

Factors for calculating lender returns

	<i>Percent</i>
Gross return.....	6
Less:	
Placement cost of first loan \$——×0.0086.....	
Placement cost of subsequent loans \$——×0.0143.....	
Loan conversion cost \$——×0.0073.....	
Monthly servicing cost during repayment \$——×0.449.....	
Equals:	
Net lender return to cover cost of money.....	

The following example, using hypothetical figures, is intended only to illustrate the use of the factors:

	<i>Percent</i>
Gross return.....	6
Less:	
Placement cost of first loan \$25×0.0086.....	.215
Placement cost of subsequent loans \$20×0.0143.....	.286
Loan conversion cost \$15×0.0073.....	.110
Monthly servicing cost during repayment \$1×0.4491.....	.449
Equals:	
Net lender return to cover cost of money.....	4.94

There is some question also regarding the statement in the Comptroller's report that the cost of money for lending institutions in early 1967 was in the vicinity of 4½ percent. The Comptroller's representatives were advised that market yields on Treasury obligations of comparable maturity in January-March 1967 averaged approximately 4½ percent. The connection between this rate and the cost of money for lending institutions, however, is somewhat tenuous. Also, the data presented in the Comptroller's report on average rates paid on time and savings deposits does not directly answer the question, since it does not take into account the noninterest costs incurred by the institutions in obtaining and maintaining deposit accounts.

The Committee recognized that lender operating costs can be reduced in the program if the guarantee procedures are simplified. It also stated that the "encouragement of efficiency in operations, therefore, should be a fundamental consideration in the method adopted to increase lender returns." Whether larger volume operations will also lead to additional economies may be more doubtful; even so, it can be necessary to provide an initial inducement for lenders to enter the program.

The Committee also recognized that the cost of placing subsequent loans may be less than the cost of placing the initial loan, and that as experience is developed under the program it should be possible to collect better cost data and to adjust the level of fees appropriately to achieve the desired level of lender participation. Thus, the Committee's report stated:

"To provide the flexibility needed to assure maximum lender participation under changing money market conditions, this [fee payment] authority should be broad enough to permit the fees to be varied with changes in lender costs and market rates of interest. It should also allow the placement fees to be reduced for the second and subsequent loans to the same student, since the costs of making later loans to a student should be less than the cost of making the first loan."

It is somewhat astonishing that the Comptrollers' report indicates lack of knowledge of conversion costs, since the names of specific institutions with such experience were furnished to the GAO representatives.

The record should also be corrected at this point to indicate that Mr. Barr did not testify that lenders were incurring out-of-pocket losses from the guaranteed student loan program.

The thrust of Mr. Barr's testimony has been that lenders will not willingly engage in volume operations in this program, which are necessary if it is to support higher education adequately, if their rate of return is very unfavorable relative to rates of return in other forms of investment. In this connection, it may be noted that VA and FHA mortgages bear a 6% interest rate, but the gross yield, taking into account points and prepayment experience, is in excess of 6¾%, substantially more than on guaranteed student loans.

The maximum fees recommended by the Barr Committee would increase gross lender returns on guaranteed student loans to approximately 7.05% computed