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CHAPTER 4

Lending Experience of Federal Credit Agencies

THE variety of federal lending and of loan insurance programs is such that it is exceedingly difficult to generalize concerning the credit experience of the government. A few facts, however, stand out clearly. First, it is fairly well established that the federal government had an exceptionally favorable record in those programs in which it refinanced debts that were in default during the economic depression of the thirties. The outstanding examples are the home mortgage refunding operations of the Home Owners' Loan Corporation and the farm mortgage refinancing carried out by the Land Bank Commissioner, both in the thirties. We shall come at a later point to the details concerning these programs; mainly, the explanation for the favorable credit experience is that the borrowers for the most part were only temporarily embarrassed and economic recovery rather quickly put them back on their feet.

A second conclusion, equally well-established, seems to be that the federal government has had an unfavorable credit experience when it has attempted to supply credit, sometimes during depression but even during periods of general economic prosperity, to business firms and farm enterprises unable—because of their newness, or owing to some weakness in financing position or management—to find financing on reasonable terms through private lenders. Large parts of the Reconstruction Finance Corporation's activities and certain of the programs in the agricultural field fall within this category.

Third and last, it is generally clear that the cooperative financial institutions sponsored by the federal government have fared well as lenders; indeed, they have shown a tendency to become more and more like private institutions, with which they often compete closely, and have registered a broadly comparable credit experience.

Default and Loss Experience

The general observations concerning loan experience may be illustrated by reference to those programs on which sufficient data are available to permit at least rough appraisals of default and loss experience.

AGRICULTURE

In agriculture this includes the experience of the federal land banks, the so-called Commissioner loans, the loans made since 1933 by the production credit associations, and the activities of the banks for cooperatives, the Rural Electrification Administration, and the Farmers Home Administration. The federal land banks have been active over a long period of time, and it is therefore possible to examine their experience under different economic conditions. From their establishment in 1917 until 1929, the twelve district banks had a largely favorable experience; indeed, it was slightly more favorable than the experience of life insurance companies. The percentage of their outstanding loans that were delinquent was around 5 percent over this period, and less than 3 percent of the loans made through the end of 1929 ended in foreclosure. Recoveries on properties sold during the period equaled 88 percent of the banks' investment in them and total losses on mortgage loans and real estate investments amounted to about 3 percent of loan extinguishments or 0.13 percent of cumulative outstanding loan balances.

Compared with the experience of the land banks, the record of a group of fifteen large life insurance companies during the twenties was considerably less favorable. At the end of 1929, the value of the properties which they held as a result of foreclosure amounted to 7.6 percent of their total farm mortgage investment, compared to 2.5 percent for the land banks. On the other hand, the life insurance companies recovered a larger percentage of their investment in foreclosed properties. Thirteen companies reported that they recovered about 95 percent of their total investment in properties sold in 1928 and 1929, compared with the 88 percent cited for land banks. Since the land banks were permitted during the twenties to lend up to 50 percent of the appraised value of land plus 20 percent of the value of insured permanent improvements, they were not compelled to follow a rigidly conservative lending program; but the evidence indicates that they did in fact lend conservatively and that they managed, by and large, to build a record that was somewhat better than that of typical private institutions.

As might be expected, delinquencies on the mortgage loan accounts of the land banks increased sharply in the decade 1930–1940, but not more so than the delinquencies on loans of private institutions. By the beginning of 1933, about half of the loans held by the land banks were delinquent or had been extended in order to prevent default;

land bank foreclosures averaged somewhat under 10,000 per year for the decade 1930–1940, compared with a cumulative total of less than 15,000 for the whole history of the land bank system up to 1930. This was not an unusual record, however, considering the fact that fifteen of the largest life insurance companies were forced to foreclose by 1937 on more than one-third of the loans that they had outstanding in 1928. Also, the loss experience of the land banks was severe, especially during the latter part of the decade. Throughout the period 1930–1940 total losses incurred on mortgage loans and real estate transactions averaged 0.70 percent of year-end loan balances. Finally, the available evidence suggests that in the thirties, as in the predepression years, life insurance companies were more successful than the land banks in disposing of farm properties. From 1930 to 1937, land bank recoveries averaged about 75 percent of the total cost of acquired properties, compared to nearly 90 percent for thirteen large insurance companies.

