TSN 78190
PDABE 429

A.I.D. EVALUATION SUMMARY - PART I

1. BEFORE FILLING OUT THIS FORM, READ THE ATTACHED INSTRUCTIONS.
2. USE LETTER QUALITY TYPE, NOT "DOT MATRIX" TYPE.

IDENTIFICATION DATA

A. Reporting A.I.D. Unit:
Mission or AID/W Office USAID/INDIA
(ES#)

B. Was Evaluation Scheduled In Current FY Annual Evaluation Plan?
Yes [X] Slipped [ ] Ad Hoc [ ]
Evaluation Plan Submission Date: FY 90 Q 3

C. Evaluation Timing
Interim [ ] Final [X]
Ex Post [ ] Other [ ]

D. Activity or Activities Evaluated (List the following information for project(s) or program(s) evaluated; if not applicable, list title and date of the evaluation report.)

Project No.	Project /Program Title	First PROAG or Equivalent (FY)	Most Recent PACD (Mo/Yr)	Planned LOP Cost (000)	Amount Obligated to Date (000)
386-HG003	Housing Guarantee (HG003)	1990	09/93	$50,000	$50,000

ACTIONS

E. Action Decisions Approved By Mission or AID/W Office Director

Action(s) Required	Name of Officer Responsible for Action	Date Action to be Completed
No MRC meeting on evaluation report was held. However, in a debriefing with Mission the following decisions/actions were taken.		
1. Work with National Housing Bank to design and introduce MIS in HFCs and streamline staffing in NHB for more effective supervision of HFCs.	TDE	March 20, 1992
2. Address the issues of strengthening the resource base of NHB and HFCs and local training capability on housing finance in the supplementary project paper and during the design and implementation of the expanded program.	TDE	December 30, 1991

(Attach extra sheet if necessary)

APPROVALS

F. Date Of Mission Or AID/W Office Review Of Evaluation: (Month) June (Day) 21 (Year) 1991

G. Approvals of Evaluation Summary And Action Decisions:

	Project/Program Officer	Representative of Borrower/Grantee	Evaluation Officer	Mission or AID/W Office Director
Name (Typed)	Charles S. Billand		B.R. Patil	Walter G. Bollinger
Signature	[signature]		[signature]	[signature]
Date	21 April 92		4/14/92	5/7/92

ABSTRACT

H. Evaluation Abstract (Do not exceed the space provided)

1. Evaluation Purpose: This evaluation's purpose is to analyze the performance of the organizations which have participated in the USAID HG-003 loan program. Its focus is on the extent to which Housing Finance Companies (HFCs), have developed under the National Housing Bank's (NHB's) initiatives, the degree to which HFCs are lending to lower income families, and NHB's effectiveness in promoting the development of the housing finance system.

2. Evaluation Methodology: The evaluation relies on three years of financial data for nine HFCs which are participating in NHB's refinancing program; in-depth interviews at four of these HFCs; interviews with staff at the NHB and other financial institutions, and with USAID staff; and, a series of reports on housing finance in India.

3. Findings and Conclusions:

i) The project has broadly met the goals.

ii) The past three years have witnessed a very substantial expansion in the HFC network.

iii) The number of loans sanctioned by HFCs grew at a compound rate of 44 percent from 1988-1989 to 1990-1991. In the final year about 153,524 loans were sanctioned by these nine HFCs.

iv) Overall, the HFCs performed well in raising funds, leveraging equity, and reaching a minimum level of profitability. Credit risk on HFCs' individual loans appears to be low. The liquidity and capital risks of HFCs are low; however, interest rate risk could become a problem in the future. There is also a risk of some private HFCs becoming overly dependent on NHB's refinancing facility.

v) Below median income households account for one-quarter of all HFC borrowers.

vi) NHB's record with respect to the supervision of HFCs is weak overall. It has very large implicit outstanding commitments for providing refinance to HFCs.

vii) NHB has been very active in promoting the development of the housing finance system. Similarly, USAID, working with NHB, has executed a substantial complementary program of training, studies and technical assistance. It has moved in a surprisingly large number of areas to reduce constraints to the development of the housing finance system.

viii) Overall, management of the program by USAID and NHB appears to have been effective.

COSTS

I. Evaluation Costs

1. Evaluation Team

Name	Affiliation	Contract Number OR TDY Person Days	Contract Cost OR TDY Cost (U.S. $)	Source of Funds
Raymond Struyk	Urban Institute	PDC-1008-I-00-9067-00	$65,000	Project
Bruce Ferguson	- do -	- do -	$65,000	-do-
Marisol Raviez	- do -	- do -	$65,000	-do-

2. Mission/Office Professional Staff Person-Days (Estimate) ____________

3. Borrower/Grantee Professional Staff Person-Days (Estimate) ____________

A.I.D. EVALUATION SUMMARY - PART II

SUMMARY

J. Summary of Evaluation Findings, Conclusions and Recommendations (Try not to exceed the three (3) pages provided)
Address the following items:

- **Purpose of evaluation and methodology used**
- **Purpose of activity(ies) evaluated**
- **Findings and conclusions (relate to questions)**
- **Principal recommendations**
- **Lessons learned**

Mission or Office:	Date This Summary Prepared:	Title And Date Of Full Evaluation Report:
USAID/INDIA	March 1992	Market-oriented Housing Finance in India: The National Housing Bank's first two years ~~Interim Eval. of HG-003 Program (Sept. 1991)~~

1. Project Purpose: The long term goal of USAID's "Housing Finance System Program" is to assist the National Housing Bank (NHB) in increasing the availability of formal housing finance to lower income households nationwide. This goal is to be reached through the development of a financially sound, market-oriented housing finance system which makes long-term loans available to a wide range of households, particularly those with incomes below the median income level.

2. Evaluation Purpose: This evaluation's purpose is to analyze the performance of the organizations which have participated in the USAID HG-003 loan program. Broadly speaking, its focus is on the extent to which Housing Finance Companies (HFCs), have developed under the National Housing Bank's (NHB's) initiatives, the degree to which HFCs are lending to lower income families, and NHB's effectiveness in promoting the development of the housing finance system.

3. Evaluation Methodology: The evaluation relies on information from four sources: financial data on operations over the past three years for nine HFCs which are participating in NHB's refinancing program; in-depth interviews and additional data collection at four of these HFCs; interviews with staff at the NHB and other financial institutions, and with USAID staff; and, information contained in a series of reports on housing finance in India prepared over the past two years.

4. Findings: The team's overall conclusion is that the project has broadly met the goals set out for it in the logical Framework contained in the Project Paper. The main findings are summarized below.

i) Growth of the HFC Network. The past three years have witnessed a very substantial expansion in the HFC network. The total number of officially registered HFCs has grown explosively from approximately 30 in 1988 to 250 or more in 1991. Furthermore, 16 HFCs have been recognized to receive refinancing from NHB, and two others are in the process of attaining this status; such recognition indicates significant maturity on the part of each HFC. The 16 recognized HFCs increased their number of offices from 51 in 1988-89 to 136 in 1990-91.

ii) Performance of HFCs over the Period. Based on data for nine of the largest HFCs, the number of loans sanctioned by HFCs grew at a compound annual rate of 44 percent from 1988-89 to 1990-91, excluding HDFC, this figure is 113 percent. In the final year these nine HFCs sanctioned about 153,524 loans.

Other key findings include:

-- Overall, the HFCs performed well in raising funds, leveraging equity, and reaching, on average, a minimum level of profitability. But rapid increases in their costs of funds are constricting their access to resources they can afford.

