21
Housing Finance

Chapter Objectives

This chapter will enable you to develop an understanding of the following:

1 *Meaning of housing finance*
2 *Role of housing and housing finance in the economy*
3 *Evolution of housing and housing finance in India*
4 *Policy initiatives and measures to develop the housing sector in India*
5 *Housing-finance institutions (HFIs)*
6 *Types of housing loans*
7 *Risk management by HFIs*
8 *Marketing strategies of HFIs*
9 *National Housing Bank and its role in housing finance*
10 *Residential mortgage-backed securitization*
11 *Reverse-mortgage loan*
12 *Housing-finance Industry: Issues and future outlook*

INTRODUCTION

Shelter being one of the three basic human needs, every human being aspires to own a home. Homes are not just houses—they are environments which project the aspirations of individual families to live a better life. An individual shares an emotional bond with his home. It gives him a sense of security and comfort. It is the possession of a home that makes an individual a good citizen and provides citizens with a stake in their society. Housing and housing amenities are major indicators to gauge human well-being of a country.

The UN Conference on Environment and Development, 1991, has stated that 'access to safe and healthy shelter is essential to a person's physical, psychological, social, and economic well-being, and should be a fundamental part of our urgent actions for the more than one-billion people without decent living conditions. Our objective is to achieve adequate shelter for all, especially, the deprived urban and rural poor, through an enabling approach to the development and improvement of shelter that is environmentally sound.' Yet, even today, one-sixth of the world's total population does not have a proper housing. As per the 2011 Census, the total number of houses in India was 330.84 million. The number of houses in rural area was 220.70 million while in urban areas the number was 110.14 million total houses. According to the National Building Organization (NBO), the total demand for housing is estimated at 2-million units per year and the total housing shortfall was 18.78 million units in 2012. This shortage is acute in rural areas. It is worth noting that 96 per cent of this shortage pertains to the economically weaker sections and the lower income groups of the society.

In India, up to the late 1970s, housing finance was a key constraint to ownership of a house. An individual could think of owning a home only at the time of retirement, when he would receive the benefits of retirement. The concept of housing finance was pioneered by Housing Development Finance Corporation (HDFC) in October 1977. It was not only a trend-setter for housing finance in the whole Asian continent, but also built up the industry by setting rules, policies and procedures to protect the interests of the customers.

Housing finance is a business of financial intermediation wherein the money raised through various sources such as public deposits (which are subject to the regulatory stipulations of NHB), institutional borrowings (from banks), refinance from NHB and their own capital, is lent to borrowers for purchasing a house. These intermediaries lend money by accepting mortgage by deposit of title deeds of the residential property. Section 96 of the Transfer of Property Act, 1882, has put mortgage by deposit-of-title deeds on the same footing as a simple mortgage, and attracts stamp duty and also requires registration under the Registration Act,1908. If the borrower fails to pay according to the contract, the lender has the right to sell off the mortgaged property by the intervention of the court.

- HDFC is the market leader with 21 per cent share in the housing finance market

The prominent players in this industry continue to be housing-finance companies (HFCs) and commercial (local as well as foreign) banks. Cooperative banks and other cooperative-sector institutions have developed their own niche and have been catering to their markets, extensively.

ROLE OF HOUSING AND HOUSING FINANCE IN THE ECONOMY

Real estate forms the largest asset class of the world and is one of the largest sources of wealth for families. Real estate is defined as land, including the space above it and the ground below it, and any building or structures on it. Real estate is a vast asset class that spans direct markets, real-estate stocks, real-estate mutual funds and real-estate investment trusts. It is also the most imperfect asset as different people pay different prices for the same commodity. No two homes are alike nor are there exchanges where the prices are recorded.

Housing is an industry with tremendous potential for contributing towards the economic growth of any country.

- It is one of the top employment generators for the economy.
- It has both forward as well as backward linkages with over 250 industries, including such core industries like cement, steel, timber, ceramics, tiles, etc.
- A small initiative in housing can boost multiplier effects in the whole economy through the generation of demand and strong multiplier effects on income and employment.
- It is supposed to be the most-preferred investment avenue in a recession-prone economy.

The primary objective of the governments of the developed countries like the United States and the United Kingdom was developing the housing market. The financial sectors of these countries grew in consonance with the housing industry.

Housing finance acts as a catalyst for the growth of this industry. Pricing of housing loans is a crucial factor driving the growth of the business of housing finance and, thereby, the housing industry. Pricing of housing loans also set up lending-rate curve and influences the pricing of short-term loans.

The growth in the housing and housing finance activities in the recent years reflect the buoyant state of the housing-finance market in the country. The proportion of outstanding housing loans as the percentage of gross domestic product (GDP) increased from 3.4 per cent in 2001 to 8.5 per cent by 2016. This proportion is abysmal when compared to the proportion of investment in housing in the other developed and emerging economies. The proportion of investment in housing to the GDP is 54 per cent in the United States, 57 per cent in the United Kingdom, 40 per cent in the European Union, 17 per cent in Thailand, 34 per cent in Malaysia and 24 per cent in China.

In view of the rising growth in urbanization, it is expected that the share of housing in GDP will increase. These fiscal measures and incentives have led to an increase in the demand for the housing loans, resulting in increased disbursements of housing finance by the primary lenders over the years. As a result, housing stock in the country increased from 14.8 million units in 1991 to 18.7 million units in 2001, and is expected to further go upto 26.53 million dwelling units by the end of the eleventh five year plan. The urban land stock in India, which is only 2.3 per cent of the countries total geographical area is housing 30 per cent of India's population.

- Growing levels of urbanization, rising disposable incomes and affordable interest rates have contributed to the growth of housing finance industry.

EVOLUTION OF HOUSING AND HOUSING FINANCE IN INDIA

The accessibility of housing finance for people in general has evolved, developed and improved over the years. In the early years of independent India, housing was through the self-construction route, and later on emerged the concept of housing cooperatives which encouraged group housing. Housing cooperatives have a prominent place in the cooperative movement in the country. Today, it is estimated that there are over 92,000 primary-housing cooperatives with over 6.5-million members.

Also, the government/quasi-government entities, like housing boards and development authorities, allotted land and housing sites to facilitate the development of this sector. Today, the private-sector participation in the housing projects has increased. In many cases, public–private partnerships in complex projects that take the shape of mini-cities, malls and multiplexes, information-technology parks and housing communities, specialized townships, special-economic zones and even the concept of private towns, is found.

A noteworthy change has been in the financing opportunities for housing and real estate. It was difficult for builders/developers to find financiers for funding housing and real estate. In cases where funding was possible, the developers, generally, had to be content with plain vanilla-loan structures that provided a minimal flexibility.

Today, there are a number of options to finance housing and real-estate projects through initial public offerings (IPOs), foreign-direct investment (FDI), venture capital, private equity, listings on the alternative investment market, in addition to the traditional debt-financing options.

In order to enable HFCs to finance big construction projects, they have been allowed to raise funds through foreign-currency bonds. They can mobilize resources by selling 15-year, upper-tier-II instruments, including foreign-currency bonds, which need the clearance of the Reserve Bank of India (RBI). These options would be a cheaper source option to raise capital, boost housing-finance market and help maintain regulatory stipulations. Foreign institutional investors (FIIs) can invest up to $500 million in upper-tier-II rupee-denominated bonds.

POLICY INITIATIVES AND MEASURES TO DEVELOP HOUSING SECTOR IN INDIA

Housing is regarded as a critical sector in terms of policy initiatives and interventions. This is reflected in the efforts of the government to improve housing and habitat conditions by way of financial allocations in the five-year plans and fiscal measures related to housing announced in the Union Budgets.

Some of these measures include:

Rural Housing

- Indira Awas Yojana
- Golden Jubilee Rural Housing Finance Scheme
- Bharat Nirman
- Rural Housing Fund

- The National Housing and Habitat Policy (NHHP) was formulated in 1998 and stressed on:
  - removing legal, financial and administrative barriers for facilitating access to loans, finance and technology;
  - ensuring that housing, along with supporting services, was treated as a priority and at par with the infrastructure sector;
  - creation of surpluses in housing stock;
  - providing quality and cost-effective shelters, especially, to the vulnerable groups and the poor.
- The National Urban Housing and Habitat Policy, 2007, while focusing on urban shelters, emphasized on the promotion of larger flow of funds, to meet the revenue requirements of urban housing and infrastructure using innovative tools. The Policy seeks to promote various types of public–private partnerships for realizing the goal of "Affordable Housing for All".
- The Goal of the Draft "National Rural Housing & Habitat Policy" is to ensure adequate and affordable housing for all and to facilitate development of sustainable and inclusive habitats by expanding Government support, promoting community participation, self-help and public-private partnership within the framework of Panchayati Raj.
- The Golden Jubilee Rural Housing Finance Scheme (GJRHFS) was launched in the year 1997–98 to provide people living in the rural areas an improved access to housing finance. HFCs and banks have financed 24,71,454 dwelling units during the period 1997–2009.
- To improve the habitat conditions in the rural areas, construction of 60-lakh houses in rural areas under Bharat Nirman undertaken. A new scheme, Rajiv Awas Yojana (RAY), has ben announced to make the country slum free in the five year (2010–2015) period. The allocation for the Indira Awas Yojana (IAY) has been increased by 63 per cent to ₹8,800 crore in Budget estimates 2009–10. Indira Awaas Yojana (IAY) was launched during 1985–86 initially as a sub-scheme of Rural Landless Employment Guarantee Programme (RLEGP) and thereafter continued as a sub-scheme of Jawahar Rozgar Yojana (JRY) since its launching in April, 1989. IAY was de-linked from JRY and made an independent scheme with effect from January 1, 1996. IAY is now a cash subsidy based programme, under which assistance is provided to rural below poverty line (BPL) families for constructing dwelling units on their own using their own design and technology.
- To increase the pace of rural housing, a sum of ₹2,200 crore has been allocated from the shortfall in the priority sector lending of commercial banks, for Rural Housing Fund in the NHB for extending financial assistance to the weaker sections only.
- Fiscal concessions to individuals increased under Section 80C of the IT Act [rebate up to ₹1 lakh in respect of the repayment of principal], Section 24(2) [interest deduction up to a limit of ₹1.50 lakhs, in respect of properties acquired or constructed with the borrowed capital and self occupied.
- Increase in the rebate on the repayment of principal under Section 88 to 30 per cent in certain cases.
- Deduction in respect of rental income from property allowable to an extent of 30 per cent of its annual value.
- Clearance under Section 230(A) of the Income Tax Act, 1961, for sale of property is no longer required.
- NHB and Housing and Urban Development Corporation Limited have been allowed to issue tax-free bonds.
- No specific permission is required for transfer of property.
- NHB is in the process of operationalizing foreclosure of mortgages.
- NHB has launched Mortgage Credit Guarantee Scheme.
- RBI has reduced the risk weights on investments made by banks in mortgage-backed securities (MBSs) to 50 per cent.
- NHB has reduced the risk weights on individual housing loans to 75 per cent.
- The definition of 'securities' amended under the Securities Contract (Regulation) Act,1956, to include Mortgage Backed Securities (MBS) as 'securities' tradable, in the capital market.
- To strengthen the recovery mechanism, Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI Act), was enacted and Housing-finance Institutions (HFIs) included in the eligible list of institutions.

- FDIs allowed up to 100 per cent under the automatic route in townships, housing, built-up infrastructure and construction-development projects, to catalyze investment in a vital infrastructural sector of the economy.
- Housing loans up to ₹20 lakhs to individuals for purchase/construction of one dwelling unit per family (excluding loans granted by banks to their own employees) and loans given for repairs to the damaged dwelling units of families up to ₹1 lakh in rural and semi-urban areas and up to ₹2 lakhs in urban and metropolitan areas, brought under priority-sector lending of banks. Further, in order to give a boost to the secondary-mortgage market, investments by banks in the MBS have been classified as direct lending to housing, within priority-sector lending, subject to certain conditions.
- The RBI has allowed mortgage-guarantee company to commence the business of providing mortgage guarantee in India after (a) obtaining a certificate of registration from the RBI and (b) having a net-owned fund of one-hundred-crore rupees or such other higher amount, as the RBI may, by notification, specify. The mortgage-guarantee company shall be under the regulatory and supervisory jurisdiction of the RBI. However, mortgage-guarantee companies cannot accept public deposits. They can also not avail external commercial borrowings.

Urbanization is on the rise according to the 2014 "Revision of World Urbanization Prospects"1 by the United Nations. Three countries, India, China and Nigeria, together are expected to account for 37 percent of the projected growth of the world's urban population between 2014 and 2050. India is projected to add 404 million urban dwellers, China 292 million and Nigeria 212 million. As the world continues to urbanize, sustainable development challenges will be increasingly concentrated in cities, particularly in the lower-middle-income countries where the pace of urbanization is the fastest. Integrated policies to improve the lives of both urban and rural dwellers are needed.

Some major policy decisions taken by the government to address the problems of urbanization, housing and housing finance are:

The Hon'ble President of India, in his address to the Joint Session of Parliament on June 9, 2014, had announced that "By the time,nation completes 75 years of its Independence, every family will have a *pucca* house with water connection, toilet facilities, 24*7 electricity supply and access." The Hon'ble prime minister of India has envisioned housing for All by 2022 when the nation completes 75 years of its Independence. In order to achieve this objectives, the central government has launched a comprehensive Mission, "Housing for All by 2022", with the objective of holistic development. The Housing for All (Urban) Mission has been launched in compliance with this objective of government and with the approval of competent authority. The Mission seeks to address the housing requirement of the urban poor, including slum dwellers, through the following programme verticals:

- Slum rehabilitation of slum dwellers with the participation of private developers using land as a resource.
- Promotion of affordable housing for the weaker section through credit-linked subsidy.
- Affordable housing in partnership with the public and private sectors.
- Subsidy for beneficiary-led individual house construction.