Between 1940 and 1953 there were virtually no delinquencies or foreclosures, and losses on real estate and mortgage transactions were negligible both for public and private institutions. The delinquency ratio of the land banks was reduced to the 5 percent level characteristic of the years before 1930; foreclosures declined from 859 in the fiscal year 1944 to 20 in fiscal 1953; and after 1948, recoveries on farms sold exceeded the land banks' investment in them.

The Land Bank Commissioner program (set up in 1933 with the idea of providing credit to farmers which could not be had through the facilities of the land bank system nor through the channels of private finance) was distinctly an emergency program, and the expectation from the beginning was for substantial losses. The Commissioner was authorized to make first mortgage loans to borrowers whose credit needs were not being met by the land banks or by private banking institutions, and second mortgage loans to supplement borrowing from the land banks. As might be imagined, many of the first mortgage loans involved the refinancing of defaulted loans held by the land banks. Moreover, the Federal Farm Mortgage Corporation, from whose funds Commissioner loans were made, followed a liberal policy in resetting and extending loans, provided the borrower was making a reasonable effort to carry them. As a result, from 1933 through 1940 the corporation's farm real estate acquisitions totaled about 10 percent of the total amount loaned. By the end of 1940, three-fourths of the acquired properties had been sold and about 72 percent of the corporation's investment in them had been recovered. Moreover, as of this date the losses on Commissioner loans were 0.42 percent of cumulative outstanding loan balances, compared to 0.51 percent for the land banks. The two are not in every way comparable, because the bulk of the Commissioner loans were made during the very bottom of the depression and had the full advantage of the recovery that followed, whereas the land bank experience reflected lending in the late twenties as well as in the early years of the thirties. Yet the comparison is instructive.

From 1941 on, experience under the Commissioner program paralleled that of other farm mortgage lenders. Delinquencies declined from about 25 percent of outstandings in 1939–1940 to 8 percent in 1945–1947. The percentage of investment recovered on properties sold increased from 70.4 percent in 1940 to 89.6 percent in 1946. Total losses from 1941 to 1951 on property acquired and subsequently sold equaled 0.57 percent of the cumulative amount of outstanding loans.

Experience with Land Bank Commissioner loans was far more favorable than had been anticipated. Furthermore, on the whole it was better than the experience of other federal programs designed to relieve distressed borrowers during the early thirties, primarily because Commissioner loans were made on a long-term basis, with liberal amortization requirements, and had the advantage of a subsequent long period of recovery. Loans that were made on shorter term, and which came to maturity before economic recovery had had its full effect, had a much less favorable record.

The relatively favorable experience of the programs designed to help borrowers who, by and large, could meet the credit standards of private finance but were unable to borrow because of inadequate credit facilities is well illustrated by the history of the production credit associations. The losses incurred by these cooperative financing agencies varied widely from one district to another, and among individual associations, but over all the record was approximately the same as that of commercial banks operating under similar conditions. Net losses for PCA's averaged about one-half of one percent of yearly outstanding loan balances in 1936–1940, compared to 0.58 percent for country national banks. From 1941 to 1946, both PCA's and country national banks reported recoveries in excess of losses in some years and for the remaining years, small net losses in relation to yearly outstandings. At the end of 1950 the loss rates for both PCA's and banks were less than 0.10 percent. Over the entire twenty-year history of the PCA's net losses and provision for losses have amounted to only 0.14 percent of total cash advanced under loan contracts, exclusive of renewals. This percentage has varied from a low of 0.08 percent in the Midwest (the Louisville, St. Louis, and Wichita farm credit districts) to a high of 0.33 percent in the northeastern section of the country.

Similarly, favorable records of loan experience have been built by the banks for cooperatives. The total net losses of these institutions have been only 0.13 percent of the cumulative outstanding loan balances, or 0.07 percent of the total amount of loans made from the beginning in 1933 through 1953. Like the land banks and the PCA's, the banks for cooperatives incurred much higher losses in the 1930's than during the years following 1940. At the end of 1941 the cumulative net losses were 0.2 percent of the loans made to that date and 0.29 percent of cumulative outstandings.