-- Credit risk on HFCs individual loans appears to be low and repayment rates are very good. HFCs' liquidity and capital risks are low. However, interest rate risk could become a problem if the cost of funds continues to rise and HFCs refrain from exercising their option to raise rates on outstanding loans.

-- There is risk of some private HFCs becoming highly independent on NHB for their loanable funds because these firms have difficulty raising deposits and term loans.

iii) Lending to Households Below Median Income. The information available indicates that below median income households account for one-quarter of all HFC borrowers. This represents a modest increase in share over the past two years; given the explosive growth in total lending by the HFCs, this is a substantial achievement. This growth is largely market driven, but NHB has played a role in encouraging firms to direct their resources to this market segment. All HFCs say there is no discrimination against female headed households. However, data available to the team on lending to women and households headed by an elderly person are too limited to permit estimates of lending volume.

iv) Future Demand for Refinancing of Loans to HG-Eligible Households. Under conservative assumptions, substantially more than $25 million in eligible loans will be presented each year to NHB for refinancing.

v) Supervision, NHB Funds Mobilization, and Developing the System. NHB's record with respect to the supervision of HFCs is weak overall. It is particularly poor for those HFCs which are registered but are not recognized as being able to obtain refinance from NHB, and even for the recognized companies much improvement is needed. NHB recognizes these weaknesses and some action may be taken soon. On the other hand, NHB has been more aware of the limitations in its regulatory authority and has taken steps to provide it with most of the powers which outside observers believe it needs.

NHB has very large implicit outstanding commitments for providing refinance to the HFCs. NHB is aware that its commitments likely exceed the volume of resources it will be able to obtain from low cost funds allocated by government bodies. It has, therefore, begun exploring options for obtaining capital from the market.

Over the past two years, NHB has been very active in promoting the development of the housing finance system. Similarly, USAID, working with NHB, has executed a substantial complementary program of training, studies, and technical assistance, over the period.

vi) Addressing constraints to sector development. In the comparatively brief period of two years the NHB has moved with some effect in a surprisingly large number of areas to reduce the constraints to the development of the housing finance system. Of course, much remains to be done.

vii) Program management. Overall management of the program by USAID and NHB appears to have been effective. NHB succeeded in meeting all of the Conditions Precedent in the loan agreement although USAID staff might have been more diligent in pursuing some of the areas stated in the MPIP.

The presence of the Conditions Precedent clearly caused NHB to devote more energy to technical assistance, training and regulatory issues than it would have otherwise. Funds disbursement has proceeded in a timely manner.

viii) The USAID Role. The team's overall assessment is that USAID's involvement has been highly constructive in this stage of the development of the Indian housing finance system. Both capital and technical assistance have been productive.

5. Recommendations: The team's priority recommendations are as follows:

i) Supervision and Regulation. That NHB give its high priority to strengthening this system. An adequate number of staff, well-trained and dedicated full time to supervision under a managing director charged solely with this responsibility is essential.

ii) Promotion. That the next logical step in enhancing the development and competition of the sector will involve giving the HFCs some latitude in setting the interest rates on their loans.

iii) Lending to Low Income Households. That the necessary data be assembled to determine with precision the share of funds going to low-income households. Furthermore, that if at any time NHB decides to limit the volume of refinancing any one HFC can take for any reason, that loans to low income households be exempted from the limit.

iv) Funds Mobilization by NHB. That NHB prepare careful estimates of its probably future (multi-year) refinancing obligations. Also, the team recommends that in future loans from USAID to NHB due attention be given to NHB's success in mobilizing an increasing percentage of its total resources from the more open financial markets.

v) meeting All the Conditions in the MPIP. That future disbursements should depend on meeting all terms stipulated in the MPIP.

6. Lessons Learned: The primary lesson learned from this evaluation is that new institutions often concentrate on fulfilling some aspects of their mandate more than others. In NHB's case, management focused very successfully on industry promotion but paid insufficient attention to funds mobilization and supervision. An outside evaluation performed when a new organization is fully operational, but before practices have become deeply entrenched, can be very useful in helping to highlight areas to which management might wish to direct more attention in the future.

ATTACHMENTS

K. Attachments (List attachments submitted with this Evaluation Summary; always attach copy of full evaluation report, even if one was submitted earlier; attach studies, surveys, etc., from "on-going" evaluation, if relevant to the evaluation report.)

Copy of the report

COMMENTS

L. Comments By Mission, AID/W Office and Borrower/Grantee On Full Report

1. Findings and recommendations are useful for the supplementary project and also for program modifications in future.

2. Findings concur with those of AID and GOI staff concerned.

3. Major issues and questions posed in the scope of work are adequately addressed and answered.

THE URBAN INSTITUTE

MARKET-ORIENTED HOUSING FINANCE IN INDIA: THE NATIONAL HOUSING BANK'S FIRST TWO YEARS

Interim Evaluation of the HG-003 Program

INTERNATIONAL ACTIVITIES

1

MARKET-ORIENTED HOUSING FINANCE IN INDIA: THE NATIONAL HOUSING BANK'S FIRST TWO YEARS

Interim Evaluation of the HG-003 Program

Prepared by
Raymond Struyk, Bruce Ferguson, Marisol Ravicz
The Urban Institute

Prepared for
U.S. Agency for International Development
New Delhi, India

8'

ABSTRACT

The following document is an interim evaluation of the "Housing Finance System Program" (HG-003). This evaluation's purpose is to analyze the performance of the organizations which are participating in the HG-003 program. Its focus is on the extent to which Housing Finance Companies (HFCs) have developed under the National Housing Bank's (NHB's) initiatives, the degree to which HFCs are lending to lower income families, and NHB's effectiveness in promoting the development of the housing finance system.

The evaluation relies on three years of financial data for nine HFCs which are participating in NHB's refinancing program; in-depth interviews at four of these HFCs; interviews with staff at the NHB and other financial institutions, and with USAID staff; and, a series of reports on housing finance in India.

The evaluation's overall findings are: 1) India's housing finance industry is growing very rapidly, 2) A very significant portion of HFC borrowers are below-median income households 3) Most recognized HFCs are financially stable and profitable 4) The NHB has been very successful in its role of housing finance industry promotor but has not focused adequately on industry supervision and 5) The HG-003 program has made a significant contribution to the sound development of the housing finance industry.

9

TABLE OF CONTENTS

10

11

12

ACKNOWLEDGMENTS

This interim evaluation of the "Housing Finance Assistance Program" (HG-003) has benefitted from the help of many people. Among USAID staff, several persons deserve mention: Jeremy Hagger in Washington, Charles Billand and Nabaroon Bhattacharjee in New Delhi, and Michael Lee and Julie Otterbein at the regional office in Bangkok. Combined they prepared comprehensive terms of reference for the project, provided immense help in organizing the field work, and gave valuable information and commentary on the development of the housing finance sector in India.

The many persons with whom we met during the field work are listed in Annex 1.3; we are grateful to all of them for generously sharing their time with us. The team wishes to offer special thanks to the management of the National Housing Bank for their willing cooperation with the evaluation. We acknowledge particularly M. J. Pherwani, P. K. Parthasarathy, J. S. Varshneya, S. P. Ghosh, P. R. Singh, S. D. Hosangadi, P. K. Handa, and M. K. Rakshit.

Finally, we are especially grateful to the senior management at the four housing finance companies with whom we met for day-long intensive interviews. We appreciate in particular the openness and frankness with which these men responded to our inquiries. They are: M. D'Souza, CanFin Homes; Ashish Kumar Sen, SBI Home Finance; Rakesh Kumar Wadhawan, Dewan Housing Development Finance; and, Nitin Palany, Gujarat Rural Housing Finance Corporation.

