

CHAPTER V

ACTIVITIES OF THE NATIONAL HOUSING BANK : 2002-03

The National Housing Bank (NHB) completed its fifteenth year of operation in 2002-03 working on the mandate to function as the principal agency to promote housing finance system and to provide financial and other support to housing finance institutions. The objectives of NHB are to promote a sound, healthy, viable and cost effective housing finance system to cater to all segments of the population by augmenting resources for the sector and channelising them for housing in order to make housing credit more affordable. NHB's promotional endeavours are also directed towards capacity building for the housing finance system besides enlarging the credit absorption capacity. The Bank has also been entrusted with the task of introducing new product /service features in the Indian mortgage market in line with international developments such as creation of a secondary mortgage market for residential mortgage backed securitization and mortgage credit guarantee. The major functional developments during 2002-03 are detailed below:

A. Regulatory Issues

Change in Regulation

With a view to imparting a more vibrant regulatory regime for the HFCs, NHB had been making suitable amendments to Housing finance Companies (NHB) Directions from time to time to keep pace with the changing market dynamics. The following amendments have been made to the Housing Finance Companies (NHB) Directions, 2001 during the year 2002-03:

- i) New provisions for exposure to stock market including stipulation on engaging brokers and policy/prudential norms applicable to demand/call loans have been introduced. HFCs are now required to put in place clear cut policy for demand/call loans. Prudential norms relating to asset classification and provisioning have been made applicable to such loans as well. Besides, the 'past due' concept has been dispensed with. The period of default for asset-classification has also been made more stringent with effect from March 31, 2005 onwards.
- ii) The ceiling on borrowing and deposits that can be accepted by HFCs has been increased from 10 times to 16 times of their net owned fund in order to offer them a level playing field in the face of stiff competition.
- iii) The ceiling on rate of interest payable by HFCs for public deposits has been reduced from 12.5% per annum to 11% per annum
- iv) NHB has also permitted all HFCs registered with the Bank under section 29A of the National Housing Bank Act, 1987 to enter into ready forward transactions in Government Securities and issued necessary circular specifying the terms and conditions to be complied by such HFCs.

Supervision

Twenty-nine HFCs were inspected during the year 2002-03 to assess their financial position and verify their compliance with the Directions issued by NHB. Besides, the Bank also recovered penal interest amounting to Rs.77.15 lakhs from 14 HFCs during 2002-03 as recourse against their failure to maintain the prescribed level of liquid assets in terms of Section 29B of the National Housing Bank Act.

Registration of housing finance companies

In terms of Section 29A of the National Housing Bank Act, 1987 (as amended in 2000) HFCs are required to obtain a Certificate of Registration (COR) from the National Housing Bank so as to commence or carry on the business of a housing finance institution. During the year under review, 17 HFCs were granted COR without permission to accept public deposits, of which COR issued to one HFC has been cancelled. Further, applications for COR were rejected in 46 cases.

Out of the 161 applications received by the Bank for Certificate of Registration, 48 HFCs have been granted the COR, 51 companies' applications were rejected by NHB till June 30, 2003 and 30 applications are at various stages of processing. 31 Companies with NOF below the minimum threshold limit of Rs.25 lakhs had time till June 11, 2003 to fulfill the minimum NOF requirement and they have been given time till September 11, 2003 to report such compliance to NHB. As stated earlier, one COR granted was cancelled during the year.

HFCs which have not applied for registration have become ineligible to carry on the business of housing finance institutions and action would be initiated against such companies, if they are found to be carrying on the business of an HFI or accepting deposits from public.

The Bank is keeping in touch with the latest developments through market intelligence and coordination with other regulatory bodies so as to protect the sector from any systemic failure.

B. Promotional Issues

Equity Support

During the year 2002-03 NHB revised its Guidelines for extending Equity Support to HFCs w.e.f March 1, 2003, enhancing the requirement of minimum paid up capital of the HFC to Rs. 10.00 and restricting NHB's participation in equity to 10% of paid up capital. Besides, HFCs are required to get their shares listed on any recognised stock exchange(s) in India as also to enter into a shareholder's agreement with NHB which, inter-alia, contains the clause of buy-back of equity shares.