The REA has had very few losses on its loans made to local cooperative power and light companies. Through June 30, 1953, only two loans resulted in loss, and in both cases the amounts were small.

The heaviest losses in the agricultural field have come in those programs, currently administered by the Farmers Home Administration, in which credit was extended for general farm operating and production or emergency and disaster purposes, either on the security of farm real estate or on relatively short term. The credit programs of the Farmers Home Administration and its predecessors were specifically designed to assist low-income farmers, farm tenants, or farm laborers who could not obtain financing from private sources at reasonable rates of interest. It was to be expected, therefore, that losses under them would be substantial. The available evidence indicates that losses actually incurred to mid-1953 on all except the farm ownership and farm housing programs have not fallen short of expectations. Thus, the over-all loss rate in relation to the $2.9 billion loaned by the FHA since 1946 and by its predecessors as far back as 1918 was 5.3 percent, and nearly 7 percent if the total amount of interest written off is also included.[1]

However, losses through the FHA real estate credit program were not unduly severe. Amounts written off (including accounts on which judgments were pending) under the Bankhead-Jones farm tenant purchase program equaled only 0.32 percent of the $428 million ad-

[1] *Report of the Administrator of the Farmers Home Administration,* 1953, p. 32.

vanced from 1937 to mid-1953. No losses were reported as of June 30, 1953 for the farm housing program authorized under Title V of the Housing Act of 1949, nor for the farm ownership insured loan program set up in October 1947. Over its four years of operation, loans under the former totaled $81 million, of which more than 85 percent was still outstanding as of mid-1953. In addition, grants totaling about $364,000 were made from November 1949 to mid-1953. At the end of 1952, FHA contributions to delinquent accounts, as provided under the enabling legislation, amounted to nearly $54,000, covering both interest and principal installments.[2] Under the farm-ownership insured loan program only about 10 percent of the $64 million extended to farmers by private lenders through June 30, 1953 had been repaid. In summary, FHA's experience with its real estate credit programs was fairly successful up to 1953, as compared with the record of the land banks or the Land Bank Commissioner, a comparison in which allowance should be made for the fact that the program has operated since its beginning in a favorable economic climate.

Experience under FHA's various non-real-estate credit programs, and those of its predecessors, is not easily summarized from the information available in published reports. Additional recoveries on certain programs under liquidation, such as the rural rehabilitation loan programs of the Farm Security Administration and the emergency crop and feed loan program of the Farm Credit Administration, are still anticipated. To date, however, principal charged off on rural rehabilitation loans represented 7.0 percent of about $1 billion advanced from 1934 through November 1, 1946, when the program was discontinued.[3] The heaviest losses were experienced in the emergency crop and feed loan program, which began in 1918 as a means of giving temporary relief to farmers suffering from production disasters. Through June 30, 1953, principal charged off represented 13.5 percent of total loans made, and as of that date nearly $24 million of the $576 million extended before the program was discontinued in November 1946, remained unpaid.[4]

The record of the FHA with its production and subsistence, water facilities, and disaster loan programs has been more satisfactory.

[2] *Ibid.*, p. 23.

[3] Compiled from the *Report of the Administrator of the Farmers Home Administration, 1953*, p. 22.

[4] *Ibid.*, p. 22, and *Agricultural Finance Review* (Agricultural Research Service), Vol. 16, November 1953, p. 105.

From 1946 through mid-1953 only 0.25 percent of the $614 million advanced for production and subsistence loans had been written off or was in process of judgment. Less than 6 percent of the matured principal of such loans was unpaid as of June 30, 1953.[5] The water facilities loan program, begun in 1937 by the Farm Security Administration and continued by the Farmers Home Administration, has shown the most favorable record. Disbursements through mid-1953 were only about $28 million; write-offs and judgments in process accounted for less than 0.04 percent of this amount; and repayments of principal were slightly in excess of the total amount of matured principal.[6] The outcome of the disaster loan program (including fur and orchard loans) is by its very nature unpredictable. Losses to June 30, 1953 had been moderate. Less than 0.01 percent of the $129 million advanced from 1949 to mid-1953 was written off, but nearly $80,000 or 0.06 percent was in process of judgment. About 9 percent of the matured principal was unrepaid, and more than 40 percent of these short-term credits were still outstanding, as of June 30, 1953.[7]

On balance, the Farmers Home Administration has experienced severe losses in providing non-real-estate credit to farmers. To mid-1953 the over-all loss rate on loans for general farm operating and production purposes—covering rural rehabilitation, production and subsistence, and water facilities programs—was 4.4 percent, and the combined loss rate for loans of the emergency type, such as the disaster loan and emergency crop and feed programs, was in excess of 10 percent.