13

CURRENCY NOTATION

1 lakh = 100,000

1 crore = 10 million

Rs. 21 = US$1

Thus, Rs. 21 crore = US $10 million

14

ABBREVIATIONS USED IN TEXT

Akshya	Akshya Awas Nirman Vitta Ltd.
CanFin	CanFin Homes Ltd.
CBDT	Central Board of Direct Taxes
CHF	Center for Housing Finance
Dewan	Dewan Housing Development Finance Ltd.
EWS	Economically Weaker Sector
FNMA	Federal National Mortgage Association
GIC	General Insurance Corporation of India
GOI	Government of India
GRUH	Gujarat Rural Housing Corporation
HDFC	Housing Development and Finance Corporation
HFC	Housing Finance Company
HG	Housing Guaranty Loan Program of USAID
HG-003	Third Segment of the HG Program
HLA	Home Loan Account Scheme of NHB
HSMI	Human Settlement Management Institute
HUDCO	Housing and Urban Development Corporation Ltd.
IHFD	India Housing Finance Development Ltd.
LIC	Life Insurance Corporation of India
LIG	Lower Income Group
MOUD	Ministry of Urban Development
NHB	National Housing Bank
RBI	Reserve Bank of India
RoC	Registry of Companies
SBI	SBI Home Finance Ltd.
Tapoban	Tapoban Housing Finance Ltd.
USAID	United States Agency for International Development
UTI	Unit Trust of India

15

EXECUTIVE SUMMARY

The long-term goal of USAID's "Housing Finance System Program" is to assist India's National Housing Bank (NHB) increase the availability of formal housing finance to lower income households nationwide. This goal is to be reached through development of a financially sound, market-oriented housing finance system to make long-term loans available to a wide range of households, particularly those with incomes below the median-income level.

The program seeks to develop a system of market-oriented housing finance companies (HFCs) by (1) providing critically needed lending capital to meet near- and mid-term needs of eligible HFCs serving a number of geographic areas, with the assistance provided through the refinancing by NHB of loans made by private and joint sector HFCs to households with incomes in the lower half of the income distribution; (2) fostering a relationship between recent entrants to the sector and the NHB, in order to improve the new firms' ability to mobilize resources, manage their portfolios, increase lending to low income households, and operate within the existing financial public policy environment; and, (3) addressing a number of sectoral constraints to expanding the system, through technical assistance and training.

The HG-003 project, authorized in September 1988, builds upon the highly successful prior loan-and-technical assistance projects to the Housing Development Finance Corporation, by far the largest private housing lender in India. Under HG-003, US $50 million in capital assistance is being provided to NHB, complemented with US $2.9 million for technical assistance and training. To date, US $25 million capital assistance has been disbursed and US $1.7 million technical assistance provided.

Evaluation Method

This report presents the findings of the interim evaluation of the program. Its focus is on the extent to which HFCs, especially private and joint sector HFCs, have developed under NHB's initiatives, the degree to which HFCs are lending to lower income families, and NHB's effectiveness in promoting development of the housing finance system.[1] The evaluation relies on information from four sources: financial data on operations over the past three years for the nine HFCs participating in NHB's refinancing program; in-depth interviews and additional data collection at four of these HFCs;[2] interviews with staff at the NHB and other financial institutions, including HDFC, and with USAID staff; and, information contained in a series of reports on housing finance in India prepared over the past two years. The evaluation team spent a week before going to India reviewing previous reports and analyzing data sent by NHB on the nine HFCs. The team then spent two and one-half weeks in India conducting interviews, visiting HFCs, analyzing the assembled data, and preparing this report.

[1] Under the definitions used in this program, a private HFC is one having less than 50 percent of its equity capital allocated to Indian central and/or state governments and/or entities that themselves are at least 80 percent owned by these governments. A joint sector HFC is one having at least 50 percent but less than 80 percent of its equity capital allocated to Indian central and/or state governments as described above.

[2] These are Can Fin Homes Ltd. (Bangalore), Gujarat Rural Housing Finance Corporation (Ahmedabad), Dewan Housing Development Finance Ltd. (Bombay), and SBI Home Finance Ltd. (Calcutta) - formerly HPFC.

17

Findings and Conclusions

As detailed below, the team's overall conclusion is that the project has broadly met the goals set out for it in the Logical Framework contained in the Project Paper. A comparison of Logical Framework Indicators versus evaluation conclusions appears directly after this summary. In brief, in the past two years there has been a sharp expansion in formal sector lending for housing, an impressive increase in the number of HFCs operating and a larger expansion in the total number of offices making loans, rapid expansion in the operations of private HFCs, and due attention given to reaching lower income borrowers. However, a definite area of weakness is in the supervision of the HFCs by the National Housing Bank--a result clearly at odds with the objective of creating a "financially sound market-oriented" housing finance system. While this can be attributed in part to the recency with which NHB took over full responsibility for supervision, the fact of limited oversight remains.

The specific findings are organized around the central topics addressed in the evaluation's Statement of Work;[3] these topics also serve as the basis for defining chapters in the report.

1. Growth of the HFC Network. The past three years have witnessed a substantial expansion in the HFC network. The total number of HFCs officially registered--a very undemanding task--has grown explosively from 30 in 1988 to 250 or more in 1991. The majority of HFCs are very small, however, and a large number of the officially registered HFCs may have gone out of business.

Perhaps a better indicator of industry size is that 16 HFCs have been recognized to receive refinancing from NHB, and two others are in the process of attaining this status; such recognition indicates significant maturity on the part of these HFCs. Of the 16, 10 are private and 4 joint sector

[3] The Statement of Work is included at Annex 1.1.

18

companies. Another 13 companies (exclusive of those just mentioned) have been confirmed by NHB to be HFCs and have in principle been brought under NHB's oversight for taking deposits.

The 16 recognized HFCs increased their number of offices from 51 in 1988-89 to 136 in 1990-1991. (All references in this report are to fiscal years.) Importantly, expansion in the branch network favors cities of under one million population; the percentage of offices in such cities rose from 22 to 36 percent over the period. Given the lower housing costs in the smaller cities, it is easier for HFCs to reach low-income families there than in metropolitan areas.

2. Performance of HFCs over the Period. Based on data for nine of the largest HFCs, the number of loans sanctioned by HFCs grew at a compound rate of 44 percent from 1988-1989 to 1990-1991, and the volume of sanctioned loans increased at 47 percent. Excluding HDFC, the figures are 113 and 116 percent, respectively. In the latter period about 153,524 loans were sanctioned by these nine HFCs.

Other key findings:

-- Overall, the HFCs performed well in raising funds, leveraging equity, and reaching, on average, a minimum level of profitability. But rapid increases in the cost of funds are constricting their access to resources they can afford, and forcing greater reliance on NHB financing to remain profitable. If HDFC is excluded, NHB refinancing accounts for 18 percent of the new resources of HFCs in 1990-1991.

-- Credit risk on HFCs individual loans appears to be low. The good repayment record is remarkable and should be carefully safe-guarded.

-- The liquidity and capital risks of HFCs are low; interest rate risk could become a problem if the cost of funds continues to rise and HFCs refrain from exercising their option to raise rates on outstanding loans.

-- There is risk of some private HFCs becoming highly dependent on NHB for their loanable funds. Given NHB's policy of not including debt to NHB in computing an HFC's debt-to-equity ratio, there is the possibility of some HFCs becoming overleveraged, although this has not yet happened. The dependence on NHB is a reflection of the difficulty these small companies have in raising deposits and term loans.

