in Chapter 5.

Reduction in FNMA Support of the Mortgage Market

Reinforcing the limitations of mortgage market activity through direct and indirect credit restraints, so far noted, were a series of administrative and statutory actions reducing the broad support of the Federal National Mortgage Association. The advance commitment authority of the Association had already been repealed in April 1950, and contracts to purchase new mortgages were being made on an "over-the-counter" basis only. Further actions circumscribing FNMA support during the next three years included: (1) the requirement that mortgages, to be eligible for purchase, must be insured or guaranteed by FHA and VA and held by the originator, all within specified time limits; (2) reduction in the proportion of its loans that could be sold to FNMA by a lender; (3) allocation of funds for purchase of mortgages under emergency housing programs, reducing the amount available for general market support; and (4) suspension of purchases of mortgages not covered by those special programs.[27]

The first action, involving time limitations, was taken June 29, 1951, when FNMA announced that it would confine its purchases to mortgages insured or guaranteed on or after March 1, 1951, and held by the originator for not less than two months or more than one year. The motive underlying it was to prevent possible large-scale disposal of mortgages by lenders in order to fulfill earlier mortgage commitments or to purchase securities, following the Federal Reserve-Treasury accord and subsequent capital market changes. The second, allocation of funds for special housing, occurred during the next six months. FNMA set

[27] "FNMA in the Postwar Mortgage Market," *Monthly Review of Credit and Business Conditions*, Federal Reserve Bank of New York, December 1955, p. 160.

aside a total of $600 million of its uncommitted funds for the purchase of mortgages on emergency types of housing programmed by the Housing and Home Finance Administrator in critical defense areas, for military use under Title VIII of the National Housing Act, and for victims of major disasters.[28] In addition, the Association was authorized to issue advance commitments to purchase such mortgages in an amount not to exceed $200 million outstanding by the end of 1951.[29] By the end of March 1952, less than $50 million was available for the purchase of mortgages not on defense, military, or disaster housing.

In early April, with the complete exhaustion of uncommitted funds, FNMA took its third action, suspending purchase of mortgages not covered by special federal programs.[30] Purchases were resumed in early September of that year, following passage of the Housing Act of 1952. Its authorization of $900 million for advance FNMA commitments to purchase mortgages on defense, military, and disaster housing freed the remaining $362 million reserved for such purchases to be spent for other types of mortgages. Resumption of purchases outside the special federal programs by FNMA, however, restricted lenders to sale of not more than half their eligible FHA and VA mortgage loans made after March 1, 1952.[31] Previously lenders could sell to FNMA all of the VA loans they had originated during a specified period.

The additional relatively small amount of funds made available to FNMA for purchase of mortgages on nondefense and nondisaster housing was soon exhausted, and in early April 1953, the Association again suspended those purchases until the reorganization of FNMA under a new charter on November 1, 1954. Nondefense and nondisaster mortgages, however, again became eligible for purchase in July 1953, under a new "one-for-one" program authorized by the Housing Amendments of 1953.[32] The inauguration of that program brought to an end a period of about two years during which FNMA had provided little or no support to the mortgage market.

[28] Funds were set aside by administrative action for housing on three separate occasions: July 16, 1951, $350 million (FNMA Bulletin No. 185); August 31, 1951, $50 million (FNMA Bulletin No. 192); and October 2, 1951, $200 million (FNMA Bulletin No. 198).

[29] P.L. 139, 82nd Congress, approved September 1, 1951.

[30] *Background and History of the Federal National Mortgage Association*, Federal National Mortgage Association, April 30, 1955 (multilithed) p. 31.

[31] P.L. 531, 82nd Congress, approved July 14, 1952. This act also raised the advance commitment authority of FNMA to purchase defense, military, and disaster mortgages to $1,152 million. Previously the commitment authority had been increased to $252 million by Public Law 309, 82nd Congress, approved April 9, 1952.

[32] P.L. 94, 83rd Congress, approved June 31, 1953. The "one-for-one" program is discussed in the next section.