BUSINESS

The experience of federal and federally sponsored agencies in lending to business enterprises has been approximately what would have been expected considering the nature of the programs. That of the Reconstruction Finance Corporation comes to mind first, of course, but it bears very close similarities to the program of industrial advances carried on by the Federal Reserve Banks and the two may be considered together. Both programs were devised to provide intermediate-term credit to business concerns unable to meet the credit standards of private agencies; both, furthermore, were most active during the thirties, in the years of most severe economic depression, that of the RFC beginning in 1932 and of the Federal Reserve Banks

[5] *Ibid.*, p. 22. [6] *Ibid.*, p. 23. [7] *Ibid.*, pp. 22 and 30.

in 1934. As might be expected, the records achieved by the two agencies were distinctly less favorable than those characteristic of private financing institutions; indeed, their losses were greater than could be sustained by private agencies functioning under the requirement of earning a reasonable return on invested capital.

Up to the end of 1951 the RFC had incurred losses equal to about 2 percent of all disbursements on loans extinguished to that date; and over its entire history somewhat less than 10 percent of the number of loans extinguished had involved some loss. A fair comparison of RFC experience with that of commercial banking institutions is not easily made, since there was always a tendency for the better loans in the portfolio of the federal agency to be taken over by private financing institutions. The RFC, accordingly, was left with an adverse selection of credit risks. For what it is worth, however, it may be pointed out that at the end of 1951, 13 percent of RFC loans then outstanding were delinquent, whereas during 1951 less than 1 percent of all bank loans were classified as substandard by supervisory agencies.

The experience of the industrial loan program of the Federal Reserve Banks can best be described (for reasons that will appear) in terms of its activity during the period before 1941 when the depression forced many small business firms to utilize the credit services of the program in financing their working capital needs. Up to December 31, 1940 just over 2,000 loans had been made—slightly more than one-half in cooperation with banks and other financial institutions, and the remainder as direct loans. Losses were subsequently charged off on 4 percent of the former and on 6 percent of the latter. In anticipation of severe losses, the Federal Reserve Banks had set up reserves which, in addition to a small amount of losses charged off as of that date, amounted to about 5 percent of total loan advances through the end of 1940. During the late forties and early fifties, there were both substantial recoveries on loans previously charged off and withdrawals from reserves. In addition, fewer loans were made, although average loan size increased. The banks were also more thorough in their investigation of prospective borrowers. All things considered, therefore, it seems reasonable to evaluate the loss experience of the program by reference to the loan advances made through 1940. On this basis, net losses actually charged off to the end of 1951 represented 3 percent of total advances from 1934 to the end of 1940, a rate that is slightly higher than the over-all loss ratio of the RFC program. However, if the highly favorable lending operations of recent years are taken into consideration, net losses through December 31, 1951 form only 0.6 percent of the total amount of loans extinguished to that date.

The close relationship between the loss experience of a federal credit agency and the type of credit function which it is called upon to perform is vividly illustrated in the case of the RFC. Nearly two-thirds of the RFC business loans extinguished with loss were made to newly established firms. It is also quite clear from an examination of RFC loan experience—given in greater detail in Part II and in Appendix B—that a factor closely connected with loss experience has been the availability of information concerning the financial condition of the borrower. The proportion of loan extinguishments involving some loss was significantly higher for those loans on which the credit files were inadequate than for other loans. Absence of information on the previous financial condition of the borrower might reflect the fact that the enterprise was new and to all intents and purposes had no previous experience. Alternatively, it might result from an even more ominous condition, namely, inadequate management of the enterprise. In any case, either because of the newness of the firm or the inadequacy of its management, this characteristic was closely associated with unfavorable experience.