3. Lending to Households Below-Median-Income. The information available indicates that below-median-income households account for one-quarter of all HFC borrowers and one-fifth of total loan volume. This represents a modest increase in share over the past two years; given the explosive growth in total lending by the HFCs, this is a substantial achievement. Furthermore, the share of loans going to this group may well increase in the future, as HFCs continue to locate new branches in smaller cities where incomes and housing costs are lower.

While growth in lending to these families is largely market driven, NHB as played a role in encouraging firms to direct their resources to this market segment. The unit and loan size restrictions in NHB's refinancing program has been a definite factor, as has its efforts to promote the location of HFC branches in smaller cities. Its HLA program should result in more lower income borrowers in the future. Additionally, as the refinancing program expands, its ability to influence HFCs' marketing of loans should increase.

All HFCs say there is no discrimination against female-headed households. This cannot be confirmed, however, since data available to the team on lending to women and households headed by an elderly person are too limited to permit estimates of lending volume. These patterns could be monitored if NHB required HFCs using its refinancing facilities to routinely report information on borrower profiles.

4. Future Demand for Refinancing of Loans to HG-Eligible Households. Under conservative

20

assumptions, substantially more than $25 million in eligible loans will be presented each year to NHB for refinancing.

5. Supervision, NHB Funds Mobilization, and Developing the System. NHB's record with respect to supervision of HFCs is weak overall. It is particularly poor for those HFCs that are registered but not recognized as being able to obtain refinance from NHB. Even for the recognized companies, however, much improvement is needed. Except for HFCs using NHB's refinancing facility, the HFCs are providing NHB little financial information on a regular basis, and on-site supervisory visits are almost wholly absent. NHB recognizes these weaknesses and some action may be taken soon. NHB has been more aware of the limitations in its regulatory authority, however, and has taken steps in the form of preparing and vetting amendments to the NHB Act to provide it with most of the powers outside observers believe it needs.

NHB has very large implicit outstanding commitments for providing refinance to the HFCs. It has not made any systematic estimate of the size of these commitments, and this should be done. Nevertheless, the NHB is aware that its commitments probably exceed the volume of funds it will be able to obtain from "favored sources," i.e., low cost funds allocated by government bodies. It has, therefore, begun exploring options, such as creating a mutual fund and a subscription retirement scheme, for obtaining funds from the market. These ideas have not yet been converted to plans. A sound strategy is obviously required.

Over the past two years NHB has been very active in promoting development of the housing finance system. Eight separate areas of positive intervention are reviewed in the report. While more could be done in several areas, particularly assisting HFCs with funds mobilization from sources other than refinancing, there is a solid record of accomplishment. Similarly, USAID, working with

21

NHB, has executed a substantial complementary program of training, studies, and technical assistance, over the period.

6. Addressing Constraints to Sector Development. In a comparatively brief period of two years the NHB has moved with some effect in a surprisingly large number of areas to reduce constraints to the development of the housing finance system. Of course, much remains to be done.

In summarizing the record it is useful to divide the eight areas reviewed into two groups: those posing the more serious and immediate constraints to system development and those whose resolution is important to longer-term development. The first group includes:

-- mobilizing savings from households
-- raising the currently low interest rates on small housing loans
-- strengthening the mortgage instrument
-- expediting foreclosure procedures.

NHB has made significant progress in addressing the latter three constraints: it has dealt directly with the low interest rate on small loans through its refinancing program and the proposed amendments to its Act will result in very substantial progress the other two areas. The record on mobilizing savings from households is more mixed and the situation more complex. The HLA scheme certainly should be a help to HFCs, but it has been withheld from most of them on what appears to be the questionable grounds of helping HFCs control maturity mismatch between deposits and loans. In addition, HFCs feel themselves badly disadvantaged compared to commercial banks by the RBI's prohibition on their accepting deposits for less than 24 months, although the extent of this handicap is unclear.[4]

[4]. Since the nationalization of the banking system, most commercial banks are public banks.

22

NHB has been notably less active in the four areas important to longer-term development:

-- mortgage instrument standardization
-- introduction of additional types of mortgages
-- creative underwriting of loans for lower income borrowers
-- simplification of title investigation.

While it is easy to point to lack of action on the middle two items as evidence of lack of concern for the lower income borrower, this may not be the central point, because NHB's targeted refinance program and improving foreclosure procedures may, in any case, be more important in delivering loans to this group. Nevertheless, progress in all of these areas will be important to future system development and to how well lower income households are served by the housing finance system.

7. Program Management. Overall, management of the program by USAID and NHB appears to have been effective. The thoughtful training and technical assistance program designed by USAID in collaboration with NHB at the beginning of the program was largely executed. Failure to complete some planned activities that was not due to lack of diligence by USAID or the NHB. NHB succeeded in meeting all the Conditions Precedent in the loan agreement.

USAID staff might have been more diligent than they were in pursuing some of the areas stated in the MPIP.

The presence of the Conditions Precedent clearly caused NHB to devote more energy to technical assistance, training and regulatory issues than it would have otherwise. The project, while initially off to a slow start compared with a perhaps unrealistically optimistic schedule, has now "caught up," and the second tranche of funds may well be disbursed ahead of the original schedule.

8. The USAID Role. The team's overall assessment is that USAID's involvement has been highly constructive in this stage of the development of the Indian housing finance system. Both

capital and technical assistance have been productive.

With respect to the capital assistance, several of the conditions in the Master Program Implementation Plan (MPIP) were effective. The norms set in the MPIP for sub-borrowing HFCs have been adopted for general use by NHB. The half-yearly reports and other monitoring required in the MPIP have been the core of NHB's supervisory activity, and the poor performance in gathering data from even the recognized HFCs under these provisions has alerted senior management to the larger supervision problems. Similarly, the conditions in the MPIP requiring technical assistance and training plans caused NHB to turn to these activities; the impact of the MPIP is clear when it is observed that work began in these areas only when NHB wished to draw on the HG loan funds. NHB management now admits these areas were neglected during its "start up phase" and that more needs to be done. The technical assistance components have also proven valuable. Three of the studies had demonstrable impacts on NHB thinking: Croft's on regulation (which built on Wilson's earlier paper); Madway's on foreclosure; and Struyk's on possibilities for a secondary mortgage market. In addition, the team's sense is that those who participated in the training courses profited from them, not simply in acquiring technical knowledge but in becoming more receptive to new ideas for development of the Indian housing finance system.

Recommendations

The team's priority recommendations are as follows:

1. <u>Supervision and Regulation</u>. The team recommends that NHB give its highest priority to strengthening this system before one or more HFCs fail and damage the reputation of the entire system, which would undo much of NHB's laudable and effective work in promoting the housing

finance system. An adequate number of staff, well-trained and dedicated full time to supervision under a managing director charged solely with this responsibility, is essential.

2. Promotion. By nearly any standard NHB has been highly successful in producing a surge in the number of housing finance companies and the volume of formal lending for housing. The team believes that the next logical step in enhancing the development and competition of the sector will involve giving the HFCs some latitude in setting the interest rates on their loans. This could be accomplished by NHB establishing substantial ranges within which lenders could set their rates or by establishing minimum or floor rates for loans of different sizes. The rate on large loans, i.e., those above Rs. 2 lakhs, would remain market determined--a pattern in existence through NHB's setting a floor rate for those loans. NHB can in effect control the minimum rates on small loans through its refinancing rates.

With this flexibility, all HFCs could vary interest rates-- even for the same loan amount--with the perceived riskiness or ease of servicing (e.g., payroll deduction or not) of the loan. Moreover, it will give HFCs more flexibility in raising funds from higher cost sources than is now the case. Individual HFCs should be able to identify "market niches" in which to work successfully. In light of the large interest rate increases on loans recently granted to the urban cooperative banks, an NHB request to the Reserve Bank of India for such a change may well be accepted.

