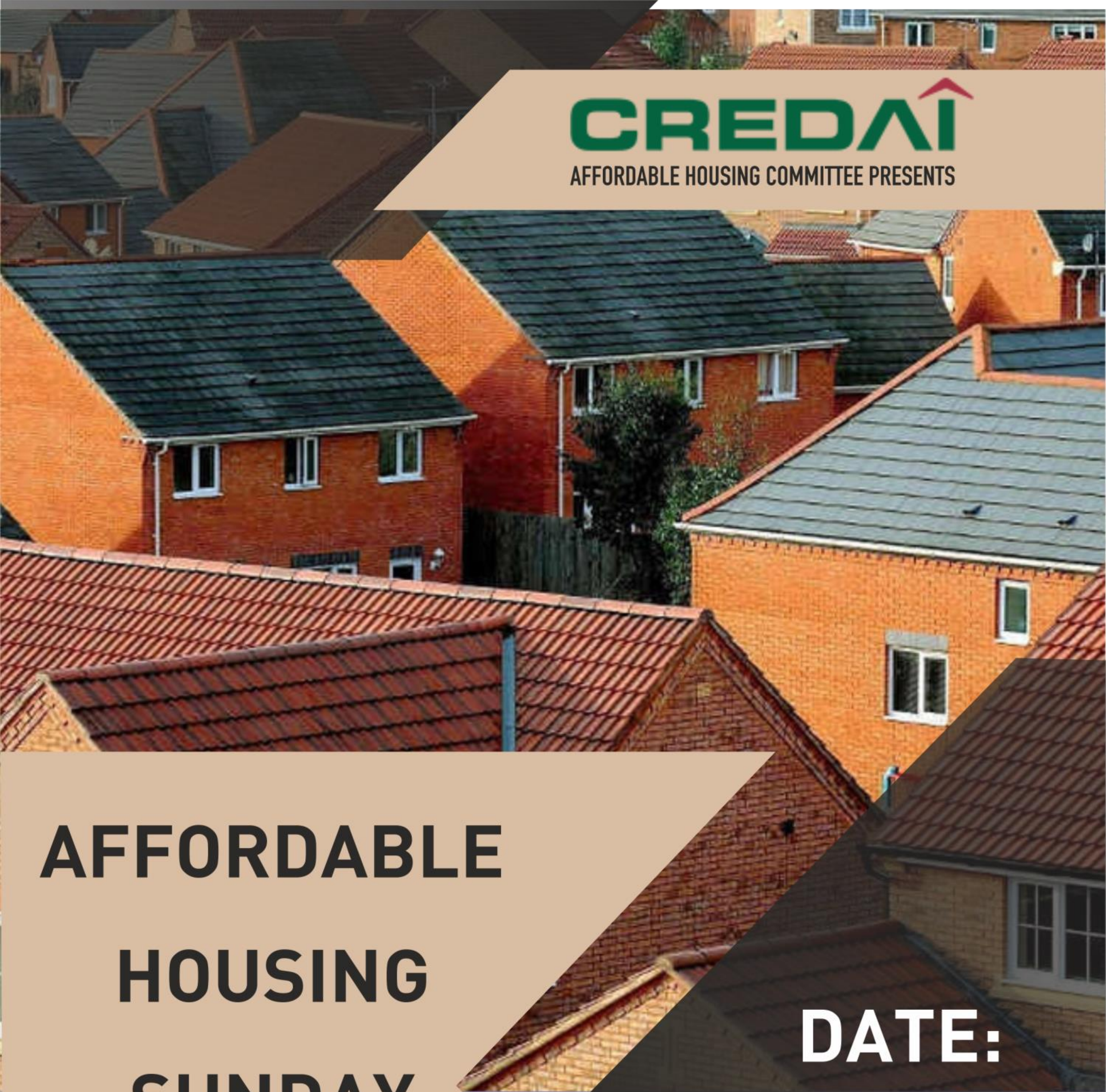

CREDAI

AFFORDABLE HOUSING COMMITTEE PRESENTS

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Housing Finance Scenario in Affordable Housing Segment-Formal Sector Loans/Informal Sector Loans

Introduction:-

The demand for housing is ever-increasing with the growing population and urbanisation and access to housing finance needs to keep pace with it. Housing finance holds a strong promise, both for traditional as well as affordable housing finance. As for banks, housing finance is a very important component of retail lending books of banks. As a major incentive for banks in affordable housing finance, the RBI allowed banks to issue infrastructure bonds, with substantial regulatory advantages. While the housing finance market in India is served by both banks and HFCs, but the percentage market share of HFCs is consistently growing. What is quite an interesting change over time is that the average rates of interest charged by banks, and by leading HFCs, have almost converged, leading to a conclusion that HFCs have attained a cost of capital comparable to banks.

In terms of housing finance, majority of the loans disbursed have naturally been to the high/mid-income groups due to easier availability of proofs for credit assessment. Conversely, the ability to raise finance has been tough for the mid/low-income and informal population till recent past. Affordable housing finance is a focus area of the Government now, given its objective of financial inclusion and thus access to housing loans for informal class has gained momentum.

