

This disproportionate impact on housing was dramatically underscored by a Department of Commerce study being released this week. According to the Associated Press (Wednesday, Aug. 23, 1967) the Commerce Department found that the "1966 money crisis" overall impact was 'quite small.' But the press story went on significantly:

The Department said that the "shock effect" fell on housing which was undercut by \$2.5 billion or 10 percent of 1966 spending for residential construction.

The story goes on to cite numerous other sectors of the economy which suffered little or no restrictions as a result of "tight money." Plant and equipment expenditures actually increased 16.7 percent in 1966. Inventory investment declined only 4 percent because of "tight money."

No one can predict with complete assurance that a tax increase will avoid some higher interest rates and continued inflationary pressures in the economy. On the other hand, we are afraid that in the absence of a tax increase or massive reductions in Government spending there will be very high interest rates and a serious, if not severe, inflationary problem as well as great dislocations in the money market.

Currently, as every American household is aware, there is already substantial inflationary pressure in the economy with price levels having increased rather rapidly since the first quarter of 1966.

If the Treasury has to finance its deficit without the creation of a great deal more credit by the Federal Reserve, the result will be intolerably high interest rates, and the cost of sharing the deficit and the cost of our Military Establishment would be borne most unevenly—essentially by those least able to pay higher interest costs—the home owner and the typical American family that uses credit.

There has been some concern expressed before this committee that a tax increase of the magnitude proposed by the administration would aggravate the slowdown which became apparent in some phases of the civilian economy early this year.

I do not appear before you as an economist, and am not competent to pass judgment on the action of whether a tax increase would trigger a recession that would result in the collection of less in the way of Federal revenue.

I do know, however, that a return to very high interest rates will strike another severe blow at the homebuilding industry just at a time when housing industry is beginning to recover from the sledge hammer blows it received last year as a result of high interest rates and the sharp decline of money available for home buying and homebuilding.

So far as the homebuilding industry is concerned and the mortgage sector of the economy, it is clear that a tax increase would have less of a depressing effect than failure to cover at least part of the forthcoming Federal deficit with an increase in income taxes.

We commend the efforts of Members of Congress to reduce spending. Whether Government spending can or will be reduced \$1 billion, \$2 billion, or \$5 billion is not within my area of knowledge. Even with a reduction of Federal spending and an increase in income taxes so that the Federal deficit will be in the range of \$15 billion, there would still be extensive competition for the housing market from the Treasury. It would not, however, be nearly as disruptive as a \$30 billion deficit or even a \$25 billion deficit.

The mortgage market will require considerably more funds in the second half of 1967 and first half of 1968 than were required during the first half of this year. There was little mortgage loan business in the pipeline in the early part of 1967 because of the drastic cutbacks in loan commitments in the second half of last year.

More recently, loan demands in lending volume have improved, and more and more new houses are being completed and coming on the market.

To illustrate: From a low monthly volume of \$850 million in January, lending by savings and loan institutions reached almost \$2.3 billion in June. It is interesting and significant, however, that the steady rise in lending was interrupted in July and the preliminary figures for this month indicate a lending volume of only about \$1.8 billion.

Quite clearly, the recent thrust upward, the long-term rates and short-term rates, is creating a cautious mood among mortgage lenders. We find many institutions reluctant today to expand their loan commitments because of apprehension that another bout with severe tight money resulting from the competition of high-rate Government and Government agency obligations may take place in the next 6 to 12 months.

Savings institutions which supply the bulk of the funds to the housing market enjoyed favorable savings inflow during the first half of 1967 because short-term interest rates dropped almost two full percentage points from the peaks of last fall and there was also some decline in long-term corporate bond rates.

Since the spring of 1967, however, corporate bond yields have begun to rise rapidly and in the past 2 months have exceeded the record peak yields established last fall. Rarely a business day has gone by in recent weeks without the appearance of numerous corporate bond issues and yields of 6 percent or more.

As for short-term interest rates, they bottomed out in June of this year and since then have recovered half of the decline recorded between last fall and this June. Thus, the trend in bond long-term and short-term rates is moving upward and with some rapidity.

If the Treasury come to the market with demands to finance the deficit of the proportions indicated by President Johnson, it will have a staggering impact on the credit markets generally and accelerate the upward trend of short-term and long-term rates. The year 1966 demonstrated that the housing industry has plenty of trouble competing with corporates for available credit; most certainly it would have even more serious trouble competing with the Treasury for funds.

A tax increase of the scope suggested by President Johnson does not mean that there will not be some tightening in money and credits in the months ahead. What it probably would do is dampen the threat of inflation and reduce Treasury borrowing so that a return to the chaotic tight money conditions of a year ago can be substantially avoided.

We believe that it is imperative to avoid a new depression in the housing industry and the hazards of major dislocations in the movement of capital. We have reached the conclusion that the imposition of an increase in personal and corporate income taxes along the general lines suggested by the President is the best of the alternatives available for dealing with the situation.

The CHAIRMAN. Mr. Mitchell, we thank you, sir, for bringing to us the views of the organization you are representing today.

Are there any questions of Mr. Mitchell?

If not, we thank you, sir.

Mr. MITCHELL. Thank you, sir.

The CHAIRMAN. That completes the calendar for today and without objection the committee adjourns until 10 o'clock Monday morning.

(Whereupon, at 10:51 a.m., the committee adjourned to reconvene, Monday, Aug. 28, 1967.)

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