3. Lending to Low-Income Households. Given the rule-of-thumb assumption that loans of Rs 50,000 refinanced by NHB were taken by households below the urban median income level, and the fact that most reporting is on this basis, it is not possible to know with precision the extent to which lower income households are being served. Consequently, the team's first recommendation is that the necessary data be assembled to determine this share with precision.

25

The team also recommends that, if at any time NHB decides to limit the volume of refinancing any one HFC can take for any reason, loans to low-income households be exempted from the limit. This should provide a significant increase over the present incentives to do such lending.

4. Funds Mobilization by NHB. The team strongly recommends that NHB prepare careful estimates of its probable future (multi-year) refinancing obligations as soon as possible after further discussions with the principal HFCs. NHB is aware that it will probably soon have to turn to the market for finance. To encourage NHB to make progress in this direction, the team recommends that, in future loans from USAID to NHB, due attention be given to NHB's success in mobilizing an increasing percentage of its total resources from the more open financial markets. The team is aware that implementation of this recommendation may require that refinancing rates (and therefore mortgage interest rates) will have to be increased. Nevertheless, without turning to the market, NHB will probably soon have to ration the amount of financing it can provide to HFCs.

5. Meeting All the Conditions in the MPIP. USAID insisted that the financial terms for sub-borrowers be met before the first disbursement of HG funds to NHB. However, other conditions regarding training, technical assistance, and reporting by the HFCs were not fully met. Future disbursements should depend on meeting all of these terms.

LOGISTICAL FRAMEWORK FOR HG-003 EVALUATION

Objectively Verifiable Indicators	Means of Verification	Conclusions
Increase in the amount of funds lent for housing by the formal sector. Increased borrowing for housing by low income households.	Special financial sector studies. Project records.	There were insufficient data to establish by how much formal sector housing finance funds had increased for for the period under review. However, evidence strongly indicates that HFC lending growth did not come at the expense of funding for other formal sector housing institufions. Thus, the volume of loans sanctioned by the HFCs reviewed can be taken as a lower bound estimate of this expansion. From 1988-1989 to 1990-1991, the volume of loans sanctioned by the eight HFCs for which data were available increased from Rs. 50,188 lakhs to Rs. 108,084 lakhs. The available data, while limited, strongly indicate that there has been increased lending to low income households. HFCs are the only financial entities which make mortgage loans to low-income households. Over the past three years, seven HFCs have increased their annual loans sanctioned to this group from approximately 14,414 to 32,266.
A network of financially sound market-oriented HFCs serving households below the median income as well as those above.	Monitoring of number and distribution of commercial HFCs and their branches; studies of: financial structure; soundness; market shares; loan collection rates; terms of loans and types of facilities;	The number of HFCs and HFC branches have grown very rapidly over the period. The total number of HFCs increased from an estimated 30 in 1988 to over 250 in 1981. The industry has also become less concentrated. The largest HFC's

27

Objectively Verifiable Indicators	Means of Verification	Conclusions
	volume of lending to low income house-holds, etc.	share of the total volume of eight HFCs' loans declined from 89 percent to 75 percent from 1988-1989 to 1990-1991. The firms for which data were available have low capital, liquidity and credit risks and very good collection records. Interest rate risk is low but may increase in the near future. Most firms show strong and/or increasing profitability. Interest rates on loans above Rs. 200,000 and for homes larger than 40 square meters are unsubsidized. Loans of less than Rs. 200,000 for homes under square meters carry a slightly below-market interest rate.
1. Increased loan volume by project HFC. 2. Substantial increase in branches of HFCs. 3. Introduction of GPMs, ARMs or other creative instruments. 4. Improved compliance with inter-mediary's criteria; reduced management costs.	1. Project reporting requirements. 2,3,4. Mid-term and final evaluations.	1. HFCs grew very rapidly over the period reviewed. Loan volume of eight HFCs grew by 47 percent per year from 1988 to 1991. 2. Branches of recognized HFCs increased from 51 to 136 over the same period. 3. Because inflation is relatively low in India, there is less scope for the use of innovative mortgage products than in other countries. Nevertheless, HFCs did introduce GPMs, products geared to older families and products designed for extended families. 4. Over the period, 16 firms were able to meet the NHB's criteria for admission to the refinancing program. As HFCs matured and increase their volumes,

Objectively Verifiable Indicators	Means of Verification	Conclusions
		they were increasingly able to cover their fixed costs with fee income.
1. US $50 million guaranty authorization with disbursements over 3-4 years. 2. $2.9 million in grant funds. 3,4. In-kind contributions from implementing organizations.	1. Project records. 2. Project records. 3,4. Availability of staff and resources of implementing organizations to absorb Ia, training and implement project.	1. The project got off to a somewhat slow start but the pace rapidly accelerating, and complete. Disbursement is anticipated before the initially-projected date of December, 1982. 2. To date, $1.7 million in grant funds have been disbursed. Grant funds have been put to excellent use. Funds have been used to send NHB, commercial bank and HFC managers to domestic and international training programs, seminars and study tours. Additionally, USAID has commissioned a number of studies which have been widely accepted by management of recognized HFCs. However, dissemination of commissioned studies was ad hoc and did not extend beyond recognized HFCs. 3,4. The Project Paper called for NHB to develop a detailed schedule of HFCs' training needs by approximately September, 1989. As of June, 1991, this had still not been accomplished. Although the Project Paper is somewhat vague in its expectations for training HFC management, it appears that overall, NHB undertook less training than envisioned in the PP.

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1. Introduction

The National Housing Bank (NHB) was created in July 1988, as a wholly owned subsidiary of the Reserve Bank of India, to foster development of a high volume housing finance system that would serve households in most parts of the income distribution. Broadly speaking, the NHB has three missions: (a) to promote expansion of a market-oriented housing finance system; (b) to mobilize additional funds for lending for housing and associated land and infrastructure projects; and (c) to supervise and regulate housing finance institutions so as to insure the financial health and stability of the housing finance system. As a subsidiary of the Reserve Bank of India, the NHB enjoys considerable independence from the Government of India (GOI).[1] As an apex institution, it does not lend directly to households or developers, but rather operates through existing financial institutions, including commercial banks and specialized housing finance companies.

Consistent with the GOI's shift to the housing sector approach embodied in the Eighth Five-Year Plan (1990-1995), the NHB is trying to implement a new vision of the housing finance system. NHB envisions the government acting more as a facilitator of resource mobilization and less as a direct participant. Its view is that local development authorities should restrict themselves primarily to the preparation and allocation of serviced sites. Construction and financing of housing should be left to the more efficient practices of the

[1] In the U.S. context, the NHB should be thought of as the equivalent of a subsidiary to the Federal Reserve Bank, which maintains considerable independence from the Department of the Treasury.

30

private sector, including households, employers, and developers.[2]

The National Housing Bank was created when the housing finance system was fairly primitive and had two clear characteristics: it was heavily dominated by government bodies, and it was delivering a low volume of financing for home purchase and even less for housing development by the private sector. At the same time, however, an innovative private housing finance company--the Housing Development Finance Corporation (HDFC)--had been demonstrating for a decade what could be done by private firms if given modest latitude to operate in the financial markets. A major part of NHB's mission is to foster the creation and growth of additional housing finance corporations (HFCs) as vehicles for expanding the availability of housing finance.

During the few years preceding the NHB's creation in 1988, USAID had been active in the Indian housing sector, most prominently through its substantial support to HDFC--loan support that ultimately totaled $125 million.[3] USAID, then as now, had the following broad goals: mobilizing additional domestic resources for housing; increasing market orientation in housing finance; and, increasing the access of lower income families to housing finance.