Announcements made in the Union Budget 2015–16 on Housing

- *Housing for All:* Completion of two crore houses in urban areas and four crore houses in rural areas by 2022.
- Creation of the National Investment and Infrastructure Fund (NIIF).
- Rationalization of capital gains applicable on sponsors exiting at the time of the listing of the units of the Real Estate Investment Trusts (REITs) and pass through the taxation structure for the rental income earned by the REITs from their own assets.
- Tax pass through to both Category-I and Category-II Alternative Investment Funds (AIFs).
- Introduction of the Benami Transactions (Prohibition) Bill to curb domestic black money in real estate. Sections 269SS and 269T of the Income Tax Act to be suitably amended to prohibit the acceptance or repayment of advance in cash of ₹20,000 or more for any transaction related to immovable property.
- Raising of consolidated service tax from 12.36 percent to 14 percent.
- Comprehensive Bankruptcy Code to be introduced in fiscal 2015–16.

Smart Cities Mission

Nearly 31 percent of India's current population lives in urban areas and contributes 63 percent of India's GDP (Census 2011). With increasing urbanization, urban areas are expected to house 40 percent of India's population and contribute 75 percent of India's GDP by 2030. The smart cities initiative will improve the quality of life and attract people and investments to the city. The core infrastructure elements in a smart city would include:

- Adequate water supply
- Assured electricity supply
- Sanitation, including solid waste management
- Efficient urban mobility and public transport
- Affordable housing, especially for the poor
- Robust IT connectivity and digitalization
- Good governance, especially e-Governance and citizen participation
- Sustainable environment
- Safety and security of citizens, particularly women, children and the elderly
- Health and education

The 100 potential smart cities were nominated by all the states and union territories based on Stage-1 criteria. Smart city plans were prepared, which were evaluated in Stage-2 of the competition for prioritizing cities for financing. In the first round of this stage, 20 top scores were chosen for financing during 2015–16. The remaining will be asked to make up the deficiencies identified by the Apex Committee in the Ministry of Urban Development for participation in the next two rounds of the competition. Forty cities each will be selected for financing during the next rounds of the competition.

The Pradhan Mantri Awas Yojana (PMAY) Housing for All (Urban) Mission will be implemented during 2015–22. It will give central assistance to implementing agencies through states and UTs for providing houses to all eligible families/beneficiaries falling under the EWS/LIG categories, who do not own a *pucca* house anywhere in India, by 2022. The Mission will be implemented through four verticals that give options to the beneficiaries, Urban Local Bodies (ULBs) and State Governments as a Centrally Sponsored Scheme (CSS). This does not, however, includes the credit-linked subsidy, which will be implemented as a Central Sector Scheme. The guidelines for these were released by the Hon'ble prime minister on June 25, 2015. All statutory towns as per Census 2011 and towns notified subsequently would be eligible for coverage under the Mission. While the centrally sponsored schemes cover the cities in a phased manner, the central sector scheme covers the entire urban area, consisting of 4,041 statutory towns as per Census 2011.

Affordable housing is now the driver of the growth of housing finance. This is due to the subsidy available under the Pradhan MantriAwasYojna. This scheme, available until December 2017, provides 4 percent subsidy on home loans of upto ₹9 lakh for those with an income of upto ₹12 lakh per year, and 3 percent subsidy on loans of upto ₹12 lakhs for those earning upto ₹18 lakh per year. Housing finance providers are now expecting the affordable homes segment to grow at 25% given the subsidy under the Pradhan Mantri Awas Yojana. The scheme, available until December 2017, provides 4% subsidy on home loans of up to ₹9 lakh for those with an income of up to ₹12 lakh per year, and 3% subsidy on loans of up to ₹12 lakh for those earning up to ₹18 lakh per year. Housing finance providers are now expecting the affordable homes segment to grow at 25% given the subsidy under the Pradhan Mantri Awas Yojana. The scheme, available until December 2017, provides 4% subsidy on home loans of up to ₹9 lakh for those with an income of up to ₹12 lakh per year, and 3% subsidy on loans of up to ₹12 lakh for those earning up to ₹18 lakh per year. Housing finance providers are now expecting the affordable homes segment to grow at 25% given the subsidy under the Pradhan Mantri Awas Yojana. The scheme, available until December 2017, provides 4% subsidy on home loans of up to ₹9 lakh for those with an income of up to ₹12 lakh per year, and 3% subsidy on loans of up to ₹12 lakh for those earning up to ₹18 lakh per year.

Credit Risk Guarantee Fund Scheme for Low Income Housing (CRGFT)

Under this scheme, the Credit Risk Guarantee Fund Trust (CRGFT) will provide credit risk guarantee to the lending institutions against their housing loans of up to ₹5 lakh. This will be granted to the borrowers in the EWS/LIG categories in urban areas without requiring any collateral security and/or third party guarantee. The extent of guarantee cover to be provided under the scheme is 90 percent of the amount in default in respect of a loan amount up to ₹2 lakh and 85 percent of the amount in default for a housing loan above ₹2 lakh and up to ₹5 lakh.

The Credit Risk Guarantee Fund is expected to catalyse a flow of credit of about ₹20,000 crore to the low income housing sector and generate an enabling environment for the creation of affordable housing stock. The availability of bank credit without the constraint of collaterals/third party guarantees would be a key enabler for the urban poor to realize their objective of upgrading/buying their own house.

The Draft National Rental Housing Policy, 2015 seeks to enable a vibrant and formal rental housing sector by adopting regulatory and legal reforms, enhancing fund flows, promoting institutions for construction, managing maintenance and creation of rental housing stock, along with necessary incentives which will improve the housing availability for the needy.

Real Estate (Regulation and Development) Act, 2016

The Real Estate (Regulation and Development) Bill, 2016, which was passed by Parliament in March 2016, protects home buyers largely and encourages genuine private players. The Real Estate Act, has become effective from May 1, 2016. The Act will ensure accountability and transparency in the sector and it is an attempt to make the homebuyers king as it puts buyer's interest at the forefront. Only 13 states and UTs have so far notified rules.

Under the Act, rights and duties of buyers and promoters have been clearly defined. Moreover, there is a provision of mandatory registration and requirement of keeping 70% of the project money into an escrow account. This is likely to reduce the buyer risk to a certain extent and will ensure that developers are not able to invest in numerous new projects with the proceeds of the booking money for one project, thus delaying completion and handover to consumers. The provisions of promotor's liability for clear title, inclusion of real estate agent under the purview of Act and penalty clauses will increase the overall transparency and accountability in the system. It also puts responsibilities on the authority to grant approvals and declines in a defined time-period, hence pre-eliminating potential bureaucratic delays. Online real estate platforms will be developed which can help in creating a trustworthy environment based on tangible data.

Together with interest subsidy scheme, GST and other initiatives by the government, RERA will encourage genuine interest in real estate investments in India. It will also streamline the entire process of dispute resolution with an unbiased and empowered regulator.

HOUSING-FINANCE INSTITUTIONS (HFIs)

There are different types of institutions which cater to the need of long-term finance, for housing in urban and rural areas. They are:

Scheduled Commercial Banks (SCBs)

These banks have floated housing-finance arms to avail the National Housing Bank's refinance facilities and the tax concessions available to HFCs. Both public and private sector as well as the foreign banks' large network and access to the low-cost retail deposits have helped them to offer home-loan products at competitive rates, giving a stiff competition to the housing-finance business by the HFCs. Housing loans enjoy the largest share of 50 per cent in the retail-loan portfolio of the banks. Banks have to earmark 3 per cent of incremental deposits to finance housing activities, and this financing becomes a part of the 40 per cent priority-sector lending. Moreover, security, by way of mortgage of property and robust demand, has been a major consideration for banks to lend to this sector.

- Banks and HFCs are major players in the housing finance industry.

Scheduled Cooperative Banks

They include scheduled state-cooperative banks, scheduled district-cooperative banks and scheduled urban-cooperative banks. These banks are connected with the semi-urban and rural areas. Scheduled state-cooperative banks give housing loans either directly or through the district central-cooperative banks/ primary, agricultural credit societies. These banks are eligible for availing the refinance facility from NHB.

Regional Rural Banks (RRBs)

They were set up to develop the rural economy by providing credit and other facilities, particularly to the small and marginal farmers, agricultural labourers, artisans and small entrepreneurs. They lend housing loans in rural areas and are refinanced by NHB.

Agriculture and Rural Development Banks (ARDBs)

Keeping in view the housing shortage in rural areas, a few state governments permitted them to lend for housing. They do not fall under the category of either the SCBs or the specialized HFIs. The NHB has formulated a scheme to subscribe to special rural-housing debentures floated by ARDBs, backed by the mortgages originated by them, in order to extend financial assistance to this category of institutions.

Housing-finance Companies (HFCs)

A housing-finance company (HFC) is a company which mainly carries on the business of housing finance or has one of its main object clauses in the Memorandum of Association, of carrying on the business of providing finance for the housing. A HFC is required to have certificate of registration from NHB, a minimum net-owned funds of ₹200 lakhs. About 43 HFCs have been granted certificate of registration under Section 29A of the NHB Act, 1987. Of 43 HFCs, only 20 can accept public deposits. They are:

Cent Bank Home Finance Limited, Can Fin Homes Limited, Deutsche Post Bank Home Finance Limited, Dewan Housing Finance Corporation Limited, DHFL Vysya Housing Finance Limited, GIC Housing Finance Limited, GRUH Finance Limited, Housing and Urban Development Corporation Limited, HDFC Limited, ICICI Home Finance Company Limited, IDBI Home Finance Limited, Ind Bank Housing Limited, LIC Housing Finance Limited, Manipal Housing Finance Syndicate Limited, National Trust Housing Finance Limited, PNB Housing Finance Limited, REPCO Housing Finance Limited, Sundaram BNP Paribas Home Finance Limited, Vishwakriya Housing Finance Limited and AIG Home Finance Limited.

The housing-finance industry is capital-intensive in nature, coupled with long payback period which discouraged many banks from entering into this sector. Looking to the potentiality of this untapped sector, many HFCs forayed into this sector.

HFCs are regulated and supervised by National Housing Banks (NHB).

The National Cooperative Housing Federation of India (NCHF)

- The outstanding housing loan portfolio of banks and HFCs was around ₹4500 billion as of December 31, 2009.

It is an apex organization for coordinating, guiding and promoting cooperative housing activities in the country. The cooperative housing structure consists of primary housing cooperatives at the grass-root level and apex-cooperative, housing-finance societies (ACHFS) at the state level. ACHFS at the state level are affiliated to NCHF, which looks after their growth strategies, policy formulations and evolving housing programmes, besides interfacing with various institutions to channel finances for these societies, for onward lending to the ultimate borrowers. In addition, NCHF also helps the ACHFS in improving their financial, organizational and technical capabilities.

Apex-cooperative Housing-finance Societies (ACHFS)

The primary housing cooperatives are functioning all over the country with a membership of over 6.5 million. These ACHFS represent about 92,000 housing cooperatives all over the country, out of which, about 31,000 housing cooperatives are affiliated to state-level ACHFS for getting financial assistance. The rest of the cooperatives are (i) those that get finances from other sources, (ii) those that have not yet started construction activities and (iii) those that have repaid their loans fully.

TYPES OF HOUSING LOANS

The following types of home loans are generally available in the market:

1. **Home-equity loans:** A form of finance to the customer by way of mortgage of existing property to the financier for taking a loan for some other purpose. The current market value of the property is the basis for providing home-equity loans.
2. **Home-extension loans:** The purpose of this loan is the extension of existing houses like addition of rooms, toilet facilities and so on. Such loans fall under the category of home loans.
3. **Home-improvement loans:** These loans are provided mainly for repairs and maintenance of existing houses. These could include internal and external repairing, waterproofing and roofing, complete interior renovation, tiling and flooring and so on.
4. **Home-purchase loans:** Finance provided for the purchase of ready-made houses.
5. **Land-purchase loans:** These loans are being provided for the purchase of land for the purpose of construction of residential houses. Finance to public and private builders to increase the supply of land suitable for building houses.

6. **Home loans to self-help groups (SHGs)/Micro-finance institutions (MFIs):** To achieve the objective of inclusive growth, HFIs now finance self-help groups (SHGs) and micro-finance institutions (MFIs). Generally, the individual housing loans of a house is priced lower as compared to the loan to builders or corporate/s for project finance.
7. **Loan to NRIs:** This loan is sanctioned to NRI wishing to build or buy a home in India in accordance with the guidelines issued by the RBI.

The loan amount generally depends on:

1. the period for which the loan is needed,
2. the repayment capacity of the borrower,
3. the estimated value of property and
4. clear title deeds of the borrower.

The rate of interest on these loans depends on a number of factors, such as the tenure of the loan, loan amount, purpose of loan, repayment capacity of borrowers and the cost of the fund of the financier. Two types of interest rates (i) floating [Adjustable Rate Mortgage (ARM)] and (ii) fixed rates are offered to home-loan borrowers. Under fixed home loan rates, a reset clause is inserted which gives a right to the HFI to increase the rate of interest after the prescribed interval.

The repayment of the loan is generally done through the equated monthly instalment (EMI) method. In case of borrowers expecting a reasonable growth in their future income, instalments may be on a graduated basis.

- EMI is the amount payable to the HFI every month, till the loan is paid back in full. It consists of interest due as well a portion repayable towards the principal. The interest on home loans is usually calculated on monthly reducing balance.