RESUMPTION OF EXPANSIONARY FORCES, 1953–1956

With the abatement of inflationary pressures, the Federal Reserve moved vigorously in the spring of 1953 to reverse its earlier policy of credit restraint. The first open-market purchases of Treasury securities in May were followed by purchases in June, August, and September to supply additional reserves to the banking system. In July, moreover, the Federal Reserve reduced bank reserve requirements on net demand deposits. In December, the Federal Open Market Committee declared its policy to be the promotion of economic growth and stability "by actively maintaining a condition of ease in the money market."[33] This policy was continued through most of 1954, implemented by reductions in the Reserve Bank discount rate in February and April, additional open market purchases in late spring, and a further lowering of member bank reserve requirements around mid-year.

Accompanying the Federal Reserve policy of "active ease," a supply of funds in excess of demand generally characterized financial markets during 1954. With the mild recession also, the net flow of savings into financial intermediaries increased at an accelerated rate and debt repayments were large. The volume of new corporate securities available to investors, on the other hand, was well below the 1952–1953 peak as plant and equipment expenditures declined. Moreover, net borrowings of the federal government were sharply reduced in 1954 and no long-term bonds were offered. Short-term credit demands by businesses and consumers were also markedly reduced in that year.

The interaction of reduced credit demands and increased availability of funds resulted in a marked general decline in interest rates and yields in financial markets. The competitive position of mortgages, therefore, especially federally underwritten mortgages, was considerably improved. Mortgages regained favor as investment media for financial intermediaries, and they made funds available through 1954 and into 1955 on far more favorable terms than in preceding years.

Coincident with the developing ease in financial markets from mid-1953 through 1954, federal actions were directed specifically towards broadening and stimulating housing and mortgage markets. In April 1953, remaining restrictions on FHA and VA loans, imposed in October 1950, were removed by administrative action, and on June 30 statutory authority to restrain such credit under the Defense Production Act of 1950 expired. Maturities up to previous statutory maxima were again permitted, for FHA loans twenty-five years (thirty years in some cases for loans on small

[33] Board of Governors of the Federal Reserve System, *Fortieth Annual Report*, 1953, Appendix, "Record of Policy Actions, Board of Governors," p. 101.

houses) and for VA loans, thirty years. Further, minimum downpayments on houses purchased with VA loans were no longer required. With the earlier suspension of Regulation X and the Voluntary Credit Restraint Program, mortgage markets thus were completely free of restrictions for the first time in nearly three years.

Moreover, to improve the competitive position of federally underwritten mortgages in the capital market, maximum interest rates of 4 per cent previously permitted on VA-guaranteed and 4¼ per cent on most FHA-insured home mortgage loans were increased in early May 1953, to 4½ per cent. This action followed several months of reduced availability of funds for FHA and VA loans in the face of rising yields on alternative investments.[34] Under the housing amendments of 1953, maximum interest rates on other FHA home loans were increased (June 30). More important for its basic effect on mortgage markets was an amendment of earlier legislation, permitting builders and sellers to absorb discounts associated with the sale of VA-guaranteed mortgages. Thus VA loans could compete more effectively in the capital market with other loans and securities whose rates were flexible.[35] Other provisions of the Housing Amendments of 1953 made it possible for FNMA to participate more actively in mortgage markets by authorizing the Association to use, for the general purchase of mortgages, part of the $900 million reserved a year earlier for purchases of defense, military, and disaster mortgages only, and by establishing the "one-for-one" program. Under that program, FNMA was permitted to enter firm agreements with purchasers of its mortgages to buy an equal amount of eligible mortgages from such purchasers within one year. Armed with firm FNMA commitments to purchase permanent residential mortgages, builders and mortgage originators were able to obtain interim short-term financing for construction projects that probably would not be otherwise obtainable.[36]

[34] The FHA increase was authorized, effective May 2, by the Commissioner of the Federal Housing Administration, as permitted under the National Housing Act. The VA increase was authorized, effective May 5, by the Administrator of Veterans Affairs, with the approval of the Secretary of the Treasury, as provided for in the Housing Act of 1948.

[35] See Chapter 4 for a more complete discussion of mortgage interest rates and yields and the history and operation of mortgage discounts.