Having worked closely with HDFC to demonstrate the potential of private housing finance companies (HFCs), USAID in 1988 re-oriented its lending program to assist the NHB in expanding the overall housing finance system. In particular, the loan to NHB under the Housing Guaranty Program (HG-003 authorized in September 1988), had three objectives:

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[2] Ministry of Urban Development (1990); Diamond (1990), p.7.

[3] For a detailed description of this program see Buckley et al. (1989).

(1) provide critically needed lending capital to meet near- and mid-term needs of eligible companies serving a number of geographic areas;

(2) foster a relationship between recent entrants to the sector and the newly established National Housing Bank in order to improve the new firms' ability to mobilize resources, manage their portfolios, increase lending to low- income households, and operate more effectively within the existing public policy environment; and

(3) address a number of sectoral constraints on expanding the system, through technical assistance, training and policy dialogue.[4]

Under the loan program, $50 million in capital assistance was to be provided to NHB plus $2.9 million in grant funds for training, technical assistance, and program evaluation.

At present, the first $25 million in loan funds has been borrowed by the NHB and disbursed against eligible activities, and considerable technical assistance has been provided with some $1.7 million in grant resources.

1.1 NHB Activities

In its first years of operation, the National Housing Bank moved with alacrity in a number of areas to expand and strengthen the housing finance system. This very brief overview of these activities is designed only to give a framework for the more detailed discussions in the following chapters. A summary of the NHB's major actions is given in Table 1.1.

In terms of promoting HFCs, the NHB quickly issued guidelines setting out the requirements for an HFC to be registered with the NHB--an essential step in the process of

[4] USAID (1988), p.1.

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becoming qualified to participate in the NHB refinance program (see below) and a facilitating step for obtaining the various tax advantages associated with being a recognized HFC.[5] The NHB also began in 1990 to refinance small and moderate loans originated by qualified HFCs. Under this program, NHB refinances 100 percent of loans (a) up to Rs 200,000 for units whose built up area does not exceed 40 square meters OR (b) whose cost does not exceed Rs 150,000. Among these loans, NHB can apply funds from the Housing Guaranty Loan (HG) to those affordable to borrowers in the lower half of the income distribution. Presently, NHB is refinancing loans from 9 of the 16 HFCs it has qualified to receive refinance. By July 1991, it had refinanced about Rs 536 crores ($260 million) in loans by HFCs.

As for funds mobilization for the housing sector, the NHB has moved on two fronts. First, it launched a contract savings scheme--Home Loan Account Scheme--under which participants save regularly for five years and then obtain a mortgage loan for two to four times their savings. This scheme, initially offered only through the commercial banking system, which generally did little to promote it, was expanded in 1990 for use by some HFCs. NHB has promised to refinance loans made under the HLA if the bank holding the HLA account is unable or unwilling to hold the loans as investments. Second, NHB has tapped into various sources of funds to support its loan refinancing operations. To this end it has been issuing Capital Gains Bonds, availing itself of other government-guaranteed and directed credit, and drawing on foreign sources, including the Housing Guaranty Loan.

Lastly, with regard to supervision and regulation of the housing finance system, the NHB has taken over supervision of HFCs from the Reserve Bank of India. Principally,

[5] These advantages are detailed in National Housing Bank (1990), Annexure 3.

37

beyond setting the requirements for recognizing HFCs, it has issued directions concerning the acceptance of deposits and has established maximum interest rates and established maximum loan-to-value ratios for mortgage loans.

1.2 The Evaluation

This report presents the findings of the interim evaluation of the program. Broadly speaking, it focuses on the extent to which HFCs, especially private and joint sector HFCs, have developed under NHB's initiatives, the degree to which HFCs are lending to lower income families, and NHB's effectiveness in promoting development of the housing finance system.[6] The evaluation relies on data from four sources: (a) financial data on operations over the past three years for nine HFCs which are participating in NHB's refinancing program (described below) and which together account for the great majority of lending by HFCs; (b) in-depth interviews, guided by a protocol, and additional data collection at four of these HFCs;[7] (c) interviews with staff at the NHB and other financial institutions, including HDFC, and with USAID staff; and, (d) information contained in a series of reports on housing finance in India prepared over the past two years.

Coming as it does at the mid-point in the capital assistance program, the evaluation

[6] Under the definitions used in this program, a private HFC is one having less than 50 percent of its equity capital allocated to Indian central and/or state governments and/or entities that themselves are at least 80 percent owned by these governments. A joint sector HFC is one having at least 50 percent but less than 80 percent of its equity capital allocated to Indian central and/or state governments as described above.

[7] These are Can Fin Homes Ltd. (Bangalore), Gujarat Rural Housing Finance Corporation (Ahmedabad), Dewan Housing Development Finance Ltd. (Bombay), and SBI Home Finance Ltd. (Calcutta). Less detailed interviews were conducted at four other HFCs.

affords the opportunity for "mid-course corrections." The timing of the evaluation is appropriate; it comes as NHB just completes its first two years of assistance and support for HFCs. Naturally these were frenetic years; with basic programs in place, now is an appropriate time for reviewing operations. Changes in operations and policies at this stage in a young institution's development are to be expected.

The evaluation can have another benefit. Many countries are intensely interested in the possibility of establishing an apex institution like the National Housing Bank. To date many have created government-affiliated housing banks which make direct loans to borrowers--often at the cost of stifling the development of private lenders and perpetuating inefficient operations.[8] The evaluation provides the first critical description of NHB's early experience and can serve as the basis for transferring information on the "apex model" to policy makers in these countries.

1.3 Report Organization

The balance of this report is organized into eight chapters. The topics of the first seven of these chapters correspond to the areas the Terms of Reference indicated should be explicitly addressed in the evaluation. The final chapter presents the team's recommendations.

In order to keep the report to a reasonable length, it has been necessary to assume that the reader is generally informed about financial markets and the housing finance system in

[8] For a detailed discussion of this problem in Indonesia, see Struyk et al. (1990), chapter 6.

India.[9] In addition, detailed descriptions of the National Housing Bank's programs have been relegated to Annex 1.4.

[9] For an overview of the housing finance system, see, for example, Munjee et al. (1991), Buckley et. al (1989), Buckley (1990), or Diamond (1990).

Table 1.1
Significant National Housing Bank Milestones[10]

December 1987	National Housing Bank Act passed.
July 1988	National Housing Bank begins operations.
September 1988	U.S. Housing Guaranty Loan (003) authorized.
November 1988	NHB announces the role it envisages for the commercial banking system in housing finance.
January 1989	NHB introduces refinance scheme for use by commercial banks.
March 1989	Reserve Bank of India issues guidelines for housing finance companies (HFCs), including minimum maturities on deposits, debt/equity ratios.
March 1989	NHB introduces Home Loan Account scheme (HLA) for use by commercial banks.
May 1989	NHB introduces refinance program for qualifying housing loans issued by HFCs.
June 1989	NHB issues housing finance companies Directions; takes over supervision from RBI.
July 1989	NHB issues Directions for Home Loan Account Scheme.
October 1989	NHB issues guidelines for the Land Development and Shelter Projects program, for projects undertaken by public companies.[11]
January 1990	RBI issues directive permitting larger volume of term loans from commercial banks to HFCs.
March 1990	NHB liberalizes terms of refinancing program for HFCs, making

[10] The milestones have been selected which are most important for the main NHB programs and those most effecting housing finance companies.