The effective home loan rate is around 2–3 per cent lower than its prime lending rate (PLR). The bank's PLR is dependent on its cost of funds. If the cost of funds for a bank increases, it hikes its PLR, which, in turn, leads to a rise in home-loan rates. A bank/HFC resets the floating rates once in every quarter. In the past few years, there was a huge demand for home loans when home loans fell to 7.5 per cent.

The banks and the HFCs also levy a fee for processing the application and the fee varies from 0.5 per cent to 1 per cent of the loan amount. In addition, they also charge an administrative fee of 1 per cent of the loan amount.

RISK MANAGEMENT BY HFCs

HFCs have to manage various risks associated with the mortgage business. These risks include credit risk, liquidity risk, foreign-exchange risk and interest-rate risk.

HFCs manage credit risk through stringent credit norms. Liquidity risk and interest-rate risks arising out of maturity mismatch of assets and liabilities, are managed through regular monitoring of the maturity profiles. They also enter into interest-rate swaps wherein the fixed-rate rupee liabilities for varying maturities of a notional amount are converted into floating-rate liabilities linked to various benchmarks. The currency risk on the borrowings is hedged through a combination of dollar-denominated assets, long-term forward contracts, principal-only swaps (POS), full-currency swaps and currency options.

Longer tenure of housing loans poses a significant challenge of asset–liability mismatch for banks, as they finance these long-term loans' average tenure of 15 years with deposits' average tenure of 2 years. The level of NPAs in the housing-loan segment is around 4 per cent. As Indians share an emotional bond with their house and have a high stake in their own house, they are less likely to default in case of a housing loan among all their liabilities. Defaults in the housing-loan segment occur when the borrower reaches a point of indifference due to changes in the external environment. HDFC has the lowest bad loans in the housing sector, not just in India, but perhaps in the world itself on the whole. Since inception, the corporation has lent around ₹1,52,000 crores towards housing loans. Of which, it had only ₹66 crores of loan losses.

MARKETING STRATEGIES OF HFCs

Housing finance is an attractive business on account of acute shortage of housing units, increased urbanization, higher levels of disposable incomes, fiscal incentives and rise in property prices. The sector offers safe and secure residential assets, good business opportunities for the lending agencies and attractive terms for the borrowers making it a buyers' market.

With a growing number of players and increased competition, the housing sector has become increasingly market-driven.

- Marketing approaches now take into account the changing preferences of the customer, who is more aware of what he wants and the choices available to him.

- Positioned themselves not just as a company providing finance to customers but a company that also provides loan counselling, technical and legal assistance and other property-related solutions.
- Build up credit-appraisal skills and trained their personnel to become customer focussed.
- Using mobile telephony to communicate with new and existing customers.
- Cross-selling of financial products and services.
- Expanding network of offices.
- Organizing property fairs in different parts of the country.
- Appointing direct-selling agents to cater to customers who prefer door service.
- Designing and developing web sites as a marketing tool, especially for attracting non-resident Indian customers.

NATIONAL HOUSING BANK

It is the apex-level financial institution for the housing sector. The National Housing Bank (NHB) is a wholly owned subsidiary of the RBI and the regulator of non-banking HFCs. The NHB was established on July 9, 1988, under an Act of the Parliament, namely, the National Housing Bank Act, 1987, to function as a principal agency to promote HFIs and to provide financial and other support to such institutions. The Act, inter alia, empowers NHB to:

- Issue directions to HFIs to ensure their growth on sound lines,
- Make loans and advances and render any other form of financial assistance to scheduled banks and HFIs or to any authority established by or under any Central, State or Provincial Act and engaged in slum improvement and
- Formulate schemes for the purpose of mobilization of resources and extension of credit for housing.

The NHB registers, regulates and supervises housing finance companies (HFCs). It also extends refinance to HFCs, SCBs and co-operative sector institutions against their housing loans, and project lending to borrowers in the public sector and public-private space. Over the years, NHB's key concern has been to promote innovative market-based solutions for affordable housing finance to low income housing segments. The Reserve Bank contributed ₹10 billion towards the paid-up capital of NHB on January 12, 2016, thereby increasing its shareholding from ₹4.5 billion to ₹14.5 billion.

Role of NHB in Housing Finance

(i) Promotion and development of HFIs: NHB frames, reviews and modifies guidelines for HFCs for their healthy and sound growth. All HFCs, registered with NHB, under Section 29A of the National Housing Bank Act, 1987, and scheduled commercial/cooperative banks, are eligible for refinance support, subject to terms and conditions as laid down under the respective refinance schemes. It extends guarantee to bonds/debentures floated by HFCs meeting certain laid-down criteria. It also extends equity support to HFCs. NHB's participation in equity is at par and restricted to 25 per cent of the paid-up capital of the HFC. However, where the HFC is permitted with the main object of catering to the home-loan requirements of economically weak sector/low-income group/rural segments of the society, NHB's participation can be up to 50 per cent of the paid-up capital. In the case of rights issue, NHB can subscribe at a premium. NHB has equity participation in three HFCs, namely, GRUH Finance Limited, Cent Bank Home Finance Limited and Mahindra Rural Housing Finance Limited.

(ii) Regulation and supervision of HFCs: NHB regulates the housing-finance sector under the regulatory provisions of the National Housing Bank Act, 1987, to prevent the affairs of any HFI being conducted in a manner detrimental to the interest of the depositors or in a manner prejudicial to the interest of the HFIs. For this, it has been empowered to determine the policy and give directions to the HFIs and their auditors. It has issued the Housing Finance Companies (NHB) Directions, 2001, as also Guidelines for Asset Liability Management System in HFCs. These are periodically updated through issue of circulars and notifications. All HFCs have to register themselves, under Section 29A of the National Housing Bank Act, 1987, with NHB. It regulates the deposit-acceptance activities of HFCs and also issues prudential norms relating to capital adequacy, asset classification, income recognition and provisioning for bad and doubtful debts. It also supervises the sector through a system of on- and off-site surveillance. It has also developed a model code of conduct for HFIs and ensures that they are adopted and followed.

(iii) Refinancing: HFIs provide finance to individual borrowers, builders, corporate houses, and so on, for purchase/construction of houses and for repair/upgradation of the existing house. With the objective of providing long-term funds to these institutions, NHB extends refinance in respect of the loans extended by them. It provides refinance to retail-lending institutions such as RRBs, scheduled state-cooperative banks, specialized HFIs, ACHFS and rural-development banks. Refinance for rural housing is provided at a concessional rate of 8 per cent per annum for 7 years. NHB introduced a new refinance scheme for construction finance for affordable housing with special focus on Tier II and Tier III cities. Slum redevelopment in metros is also covered under this scheme.

(iv) Project lending: It provides financial assistance for project lending to a range of borrowers both in the public/state housing boards, state slum-clearance boards, development authorities, municipal corporations, new town-development agencies, local authorities for housing and urban development, public-sector companies for employee housing projects, and private sector agencies such as reputed developers/builders/ MFIs/SHGs/NGOs/Societies registered under the Societies Act, 1860. The extent of financing varies between 65 per cent and 100 per cent of the project cost for a maximum period of 15 years.

(v) Development of a secondary mortgage market: It supports the securitization of mortgage loans of retail-lending institutions and has taken an initiative to develop secondary mortgage market in India. Moreover, in order to protect lenders against default, it has been entrusted with the responsibility of launching a mortgage credit-guarantee scheme.

- Secondary mortgage market involves conversion of mortgages into tradable financial instruments which are then sold to prospective investors.

Various Initiatives Undertaken by NHB for the Development of Housing in India

Banks and HFCs seek funds from NHB for reasons such as meeting their short-term needs and balancing their assets and liabilities. NHB taps public funds by launching fixed-deposit programmes to diversify its resource base. In the Indian market, the finance minister in the Union Budget 2008–09, has allocated a fund of ₹1,200 crores in NHB, to enhance its refinance operations in the rural-housing sector.

NHB is working in close cooperation with banks, non-government organizations and MFIs to create a ‘refinance window’ to direct the fund flow. It is also considering setting up a separate mortgage-guarantee company that would address the issue of loan defaults. Mortgage guarantee or insurance is a key component of a well-functioning mortgage-finance system. It provides market-based default-risk protection to lenders. This would enhance the flow of housing finance, particularly to lower income groups, and thereby, help banks and HFCs to lower their risk. It is introducing this product by setting up a separate joint-venture company.

NHB is working with the government to set up a national mortgage depository, wherein loans taken against houses would be electronically linked to the property registrar. This would have the potential to become a part of the e-governance programme of the governments.

It has launched a residential-property index, NHB RESIDEX, in 2007 which is India’s first official-property index, for five cities—Bangaluru, Delhi, Bhopal, Kolkata and Mumbai, covering the period 2001–05. It has since been updated to December 2009 and has been expanded to ten more cities, viz, Ahmedabad, Faridabad, Chennai, Kochi, Hyderabad, Jaipur, Patna, Lucknow, Pune and Surat. It is the first housing-price index in India to fill price-information gap and streamline the property-development process in major cities. This would be released every 6 months and give a somewhat fair indication of the price movements in that city. NHB residex can be used to assess the movement in the value of housing stock over a period of time and also to assess the gap found between the actual and reported market prices of real estate in different locations. State government and local administration can use the indices in formulating policies on various legal issues related to property tax, property evaluation and so on. Similarly, the NHB residex can be used by housing-finance industry to mark out areas where the demand for housing finance is more likely to increase. Builders and real-estate developers too can use the index for the same purposes. The index would be useful for investors, banks and others for their ‘collaterals.’ It tracks residential property prices across 26 cities in India on a quarterly basis. After a recent review of the index, it was decided to revamp it by bringing out comprehensive housing-related indices.

NHB is also planning to launch an interactive portal for consumers that would provide assorted info on the property market. The Golden Jubilee Rural Housing Finance Scheme (GJRHFS) was launched in the year 1997–98 with a view to provide improved access to housing finance to people living in rural areas. The Scheme provides for construction of a new dwelling unit or upgradation of the existing one. The Scheme is implemented through various primarly lending institutions (PLIs), namely, HFCs, public-sector banks (PSBs) and cooperative-sector institutions. NHB is the monitoring agency, and fixes annual targets to each PLI.

NHB has launched home loan counselling programme which can be provided by independent mortgage counselors.

NHB refinances under the Rural Housing Fund (RHF) and under the Urban Housing Fund (UHF). NHB also extended refinance to HFCs at reduced rates under the Urban Housing Fund scheme to step up the flow of housing finance to flood-affected districts of Tamil Nadu.

The central government has identified NHB as the nodal agency for implementing the credit-linked subsidy scheme (CLSS) under the Pradhan Mantri Awas Yojana (Urban)–Housing for All Mission, and the solar capital subsidy scheme. As part of CLSS, NHB releases subsidy claims pertaining to households to primary lending institutions.

Prudential Norms for the Housing-finance Sector

The number of players in the housing sector has increased in the past few years as the demand for housing far exceeds the supply. This has led to an increase in the competition whereby all the players are trying to increase the slice of the cake.

In order to ensure a stability in the sector, prudential norms have been provided by the regulator. Stipulations regarding income recognition, asset classification, capital adequacy and credit concentration have been specified from time to time, depending on the industry requirements. The regulatory norms stipulate a 10 per cent capital adequacy for banks, whereas the same is 12 per cent for HFCs.

In case of housing loans extended by HFCs and SCBs, the NPA classification norm was changed from 180 days to 90 days past due. During the year 2008–09, the risk weightages for housing loans granted by the HFCs were modified and linked to loan to value (LTV) Ratios. Mortgage loans upto ₹30 lakh having LTV = or <75 per cent would attract risk weight of 50 per cent while mortgage loan above ₹30 lakh would attract risk weight of 75 per cent.

GUIDELINES RELATING TO HOUSING FINANCE

I. Applicable to all Scheduled Commercial Banks, excluding Regional Rural Banks.

1. INTRODUCTION Banks, with their vast branch network throughout the length and breadth of the country, occupy a very strategic position in the financial system and have an important role to play in providing credit to the housing sector.

Keeping in view the objectives of the National Housing Finance Policy of the Central Government, RBI had introduced a scheme of housing finance allocation wherein every year banks were required to achieve the prescribed target of 'housing finance' announced annually. The banks could deploy their funds under the housing finance allocation in any of the three categories, viz., direct finance, indirect finance, or investment in bonds of NHB/HUDCO, or combination thereof.

The allocation under the scheme was last announced for the year 2002-2003 and the scheme has since been discontinued.

Presently, banks have the freedom to evolve their own guidelines on various aspects of granting housing finance with the approval of their boards.

2. VARIOUS REGULATIONS While formulating their policies, banks have to take into account the following RBI guidelines and ensure that bank credit is used for production, constructions activities and not for activities connected with speculation in real estate.

(A) ACQUISITION OF LAND Bank finance granted only for purchase of a plot, provided a declaration is obtained from the borrower that he intends to construct a house on the said plot, with the help of bank finance or otherwise, within such period as may be laid down by the banks themselves.

(B) CONSTRUCTION OF BUILDING/READY-BUILT HOUSE

(i) Banks may grant loans to individuals for purchase/construction of dwelling unit per family and loans given for repairs to the damaged dwelling units of families.

(ii) Bank may extend finance to a person who already owns a house in town/village where he resides, for buying/constructing a second house in the same or other town/village for the purpose of self occupation.

(iii) Bank may extend finance for purchase of a house by a borrower who proposes to let it out on rental basis on account of his posting outside the headquarters or because he has been provided accommodation by his employer.

(iv) Bank may extend finance to a person who proposes to buy an old house where he is presently residing as a tenant.