[36] The Federal National Mortgage Association placed the "one-for-one" program in operation on July 27, 1953, with a total purchasing authority of $500 million. It established sales prices of 96 per cent of par on VA 4 per cent loans, 97.75 on FHA 4¼ per cent loans, and par for the then recently authorized 4½ per cent FHA and VA loans. Purchases of mortgages under that program—limited to FHA and VA loans bearing 4½ per cent interest rates—were at par, less total charges of 1½ per cent. The charges included 1 per cent for the FNMA advance contract to purchase plus ½ per cent for acquisition and service costs on mortgages actually purchased. (See "Residential Real Estate Developments," *Federal Reserve Bulletin*, August 1953, p. 814.)

The use made of the one-for-one program by the mortgage and building industries appears in figures showing that sales from FNMA's mortgage portfolio increased sharply in late 1953 and advanced to a postwar peak in spring of 1954. The $500 million authorization was exhausted before the scheduled expiration of the program on July 1, 1954. At the same time, with the easing of mortgage markets, FNMA was not called upon to honor all of its commitments to purchase mortgages, and some $70 million of such commitments expired unused.[37]

The Housing Act of 1954 authorized additional federal actions to stimulate further the demand for and supply of residential mortgage credit.[38] The actions authorized included liberalization of the FHA mortgage insurance program and of the terms of loans by federal savings and loan associations as well as establishment of the Voluntary Home Mortgage Credit Program. Brief descriptions of these and other related provisions of the act will suffice here.

Liberalization of terms under which the Federal Housing Administration could insure mortgages on both new and existing properties included: raising the maximum amount of loans on one- and two-family dwellings from $16,000 to $20,000; increasing the maximum loan-to-value ratios on new properties from 90 to 95 per cent and on existing properties from 80 to 90 per cent; and lengthening maximum maturities from twenty-five to thirty years. The difference between mortgage terms on new and existing properties, formerly substantial, was nearly eliminated by the act. The FHA program was further broadened and liberalized by a new provision of far more liberal terms for insurance of mortgages on homes for servicemen than for civilians.

Federal savings and loan associations were permitted to increase the maximum amount of their home mortgage loans from $20,000 to $35,000. Supplementing this provision of the act, the Federal Home Loan Bank Board authorized, December 1954, member savings and loan associations to lengthen mortgage loan maturities from twenty to twenty-five years.

The Voluntary Home Mortgage Credit Program was designed to encourage private lenders to make funds available for federally underwritten mortgages on housing located in small and remote communities where local capital or loan facilities may be inadequate. The services are available to minority groups in any area on terms as favorable as for others. Its national committee and sixteen regional committees composed of representatives of the mortgage industry receive applications from prospective

[37] "FNMA in the Postwar Mortgage Market," p. 160.
[38] P.L. 560, 83rd Congress, enacted August 2, 1954.

mortgage borrowers, just described, and attempt to place mortgage loans with voluntary participating lenders. The primary objective of the program is to minimize or obviate the need for direct federal mortgage lending.

The same objective—ultimate substitution of private for federal ownership of mortgages—underlies another major but not liberalizing provision of the act, which authorized the reorganization of FNMA. Under its new charter, FNMA was directed to reorganize its structure into three separate and distinct operations providing for: (1) a secondary market for federally underwritten residential mortgages; (2) special assistance for financing selected types of mortgages originated under special housing programs; and (3) management and liquidation of its mortgage portfolio held or acquired pursuant to contracts entered into under its previous charter.[39]

While the Housing Act of 1954 had a significant influence on residential mortgage markets in later years, it played no part whatever in the expansion that occurred during the second half of 1954. At the time, the view was widely held that the expansion was the direct result of the liberalizing provisions of the act. It is clear, however, that the 1954 rise in mortgage and housing activity was limited almost entirely to the VA sector of the market; the 1954 Housing Act provided no change in VA mortgage terms. The act liberalized terms only of FHA loans, and the volume of such loans showed little change during 1954.[40] The increase in FHA mortgage flows a year later, mainly for financing existing houses, is traceable in large part to the liberalizing provisions of the Housing Act of 1954 (see Chapter 5, p. 129).