[11] Similar guidelines were issued in January 1990 for project undertaken by professional developers.

either the program's maximum floor area or maximum unit cost the condition for inclusion of a loan.[12]

June 1990	NHB refinances the first batch of housing loans from HFCs.
Sept 1990	Completion of Master Program Implementation Plan and other conditions for NHB to select lender for funds under USAID Housing Guaranty Loan.
November 1990	NHB raises house cost maximum on loans qualifying for refinancing by HFCs.
January 1991	NHB increases interest rates on housing loans, following interest rate increases by RBI.
January 1991	NHB issues Directions permitting selected housing finance companies to participate in Home Loan Account Scheme, with effect on March 1, 1991.
April/May 1991	NHB borrows $25 million under the Housing Guaranty Loan and it is disbursed against qualifying loans.

[12] Similar adjustments to those described here and below to the refinancing program for HFCs were made on other dates for commercial banks and housing cooperatives.

2. Growth of HFC Network

The number of HFCs in India and the volume of the housing finance they transact has grown extremely rapidly over the years. This chapter analyzes regional distribution and branch growth of HFCs and explores why this growth has occurred.

In 1987-1988, the most recent year for which figures are available, total formal sector housing investment totaled Rs. 11,630 crore. The formal housing finance system provided approximately 22 percent of this, or Rs. 2,566 crore. As Table 2.1 indicates, the GOI (central and state), provident funds and insurance companies were the largest contributors to this market. HFC loans accounted for only 10 percent of total housing finance. Figure 2.1 on the following page displays this distribution graphically.

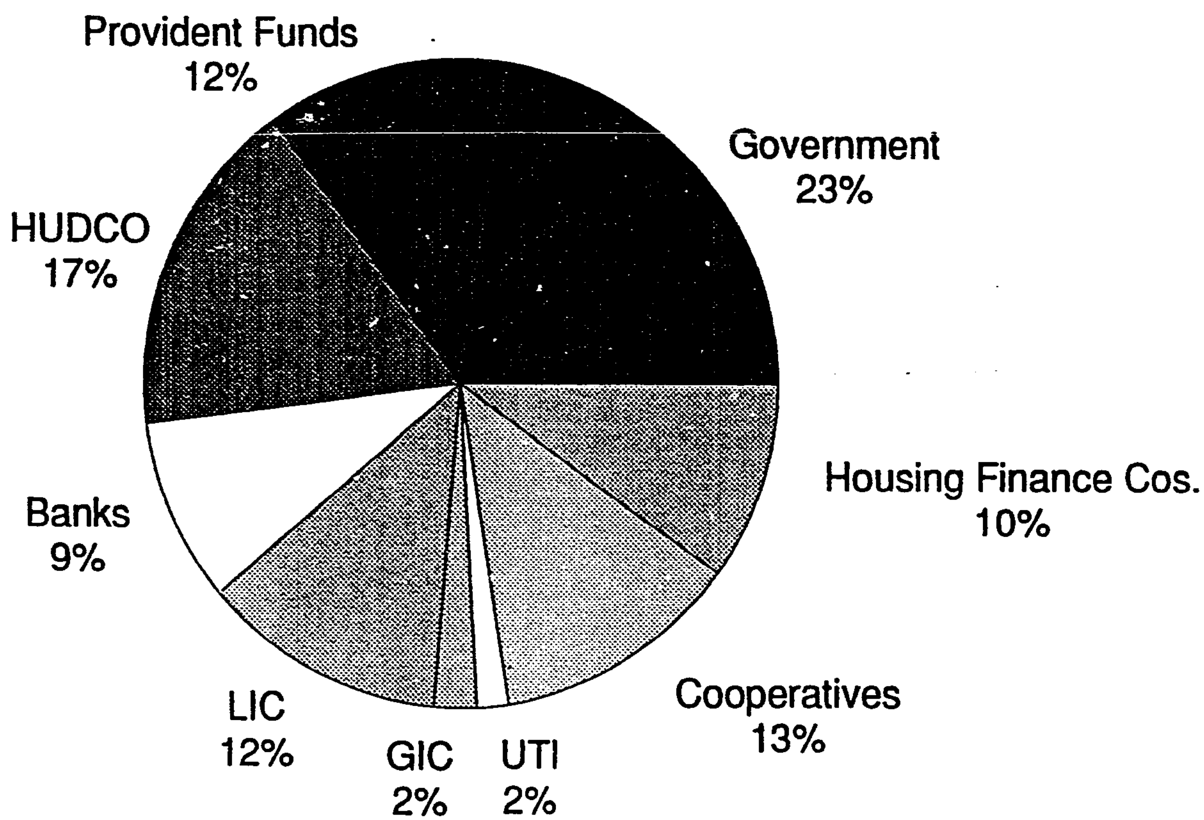
TABLE 2.1
SHARE OF TOTAL HOUSING FINANCE BY SECTOR, 1989

	source	total # of loans	% of total	volume in Rs. to state agencies	to institutions	to households
A	government, central, & state	579	22.6	----	---	---
B	provident funds	318	12.4	---	---	---
C	HUDCO	438	17.1	438	---	---
D	banks	237	9.2	151	66	20
E	insurance companies:					
	Life Ins. Co. (LIC)	319	12.4	90	131	98
	General Ins. Co. (GIC)	55	2.2	55	---	---
F	UTI	41	1.6	41	---	---
G	Specialized institutions:					
	co-operative finance	325	12.7	---	---	32
	housing finance co. (HFC)	254	9.9	48	___	206
	TOTAL	2,566	100	823	197	967

Source: Munjee (1991)

40

Figure 2.1
Financial Flows to the Housing Sector
By Source 1987-1988



Source: Munjee (1991)

7

Table 2.2
HFC Registration, Classification and Recognition

level	entrance process	privileges
registered	promoters fill out simple form and state that at least 50 percent of business will be housing finance	right to engage in housing finance.
classified	NHB determination that HFC is in compliance with NHB Directions.	no direct benefits; possibly some enhanced credibility with funding sources.
recognized	NHB determination that firm is financially healthy, well-managed and in compliance with Directions and Guidelines.	right to participate in NHB refinancing program.

Source: NHB Records

(a) Registration. Prior to commencement of operation, all companies in India must obtain a license from the Registrar of Companies. This is a pro forma exercise in which promoters fill out a simple form. If organizers state that at least 50 percent of their business will consist of financing the acquisition or construction of housing including land acquisition and development, the firm is registered under industry code 801.2, which is reserved for housing finance companies. Entry into this sector is free; neither the NHB nor any other government organization has the authority to screen firms. Nevertheless, many firms registered as HFCs are either not active or not engaged primarily in long-term residential

42

Over the last three years, HFCs' housing finance volume has increased by approximately 47 percent per year. In 1991, total loans sanctioned by nine of NHB's recognized HFCs totaled Rs. 1,265 crore. Thus, while housing investment by most of the above sectors has increased significantly over the same period, it is likely that HFCs' share of the total market has grown substantially. The NHB has contributed to the growth of the industry through creation of a refinancing facility. In fiscal 1989-1990, the NHB refinanced Rs. 115.5 crore of loans. In fiscal 1990-1991, the organization made almost Rs. 316 crore of refinancing loans to HFCs for 49,882 units.

2.1 Growth of Registered, Classified and Recognized HFCs

The total number of HFCs has grown from approximately 30 in 1988 to well over 250 in June, 1991. The number of classified and registered firms has also grown over the period, but at a slower pace than total industry expansion.

2.1.1 Entrance Requirements, Obligations and Privileges by Class. To enter the HFC industry, firms must register with the Registrar of Companies. At this point they are subject to NHB Directions. After the NHB has established that registered HFCs are, in fact, complying with the Directions, the NHB will classify them as HFCs. Firms that are financially healthy, well managed and in compliance with the Directions and additional Guidelines,[1] are eligible for participation in the NHB's refinancing program. Table 2.2 summarizes the three classes of HFCs and how companies obtain each status level. This taxonomy is explained in more detail below.