(v) Banks may finance for construction meant for improving the conditions in slum areas for which credit may be extended directly to the slum-dwellers on the guarantee of the government, or indirectly to them through the state governments.

(vi) Bank may provide credit for slum improvement schemes to be implemented by Slum Clearance Boards and other public agencies.

(vii) Banks are advised to also adhere to the following conditions, in the light of the observations of Delhi High Court on unauthorized construction:

(a) In cases where the applicant owns a plot/land and approaches the banks/FIs for a credit facility to construct a house, a copy of the sanctioned plan by competent authority in the name of a person applying for such credit facility must be obtained by the banks/FIs before sanctioning the home loan.

(b) An affidavit-cum-undertaking must be obtained from the person applying for such credit facility that he shall not violate the sanctioned plan, construction shall be strictly as per the sanctioned plan and it shall be the sole responsibility of the executants to obtain completion certificate within 3 months of completion of construction, failing which the bank shall have the power and the authority to recall the entire loan with interest, costs and other usual bank charges.

(c) An architect appointed by the bank must also certify at various stages of construction of building that the construction of the building is strictly as per sanctioned plan and shall also certify at a particular point of time that the completion certificate of the building issued by the competent authority has been obtained.

(d) In cases where the applicant approaches the bank/FIs for a credit facility to purchase the built up house/flat, it should be mandatory for him to declare by way of an affidavit-cum-undertaking that the built up property has been constructed as per the sanctioned plan and/or building bye-laws and as far as possible has a completion certificate also.

(e) An architect appointed by the bank must also certify before disbursement of the loan that the built up property is strictly as per sanctioned plan and/or building bye-laws.

(f) No loan should be given in respect of those properties which fall in the category of unauthorized colonies unless and until they have been regularized and development and other charges paid.

(g) No loan should also be given in respect of properties meant for residential use but which the applicant intends to use for commercial purposes and declares so while applying for loan.

(viii) Supplementary Finance

(a) Banks may consider requests for additional finance within the overall ceiling for carrying out alterations/additions/repairs to the house/flat already financed by them.

(b) In the case of individuals who might have raised funds for construction/acquisition of accommodation from other sources and need supplementary finance, banks may extend such finance after obtaining *paripassu* or second mortgage charge over the property mortgaged in favour of other lenders and/or against such other security, as they may deem appropriate.

(c) Banks may consider for grant of finance to

(i) the bodies constituted for undertaking repairs to houses, and

(ii) the owners of building/house/flat, whether occupied by themselves or by tenants, to meet the need-based requirements for their repairs/additions, after satisfying themselves regarding the estimated cost (for which requisite certificate should be obtained from an engineer/architect, wherever necessary) and obtaining such security as deemed appropriate.

(ix) Bank finance should, however, not be granted for the following:

(a) Banks should not grant finance for construction of buildings meant purely for government/semi-government offices, including Municipal and Panchayat offices. However, banks may grant loans for activitieswhich will be refinanced by institutions like NABARD.

(b) Projects undertaken by public sector entities which are not corporate bodies (i.e., public sector undertakings which are not registered under companies act or which are not corporations established under the relevant statute) may not be financed by banks. Even in respect of projects undertaken by corporate bodies, as defined above, banks should satisfy themselves that the project is run on commercial lines and that bank finance is not in lieu of or to substitute budgetary resources envisaged for the project. The loan could, however, supplement budgetary resources if such supplementing was contemplated in the project design. Thus, in the case of a housing project, where the project is run on commercial lines, and the government is interested in promoting the project either for the benefit of the weaker sections of the society or otherwise, and a part of the project cost is met by the government through subsidies made available and/or contributions to the capital of the institutions taking up the project, the bank finance should be restricted to an amount arrived at after reducing from the total project cost the amount of subsidy/capital contribution receivable from the government and any other resources proposed to be made available by the government.

(c) Banks had, in the past, sanctioned term loans to corporations set up by government like State Police Housing Corporation, for construction of residential quarters for allotment to employees where the loans were envisaged to be repaid out of budgetary allocations. As these projects cannot be considered to be run on commercial lines, it would not be in order for banks to grant loans to such projects.

(C) LENDING TO HOUSING INTERMEDIARY AGENCIES

(i) Financing of Land Acquisition

(a) In view of the need to increase the availability of land and house sites for increasing the housing stock in the country, banks may extend finance to public agencies and not private builders for acquisition and development of land, provided it is a part of the complete project, including development of infrastructure such as water systems, drainage, roads, provision of electricity, etc. Such credit may be extended by way of term loans. The project should be completed as early as possible and, in any case, within three years, so as to ensure quick re-cycling of bank funds for optimum results. If the project covers construction of houses, credit extended therefore in respect of individual beneficiaries should be on the same terms and conditions as stipulated for financing the beneficiary directly.

(b) Banks should have a Board approved policy in place for valuation of properties including collaterals accepted for their exposures and that valuation should be done by professionally qualified independent valuers.

(c) As regards the valuation of land for the purpose of financing of land acquisition as also land secured as collateral, banks may be guided as under:

(i) Banks may extend finance to public agencies and not to private builders for acquisition and development of land, provided it is a part of the complete project, including development of infrastructure such as water systems, drainage, roads, provision of electricity, etc. In such limited cases where land acquisition can be financed, the finance is to be limited to the acquisition price (current price) plus development cost. The valuation of such land as prime security should be limited to the current market price.

(ii) Wherever land is accepted as collateral, valuation of such land should be at the current market price only.

(ii) Lending to Housing Finance Institutions

Banks may grant term loans to housing finance institutions taking into account (long-term) debt-equity ratio, track record, recovery performance and other relevant factors including the other applicable regulatory guidelines.

(iii) Lending to Housing Boards and Other Agencies

Banks may extend term loans to state level housing boards and other public agencies. However, in order to develop a healthy housing finance system, while doing so, the banks must not only keep in view the past performance of these agencies in the matter of recovery from the beneficiaries but they should also stipulate that the Boards will ensure prompt and regular recovery of loan instalments from the beneficiaries.

(iv) Term Loans to Private Builders

(a) In view of the important role played by professional builders as providers of construction services in the housing field, especially where land is acquired and developed by state housing boards and other public agencies, commercial banks may extend credit to private builders on commercial terms by way of loans linked to each specific project.

(b) Banks, however, are not permitted to extend fund based or non-fund based facilities to private builders for acquisition of land even as part of a housing project.

(c) The period of credit for loans extended by banks to private builders may be decided by banks themselves based on their commercial judgment subject to usual safeguards and after obtaining such security, as banks may deem appropriate.

(d) Such credit may be extended to builders of repute, employing professionally qualified personnel. It should be ensured, through close monitoring, that no part of such funds is used for any speculation in land.

(e) Care should also be taken to see that prices charged from the ultimate beneficiaries do not include any speculative element, that is, prices should be based only on the documented price of land, the actual cost of construction and a reasonable profit margin.

(v) Terms and Conditions for Lending to Housing Intermediary Agencies
   (a) In order to enhance the flow of resources to housing sector, term loans may be granted by banks to housing intermediary agencies against the direct loans sanctioned/proposed to be sanctioned by the latter, irrespective of the per borrower size of the loan extended by these agencies.
   (b) Banks can grant term loans to housing intermediary agencies against the direct loans sanctioned/proposed to be sanctioned by them to non-resident Indians also. However, banks should ensure that housing finance intermediary agencies being financed by them are authorized by RBI to grant housing loans to NRIs as all housing finance intermediaries are not authorized by RBI to provide housing finance to NRIs.
   (c) Banks have freedom to charge interest rates to housing intermediary agencies without reference to Benchmark Prime Lending Rates (BPLR) upto June 30, 2010. Under the Base Rate System effective from July 1, 2010, all categories of loans will be priced with reference to base rate which is the minimum interest rate for all loans.

(vi) Adherence to guidelines on Commercial Real Estate (CRE) exposure

Lending to housing intermediary agencies will be subject to the guidelines on commercial real estate exposure.

3. QUANTUM OF LOAN

(a) While deciding the quantum of loan to be granted as housing finance, banks should ensure that the LTV ratio for individual housing loans are as under:

Outstanding loan	*LTV ratiop (%)*	*Risk Weight (%)*	*Standard Asset Provision (%)*
Up to ₹30 lakh	≤80	35	0.25
	>80 and ≤90	50	
Above ₹30 lakh and up to ₹75 lakh	≤80	35	
Above ₹75 lakh	≤75	50	

(b) In order to have uniformity in the practices adopted for deciding the value of the house property while sanctioning housing loans, banks should not include stamp duty, registration and other documentation charges in the cost of the housing property they finance so that the effectiveness of LTV norms is not diluted.

(c) However, in cases where the cost of the house/dwelling units does not exceed ₹10 lakh, bank may add stamp duty, registration and other documentation charges to the cost of the house/dwelling unit for the purpose of calculating LTV ratio.

(d) It has been observed that some banks have introduced certain innovative housing loan schemes in association with developers/builders, e.g., upfront disbursal of sanctioned individual housing loans to the builders without linking the disbursals to various stages of construction of housing project, Interest/EMI on the housing loan availed of by the individual borrower being serviced by the builders during the construction period/specified period, etc. This might include signing of tripartite amongbetween the bank, the builder and the buyer of the housing unit. These loans products are popularly known by various names like 80:20, 75:25 schemes.

(e) Such housing loan products are likely to expose the banks as well as their home loan borrowers to additional risks, e.g., in case of dispute between individual borrowers and developers/builders, default/delayed payment of interest/EMI by the developer/builder during the agreed period on behalf of the borrower, non-completion of the project on time, etc. Further, any delayed payments by developers/builders on behalf of individual borrowers to banks may lead to lower credit rating/scoring of such borrowers by Credit Information Companies (CICs) as information about servicing of loans get passed on to the CICs on a regular basis. In cases, where bank loans are also disbursed upfront on behalf of their individual borrowers in a lump-sum to builders/developers without any linkage to stages of constructions, banks run disproportionately higher exposures with concomitant risks of diversion of funds.

(f) Banks are advised that disbursal of housing loans sanctioned to individuals should be closely linked to the stages of construction of the housing project/houses and upfront disbursal should not be made in cases of incomplete/under-construction/green field housing projects.

(g) However, in cases of projects sponsored by government/statutory authorities, banks may disburse the loans as per the payment stages prescribed by such authorities, even where payments sought from house buyers are not linked to the stages of constructions, provided such authorities have no past history of non-completion of projects.

(h) It is emphasized that banks while introducing any kind of product should take into account the customer suitability and appropriateness issues and also ensure that the borrowers/customers are made fully aware of the risks and liabilities under such products.

4. RATE OF INTEREST Banks should charge interest on housing finance granted by them in accordance with the directives on "Interest Rates on Advances" issued by Reserve Bank of India from time to time.

5. APPROVALS FROM STATUTORY/REGULATORY AUTHORITIES While appraising loan proposals involving real estate, banks should ensure that the borrowers should have obtained prior permission from government/local governments/other statutory authorities for the project, wherever required. Loan approval process is not hampered on account of this, while the proposals could be sanctioned in normal course, the disbursements should be made only after the borrower has obtained requisite clearances from the government authorities.

6. DISCLOSURE REQUIREMENTS In view of the observations of Hon'ble High Court of Judicature at Bombay, while granting finance to specific housing/development projects, banks are advised to stipulate as a part of the terms and conditions that:

(a) the builder/developer/company would disclose in the Pamphlets/Brochures etc., the name(s) of the bank(s) to which the property is mortgaged.
(b) the builder/developer/company would append the information relating to mortgage while publishing advertisement of a particular scheme in newspapers/magazines, etc.
(c) the builder/developer/company would indicate in their pamphlets/brochures that they would provide No Objection Certificate (NOC)/permission of the mortgagee bank for sale of flats/property, if required.
(d) Banks are advised to ensure compliance of the above terms and conditions and funds should not be released unless the builder/developer/company fulfils the above requirements.
(e) The above mentioned provisions will be mutatis-mutandis, applicable to commercial real estate also.

7. EXPOSURE TO REAL ESTATE Banks are well advised to frame comprehensive prudential norms relating to the ceiling on the total amount of real estate loans, single/group exposure limit for such loans, margins, security, repayment schedule and availability of supplementary finance and the policy should be approved by the bank's board. While framing the bank's policy, the guidelines issued by the reserve bank should be taken into account.

8. HOUSING LOANS UNDER PRIORITY SECTOR The grant of housing loan for the purpose of the priority sector lending targets including reporting requirements will be subject to the instructions on "Priority Sector Lending" as amended from time to time.

9. FINANCING OF AFFORDABLE HOUSING-ISSUE OF LONG TERM BONDS BY BANKS Banks can issue long-term bonds with a minimum maturity of seven years to raise resources for lending to affordable housing subject to the conditions mentioned in the guidelines on "Issue of Long term Bonds by Banks-Financing of Infrastructure and Affordable Housing".

II. Applicable to Urban Co-operative Banks (UCBs)

1. General

1.1 The role of primary (urban) co-operative banks (UCBs) in providing housing finance with their vast network, occupy a very strategic position in the financial system and have an important role to play in providing credit to the housing sector. Further, housing finance to specified categories up to prescribed limits is treated as priority sector lending, and the need for UCBs providing credit to priority sector has come to be increasingly recognized consistent with the social objectives placed before the banking system.

1.2 Therefore, with a view to enabling the UCBs to play a more positive role in providing finance for housing schemes, particularly to the weaker sections of the community, these banks are permitted to grant loans for housing schemes up to certain limits from their own resources subject to the guidelines detailed hereunder.