MORTGAGE MARKETS ONCE AGAIN UNDER RESTRAINT, 1955–1956

The pace of business activity began to quicken in late 1954 and continued strongly upward during 1955. Demands for credit by business, consumers, and governments to finance expenditures for plant and equipment, durable goods, and public projects increased to record levels. The demands strained capital and money markets and also the productive resources of the nation. A rapid upturn in interest rates, costs, and prices followed during 1955. In the construction industry cost and price advances came after nearly three years of remarkable stability. In that rapidly developing inflationary setting, federal actions were turned once

[39] See Chapter 7, section on Federal National Mortgage Association, for a fuller discussion of the reorganization of FNMA. See also "FNMA in the Postwar Mortgage Market," pp. 161–162.

[40] See Saul B. Klaman, "Effects of Credit and Monetary Policy on Real Estate Markets, 1952–1954," *Journal of Land Economics*, August 1956, pp. 246–247.

again toward restraining demands for mortgage credit and supply of it and toward limiting credit expansion generally.

Thus, during the closing years of the first postwar decade, activity in mortgage markets was again under restraint as in 1951–1953. There were important differences between the two periods, however, in the nature of the restraints operating. Throughout most of the earlier period, both general credit and monetary policies and specific federal mortgage programs and policies were directed towards restraint; during most of 1955 those policies were coordinated, but during 1956 they operated in opposite directions. As mortgage credit became increasingly stringent during 1955, the federal government reversed its policy of restraint in administering mortgage programs. During 1956, all major administrative and statutory actions were directed chiefly towards easing the tightness that had developed in mortgage markets. As the year and the decade ended, however, the effectiveness of the policies proved to be limited in the face of continuing strong demands for both short- and long-term loans, the effects of restrictive Federal Reserve credit and monetary policy, and the resulting rising interest rates and yields on corporate, state and local, and federal government securities.

Coordinated Actions Restraining Mortgage Activity

As the general business recovery accelerated, the Federal Reserve gradually modified its policy of "active ease" in effect through most of 1954. In its directive of December 7, 1954, the Federal Open Market Committee declared its policy to be promotion of economic growth and stability "by maintaining a condition of ease in the money market."[41] The word "actively," included in the policy directive of December 15, 1953 (see page 66) was deleted, and the new policy was designed to restrain inflationary tendencies. Between April and November 1955, four increases in the Reserve Bank rediscount rate raised it from $1\frac{1}{2}$ per cent to $2\frac{1}{2}$ per cent. Open market operations limiting bank credit expansion were initiated around early August. An increasingly restrictive monetary policy in 1956 brought the rediscount rate to 3 per cent by late summer, the highest in nearly twenty-five years.

Supplementing the monetary actions of the Federal Reserve, the federal mortgage insurance and guaranteeing agencies acted to restrain demands for mortgage credit. Effective April 28, 1955, the Federal Housing Administration and Veterans Administration required that all

[41] Board of Governors of the Federal Reserve System, *Forty-first Annual Report*, 1954, Appendix, p. 98.

closing costs for houses purchased with FHA and VA loans be paid in cash.[42] This meant that for VA mortgages the "no downpayment loan," (in total amount, with closing costs, exceeding the appraised value of the property) was eliminated. Shortly thereafter, both federal agencies increased minimum downpayments by 2 percentage points and reduced maximum loan maturities from thirty to twenty-five years.[43]

In mid-July, the Federal Home Loan Bank Board joined other federal agencies attempting to limit mortgage credit expansion by urging savings and loan associations to curb their forward commitments to make loans. This advice was followed, September 13, by requests to each Federal Home Loan Bank "to advise its member institutions to follow a loan program which will meet loan demands out of savings and loan repayments."[44] Savings and loan associations had been relying more than usually on borrowings to finance their expanded mortgage lending programs. By the end of summer advances from Federal Home Loan Banks amounted to a record $1.2 billion compared with less than $700 million a year earlier. The Federal Home Loan Banks had, in the meantime, increased interest rates to member associations in line with rates on funds borrowed in the capital market.

Reversal of Federal Mortgage Policies

Before 1955 had ended, federal mortgage policies were reversed and through 1956 were directed towards stimulation of market activity. On December 13, 1955, the Federal Home Loan Bank Board eased somewhat the restrictions imposed in September. It permitted member institutions to borrow funds for mortgage lending in amounts not to exceed 10 per cent of savings capital.[45] In January 1956, the Federal Housing Administration and Veterans Administration rescinded their previous reduction of loan maturities and restored the maximum maturities to thirty years.[46] The Federal National Mortgage Association announced an optional mortgage repurchase plan allowing, for a 1 per cent fee, repurchase within nine months of mortgages sold to FNMA at the selling price.[47] Institutions

[42] Veterans Administration, Information Service, press release, April 27, 1955; Federal Housing Administration, 1955 Annual Report of Housing and Home Finance Agency, p. 45.