HOME LOAN OPTIONS FOR BUYERS IN AFFORDABLE HOUSING

FORMAL SECTOR LOANS	INFORMAL SECTOR LOANS
Formal Sector Loan is the general and regular way of opting the loan, where based on your income proof, banks offer you loan.	Informal Sector loans are for those customers that do not have all the documents (without income proof documents).
Provided by SBI,HDFC and other such PSUs / Government banks	**Provided by** MHFC, HFFC, DHFL, Muthoot and other such HFCs
Average interest rates 8.35-11.5% depending on client profile	**Average interest rates** 9.90-14%
Documents needed Salary slip, PF, Form16, ITR, Normal KYC, latest 6 months bank statement etc.	**Documents needed** Bank statement, Normal KYC, rent agreement, physical visit (from finance company to the place where the client is working for verification of his income).

CASE STUDY:- FORMAL LOAN + CLSS BENEFIT TO BUYER

AFFORDABLE HOUSING: Benefits to the buyer under PMAY			
LOAN AMOUNT: **Rs 15 lakhs**			
Annual Income (INR)			**5 lakhs**
Category			EWS/LIG **(Annual Income: 0 to 6 lpa)**
Loan Tenor (Years)			15
Subsidy Amount (PMAY) - based on Loan amount and tenor			220187
EMI (Loan to Value <= 80%)	**Interest Rate (8.40%)**	EMI based on Loan Amount	14683
		Actual EMI after Subsidy credit	12528
		Yearly Benefit under PMAY	**25860**

CASE STUDY:- INFORMAL LOAN + CLSS BENEFIT TO BUYER

AFFORDABLE HOUSING: Benefits to the customer under PMAY				
Annual Income (INR)		1.2 Lac	2.4 Lac	3.6 Lac
Loan Tenor (Years)		20	20	20
Loan Amount		4,00,000	9,00,000	13,00,000
ROI - 9.9%	EMI based on Loan Amount	3,436	7,731	11,167
Post CLSS Subsidy customer can reduce EMI / Tenor of the Loan				
Informal Loans finance are available for following customer profile i.e. Housemaid, Vegetable Vendor, Rickshaw / Taxi Driver, Security Guard, Small Informal business Owner, Small Contractor etc				

OPERATIONAL CRITICALITIES IN HOUSING LOAN PROCESS

1) **Field-based credit assessment:** This is one of the critical elements of the entire enterprise. While risk assessment for salaried clients is amore straightforward process, the process is slightly complicated for those in the self employed and informal categories. For salaried borrowers, it is typically a 5-7 day process involving collection of income/tax proofs, CIBIL credit check, analysis of source of equity/banking behaviour, preparation of CAM up to appraisal and approval. However, self employed borrowers do not have consistent monthly income as their earnings are prone to business cycles and can vary month-on-month. Similarly, those in the informal sector may not have income/tax/banking documentation. These people are working in diverse work areas and the income generation capability of each work is different. Hence, credit assessment processes needs to be dynamic.

2) **Retaining quality credit appraisal staff and training fresh recruits**: Given the relatively complicated process of establishing the viability of lending to low-income or self-employed borrowers, the credit officer's role is extremely critical. The experienced ones with good strike rates (in terms of bringing in genuine borrowers who repaid in time) might claim a premium for their quality work, hence salary costs as a % to top line needs to be monitored. HFCs might need to benchmark/document the best-practices processes of experienced officers which can help training the newer, fresh recruits who will typically come at a lower price.

<u>**OPERATIONAL CRITICALITIES IN HOUSING LOAN PROCESS**</u>

3) Early-warning systems in collection process: After credit appraisal, collection and default monitoring are another key area in this segment from operations' perspective. In cases of borrowers in low-income/informal sector, the repayment frequency can be weekly or fortnightly, instead of monthly. Repayment frequency can be more than monthly also for cases where the income flows are such. MIS systems need to identify cases of slippages and alert the recovery team through early-warning systems. This can ensure better monitoring of the cash flows and faster turnaround for recovery initiation in case of default. During defaults, the credit officer who checked that client is typically involved in the follow-up process with that client by way of personal visits. In cases of genuine difficulty, the loan might be restructured by extending the tenure.

4) Project risk: HFCs need to house legal and technical officers to do checks on the property to ensure it is free of litigation, encumbrance etc. Smaller HFCs might often outsource this function to specialist providers. Not only does this help the HFCs to identify clean projects for the viability of its own business, but it also helps the potential home-buyers by giving them a comfort factor in terms of project's risks.

CHALLENGES

1) Demand for home finance might be impacted if there are more ‘pure investors’ purchasing homes rather than ‘genuine home-buyers’.

2) Credit risk assessment, retention of quality credit staff, early warning systems for default monitoring/follow-up are operational challenges.

3) Higher servicing costs due to more involved nature of credit appraisal can put opex pressures.

4) Ability to build scale ahead of competitors to ensure profitability in a high opex/lower margin environment.

5) Lower asset appreciation and less liquid markets in smaller towns/rural areas can lead to difficulty in sale during cases of recoveries.

6) Timely completion of projects without cost escalations is a key concern faced by borrowers and financiers alike.

7) Ability to build an enabling environment via faster approvals, support-infrastructure, easier FDI processes, low cost funds, tax incentives etc.

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