1.3 Bigger banks that have large surplus resources may undertake larger lending for housing, as this will provide a remunerative avenue for investment of their surplus funds.

1.4 Wherever banks are still required to obtain special permission of the Registrar for financing housing societies, it is suggested that these banks should obtain general permission to finance housing societies subject to such terms and conditions as may be prescribed for the purpose.

2. Eligible Category of Borrowers UCBs may grant loans to the following categories of borrowers:

(i) Individuals and co-operative/group housing societies
(ii) Housing boards undertaking housing projects or schemes for Economically Weaker Sections (EWS), Low Income Groups (LIG) and Middle Income Groups (MIG).
(iii) Owners of houses/flats for extension and up-gradation, including major repairs.

3. Eligible Housing Schemes The borrowers in the above categories will be eligible for finance for the following types of housing schemes:

(a) Construction/purchase of houses/flats by individuals
(b) Repairs, alterations and additions to houses/flats by individuals
(c) Schemes for housing and hostels for scheduled castes and scheduled tribes
(d) Under slum clearance schemes - directly to the slum dwellers on the guarantee of the government, or indirectly through statutory boards established for this purpose
(e) Education, health, social, cultural or other institutions/centres which are part of a housing project and considered necessary for the development of settlements or townships
(f) Shopping centres, markets and such other centres catering to the day to day needs of the residents of the housing colonies and forming part of a housing project

4. Terms and Conditions for Housing Loans Finance provided by the UCBs to the eligible categories of borrowers for eligible housing schemes will be subject to the following terms and conditions:

4.1 Maximum Loan Amount & Margins

(i) UCBs, based on their commercial judgment and other prudential business considerations, with the approval of their board of directors, are free to identify the eligible borrowers, decide margins and grant housing loans depending upon the repaying capacity of borrowers.
(ii) Tier-I UCBs are permitted to extend individual housing loans upto a maximum of ₹30 lakh per beneficiary of a dwelling unit and Tier-II UCBs (UCBs other than Tier I) to extend individual housing loans up to a maximum of ₹70.00 lakh per beneficiary of a dwelling unit subject to extant prudential exposure limits.
(iii) The maximum loan should not exceed 15 percent of capital funds of the bank in case of individual borrowers and 40 per cent of the capital funds in case of group of borrowers. The capital funds for the purpose shall include both Tier-I Capital and Tier-II capital.

- Tier I UCBs are categorised as under:
  - Banks having deposits below ₹100 crores operating in a single district
  - Banks with deposits below ₹100 crores operating in more than one district will be treated as Tier I-provided the branches are in contiguous districts and deposits and advances of branches in one district separately constitute at least 95% of the total deposits and advances respectively of the bank and
  - Banks with deposits below ₹100 crores, whose branches were originally in a single district but subsequently, became multi-district due to reorganization of the district deposits and advances as referred to in the above definition may be reckoned as on 31st March of the immediate preceding financial year.

4.2 A. Interest: Banks may, with the approval of their boards, determine the rate of interest, keeping in view the size of accommodation, degree of risk and other relevant considerations.

B. Foreclosure Charges/Prepayment Penalty With effect from June 26, 2012, it has been decided that UCBs will not be permitted to charge foreclosure charges/prepayment penalties in home loans on floating interest rate basis.

4.3 **Charging of Penal Interest:** Banks may formulate, with the approval of their boards, transparent policy for charging penal interest rates to be levied for reasons such as default in repayment, non-submission of financial statements, etc. The policy should be governed by well-accepted principles of transparency, fairness, incentive to service the debt and due regard to genuine difficulties of customers.

4.4 **Security**

(i) UCBs may secure housing loans either
- (a) by mortgage of property, or
- (b) by government guarantee where forthcoming, or
- (c) by both.

(ii) Where this is not feasible, banks may accept security of adequate value in the form of LIC policies, government promissory notes, shares/debentures, gold ornaments or such other security as they deem appropriate.

4.5 **Period of Loan**

(i) Housing loans may be repayable within a maximum period of 20 years, including moratorium or repayment holiday.

(ii) The moratorium or repayment holiday may be granted
- (a) at the option of the beneficiary, or
- (b) till completion of constructions, or 18 months from the date of disbursement of first instalment of the loan, whichever is earlier.

4.6 **Graduated Instalments**

(i) The instalments should be fixed on a realistic basis taking into account the repaying capacity of the borrower.

(ii) In order to make housing finance affordable, banks may consider fixing the instalments on a graduated basis if there is reasonable expectation of growth in the income of the borrower in the coming years. Graduated basis means fixing lower repayment instalments in the initial years and gradually increasing the instalment amount in subsequent years coinciding with expected increase in income in subsequent years.

4.7 **Aggregate Limit for Housing Finance**

4.7.1 The exposure of UCBs to housing, real estate and commercial real estate loans would be limited to 10 per cent of their total assets. The above ceiling of 10 per cent of total assets can be exceeded by an additional limit of 5 per cent of total assets for the purpose of grant of housing loans to individuals up to ₹25 lakh, which is covered under priority sector.

4.7.2 The total assets may be reckoned based on the audited balance sheet as on March 31 of the preceding financial year. For reckoning total assets, losses, intangible assets, contra items like bills receivables, etc., would be excluded.

4.7.3 The exposure should take into account both fund-based and non-fund based facilities.

4.7.4 Working capital loans given by UCBs against hypothecation of construction materials provided to the contractors who undertake comparatively small construction on their own without receiving advance payments as provided for in point 7 below is exempted from the prescribed limit.

4.7.5 Finance extended to the eligible category of borrowers mentioned in point 2 above will only be eligible to be treated as housing finance. While the purpose of the loan shall determine whether the loans granted against the security of immovable property need to be classified as real estate loans, the source of repayment will determine whether the exposure is against commercial real estate. For classification of such loans as real estate/commercial real estate, UCBs may be guided by the instructions contained in Annexure 1. As loans to the residential housing projects under the Commercial Real Estate (CRE) sector exhibit lesser risk and volatility than the CRE sector taken as a whole;it has been decided to carve out a separate sub-sector called 'Commercial Real Estate–Residential Housing' (CRE-RH) from the CRE sector. CRE-RH would consist of loans to builders/developers for residential housing projects (except for captive consumption) under CRE segment. Such projects should ordinarily not include non-residential commercial real estate. However, integrated housing projects comprising some commercial space (e.g., shopping complex, school, etc.) can also be classified under CRE-RH, provided that the commercial area in the residential housing project does not exceed 10% of the total Floor Space Index (FSI) of the project. In case the FSI of the commercial area in the predominantly residential housing complex exceeds the ceiling of 10%, the project loans should be classified as CRE and not CRE-RH.

4.7.6 UCBs are not allowed to exceed the limit prescribed for grant of housing, real estate, commercial real estate loans to the extent of funds obtained from higher financing agencies and refinance from national housing bank.

5. Additional/Supplementary Finance

5.1 UCBs may extend additional finance to carry out alterations, additions, repairs to houses/flats already financed by them subject to repayment capacity of borrowers.

5.2 In the case of individuals who might have raised funds for construction/acquisition of accommodation from other sources and need supplementary finance, banks may extend credit after obtaining pari passu or second mortgage charge over the property mortgaged in favour of other lenders and/or against such other security as they may deem appropriate after due assessment of aggregate repayment capacity of borrowers.

5.3 UCBs may also extend need-based credit up to a maximum of ₹2.00 lakh in rural and semi-urban areas and ₹5.00 lakh in urban areas to the owner of a house/flat only for repairs, additions, alterations, etc., irrespective of whetherthe house/flat is owner occupied or tenant occupied, after obtaining such security as the banks may deem appropriate. They should satisfy themselves regarding the estimated cost of repairs, additions, etc., having regard to the extent of such repairs or additions, materials to be used, cost of labour and other charges and after obtaining certificate/s from qualified engineers/architects in respect thereof, considered necessary.

5.4 The terms and conditions relating to margin, interest rates, repayment period, etc., in respect of additional/supplementary finance may be same as indicated in respect of loans for construction/acquisition.

6. Lending to Housing Boards

6.1 UCBs may extend loans to housing boards within their states. The rate of interest to be charged on the loans to such boards may be fixed at the discretion of the banks.

6.2 While extending loans to housing boards, banks may not only keep in view the past performance of the housing boards in the matter of recovery from the beneficiaries but should also stipulate that the boards will ensure prompt and regular recovery of loan instalments from the beneficiaries.

7. Advances to Builders/Contractors

7.1 Builders/contractors generally require huge funds, take advance payments from the prospective buyers or from those on whose behalf construction is undertaken and, therefore, may not normally require bank finance for the purpose. Any financial assistance extended to them by primary (urban) co-operative banks may result in dual financing. Banks should, therefore, normally refrain from sanctioning loans and advances to this category of borrowers.

7.2 However, where contractors undertake comparatively small construction work on their own, (i.e., when no advance payments are received by them for the purpose), banks may consider extending financial assistance to them against the hypothecation of construction materials, provided such loans and advances are in accordance with the bye laws of the bank and instructions/directives issued by the Reserve Bank from time to time.

7.3 Banks should undertake a proper scrutiny of the relevant loan applications, and satisfy themselves, among other things, about the genuineness of the purpose, the quantum of financial assistance required, creditworthiness of the borrower, repayment capacity, etc., and also observe the usual safeguards, such as obtaining periodic stock statements, carrying out periodic inspections, determining drawing power strictly on the basis of the stock held, maintaining a margin of not less than 40 to 50 percent, etc. They should also ensure that materials used up in the construction work are not included in the stock statements for the purpose of determining the drawing power.

7.4 *Valuation of land:* It has been observed that while financing builders/contractors, certain banks valued the land for the purpose of security, on the basis of the discounted value of the property after it is developed, less the cost of development. This is not in conformity with established norms. In this connection, it is clarified that UCBs should not extend fund-based/non-fund-based facilities to builders/contractors for acquisition of land even as a part of a housing project. Further, wherever land is accepted as collateral, valuation of such land should be at the current market price only.

7.5 UCBs may also take collateral security, wherever available. As construction work progresses, contractors will get paid and such payments should be applied to reduce the balance in the borrowal accounts. If possible, banks could perhaps enter into a tripartite agreement with the borrower and his clients, particularly when no collateral securities are available for such advances.

7.6 It has been observed that some banks have introduced certain innovative housing loan schemes in association with developers/builders, e.g., upfront disbursal of sanctioned individual housing loans to builders without linking the disbursals to various stages of construction of housing project, interest/EMI on the housing loan availed of by the individual borrower being serviced by the builders during the construction period/specified period, etc. In view of the higher risks associated with such lump-sum disbursal of sanctioned housing loans and customer suitability issues, UCBs are advised that disbursal of housing loans sanctioned to individuals should be closely linked to the stages of construction of the housing project/houses and upfront disbursal should not be made in cases of incomplete/under-construction/green field housing projects.

8. Housing Loans under Priority Sector

8.1 The following types of loan for housing purposes are eligible for categorization under priority sector:

(i) Loans up to ₹25 lakh to individuals for purchase/construction of dwelling unit per family (excluding loans granted by banks to their own employees). Family for this purpose means and includes the spouse of the member and the children, parents, brothers and sisters of the member who are dependent on such member, but shall not include legally separated spouse.

(ii) Loans given for repairs to the damaged dwelling units of families up to ₹2 lakh in rural and semi-urban areas and up to ₹5 lakh in urban and metropolitan areas.

(iii) Assistance given to any governmental agency for construction of dwelling units or for slum clearance and rehabilitation of slum dwellers, subject to a ceiling of ₹5 lakh of loan amount per dwelling unit.

(iv) Assistance given to a non-governmental agency approved by the NHB for the purpose of refinance for construction/reconstruction of dwelling units or for slum clearance and rehabilitation of slum dwellers, subject to a ceiling of loan component of ₹10 lakh per dwelling unit for loans sanctioned on and after May 18, 2012.

8.2 Investments made by UCBs in bonds issued by NHB/HUDCO on or after April, 1, 2007 shall not be eligible for classification under priority sector lending.

9. Precautions

9.1 A number of cases have come to the notice of Reserve Bank, where unscrupulous persons have defrauded the banks by obtaining multiple bank finance against the same property by preparing a number of sets of the original documents and submitting the same to various banks for obtaining housing finance. Similarly the salary certificates of employees of certain public sector undertakings were fabricated, so as to match the requirement of banks for availing higher amounts of loan. The estimates given were also on the higher side, so as to avoid contribution of margin money by the borrowers. Such frauds could take place on account of laxity on the part of the bank officials to follow the laid down procedures for verifying the genuineness of the documents submitted by borrowers independently through their own advocates/solicitors. Banks should, therefore, take due precaution while accepting various documents.

9.2 Banks would need to satisfy themselves that loans extended by them are not for unauthorized construction or for misuse of properties/encroachment on public land. For this purpose, they should ensure strict compliance with the procedure laid down in Annexure2.

9.3 In a case which came up before the Hon'ble High Court of Judicature at Bombay, the Hon'ble Court observed that the bank granting finance to housing/development projects should insist on disclosure of the charge/or any other liability on the plot, in the brochure, pamphlets etc., which may be published by developer/owner inviting public at large to purchase flats and properties. The Court also added that this obviously would be part of the terms and conditions on which the loan may be sanctioned by the bank. Keeping in view the above observations, while granting finance for eligible housing schemes, UCBs are advised to stipulate as part of terms and conditions that:

(a) The builder/developer shall disclose in the pamphlets/brochures etc., the name(s) of the bank(s) to which the property is mortgaged.

(b) The builder/developer would append the information relating to mortgage while advertising for a particular scheme in newspapers/magazines etc.