Four other business lending programs may be mentioned. These are the program of the VA under which small loans to veterans for business purposes were insured or guaranteed, the very large program under which guarantees were provided for loans for war production purposes, the lending program of the Export-Import Bank, and the modest loan program of the Maritime Administration for ship purchase and construction. The last two may be dismissed briefly with the observation that losses have been negligible. Credit extended by the Maritime Administration, it should be borne in mind, had not the character of a general lending program but rather was a financing arrangement that was only part of a broad program for advancement of the merchant marine. More interest attaches to the VA program of business loan guarantees and the Regulation V program. The VA program began in late 1944 and up to December 25, 1954, 8 percent of the guaranteed loans extinguished involved the payment by the VA of some claim to the financing institution that made the loan. These claims rose sharply in 1947–1949, owing in part to adverse economic conditions, but receded thereafter. Data on loss ratios are not available, but it is likely that they would be comparable to the RFC ratio of 2 percent; in fact, through December 25, 1954 net claims paid by the VA equaled less than 3 percent of the total principal collected on guaranteed loans repaid in full. As a more or less regular matter the delinquency ratio under the program has been in the neighborhood of 5 percent, which is probably higher than that of commercial banks, though bank data for a direct comparison are lacking.

The Regulation V program was established when it became clear that producers having war contracts during World War II would find it difficult to obtain the necessary short- and medium-term financing through private financing channels. It was felt at the time that the risks involved in these operations exceeded those that could properly be undertaken by private financing institutions, and accordingly a program was put together along the lines described in the preceding chapter. As will be recalled, the loans were exclusively for working capital purposes, there being an over-all prohibition against the guarantee of loans for plant and facilities. The record of the program shows that 1.8 percent of the guaranteed loans were extinguished with some loss, but as these were mainly small credits to small manufacturing plants they accounted for only 0.6 percent of the total amount of loans authorized under the guarantee program. Furthermore, settlements were so favorable that the estimated extent of loss on the program has been put at 0.06 percent of the aggregate loan authorizations. All things considered, the loans as a group produced a loss ratio very much lower than was expected.

HOUSING

The similarity between the lending experience of public and private agencies when the two operate under comparable circumstances is again evident in the record of the Home Owners' Loan Corporation. The corporation was established in 1933 to refinance defaulted home mortgages held by private financing institutions. Nearly 20 percent of the more than one million mortgages refinanced were eventually foreclosed by HOLC, but this is not an extraordinary record when it is recalled that 20.9 percent of the home mortgage loans made by major life insurance companies in the period 1925–1929 ended in foreclosure.

HOLC's record was very much better on loans made in connection with the sale of its foreclosed properties. Only about 2 percent of these so-called "vendee" accounts ended in foreclosure, a result which compares very closely with the life insurance company foreclosure rate of 1.8 percent on loans made in the years 1935–1939. A further point of similarity between the experience of the HOLC and that of private lenders is the regional variation in foreclosure rates. The HOLC rates in New York, New Jersey, and Massachusetts were as high as 40 percent, whereas the over-all rate was approximately 20 percent. The experience of private lenders, in particular the life insurance companies, was also distinctly less favorable in the New England and Middle Atlantic states than elsewhere. As a general rule, foreclosures were more frequent for both the HOLC and the life insurance companies on loans secured by properties located in highly industrialized and heavily populated areas.

In contrast to the HOLC, whose activities were directed to the relief of distressed homeowners, the RFC Mortgage Company operated in a much broader area, supplying credit on a mortgage basis directly to business firms (such as owners of apartments and commercial buildings), and purchasing such loans and also FHA-insured home mortgage loans from private lenders. The company's record makes it possible, therefore, to compare within one agency's experience the performance of loans secured by commercial and industrial properties with that of loans secured by small residential dwellings. Through June 30, 1946, just a year before its dissolution, the RFC Mortgage Company had foreclosed or charged off nearly 9 percent of the credit it had extended to business firms, directly or through loan purchases, since 1935. For the same period of lending, only 5 percent of the amount of FHA-insured home loans purchased had been so extinguished (through September 1952). Though these figures do not measure ultimate loss, they illustrate a fact common among both public and private lending agencies in the housing field, namely, that the experience on loans secured by small, medium-priced, owner-occupied homes was much more favorable than that on loans secured by income-producing properties, particularly apartment house structures. The record of the RFC Mortgage Company's refinancing activities was even more satisfactory where purchases of VA-guaranteed mortgages were involved. Through September 30, 1952, less than 3 percent of them, by amount, had ended in foreclosure.

