

CHAPTER - 8

KEY ISSUES AND FUTURE OUTLOOK

Housing Finance Issues

Sustainable Policy Support

8.1 The past few years have witnessed fierce competition in the housing finance market and may unfold surprises in the coming years. The housing sector has witnessed varying standards and practices among the lending community, be it in origination and documentation or monitoring and supervision. Variation in standards across the industry imposes systemic risks, which can be a potential threat to the sector. Due care has to be exercised in originating loans as well as in monitoring and supervision to ensure the sustained quality of assets, more so, as the housing loans are of long tenor. Thus, there is a need for evolving uniform standards for appraisal and documentation. There is also a need for adoption of uniform practice by the housing finance industry relating to matters like prepayment of housing loans, conversion of fixed rate loans into floating rate loans and vice-versa and re-schedulement of repayment instalments. Besides uniformity, there is also need for greater transparency in dealings with the borrowers to enable them to exercise informed choices about products and lending institutions. Overall, these will help the market perform more efficiently.

8.2 Growing competition coupled with reduction in risk weights on housing loans has led the lending institutions to adopt aggressive practices including very high Loan to Value [LTV] loans, softening of collateral requirements, competitive pricing etc. The housing sector, in recent years, has been the favourite destination for financial institutions because of typically low default rates witnessed in this sector. However, with aggressive approach being followed by various players in the housing finance market arising from competition may lead to increase in the default rates. There is need for establishing a mechanism to monitor the trend and analyse the results for solutions in the housing finance sector as the volumes are likely to further grow in the coming years. Monitoring the housing loans performance at the industry level as well as the retail level together with strategies for management of the NPAs at the lending institution level, state-wise, clientele-wise (rural/urban) will be emerge as important regulatory and business concerns.

Risk Factors

8.3 All the competing players in the Industry, especially Banks and HFCs are vying with each other to lure the customers in order to maintain and increase their share in the housing finance segment. The prevailing interest rate war due to reduction in deposit rates and excess liquidity in the financial market among the

players for the last few years has resulted in constant downward revision of interest rates. Further, the spreads are increasingly becoming thin as the lending rates [mostly sub PLR] are fast nearing the cost of funds. While during 1993-94, the interest rates on housing loans were in the range of 17-18 per cent the same right now are in the range of 7 per cent - 8.5 per cent. The constant rate-cuts may lead to erosion of profitability in the long run. Industry experts opine that the interest rates in India have already reached the rock bottom and may not fall further in the near future.

Security Deficit owing to Relaxed Norms

8.4 Many primary lending institutions are making terms and conditions of sanction flexible and liberal, thus enabling the borrowers to avail the loans even more than the value of security for long tenure of 20 to 25 years. The large quantum of institutional finance in the property transactions may lead to the problem of security deficit.

8.5 The constant lowering down of margin requirements by SCBs, and HFCs has to be checked by the industry players and regulators. Logically, the RBI has stipulated higher risk weightage of 75 per cent as against 50 per cent in November 2004.

Compromise on Due Diligence

8.6 Increasingly, there have been instances of dilution in due diligence on the part of lenders. Sometimes, loans are sanctioned without strictly complying with laid down rules, systems and procedures. This situation arises primarily out of fierce competitive pressures. It is observed that the growing customer expectations force the PLIs to compromise on due diligence, field verification process and appraisal norms, in a rush to sanction the loan at the earliest. Of late, instances have come to notice where housing loans were obtained on fake documents as also loans were provided by different institutions on the same documents. As such, the integrity of the borrowers has to be carefully scrutinised and internal appraisal systems have to be strengthened.

Lack of Level Playing Field for the Players

8.7 While banks and HFCs are the prominent players, HFCs face a few constraints. The regulatory norms stipulate 10 percent capital adequacy for banks whereas the same is 12 percent for HFCs. Further, banks have access to lower cost retail funds compared to HFCs. Uniformity in norms and hence a level playing field has to be ensured for a healthy housing finance system. These are newer challenges which need to be addressed and resolved in times to come.

8.8 With a view to encouraging HFCs to mobilise long-term deposits, it may be examined whether any deposit insurance system could be thought of for well-organised and financially strong HFCs. While the floating rates of interest on

deposits could take care of the volatile nature rates of interest on deposits, it appears that the potential depositors still prefer to fixed rates of interest on deposits.