(c) The builder/developer would indicate in the pamphlets/brochures that he would provide No Objection Certificate (NOC)/permission of the mortgagee bank for sale of flats/property, if required. UCBs are also advised to ensure compliance of the above terms and conditions. Funds should not be released unless the builder/developer fulfils the above requirements.

10. National Building Code The Bureau of Indian Standards (BIS) has formulated a comprehensive building Code,namely National Building Code (NBC) of India 2005, providing guidelines for regulating the building construction activities across the country. The Code contains all the important aspects relevant to safe and orderly building development, such as administrative regulations, development control rules and general building requirements; fire safety requirements; stipulations regarding materials, structural design and construction (including safety); and building and plumbing services. Adherence to NBC will be advisable in view of the importance of safety of buildings especially against natural disasters. Banks' boards may consider this aspect for incorporation in their loan policies. Further information regarding the NBC can be accessed from the website of Bureau of Indian Standards.

III. Issue of Long Term Bonds by Banks–Financing of Infrastructure and Affordable Housing

Apart from what is technically defined as infrastructure, affordable housing is another segment of the economy which both requires long term funding and is of critical importance. Government has stressed the importance of availability of cheap credit to make housing affordable for the Economically Weaker Sections (EWS), Lower Income Group (LIG) and Medium Income Group (MIG) segments of the population. Accordingly, the Reserve Bank has issued guidelines to ease the way for banks to raise long term resources to finance their long term loans to infrastructure as well as affordable housing. This will help promote both growth and stability, as well as improve the supply side.

Guidelines

1. Banks can issue long-term bonds with a minimum maturity of seven years to raise resources for lending to (i) long term projects in infrastructure sub-sectors, and (ii) affordable housing.
2. **Definitions**
   (i) *Infrastructure Sub-sectors:* Any credit facility, in whatever form, extended by lenders (i.e., banks, FIs or NBFCs) to an infrastructure facility as specified below falls within the definition of 'infrastructure lending'. In other words, a credit facility provided to a borrower company engaged in:
   - developing, or
   - operating and maintaining, or
   - developing, operating and maintaining any infrastructure facility that is a project in the subsectors specified by the RBI.

   (ii) *Affordable Housing:* Lending to affordable housing is defined as housing loans eligible under priority sector lending by the RBI.

Housing Loans Eligible under Priority Sector Lending

(i) Loans to individuals up to ₹25 lakh in metropolitan centres with population above ten lakh and ₹15 lakh in other centres for purchase/construction of a dwelling unit per family excluding loans sanctioned to bank's own employees.

(ii) Loans for repairs to the damaged dwelling units of families up to ₹2 lakh in rural and semi-urban areas and up to ₹5 lakh in urban and metropolitan areas.

(iii) Bank loans to any governmental agency for construction of dwelling units or for slum clearance and rehabilitation of slum dwellers subject to a ceiling of ₹10 lakh per dwelling unit.

(iv) The loans sanctioned by banks for housing projects exclusively for the purpose of construction of houses only to economically weaker sections and low income groups, the total cost of which do not exceed ₹10 lakh per dwelling unit. For the purpose of identifying the economically weaker sections and low income groups, the family income limit of ₹1,20,000 per annum, irrespective of the location, is prescribed.

(v) Bank loans to Housing Finance Companies (HFCs), approved by NHB for their refinance, for on-lending for the purpose of purchase/construction/reconstruction of individual dwelling units or for slum clearance and rehabilitation of slum dwellers, subject to an aggregate loan limit of ₹10 lakh per borrower, provided the all-inclusive interest rate charged to the ultimate borrower is not exceeding the lowest lending rate of the lending bank for housing loans plus two percent per annum.

The eligibility under priority sector loans to HFCs is restricted to five percent of the individual bank's total priority sector lending, on an ongoing basis. The maturity of bank loans should be co-terminus with average maturity of loans extended by HFCs. Banks should maintain necessary borrower-wise details of the underlying portfolio.

Also **housing loans to individuals** upto ₹50 lakhs for houses of values upto ₹65 lakhs located in the six metropolitan centres, viz., Mumbai, New Delhi, Chennai, Kolkata, Bengaluru and Hyderabad and ₹40 lakhs for houses of values upto ₹50 lakhs in other centres for purchase/construction of dwelling unit per family

3. Type of bond The instrument shall be fully paid, redeemable and unsecured and would rank pari-passu along with other uninsured, unsecured creditors.

4. Currency of issue The bonds shall be denominated in Indian rupees.

5. Maturity period The minimum maturity period of the long-term bonds shall be seven years.

6. Amount There will not be any restriction on the quantum of such bonds to be issued by banks; however, the regulatory incentives will be restricted to the bonds that are used to incrementally finance long term projects in infrastructure and loans for affordable housing. Any incremental infrastructure and affordable housing loans acquired from other banks and financial institutions to be reckoned for regulatory incentives will require prior approval of RBI.

Recognizing that current outstanding lending to infrastructure and affordable housing will mature steadily (the regulations below assume 6 years), the *eligible credit* to infrastructure and affordable housing will be computed as per the schedule and formulae given in next point.

7. Credit eligible for regulatory incentives

Period	*Eligible Credit = EC*
From the date of circular till March 31, 2015	B – 0.84A
April 1, 2015 – March 31, 2016	B – 0.7A
April 1, 2016 – March 31, 2017	B – 0.56A
April 1, 2017 – March 31, 2018	B – 0.42A
April 1, 2018 – March 31, 2019	B – 0.28A
April 1, 2019 – March 31, 2020	B – 0.14A
April 1, 2020 onwards	B

Where,

A = Outstanding 'Standard' loans to Infrastructure sector (project loans) and affordable housing on the date of this circular

B = Outstanding 'Standard' loans to Infrastructure sector (project loans) and affordable housing on the date of issuance of the bonds

Regulatory Incentives

8. Compliance with reserve requirements These bonds will be exempted from computation of Net Demand and Time Liabilities (NDTL) and would therefore not be subjected to CRR/SLR requirements. However, this exemption will be subject to a ceiling of the eligible credit mentioned in point 7above. Therefore, DTL for the bank which has issued long term bonds in terms of this circular will be computed as given below:

Demand and Time Liabilities (DTL) for the purpose of maintaining CRR & SLR	I
Amount of long-term credit eligible for regulatory incentives as per point 7 above.	EC
Outstanding long term bonds issued to finance infrastructure loans and affordable housing loans, in terms of this circular	LB
DTL for the bank which has issued long term bonds in terms of this circular	I – Min (EC and LB)

9. Relaxation in priority sector lending norms Eligible bonds will also get exemption in computation of Adjusted Net Bank Credit (ANBC) for the purpose of Priority Sector Lending (PSL), as per the computation given below:

Bank Credit in India (As prescribed in item No.VI of Form 'A' (Special Return as on March 31st) under Section 42 (2) of the RBI Act, 1934.	II
Bills Rediscounted with RBI and other approved Financial Institutions + Advances extended in India against the incremental FCNR (B)/NRE deposits, qualifying for exemption from CRR/SLR requirements, till their maturity.	III
Net Bank Credit (NBC)*	IV = (II-III)
Bonds/debentures in Non-SLR categories under HTM category + other investments eligible to be treated as priority sector + Outstanding Deposits, as on preceding March 31st, under RIDF, Warehouse Infrastructure Fund, Short term Co-operative Rural Credit Refinance Fund and Short Term RRB Fund with NABARD	V
ANBC (Adjusted Net Bank Credit)	VI = IV+V
ANBC after issuance of long-term bonds for infrastructure and affordable housing	VI - Min (EC and LB)
* For the purpose of priority sector only. Banks should not deduct/net any amount like provisions, accrued interest, etc. from NBC.	

Note: It has been observed that some banks are subtracting prudential write off at corporate/head office level while reporting Bank credit as above. In such cases, it must be ensured that bank credit to priority sector and all other sub-sectors so written off should also be subtracted category wise from priority sector and sub-target achievement.

All types of loans, investments or any other item which are treated as eligible for classifications under priority sector target/sub-target achievement should also form part of adjusted net bank credit.

Other requirements

10. Options The bonds should be issued in plain vanilla form without call or put option.

11. Rate of interest The bonds may be issued with a fixed or floating rate of interest. The floating rate of interest shall be referenced to market determined benchmark rates.

12. Method of issue The bonds may be issued through a public issue or private placement in full compliance with SEBI guidelines/norms including mandatory rating and listing.

13. Cross-holding Cross-holding of such bonds among the banks will not be permitted.

14. Eligibility for deposit insurance The bonds will not be eligible for deposit insurance.

15. Regulatory/Statutory compliance Banks issuing long-term bonds shall be required to comply with all relevant statutory and regulatory requirements.

16. FEMA requirement Banks shall comply with the FEMA requirements, if applicable.

17. Reporting requirements The banks issuing long term bonds shall submit a report to Department of Banking Supervision (DBS), Reserve Bank of India giving details of the bonds issued, such as amount raised, maturity of the instrument, rate of interest, together with a copy of the offer document, soon after the issue is completed.

RESIDENTIAL MORTGAGE-BACKED SECURITIZATION

NHB launched the pilot issues of MBSs in August 2000. The primary lenders create mortgages against loans provided by them to the purchasers of houses. The mortgages held as assets generate cash flows represented by repayment of both principal as well as interest on the loans. The secondary mortgage market involves the conversion of mortgages into financial instruments and the sale of these instruments to prospective investors. The cash flows which come as repayments from the borrowers to the originators, are transferred to a third party with simultaneous transfer of assets to an intermediary agency known as special-purpose vehicle (SPV) designated for the purpose of managing the bought-over pool of mortgages.

The securitization process of MBSs is as follows:

1. Assignment of retail-housing loans along with the underlying mortgages from the HFCs to NHB.
2. The loans, repayable in EMIs, are packaged and offered to investors as pass-through certificates (PTCs) by NHB, acting as an issuer and trustee. The housing loans, which constitute the receivables to be securitized, are held by NHB–SPV Trust set up by NHB. The PTCs are in the nature of trust certificates and represent a proportionate, undivided beneficial interest in the pool of housing loans. They are tradable securities without any recourse to the originator or the SPV. NHB issues Class-A and Class-B PTCs. Class-A PTCs are allotted to investors and Class-B PTCs are subscribed entirely by the originators. Class-B PTCs are subordinated to Class-A PTCs and act as a credit enhancement for Class-A PTC holders. Credit enhancement is an additional credit support and may be provided in various forms, such as setting aside a cash pool, limited corporate guarantee and third-party guarantee.
3. Issue opens and NHB receives application money.
4. Issue closes and NHB, and the issue arrangers finalize the allotment and issue-allotment letter to investors.

Benefits of Securitization

1. Improves capital-adequacy ratio through transfer of risky weighted assets.
2. Helps develop a long-term debt market in India.
3. Aids asset–liability management through deployment of long-term funds in the housing sector.
4. Enables a better-spread management and facilitates improvement of returns on assets and equity.
5. A new source of fee-based income.
6. Offers a viable and sustainable, market-oriented, fund-raising mechanism with the potential of integrating housing market with the domestic as well as international capital markets. In the past few years, the housing-finance industry has integrated, in some measure, with the capital market, through the securitization route. This integration has established functional links between savers, home-loan borrowers, financiers and capital-market investors.

This market has a huge growth potential to serve as an important funding source for the housing sector.

Box 21.1 The US Sub-prime Mortgage Crisis

The sub-prime mortgage crisis began in the United States in August 2007 and its repercussions were on the world economy. Let us understand what a sub-prime mortgage is.

There are four types of mortgages in the United States: Jumbo, Prime, Near-prime and Sub-prime. Jumbo loans are prime quality loans which exceed the $417,000 ceiling for mortgages that can be bought and guaranteed by government-sponsored enterprises (GSEs). Prime mortgages are the traditional type of loans to borrowers with good credit worthiness and full documentation of income. Near-prime are smaller than jumbo but do not qualify as prime as these borrowers are not able to fully document their income or provide traditional down payments. Sub-prime mortgages are loans to higher risk borrowers with lower income or poor-credit histories and weak documentation of income.

In the United States, there are two major mortgage companies—Fannie Mae (Federal National Mortgage Association) and Freddie Mac (Federal Home Loan Mortgage Corporation),which own or guarantee roughly half of the country's $12 trillion in the outstanding mortgage. The two companies were set up by the federal law as GSEs that operate as private companies with profits and stockholders. They encourage home-ownership by buying mortgages from banks. This frees cash for the banks so that they can make new loans. Some of the mortgages are held by them in their own portfolio and the rest are sold by packaging them as bonds and other securities known as 'residential MBS' (RMBS). These GSEs had not packaged many non-prime mortgages into RMBS.

Some 80 per cent of outstanding the US mortgages are prime, while 14 per cent are sub-prime and 6 per cent fall into the near-prime category. Sub- and near-prime loans shot up from 9 per cent of newly originated securitized mortgages in 2001 to 40 per cent in 2006. Easing of lending standards such as lower-average down payments and no requirement of full documentation of income, coupled with a sizeable rise in adjustable-rate mortgages (ARMs), facilitated the growth of sub-prime mortgages. An ARM is a mortgage loan where the interest rate on the mortgage loan is linked to an index. The interest rate is adjusted if there is a change in the index.