The different experience with small home loans as against those on larger residential properties is vividly illustrated in the record of the Federal National Mortgage Association, an agency empowered to purchase both VA-guaranteed and FHA-insured loans. Through December 31, 1953, less than 1 percent of FNMA's total purchases of federally protected home mortgage loans, but fully 10 percent of the FHA-insured housing project loans purchased, were terminated by foreclosure.

The loan insurance and guarantee programs of the Federal Housing Administration and the Veterans' Administration also illustrate the relatively low risk associated with the financing of small homes designed for owner occupancy. For example, through insuring loans for the repair, alteration, or improvement of properties—mainly single family homes—the FHA has paid claims from the beginning of the program through 1953 equal to only 2 percent of the net proceeds of loans insured. Furthermore, recoveries have amounted to at least 40 percent of the claims paid to that date. With home mortgages, experience for both the FHA and the VA has also been exceedingly favorable. Over the years 1934–1953 foreclosures represented only about 0.5 percent of both the number and original amount of FHA loans insured; and under the VA home mortgage guarantee program, claim payments through 1953 were made on only 0.6 percent of the loans, and the amount paid (less recoveries) represented a similarly small fraction of the amount of the guaranteed loans. In contrast, nearly 4 percent of the number and 3 percent of the original amount of FHA-insured multi-unit housing project loans since 1934 have been terminated by foreclosure.

Earnings and Net Operating Results

Besides the foreclosure and loss data obtainable from loan records, a means of revealing the experience of federal and federally sponsored agencies is to examine whether their operations have been self-supporting. Analyses of this type are in most instances quite complicated, since they call for a full accounting of all costs associated with a particular program and only in very rare cases are the data available for making such a record. Nevertheless, it is possible, by examining each program separately, to approximate an answer to the question whether federal lending programs have been self-sustaining.

In the field of agriculture attention is first directed to the operations of the federal land banks. Through June 30, 1954 the land banks reported cumulative net earnings of $371 million. However, if a 2 percent charge were made for the interest-free capital supplied by the government through subscriptions to their capital stock and contributions to their paid-in surplus, net earnings of the land banks would be reduced by almost one-fifth. The provision of interest-free capital was not the only basis on which financial assistance was made available. The land banks were also remunerated by the Treasury to the extent of $277 million for the reduction in interest rates which they made in 1933–1944 at the direction of Congress. If this reimbursement is deducted from the net income remaining after the charge for government-supplied funds, it appears that the program as a whole has been barely self-supporting.

The experience of the Land Bank Commissioner is in striking contrast to that of the land banks. In the emergency lending through the Commissioner the estimated cost of government-supplied capital, assuming an interest rate of 2 percent, was about $39 million and the reimbursement received by the program for its interest rate reductions was $57 million. Net earnings from 1933 to mid-1954 exceeded the combined cost of such federal assistance by 50 percent. On balance, therefore, the program may be considered as having been self-supporting. This result is surprising in view of the fact that the Commissioner loan program was intended to provide credit in high-risk areas where private capital and the capital of the land banks was unavailable or in short supply. Nevertheless, it is another indication of the remarkably good over-all record of long-term mortgage lenders whose activities were directed to areas of severe mortgage distress and whose operations were initiated at the trough of the real estate cycle.

Similarly, the production credit system has apparently been self-supporting. The production credit associations, through the purchase of their class A stock by the production credit corporations, were supplied with interest-free capital which, at a 2 percent charge, would have cost about $20 million to mid-1954. However, the cumulated net earnings of $90.8 million reported by the PCA's from 1934 to mid-1954 easily covered that cost. In addition to the capital supplied by the PCC's, the PCA's also obtain loan funds by borrowing from, or discounting their loans with, the federal intermediate credit banks; the latter, in turn, extend the major part of their credit to PCA's, and therefore can be treated as part of the production credit system. From 1923 to mid-1954 the cost to the FICB's of the interest-free capital which they employed would be $37 million at an interest rate of

2 percent. The banks, however, were required to pay franchise taxes to the government amounting to $9.2 million from the date of their organization to June 30, 1954. After offsetting this amount against the estimated interest cost of federal capital, the position of the banks, which reported cumulated earned surplus of $30.1 million to June 30, 1954, with $17.0 million in reserves, is highly favorable. Thus the system as a whole can be regarded as being more than self-supporting through mid-1954.