During the year, Bank disinvested its entire equity holding in Andhrabank Housing Finance Limited and Vysya Bank Housing Finance Limited. NHB also subscribed

Rs.1.60 crores towards 1.6 lacs equity shares of Cent Bank Home Finance Limited of Rs. 100 each at par under the Rights Issue.

The details regarding NHB's equity participation in HFCs at the end of June 2003 are given below:

(Rs. in Crore)

Name of the HFC	Face Value	Investment as on 30.06.2003
1. BOB Housing Finance Ltd.	4.94	4.94
2. Can Fin Homes Ltd.	0.50	1.75
3. Centbank Home Finance Ltd.	3.20	3.20
4. GRUH Finance Ltd.	0.45	0.85
5. Vibank Housing Finance Ltd	1.20	1.20
TOTAL	—	11.94

The Bank has been organizing meetings with CEOs of HFCs for better understanding and resolving of issues of mutual importance. During the current financial year one such meeting was organized and cumulatively, NHB has so far organized 17 such meetings.

Training

In order to endow the housing finance sector with dynamic and effective human resource capable of facing the challenge of changing market scenario, the Bank has been providing training assistance to all the primary lending institutions through specialized programmes, seminars and symposia on matters related to housing and housing finance.

During the year, NHB conducted six training programmes all over the country involving participation from HFCs, state housing boards and development authorities. The programmes addressed issues related to general awareness on housing finance as well as certain specialised topics such as regulatory framework for housing, securitization, project finance etc. In one programme, officials from leading housing finance institutions in Bangladesh also participated.

NHB also extended financial and design support to NCHF for conducting four training programmes for the personnel of housing co-operatives. The National Centre for Management Development for ARDBs (NCMDARDB) was also provided financial assistance for training programmes for officials of co-operative institutions and banks operating in the rural areas. NHB also provided design and faculty support to banks, HFCs and Human Settlement Management Institute (HSMI).

C. Financing Issues

Mobilization

During 2002-03, NHB mobilized Rs.3083.80 crore from various sources including additional share capital of Rs.100 crore from RBI and Rs.1947.90 crore from capital gains bonds 2002 issue that provided tax exemption to capital gains under Section 54 EC of the Income Tax Act 1961. With the additional infusion of share capital from RBI, the total paid up capital of NHB stood at Rs.450.00 crore as at the end of June 30, 2003, fully contributed by RBI. The Life Insurance Corporation of India also subscribed a sum of Rs.400.00 crore under Tier-II capital having a tenor of 63 months at a coupon rate of 5.77% payable annually. The rest was mobilized through taxable and tax-free bonds and line of credit from RBI.

NHB has for the first time obtained rating of its debt instruments and the Fitch Ratings India Private Limited and Credit Analysis and Research Limited have rated the same as AAA (ind) and "CARE AAA" respectively, denoting highest quality carrying negligible investment risk.

Refinancing

The prevalent refinance schemes of NHB applicable to primary lending institutions (PLIs) was introduced in 1989 with uniform pricing and security requirement irrespective of risk perception or varying capability and credibility of the PLIs. This uniform policy, though justifiable from the promotional point of view, especially in the nascent years of housing finance sector, would result in distortion in a more competitive environment as it is tantamount to intervention. Thus, the better PLIs would feel discriminated and disincentivised. With growing competition in the housing finance sector witnessing takeovers and re-pricing of loans, requirement of many primary lending institutions for varying maturities of loans, a choice of fixed and floating interest rate and finance against prospective loans based on their growth projections became evident. The felt need was to make a more meaningful market foray making NHB the "most preferred destination" for housing finance institutions in the long run. Towards this objective NHB has introduced a Liberalised Refinance Scheme (LRS) applicable to Scheduled Banks and Housing Finance Companies in February 2003.

The important policy changes effected through the LRS are as under:

- i. Introduction of internal credit rating for HFCs and risk based pricing.*
- ii. Introduction of floating rates of interest and maturity based rates of interest.*
- iii. Refinance assistance could be used for covering prospective disbursements to be made by HFCs*

The rating under internal credit rating model (ICRM) consists of 6 scales and would be done once a year to determine the rate of interest, exposure, sanction limit,

security etc. The ICRM is based on various parameters covering business risk, market risk and financial risk.