An increase in the housing loans required banks to back the risk in lending by bringing in an additional capital. Instead of bringing in the additional capital, banks started selling these loans as collateralized debt obligations (CDOs). A CDO, essentially, is a repacking of mortgage loans into marketable securities. The housing loans are categorized into pools with different risks and return characteristics. These pools known as CDOs are rated by credit-rating agencies on the basis of their past repayment history and the value of the underlying mortgaged property. Sometimes, new attributes such as credit enhancement and credit insurance are added to the pool of housing loans to make them more marketable. Credit enhancer, who, usually, is the originator, credit insurer and who guarantees payment on bonds, share the risk with the investors. The CDOs are sold to investors such as mutual funds, insurance companies and hedge funds at a yield, lesser than the contracted yield, with the individual mortgages, thus yielding cash flows and profits. The yields vary with the grade assigned by the credit-rating agency and the risk appetite of the investors.

The increase in the sub-prime borrowing, coupled with low-interest rates, led to an increase in the home-ownership rates and the demand for housing. The overall US home-ownership rate increased from 63.8 per cent in 1994 to a peak of 69.2 per cent in 2004. This demand helped to fuel housing price increases and consumer spending. American home prices increased by 124 per cent between 1997 and 2006.

However, with the increase in the interest rates from June 2004 onwards, the sales of the existing and new homes started declining from 2006 onwards. This excess supply of houses led to a significant decline in the house prices, which, in turn, increased defaults and foreclosures. With lenders tightening the credit standards and credit-rating agencies downgrading many sub-prime MBSs, these securities turned illiquid due to lack of sufficient trading volume. However, the trigger for deterioration in the credit market was provided by the news that two of Bear Stearns hedge funds, that had sub-prime exposure, had suffered heavy losses and had even almost lost their capital. The uncertainty over the financial-system exposures spread to banks and hedge funds outside the United States and also spilled over into short-term money markets, causing steep increases in the overnight interest rates in major economies in August 2007. Bear Stearns, on the point of bankruptcy, was sold to JP Morgan Chase in March 2008. Adverse news from the United States' housing sector aggravated the concerns of further weakening of the US economy. The housing downturn was so steep that the two mortgage giants—Fannie Mae and Freddie Mac saw increasing delinquencies on their conventional portfolio and were exposed to investor flight from financial assets. They could not meet their obligations and were taken over by the US government on September 7, 2008. The American International Group (AIG), once the world's biggest insurer, had to be bailed out by the US government in September 2008. AIG ran into a crash crunch, and rating declines required it to post large amount of collateral to counter-parties of credit-default swaps by a financial product unit. Hence, the US government had to pump cash into AIG to avoid a threat to the trading partners from a collapse. On November 10, 2008, the US Treasuries purchased $40 billion AIG shares. On September 13, 2008, Lehman Brothers, the oldest investment bank of the United States, filed for bankruptcy. Merill Lynch, a mortgage company, reported a loss of US$71 billion, and was merged with Bank of America. Several investment banks were allowed to convert to bank-holding companies and access the repo window. Another country which was hard hit by this crisis was the United Kingdom. The Royal Bank of Scotland reported the largest-ever British corporate loss in 2008. The UK government also bailed out its financial institutions through a variety of means.

According to the IMF's staff estimates, potential losses to banks from exposure to the US sub-prime mortgage market and from related structured securities, as well as losses on other US credit classes such as consumer and corporate loans, could be of the order of US$440 to US$510 billion out of the total potential losses of US$945 billion. The sub-prime crisis developed into the largest financial shock since the Great Depression, inflicting a heavy damage on markets and institutions, at the core of the financial system. Global financial markets lost $50 trillion assets in 2008.

The Indian housing-finance sector remained insulated from the sub-prime crisis, owing to various factors, such as:

- First, the housing-finance products in India are plain-vanilla home loans as against complex home-loan products marketed in the United States. The actual equity component in housing is much higher than in the West.
- Secondly, the financial institutions have a limited exposure to highly leveraged structured products.
- Thirdly, pre-emptive and timely measures were taken by the regulators, such as increasing risk weights and provisioning requirements to prevent the formation of property and asset bubbles.
- Further, Indians are disinclined towards debt and, therefore, prefer to repay their loans as soon as they can.

REVERSE-MORTGAGE LOAN (RML)

The proportion of senior citizens to total population is increasing not only in India but world over. While on the one hand, there is a significant increase in longevity, on the other hand, the cost of good health-care facilities is spiralling, and there is little social security. Senior citizens need a regular cash-flow stream for supplementing pension/other income and meeting their social and financial needs. There has been an increase in the residential-house prices in the past few years, which have created considerable 'home-equity wealth.' For most senior citizens, the house is the largest component of their wealth.

- RML enables senior citizens (over 60 years) to mortgage their home with a HFI and convert home equity into tax-free income without having to sell the house.

Reverse mortgage seeks to monetize the house as an asset and, specifically, the owner's equity in the house. It is a mortgage loan for senior citizens (over 60 years), who generally are not eligible for any form of mortgage loan. The loan is given on single or on joint basis with the spouse, even if one of the spouses is below 60 years. Reverse mortgage is a loan that allows senior citizens to convert home equity into cash, without leaving their homes and without making monthly-mortgage payments.

- The borrower mortgages the house property to a lender, who then makes periodic payments to the borrower during the latter's lifetime, that is, the payment stream is reversed as compared to the conventional mortgage.
- The borrower is not required to service the loan during his lifetime, that is, he does not make a payment of instalment or interest so long, till he is alive and in occupation of the property.
- The loan will be repaid on the death of the borrower and the spouse (usually, a co-obligant) or on permanent movement through sale of property.

- After adjusting the principal amount of the loan and the accumulated interest, the surplus will go to the estate of the deceased. The borrower(s)/heir(s) can also repay or prepay the loan, with accumulated interest, and have the mortgage released without resorting to sale of the property.
- The loan can be prepaid together with accumulated interest at any point in time without any prepayment charges. The maximum period of loan will be 15 years. In cases where the borrower lives longer than 15 years, the payments will not be made by the lender. Borrower will be responsible for paying property tax, house-insurance premium and so on.

Benefits of RML

- It enables senior/elderly citizens owning a house but having inadequate income to meet their needs such as renovation/repairs/hospitalization, etc.
- Borrower owns and occupies the house till demise or changes residence. Even after demise, the spouse can continue to stay until demise.
- The monthly receipts will not be taxed in the hands of the senior citizens. Reverse-mortgage payments will be considered as a loan and not as an income for tax calculations, as there is no transfer of capital asset. It will not attract capital-gain tax also. But the interest income in the books of the banks will be taxed on accrual basis.
- It unlocks the liquidity potential of an immovable asset.

NHB issued **operational guidelines** for this new product on May 31, 2007, which are given as follows:

1. RMLs are to be extended by PLIs, namely, scheduled banks and HFCs that are registered with NHB. The PLIs reserve their discretion to offer RMLs. Prospective borrowers are advised to consult PLIs regarding the detailed terms of RML, as may be applicable to them.

2. Eligible Borrowers

- Should be a senior citizen of India above 60 years of age.
- Married couples will be eligible as joint borrowers for financial assistance. In such a case, the age criteria for the couple would be at the discretion of the PLI, subject to at least one of them being above 60 years of age. PLIs may put in place suitable safeguards keeping into view the inherent longevity risk.
- Should be the owner of a self-acquired, self-occupied residential property (house or flat) located in India, with a clear title indicating the prospective borrower's ownership of the property.
- The residential property should be free from any encumbrances.
- The residual life of the property should be at least 20 years.
- The prospective borrowers should use that residential property as a permanent primary residence. For the purpose of determining that the residential property is the permanent primary residence of the borrower, the PLIs may rely on a documentary evidence, other sources supplemented by physical inspections.

3. Determination of an Eligible Amount of Loan

- The amount of loan will depend on the market value of the residential property, as assessed by the PLI, age of borrower(s) and the prevalent interest rate.
- The table given hereunder may serve as an indicative guide for determining the loan eligibility:

Age	*Loan as Proportion of Assessed Value of Property*
60–65	40%
66–70	50%
71–75	55%
Above 75	60%

- The above table is indicative, and the PLIs will have the discretion to determine the eligible quantum of loan reckoning the 'no negative-equity guarantee' being provided by the PLI. The methodology adopted for determining the quantum of loan, including the detailed tables of calculations, the rate of interest and assumptions (if any), shall be clearly disclosed to the borrower.
- The PLI may consider ensuring that the equity of the borrower in the residential property (equity–value ratio [EVR]) does not at any time, during the tenor of the loan, fall below 10 per cent.

- The PLIs will need to re-value the property mortgaged to them at intervals that may be fixed by the PLI, depending upon the location of the property, its physical state and so on. Such revaluation may be done **at least once every 5 years**, the quantum of loan may undergo revisions based on such re-valuation of property, at the discretion of the lender.

4. Nature of Payment Any or a combination of the following:

- Periodic payments (monthly, quarterly, half-yearly, annual) to be decided mutually between the PLI and the borrower upfront.
- Lump-sum payments in one or more tranches.
- Committed line of credit, with an availability period agreed upon mutually, to be drawn down by the borrower.

Lump-sum payments may be made conditional and limited to special requirements such as medical exigencies, home improvement, maintenance, upgradation, renovation, extension of residential property and so on. The PLIs may be selective in considering the lump-sum payment option and may frame their internal-policy guidelines, particularly, the eligibility and end-use criteria. However, these conditions shall be fully disclosed to potential borrowers upfront.

It is important that the nature of payments be decided in advance as part of the RML covenants. PLI, at their discretion, may consider providing for options to the borrower, to change.

The stream of income received by the senior citizen under RML would not be income as they are in the nature of capital receipt.

5. Eligible End-use of Funds The loan amount can be used for the following purposes:

- Upgradation, renovation and extension of residential property.
- For uses associated with home improvement and maintenance/insurance of residential property.
- Medical and emergency expenditure for the maintenance of family.
- For supplementing pension/other income.
- Repayment of an existing loan taken for the residential property to be mortgaged.
- Meeting any other genuine need.

Use of RML for speculative, trading and business purposes shall not be permitted

6. Period of Loan Maximum 15 years.

7. Interest Rate The interest rate (including the periodic rest) to be charged on the RML, to be extended to the borrower(s), may be fixed by PLI in the usual manner based on risk perception, the loan-pricing policy and so on, and specified to the prospective borrowers. Fixed- and floating-rate of interest may be offered by the PLIs, subject to disclosure of the terms and conditions in a transparent manner, upfront to the borrower.

8. Security

- The RML shall be secured by way of mortgage of residential property, in a suitable form, in favour of PLI.
- Commercial property will not be eligible for RML.

9. Foreclosure

- The loan shall be liable for foreclosure due to occurrence of the following events of default:
  - If the borrower has not stayed in the property for a continuous period of 1 year.
  - If the borrower(s) fail(s) to pay the property taxes or maintain and repair the residential property or fail(s) to keep the home insured, the PLI reserves the right to insist on the repayment of loan, by bringing the residential property to sale and utilizing the sale proceeds to meet the outstanding balance of principal and interest.
  - If the borrower(s) declare himself/herself/themselves bankrupt.
  - If the residential property, so mortgaged to the PLI, is donated or abandoned by the borrower(s).

- If the borrower(s) effect changes in the residential property that affect the security of the loan for the lender. For example: renting out a part or all of the house; adding a new owner to the house's title; changing the house's zoning classification; or creating further encumbrance on the property, either by taking out a new debt against the residential property or alienating the interest by way of a gift or will.
- Due to perpetration of fraud or misrepresentation by the borrower(s).
- If the government under statutory provisions, seeks to acquiring the residential property for public use.
- If the government condemns the residential property (e.g., for health or safety reasons).

NHB has asked insurance companies to bring in an annuity-based product which could be combined with the reverse-mortgage scheme of banks, so that the senior citizen continues to receive monthly payments, even after the tenure of the scheme is over. For example, suppose a senior citizen buys reverse mortgage when he is 60 years old. The bank agrees to pay him a fixed monthly sum for, say, 20 years. If the man dies after 15 years, the bank sells the house and collects its dues out of the proceeds and pays any surplus to the heir. But if the man lives on, the monthly payments stop when he is 80, but what will the 80-year-old man do if his monthly income stops? It is here that NHB wants insurance companies to step in. The insurance company could be paid a premium by the bank for an annuity fund.

The reverse-mortgage product, meant exclusively for senior citizens, is new in India. Banks began offering it about a year ago, but so far only about 1,100 senior citizens have availed themselves of the scheme.

NHB is planning to tie up life insurance with reverse mortgage for developing a Reverse-mortgage Life-time Annuity Product. This product enables the senior citizens to receive a monthly annuity for life, unlike the reverse mortgage which is available for 20 years only.

The Indian Housing Sector is one of the highest contributors to its carbon emissions accounting for 22 percent of India's total annual carbon emissions. Buildings account for up to 40 percent of the total energy consumption in India, of which over 60 percent is from residential real estate. The NHB started a first of its kind promotional program for Energy Efficient New Residential Housing, with KfW Development Bank of Germany. The scheme aims at popularizing the use of solar water heating and solar lighting equipments in homes by offering suitable incentives in the form of Capital subsidies for the purchase and installation of the solar equipment. The NHB has been designated as a nodal agency for administering and monitoring this scheme.

The NHB is also promoting the concept of Green Housing where environmentally responsible and resource–efficient buildings are becoming an integral part and future of the construction industry. The Housing Finance System is becoming a part of the overall financial system with linkages with household savings, capital markets, Foreign Direct Investment, affordable and Green Housing.

MORTGAGE GUARANTEE SYSTEM

In housing finance, the prime risk involved in lending activity is the 'credit risk', i.e., the risk of loss due to a borrower's failure to repay the loan. The risk assessment depends on many factors such as creditworthiness of the borrower, purpose of loan, repayment term, security available to fall upon in case of default, etc. Since home loan is advanced against non-income generating asset (house property) and has a long time span extending up to 30 years for repayment, the credit risk perceived is much higher compared to other loans.