Generally speaking, the banks for cooperatives have struck a rough balance between their net profit and the estimated cost of federal assistance. From 1933 through June 30, 1954, their cumulated net profit was $78.4 million, against which an estimated $67 million, at an assumed rate of 2 percent, should be charged for the interest-free capital provided by the Treasury.

A comparable analysis of the operations of the Rural Electrification Administration and of the Farmers Home Administration is not possible. For the former it is known that federal aid has involved the payment of REA administrative expenses, which amounted to $76.8 million through mid-1953, and the provision of low-cost capital at rates which have sometimes been higher than the interest rates paid by REA borrowers. As to the FHA, it is clear that various programs administered by this agency and its predecessors have not been self-sustaining, though the amount of federal subsidy entailed is unknown. Moreover, the FHA has performed a wide variety of services for its borrowers in addition to its credit extensions, and in some cases has extended grants as well as loans to the same individual. At least part of the cost of such services and of the grant program would have to be considered in determining the amount of federal assistance given to the loan program. The most that can be said is that through mid-1953 cumulative interest payments and repayments of principal have almost struck a balance with the total amount advanced under all programs.

The lending programs of federal and federally sponsored agencies in the business field have exhibited varying degrees of self-sufficiency. The lending activities of the Export-Import Bank, and presumably the loan-guaranteeing activities under Regulation V, were definitely self-supporting. Through June 30, 1954 the Export-Import Bank reported cumulated net earnings in excess of $300 million, against which only the cost of funds borrowed from the Treasury since 1945 had been charged. However, net income to date would still be sizable even if adjusted for the full cost of all Treasury borrowings from the beginning of operations in 1934.

From April 1942 to December 31, 1949, the net revenue from the V-loan guarantee program amounted to over $23 million. Although no charges had been made as of the end of 1949 for administrative expenditures, it may be inferred that the program was at least a self-sustaining, if not a profitable, one.

The business loan program of the RFC has been conducted at a concealed subsidy—a fact which was clearly faced by both the RFC management and the Congress, particularly during the later years of the corporation's life. There were no restrictions placed upon the income and cost structure of RFC lending activities, either by congressional directive or by the RFC Act itself. A recommendation was made by a special subcommittee of the Senate Committee on Banking and Currency in 1948 that "under normal conditions the (lending) activities should be conducted so as to make them self-sustaining insofar as it is possible."[8] Two years later evidence was presented in Senate hearings to show that RFC was not currently operating on a self-supporting basis from the taxpayers' standpoint. The subcommittee studying RFC in 1950 found that lending operations in fiscal 1949 (for all programs combined) would show a net loss of $6.5 million, instead of the published profit of about $5.2 million, if a deduction was made for interest on cost-free capital supplied by the Treasury, and on earned surplus not paid back into the Treasury. In its defense, the RFC maintained that the use of interest-free capital had been intended by Congress as a subsidy to small borrowers.

Apparently the RFC earned a small net profit on a full-cost basis from its combined lending programs during the five-year period after World War II, but there is reason to believe that the operating results of the business loan program compare unfavorably with the over-all record. During fiscal 1949 and during the first nine months of fiscal 1950, for example, according to estimates prepared for the Fulbright Subcommittee the RFC operated at a net deficit of $8.0 million and of $5.6 million, respectively, if the proportionate share of all expenses such as interest on cost-free capital and surplus is charged against the gross income from business loans. Moreover, during the twenty-one months ending March 31, 1950, the relation

[8] Senate Report 974, 80th Cong., 2nd sess., March 1948. Committee on Banking and Currency, *Report on the Operations of the Reconstruction Finance Corporation* to accompany S. 2287.

of costs to income was less satisfactory for deferred participation loans than for direct business loans (including immediate participations). Unfortunately, the accounting methods used by the RFC in its published financial statements do not permit this kind of analysis for the years after 1950; but even lacking the precision of detailed calculations, examination of the reported figures, with rough allowance for a full-cost basis, suggests that at best only a small net profit was realized on the business loan program from 1951 through June 30, 1953.