The introduction of LRS resulted in growth of refinance disbursement which reached the figure of Rs. 2709.72 crore, as compared to the previous year's figure of Rs. 1024.80 crore resulting in a growth of around 164% over the previous year. The comparative chart showing disbursements to various categories of PLIs vis-à-vis the corresponding figures last year is as under :

(Rs. in crore)

	2002-03			2001-02
	Fixed	Floating	Total	
Releases to HFCs	550.01	1216.68	1766.69	705.33
Old Scheme (Jul 2002 - Feb 2003)	219.61	0.00	219.61	
New Scheme (Mar 2003 - Jun 2003)	330.40	1216.68	1547.08	
Releases to Banks	770.00	20.00	790.00	76.99
Old Scheme (Jul 2002 - Feb 2003)	0.00	0.00	0.00	
New Scheme (Mar 2003 - Jun 2003)	770.00	20.00	790.00	
Releases to Cooperative Institutions	139.77	0.00	139.77	219.15
Releases Under Gujarat Earthquake Scheme	13.26	0.00	13.26	23.33
TOTAL	1473.04	1236.68	2709.72	1024.80

Cumulative Refinance Disbursements up to 30th June, 2003

Institution Category	Amount (Rs. in crore)
Housing Finance Companies	7303.00
Scheduled Banks	1232.42
Cooperative Sector Institutions	1425.66
TOTAL	9961.08

Keeping in tune with the overall softening of the interest rate regime, NHB rationalized its refinance rates in the past on an ongoing basis. Under the earlier Scheme, with the change effected in June 2002 the refinance rate ranged between 7.25%-9.50% in rural areas and 8.25%-9.50% in urban areas. Under LRS, HFCs/Banks have the option to choose either floating or fixed interest rate. In order to safeguard both NHB and primary lending institutions from extreme volatility in interest rate movements in the case of fixed rates NHB will have the option to review and revise the rates on outstanding loans on completion of 3 years. As on June 30, 2003 the interest rate range under LRS was 6.90%-8.55% (fixed option) and 6.70%-7.95% (floating option). There was a further 25 basis point relaxation for rural housing loans.

There is also option available for conversion from fixed to floating rate and vice versa on payment of a fee. Refinance availed can also be prepaid after giving 2 months notice to NHB and on payment of a nominal levy.

Project Financing

The Bank also extended financial assistance the tune of Rs. 73.06 crore in 2002-03 (including the amount lent from the Special Fund and the assistance under Gujarat earthquake scheme) to public housing and development agencies all over the country for undertaking various types of housing projects and sanctioned projects with a cost component of Rs.117.66 crore and loan amount of Rs.84.46 crore. Under the General Fund, a total of 6 Land Development & Shelter Projects (LDSP) have been sanctioned during 2002-03 having a cost component of Rs.85.27 crore and loan amount of Rs.64.05 crore and NHB disbursed a sum of Rs.58.00 crore under this window in addition to finance for projects under Gujarat earthquake scheme. Under the Special Fund, NHB sanctioned 6 Projects during 2002-03 having project cost of Rs.28.77 crore and loan amount of Rs.17.36 crore and disbursed a sum of Rs.14.79 crore. Around Rs. 0.27 crore was disbursed as assistance to Gujarat Earthquake Victims.

Cumulatively, till the end of June, 2003, NHB has disbursed Rs.586.63 crore under its project financing window. NHB has so far sanctioned 353 projects (including projects sanctioned to support Gujarat earthquake victims) where financial assistance has been made available through the direct as well as the refinance route.

The interest rates applicable to the refinance and direct finance schemes of Project Finance have also been revised downwards during the year 2002-03.

D. Other Initiatives

Golden Jubilee Rural Housing Finance Scheme

The scheme was launched in August 1997 to commemorate the Golden Jubilee year of India's independence. This is a pure housing loan scheme without any subsidy element for areas with a population less than 50,000 as per 1991 Census and the primary lending institutions are free to decide the terms and conditions of lending. The targets under the Golden Jubilee Rural Housing Finance Scheme for the year 2002-2003 were enhanced to 2.25 lakh dwelling units from 1.75 lakh dwelling units in the previous year. The target was further sub-allocated amongst the various participating institutions.