[43] Veterans Administration Information Service, press release, July 30, 1955; Federal Housing Administration, press release No. 55–57, July 31, 1955.

[44] Federal Home Loan Bank Board, press release, September 13, 1955.

[45] Federal Home Loan Bank Board, press release, December 13, 1955.

[46] Veterans Administration Emergency Interim Issue (EM 4AB-128) and Federal Housing Administration letter to all approved mortgagees, January 17, 1956.

[47] FNMA press release No. 202, January 25, 1956.

could thus obtain temporary funds for new lending without permanently disposing of favorable mortgage holdings.

Administrative actions were supplemented by the Housing Act of 1956, which in the main liberalized the terms of FHA mortgage insurance and FNMA secondary market programs.[48] Loan-to-value ratios on which FHA would insure mortgages on existing one- to four-family houses were made equal to those on new houses. On multifamily rental housing both loan-to-value ratios and maximum loan amounts were increased. The Act authorized FNMA to reduce from 3 to 2 per cent the amount of stock to be bought by sellers of mortgages to FNMA, and to 1 per cent under certain conditions. It authorized FNMA to issue "standby" commitments for one year to purchase mortgages—a practice introduced earlier by financial institutions.[49] Further statutory action at about the same time extended the VA loan guarantee program for World War II veterans until July 1958, with provision for loan applications on hand to be covered up to July 1959. For Korean War veterans the VA loan guarantee program was extended to January 1965.

The federal government continued to attack the tight mortgage credit situation on both the demand and supply fronts in a coordinated action announced by the White House, September 1956. The FHA reduced downpayment requirements on houses appraised at $9,000 or less for mortgage insurance purposes. The Federal Home Loan Bank Board increased the amount of advances member institutions could have outstanding from Federal Home Loan Banks from 10 to 12.5 per cent of their savings capital. The Federal National Mortgage Association, in addition to reducing the amounts of stock to be purchased by those selling mortgages to the Association from 2 to 1 per cent of the value of mortgages sold, raised the purchase price of its standby commitments from 92 to 94 per cent of par. The new price was not far below the bottom of the range of FNMA purchase prices for immediate delivery. In addition, in order to maximize its support of the market for new houses, FNMA announced (November 1956) limitation of its purchases under the secondary mortgage market program to mortgages insured or guaranteed no earlier than four months before the proposed sale to the Association.[50]

[48] P.L. 1020, 84th Congress, August 7, 1956.

[49] See Chapter 7, section on Mortgage Commitment Techniques, for a discussion of the standby commitments. Essentially, they are given by a financial institution in consideration of the nonrefundable fee associated with such commitments. The commitment price is so far below the prevailing market price that the institution does not expect to be called upon to fulfill it.

[50] FNMA press release No. 227, November 23, 1956.

Notwithstanding the many Federal actions, funds for federally underwritten mortgages continued to be difficult to obtain because of their competitive interest rate disadvantage. Reflecting demand pressures in all sectors of the capital market, yields on long-term corporate, municipal, and government securities had advanced rapidly to new postwar highs during 1956 (Chapter 4, Chart 7). To make insured mortgage loans more attractive to investors in this situation, the Federal Housing Administration increased their permitted maximum interest rate from $4\frac{1}{2}$ to 5 per cent, effective December 4, 1956.[51] The increase was the first since May, 1953, when interest rates on both FHA and VA loans were increased. The Veterans Administration had no administrative authority to increase further the interest rate on VA loans, however, which remained at $4\frac{1}{2}$ per cent as 1956 ended. The general subject of mortgage interest rates is dealt with in Chapter 4.

[51] Federal Housing Administration, press release No. 56–59, December 1, 1956. The permitted maximum interest rate for mortgages insured on multifamily housing (FHA Section 207 loans) and on cooperative housing (FHA Section 213 loans) was increased from $4\frac{1}{4}$ to $4\frac{1}{2}$ per cent.