Only limited evidence on earnings is available for the industrial loan program of the Federal Reserve Banks. During the early years of the program, operations were highly unprofitable, if the cost of the Treasury funds employed is included with the realized and anticipated losses on loans as operating expense. At the end of 1940, the estimated net deficit of the program was nearly $2 million; but a decade later, through substantial recoveries on losses previously charged off and because of reductions in the provision for anticipated losses during the World War II and postwar period, the program showed a modest profit.

The last program for consideration in the field of federal credit to business—a loan guarantee and insurance program of the Veterans' Administration—was designed from its beginning in 1944 as a subsidy to eligible veterans in need of bank credit for financing small business ventures. From 1944 to the end of 1952, estimated total expenses of the business loan guarantee program were in the neighborhood of $25 million. Had a self-supporting operation been intended, to achieve it the VA would have had to charge premiums equal to about 5 percent of the total principal amount loaned, or to 15 percent of the guaranteed portion, on all loans disbursed up to the end of 1952.

The records of federal credit agencies in the housing field also provide evidence as to whether federal lending programs have been self-supporting. Through March 31, 1951, by which time operations had virtually ceased, the Home Owners' Loan Corporation reported that it had earned a net income of $352 million exclusive of losses, and that losses on loans charged off were $338 million. The small indicated profit, however, might be transformed into a small loss if the costs of Treasury-supplied funds and of other services supplied by the government such as the free use of the mails were taken into account. Considering the highly speculative nature of such cost adjustments, a less harsh conclusion may be more just. Perhaps the tentative evaluation of the operations of HOLC should be that the program from its initiation in the depths of the depression to its final termination in 1951 struck an approximate balance between income and cost.

From the fragmentary published materials on the financial outcome of the RFC Mortgage Company operations, it would appear that this agency, like the HOLC, successfully balanced income against outgo. Cumulative earned surplus up to the time of its dissolution in 1947 was about $4 million and was probably adequate to absorb the costs of funds supplied, or of the exemptions and privileges allowed by the government.

The Federal National Mortgage Association has presumably also been self-supporting. Through December 31, 1953 a net income of $140.4 million had been earned, out of which $92.4 had been paid in dividends to the Reconstruction Finance Corporation and in dividends and interest to the Treasury on capital advances. Nearly three-fourths of the balance had been set aside as reserves for losses, but the reserve accumulation, although apparently adequate for a portfolio consisting entirely of insured or guaranteed loans, was low by conventional standards, amounting to less than 2 percent of FNMA's outstanding mortgage portfolio at the end of 1953.

Similarly, the financial record of the Federal Housing Administration has been one of income exceeding expense, although reserve accumulations have been relatively modest compared to the total unpaid balances of insured loans still outstanding. Thus, the combined net income of all FHA programs through June 30, 1953, exceeded the federal government's contribution to the programs by $301 million. In view of the magnitude of its operations, however, the FHA's earnings record to date after allowance for federal contributions has been relatively low, forming only 0.91 percent of the volume of insurance written through the end of 1953.

The loan guarantee and insurance program of the Veterans' Administration in the housing field, on the other hand, has not operated without federal subsidy, since no premiums have been charged for the services granted. It is impossible to determine from data presently available the extent of federal assistance to date, or even the exact amount of income and operating costs associated with this program as distinct from the other loan programs of the VA. However, estimates developed from information supplied by the VA place the cost of administering the home loan program (including gratuity payments, net claim payments, salaries, and other operating expenses) at just under $430 million through December 1952.

Surveying the major areas of federal credit programs—agriculture, business, and housing—it is found that most of the programs have been self-supporting, at least from a long-range point of view. An element of subsidy has been present only in those programs which served a particular class of borrower such as low-income farmers, veterans, or small business firms. On the other hand, it is clear that no program, except possibly that of the Export-Import Bank, has realized profits at a level which would be considered satisfactory by the conventional standards of the private financial system.