Central Registry for housing mortgages:

8.9 In order to address the issue of rising incidence of frauds in housing finance, Section 20 of the SARFAESI Act introduced the provision of setting up a central registry. The Act empowers the Central Government to set up computerized Central Registry which would go a long way in providing a statutory backing to the security interest created in favour of Banks and Financial institutions and enabling them to claim priority over other claimants while enforcing the securities. Introduction of such a registration system would be conducive to credit growth and access to credit would become easy resulting in competition amongst lenders and better interest stared for the borrowers. It will facilitate efforts towards curbing frauds on account of financing due to unlawful mortgage of property.

Other Suggestions

8.10 Some of the suggestions are as follows:

- The planning and design of buildings and public places must take care of the needs of persons who are physically challenged.
- While allotting house-sites/houses in rural and urban areas developed by either state agencies or the private sector with finance form financial institutions some percentage as specified by the State Government should be allotted to the families belonging to the Scheduled Castes/Scheduled Tribes communities.
- There is a need for the Government to encourage setting up an independent rating agency for builders/promoters to inspire public confidence in their activities. Similarly, a professional body could be set up to undertake demand assessment and survey for housing projects. This step can help in reducing speculative pressures created in the land and the housing market.
- The HFIs, which finance a project or the local authorities while approving a project, should take independent assessment into account, so that an independent agency could also take up the task of land valuation and title investigation for institutional financing.
- Industries should provide housing for employees as part of their industrial projects. Fiscal concessions could be provided to these industries. The housing for the low paid employees and workers would be planned in the close vicinity of their place of work.
- Plans of housing complexes and industrial estates must include a provision for hostel accommodation for working women, crèches and day-care centers.

- Non-conventional energy sources need to be harnessed for meeting the energy needs in both urban and rural areas and particularly to the remote and far-flung areas, which cannot be serviced through the grid supply.
- Construction of houses in rural areas by providing smokeless chulhas & latrines.
- A green belt should be developed and protected around the housing complexes to check pollution and enhance their aesthetics.
- Strengthening nation-wide Management Information System (MIS) on house building activities to help in designing, developing housing programmes & assist decision making.

Outlook

8.11 With the thrust provided by way of policy initiatives of the Government and the measures initiated by NHB and other agencies in respect of issues referred to above, the housing finance sector is expected to maintain the growth momentum witnessed during the last few years, although renewed measures are required as above to address and tackle the core issues which can improve the growth of habitat development in our country.

Housing is one of the primary human needs and is next in importance to food and clothing. A house is not only a shelter to protect the human beings from vagaries of weather but also a workshop where people are moulded for constructive roles in the future. The need for housing in India has been growing at a phenomenal pace over the years. The problem of housing shortage grows at alarming proportions in India with the rapid pace of increase in population, urbanisation, changing family structure, rising per capita income, etc. The Tenth Plan has estimated the urban housing shortage at the level of 8.9 million dwelling units and the cumulative number of houses required during the Plan period as 22.4 million units. The total investment required for the above is estimated at the level of Rs.4,15,000 crore. And such a huge amount cannot be raised by the Central and State Governments alone. Rather active private sector participation is very much essential for achieving this goal, at least partly.

Housing is an industry with tremendous potential for contributing towards economic growth of any country. In a developing economy like India, its significance need not be overemphasised. This is because of different factors, like

- It is one of the top employment generators for the economy
- It has both forward and backward linkages with over 250 industries, including such core industries like cement, steel, timber, ceramics, tiles, etc.
- A small initiative in housing can propel multiplier effects in the whole economy through the generation of demand

- It is supposed to be the most preferred investment avenue in a recession-prone economy.

Researches done in advanced countries like US, UK and many OECD countries have revealed that house prices are strongly correlated with business cycle and have a significant impact on private consumption. Strong increase in property values has been noted to have unsustainable expansion on demand.

The other emerging feature is the shift from minimum housing to theme housing where the housing unit consists of building as well as other basic amenities necessary for any household. In this case, the pricing and the financial requirements will certainly be higher as compared to the residential unit consisting of building and infrastructure only.

Considering the very low NPA levels [less than 1 per cent annualised] and also strong security in the form of mortgage of the property financed, many tax incentives to the lenders [and borrowers], etc., housing finance is considered to be a comparatively safer kind of credit by the lenders. The enactment of SARFAESI Act 2002 has made the recovery of non-performing advances much easier. Further, the growing MBS market ensures secondary market for housing loan assets and many progressive players are tapping our MBS market periodically for financing themselves.

Though Indian housing finance system has got its own share of problems and handicaps, given the huge untapped housing loan market, government support and favourable macro-economic environment, reasonably resilient banking system, the industry has got excellent growth prospects. The present growth rate at about 30 percent or even higher, appears to be sustainable in the foreseeable future. Measures to promote Residential Mortgage Backed Securitisation [RMBS] market in India can further strengthen our housing finance system and make it more competitive.