The details of the targets and the achievements under the scheme for various categories of institutions during 2002-03 are as under:

(Number of dwelling units)

Category of Institutions	Target	Achievement
Banks	1,06,300	97,295
Housing Finance Companies	1,02,400	78,807
Others including Co-operative sector institutions	16,300	2,098
TOTAL	2,25,000	1,78,200

The low credit disbursements for rural housing by primary lending institutions can be attributed to several factors such as non availability of clear land title in rural areas, difficulties in assessing repayment capabilities of rural masses due to irregular income behaviour resulting in higher credit risk etc. Besides, the higher incidence of stamp duty and non-permissibility of agricultural land for mortgaging for non-agricultural purposes in many states also hinder the growth of rural housing finance business.

Residential Mortgage Backed Securitization (RMBS)

During the year 2002-03, Reserve Bank of India issued notification assigning a risk weight of 50% for investments by Banks and Financial Institutions in Mortgage Backed Securities (MBS) originated by Housing Finance Companies registered and supervised by NHB, subject to fulfillment of specified conditions.

Recognizing the potential of RMBS as a financial instrument and its role in linking the housing sector with the Capital Market, NHB has been working towards establishing systems and procedures for standardization of primary housing finance activities and documents in order enable a sophisticated secondary RMBS market. NHB has also been continuing its efforts to sensitize the various State Governments for rationalization of Structure of Stamp Duties and Registration Charges. While five states have reduced the stamp duty structure to 0.1% so far, during the year the Government of Gujarat revised its Stamp Duty Structure in respect of MBS Instruments in terms of which the maximum stamp duty is Rs. 1.00 lakh.

The market has also witnessed a gradual expansion in the investor base of the MBS paper with Mutual Funds and Primary Dealers (besides banks and Insurance companies) having evinced interest in investing in RMBS. NHB is exploring the possibility of issuing RMBS paper with Banks both in the public and private sectors as originators. The Pass Through Certificates (PTCs) which represents the undivided interests of the pool assets is now being issued in the dematerialized form.

During 2002-03, two more RMBS issues were launched by NHB-one originated by BOB Housing Finance Limited and the other by Canfin Homes Limited. The BOB HFL Issue involved 3548 loans amounting to Rs. 77.16 crore. The issue size was Rs. 59.65 crore of a tenor of 108 months with a coupon of 6.89% p.a. payable monthly. This was the first RMBS issue of BOB HFL and was rated LAAA (SO) by ICRA. The Canfin issue comprised of a pool of 2007 mortgages involving Rs.64.13 crore with door-to-door maturity of 105 months and average maturity of 53 months at a coupon of 6.25% p.a. The issue was rated LAAA(SO) by ICRA. As a measure to boost the confidence of the investors in the RMBS papers, NHB had, for the first time, subscribed to the issue, picking up a stake of 5.45% in the deal. With these two issues NHB has so far completed securitization of 7 pools involving housing loan assets aggregating Rs.500.12 crore.

Mortgage Credit Guarantee Company

The National Housing Bank has taken a lead role in promoting and introducing the concept of mortgage default guarantee in the country. Pursuant to the announcement in the Union Budget of 2001-02, NHB undertook the venture and is collaborating with Canada Mortgage and Housing Corporation (CMHC), United Guarantee (UG), a wholly-owned subsidiary of American International Group Inc. (AIG), International Finance Corporation (IFC) and Asian Development Bank (ADB) in pursuing the implementation of the project.

Mortgage Credit Guarantee will allow lenders to penetrate broader market segments by expanding their reach by offering easier and standard mortgage terms and conditions. The guarantee support will protect lenders against risk of default by the borrowers. This will enhance confidence and help the lending institutions in reaching out to all segments of population and improving home ownership in the country. The guarantee support will improve credit flow into housing and will also result in lower interest rates due to risk cover. The mechanism will also provide a new impetus to mortgage backed securitization and will bring about improvement in lending practices in the industry. NHB has been coordinating the efforts of all the partnering institutions for investment in the project and setting up of the Company.