Moreover, lenders find it safe to lend to service-class applicants as documentary evidences are available to establish the income by way of salary particulars and income tax returns. The majority of citizens from informal employment sectors, the self-employed, businessmen and agriculturists are kept away from the housing finance system, as they are unable to produce proper income documents, their banking transactions are poor and they do nothave credit history which can be verified in CIBIL reports.

Hence, home loan lenders need insurance in the form of credit guarantee system to mitigate the risk of lending and widen the home loan market by lending to people who are excluded from the housing finance arena. Once credit risk is removed, the cost of lending comes down and regulatory authorities may also reduce provisioning for standard assets, which reduces the lending costs. Thus, home loan volumes grow faster. Even though there is cost added for the mortgage guarantee facility, the home loans may become cheaper.

The mortgage guarantee system was introduced in the U.S. after the 'Great Depression' of the 1930s.

In India, The NHB (National Housing Bank), the regulator for HFCs, has set up a Mortgage Guarantee Company (MGC) 'India Mortgage Guarantee Company' (IMGC) which primarily transacts the business of providing mortgage guarantee, under specific guidelines issued by the Reserve Bank of India. It has an initial capital of ₹120 crores with 38 per cent stake by the NHB, while U.S.-based Genworth Financial is the technical partner with 36 per cent stake. The Asian Development Bank (ADB) and International Finance Corporation (IFC) each have 13 per cent stake in the company. IMGC has come into being with a vision to make early home ownership a real possibility through the provision of Mortgage Guarantee. Itprovides credit guarantees to HFCs and commercial banks on behalf of home loan borrowers.

Banks and HFCs have to pay the company a small amount towards premium (fee) for buying mortgage guarantee for the home loans advanced. The banks/HFCs may share the guarantee fee with borrowers or may pass on such fee to borrowers, just like mortgage insurance and property insurance premiums. The premium depends on factors such as loan amount, tenure, borrower's profile, income of borrowers, credit history, and securities available.

The premium amount collected from thousands of loans by the company would be pooled and a corpus fund maintained. When a loan goes bad, the bank/HFC will invoke the mortgage guarantee and the IMGC will make good the outstanding debt to the bank/HFC from the corpus fund.

With the IMGC functioning, it will usher a new era in developing a sound mortgage finance system in the country. If home finance reaches the majority, the construction sector, aptly referred to as the 'driver of economy,' will get a big boost.

ICICI Bank Ltd, India's largest private sector bank in mortgages (constituting 43% of the bank's loan book) has launched first-of-its-kind mortgage guarantee scheme in India in association with India Mortgage Guarantee Company. This scheme allows the bank to offer home loans up to a 30-year tenure to persons up to the age of 67 years. Under the scheme, new home loan borrowers have to pay 1–2% of the total amount as a one-time premium for the mortgage guarantee which guarantees the bank against an initial default by the borrower and allows it to offer an extended tenure on the loan. The mortgage guarantee allows the bank to offer loans up to ₹75 lakh for middle-aged people who would otherwise not qualify for home loans because their loan tenure exceeds the 60-year age cut off for such loans.

India's mortgage as a percentage of GDP is just 8 percent compared to 24 percent in China and 34 percent in Singapore and the current shortage of homes is 1.8 crores units.

Although mortgage companies have helped in developing mortgages in the US, they have also led to the 'sub-prime' crisis in 2008, which not only put the U.S. economy in shambles, but shook the entire world economy. Hence, for the mortgage guarantee system to be successful, we need in-built stringent checks and balances.

HOUSING-FINANCE INDUSTRY: ISSUES AND FUTURE OUTLOOK

The Indian Housing Finance industry has rapidly evolved over the past three decades. Housing finance has successfully transited from highly regulated industry to an efficient market oriented industry. Housing Finance has rapid growth on account of factors such as increased urbanization, favorable demographics, rising disposable incomes for a section of the population along with Government tax incentives and subsidies, large supply of better quality houses and lower interest rates.

Banks and housing finance companies (HFCs) have complemented each other by promoting competition and providing consumers with an array of products and ease to access of housing finance.

Housing loans, as a percentage of the GDP, increased from 6 per cent in 2005–06 to 8.5 per cent in 2015–16. The growth in the housing-loan industry has slowed down from 25 per cent in 2006–07 to 21 percent in 2016-17, as property prices and interest rates have moved up while increase in the income levels have failed to match the property-price increase. Banks have gone slow on home loans as the demand for corporate loans has more than doubled in the past few years. Mortgage penetration is an abysmally low 8.5 per cent of GDP, which indicates that there is a huge potentiality of growth of this sector.

There are some key issues which need the attention of the regulator. They are:

1. There are varying standards and practices among the HFIs, be it in origination and documentation or monitoring and supervision which impose systemic risks that can be a potential threat to the sector. Thus, there is a felt need for standardization and uniformity in practices, in order to improve transparency in the market and bring a greater efficiency. This will require improvements in every aspect of housing—regulations, technology, products and investments.
2. High stamp duties on transfer of property, highly distorted land policies (the basic ingredient for good housing) and high taxes on building materials inhibit the growth of housing. There is a need to rationalize these duties and taxes. The central government and some states such as Karnataka, Gujarat and Punjab abolished the Urban Land Ceiling & Regulation Act (ULCRA). Repealing ULCRA in all states will help the real-estate business to grow.
3. There is a lot of migration from rural areas to cities. According to a recent UN report, 900 million people in India will be living in urban areas in another four decades—a three-fold increase from

the present 300 million urban dwellers. Cities are collapsing with little or no infrastructure, which, in turn, is a result of absence of urban planning. Infrastructure and housing capacities need to be expanded, especially. According to a World Bank estimate, India needs to invest an additional 3–4 per cent of its GDP on infrastructure to sustain its current levels of growth and to spread the benefits of growth more widely.

4. HFIs prefer to finance the salaried class as they have a steady flow of income. It is difficult for the self-employed and those at the bottom of the pyramid to get housing loans, as it is hard to estimate their income. This needs to be corrected by ensuring that all individuals have an access to housing and housing finance.
5. The major challenge for the affordable housing sector is the lack of long term finance. Government tax incentives and subsidies alone are not enough. To overcome this more private investment in the form of Pension Funds, Real Estate Investment Trust, Foreign Direct Investments are needed to provide a thrust to the affordable Housing Sector.

There is acute housing shortage in the country, and to increase home ownership in India should be the mission of the government and the HFIs.

Housing loans constitute fifty percent of the retail loan portfolio of banks as the demand for corporate loans has dried up. Affordable housing is the growth driver of home loans. Providing affordable housing and housing finance solutions should be major policy concerns.

KEY TERMS

HFIs	RMBS	Sub-prime Mortgage
Housing Finance	RML	

SUMMARY

1. Housing finance is a business of financial intermediation, wherein the money raised through various sources such as public deposits (which are subject to the regulatory stipulations of NHB), institutional borrowings (from banks), refinance from NHB and their own capital, is lent to borrowers for purchasing a house.
2. Housing is an industry with tremendous potential for contributing towards the economic growth of any country.
3. The accessibility of housing finance for people, in general, has evolved, developed and improved over the years.
4. Housing is regarded as a critical sector in terms of initiatives and interventions. This is reflected in the efforts of the government to improve housing and habitat conditions by way of financial allocations in the five-year plan and fiscal measures related to housing announced in the Union Budgets.
5. There are different types of institutions which cater to the need for a long-term finance, for housing in urban and rural areas. They are: SCBs, RRBs, ARDBs, HFCs, NCHF and ACHFS.
6. Home-equity loans, Home-extension loans, Home-improvement loans, Home-purchase loans, Land-purchase loans and Home loans to SHGs/MFIs are the different types of housing loans available in the market.
7. HFCs have to manage various risks associated with the mortgage business. These risks include credit risk, liquidity risk, foreign-exchange risk and interest-rate risk.
8. With a growing number of players and increased competition, the housing sector has become increasingly market-driven.
9. NHB is the apex-level financial institution for the housing sector. The NHB is a wholly-owned subsidiary of the RBI and the regulator of non-banking HFCs. The role of NHB is to promote and develop HFIs, regulate and supervise HFCs, refinance HFCs, undertake project-lending and develop a secondary mortgage market. NHB has launched a residential-property index, NHB Residex, for five cities—Bengaluru, Delhi, Bhopal, Kolkata and Mumbai. It is the first housing-price index in India to fill the price-information gap and streamline the property-development process in major cities. NHB launched the pilot issues of MBSs in August 2000.
10. RMBS offers a viable and sustainable, market-oriented, fund-raising mechanism, with the potential of integrating housing market, with the domestic as well as international capital markets.
11. Reverse mortgage seeks to monetize the house as an asset and, specifically, the owner's equity in the house. It is a mortgage loan for senior citizens (over 60 years), who, generally, are not eligible for any form of mortgage loan.
12. The housing-finance industry recorded a CAGR of 38 per cent, over the last 6 years (2000–01 to 2007–08), due to a decline in the interest rates, high loan to value ratio and rising income levels. Housing loans as a percentage of the GDP increased from 6 per cent in 2005–06 to 8.5 per cent in 2007–08. Growth in the housing-loan industry has slowed down from 25 per cent in 2006–07 to 12 per cent in 2007–08, as property price and interest rates have moved up while increase in the income levels has failed to match the property-price increase.

MINI CASE

You have just graduated with an MBA degree, and have been offered a job in Mumbai, with a well-known company as an associate in the project-finance division. You are very enthused and excited about this job opportunity. You have already moved to Mumbai and checked out a few flats and have decided to purchase a flat for ₹12 lakhs. You have only ₹2 lakhs in cash and you intend to finance the rest of ₹10 lakhs, by taking a mortgage loan against the house for the same amount. The mortgage manager has offered you multiple options as follows:

Option A—Traditional fixed-rate loan: A 30-year loan of ₹10 lakhs at a fixed 10 per cent annual interest with monthly payments. The house, which is priced at ₹12 lakhs, is mortgaged against the loan.

Option B—Bi-weekly, Traditional fixed-rate loan: A 30-year mortgage loan at 11 per cent annual interest but with payments every two weeks.

Option C—A 7-year Balloon loan at 8 per cent annual interest. The loan payments are calculated as if the loan was a traditional 30-year, fixed-rate, mortgage loan, at 8 per cent annual interest. However, the loan is only for 7 years, but the payments are made as if the loan was for 30 years. At the end of 7 years, the remaining principal is due.

Option D—Interest-only, 7-year loan at 8 per cent annual interest. This loan is similar to the 7-year Balloon loan, except that you pay only the interest and not the principal with every payment.

Option E—A 30-year loan with a 7-year ARM Loan: For the first 7 years, the rate stays fixed at 8.5 per cent and then becomes floating. The float = Prime index (floating) + 2 per cent Premium.

QUESTIONS FOR DISCUSSION

1. Which option has the lowest monthly payment? Why?
2. Since this is your first house purchase and as this is a small flat too, you do not expect to stay in the flat for more than 7 years. In such a case, which mortgage loans are better for you?
3. In continuation of Q1, supposing you are a savvy stock-market investor, then which loan is now better for you?
4. Suppose that this is a very big flat in a very nice neighbourhood, and, thus, you intend to stay in the flat for more than 10 years. Which loan options are good for you?
5. In continuation of Q4, suppose that your company pays your salary every 2 weeks, then which loan option is better for you? Why?
6. Why do you think the interest rate in options C, D, and E are lower than in A and B? Why do you think the interest rate in option E is lower than in the options A and B? Why do you think the interest rate in option B is higher than in option A?

REVIEW QUESTIONS

1. What is housing finance? State the role of housing finance in the economy.
2. State the policy initiatives and measures to develop housing sector in India.
3. Which are the institutions which cater to the need of housing finance in India? Also, state the different kinds of loans given by them.
4. How is the loan amount and interest rate determined?
5. ‘With growing number of players and increased competition, the housing sector has become increasingly market-driven.’ Discuss.
6. Discuss the role of NHB in housing finance.
7. What is an RMBS? Describe the process of mortgage securitization and state the benefits of mortgage securitization.
8. What is an RML? State the benefits and operational guidelines of RMLs.
9. Which factors inhibit the growth of housing-finance industry in India?
10. Which factors were responsible for the sub-prime mortgage crisis and what was the impact of this crisis?

REFERENCES

1. Mishra, J. (2007), ‘Creating Utility for Realty Investors,’ *The Economic Times,* December 3, 2007, p. 6.
2. Tiwari, D. and A. Dhall (2007), ‘In Whose Interest?,’ *The Economic Times,* December 2, 2007, p. 11.
3. DiMartino, D. and John V. Duca (2007), ‘The Rise and Fall of Subprime Mortgages,’ *Economic Letter,* 2(11), November 2007.
4. Bhat, U. R. (2007), ‘Subprime Debacle in the US,’ *The Economic Times,* August 13, 2007, p. 8.
5. RBI, *Macro economic and Monetary Developments, 2007–08*
6. HDFC, *Annual Reports*.
7. NHB, *Annual Reports*.
8. NHB, *Report on Trend and Progress of Housing in India*.
9. Dutta, B. (2009), ‘Restoring Stability in Financial Sector,’ *The Economic Times,* March 21, 2009, p. 8.
10. Chaudhuri, S. (2009), ‘Remembering Lehman’s Collapse,’ *The Economic Times,* September 2009, p. 8.
11. http://en.wikipedia.org/wiki/Subprime_mortgage_crisis
12. http://www.un-documents.net/ha-1.htm
13. Housing Finance Companies—Performance Study for Nine months Ended December 2009, http://www.careratings.com/current/3/7058