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[1] Guidelines are detailed in Annex 1.4.

information provided by the HFCs.[4] Financial viability is not a prerequisite for permanent classification. If the HFC is established by a commercial bank, insurance company or other government body it will generally be permanently classified after much less than the one to three years private HFCs must wait.

Classification generally does not provide any direct benefits to HFCs. However, it can count in their favor when they apply to the Central Board of Direct Taxes (CBDT) for the tax advantages that HFCs are entitled to.[5] The CBDT looks more favorably upon classified firms and often consults the NHB informally about applicants. The NHB attempted to make classification a necessary and sufficient condition for CBDT approval.[6] Some HFCs interviewed said that "classified" status had helped them mobilize resources from public agencies. However, others felt this designation had not improved their standing with investors of any type. Finally, firms must be classified before the NHB will consider their application for "approval" or "recognition" - both terms are used to denote permission to participate in the refinancing program.

(c) Recognition. In order for HFCs to become recognized they must comply with "Guidelines" additional to the NHB Directions. After HFCs have established an operating track record, they become eligible to apply for recognition. When firms apply, the NHB conducts a very thorough site visit of the HFC's head office and a sample of its branches, in

[4] Nevertheless, the NHB plans to conduct site visits of all classified HFCs this year in order to monitor their operations more closely.

[5] Annex 1.4 provides a description of these benefits.

[6] The CBDT did not agree to this but the NHB feels that, as it has become more established, its influence with the Tax Board has grown.

housing finance. This will be discussed in greater detail below.

(b) Classification. In theory, the Registrar of Companies (RoC) is required to send the NHB a monthly list of newly registered HFCs so that the NHB can request from them basic information[2] regarding their directors, method by which they propose to fund activities, and other administrative details, and can inform them of the NHB Directions governing the industry. However, in practice, the NHB has received only one list covering firms entering the industry between April 1989 and September 1990. NHB received the list in February or March 1991. Due to a shortage of monitoring staff, the NHB has only recently contacted these firms.

In theory, when the NHB receives initial information from registered firms, it provisionally classifies them as HFCs based on their being registered under the HFC number 801.2, their stated intention to follow NHB Directions, and their plan that at least 50 percent of their assets will be housing finance instruments. The NHB then monitors firms for from one to three years to insure that they are following the Directions and that at least one-half of their assets are indeed being devoted to housing finance. If this is the case, the NHB "permanently"[3] classifies firms as HFCs. In practice, firms may apply for permanent classification if they feel their record justifies it and the NHB has not yet awarded the status to them. The NHB does not conduct site visits; rather it makes its decisions based on written

[2] Wilson (1988) p.6 lists the information HFCs are required to supply.

[3] The NHB describes this step as awarding "permanent" classification status. Nevertheless, the regulatory body can and will strip firms of this designation if it feels the companies are no longer fulfilling the above mentioned requirements.

Companies (RoC) indicate that approximately 250 HFCs had registered as of September, 1990; and 171 of these obtained licenses in the 18-month period from April, 1989 to September, 1990. Additionally, RoC has recently furnished the NHB with a list of approximately 300 companies that may be functioning as HFCs although they were not classified under the HFC heading. Thus the potential number of HFCs--both those registered under 801.2 and those enrolled under other headings--is quite large and has grown rapidly. However, many, probably even the majority, of these firms are very small companies that either never began operating or operated for a short time only.

Several factors have contributed to the growth of this industry. HDFC's tremendous success in the field has inspired much emulation. In its fiscal 1990-1991 year, HDFC sanctioned loans totaling Rs. 810 crore and the company had an impressive 33 percent return on equity in 1989-1990.[7] Creation of the NHB has also encouraged entrance to the field. Many potential investors viewed the NHB's founding as an indication that the GOI would increasingly be targeting the housing finance sector and thus that the profitability of this sector would improve. Many commercial banks entered the market influenced by the above considerations and two additional factors. First, these firms wished to diversify their assets and second, from 1979 to 1989, the RBI consistently increased the volume of funds banks were required to dedicate to the housing finance sector. Since 1989, the RBI has required banks to make 1.5 percent of their incremental deposits available for housing finance. Inspired by HDFC and the commercial banks and feeling that their direct lending programs

[7] The NHB provided the team with this information as part of a great deal of financial data on nine of the firms participating in its refinancing program.

order to verify that it has been complying with all NHB Directions and Guidelines, that at least three-fourths of the firms assets are housing finance instruments, and that the enterprise is financially viable and well-managed.

Recognition status confers a number of significant benefits. Most importantly, recognition allows firms access to the NHB refinancing facility. As noted, from June, 1990 to June 1991, the NHB made total refinancing of Rs. 316 crore for 49,882 units.

Additionally, the NHB claims that investors and lenders perceive recognition as GOI's indication that an HFC is financially healthy and its management is sound and honest, and that this "seal of approval" facilitates the HFC's mobilization of equity participation and term loans. Some HFCs confirmed this claim, but others felt it had not aided their resource mobilization efforts. Finally, while recognition does not automatically entitle firms to take part in the NHB's Home Loan Account program, the NHB's current practice is to consider only recognized firms as candidates for the program.

2.1.2 Industry Participation by Class. A very large number of firms has registered as HFCs in recent years. However, the number actually functioning is much smaller. The NHB's classification process has not kept pace with industry growth, and the NHB is very cautious about approving private firms for participation in its refinancing program.

(a) Growth of Registered HFCs. While there is considerable confusion as to the number of firms currently registered as HFCs, it is obvious that the growth of HFCs over the last three years has been rapid. Virtually all HFCs (with the exception of HDFC) were founded after 1984 and AID's Housing Guaranty 003 Project Paper estimates that only 30 HFCs were operating as of September 1988. Yet, the most recent data from the Registrar of were becoming too large to accommodate under their general corporate structures, LIC and GIC have also launched HFCs. Many developers have also entered the field as a means of providing financing to their customers. Finally, extremely low barriers to entry and exit encouraged many investors to run HFCs as small sidelines to their principal businesses and/or to register HFCs with no immediate or definite intention to operationalize a company.

(b) Growth of Classified HFCs. In his report, Croft (1990) states that approximately 20 HFCs were classified as of August, 1990. As of June, 1991, 31 HFCs had obtained classified status. Thus the number of classified HFCs has grown but still represents only a modest share of total registered firms. The primary reason that more firms have not obtained classified status is that, as mentioned above, many, and possibly most firms registered as HFCs are very small or dormant. The NHB has experienced difficulties obtaining appropriate information from these firms, due to both the NHB's staff constraints and the firms' unresponsiveness. A number of other firms are run by developers to provide customer financing and their business practices are often highly questionable.

(c) Growth of Recognized HFCs. As of March, 1991, the NHB had recognized 16 firms and was in the process of recognizing one more. Two of the recognized firms were public sector enterprises, four were joint sector firms and ten were private corporations. Both of the firms in the process of recognition were in the joint sector.[8] Since firms must be classified before the NHB will recognize them, the growth of this sector is limited to the

[8] Under the USAID program, firms are classified as public sector enterprises if 80 percent or more of the organization's equity is held by government bodies. If the government holds from 50 percent to 80 percent of total equity, firms are classified as being in the joint sector. If private organizations or individuals own 50 percent or more of a corporation's equity, the enterprise is classified as private.

48

growth of the classified grouping and the reasons why more HFCs have not become classified also explains why more have not been recognized. The major impediment to recognition that classified firms face is the required minimum equity stake of Rs. 1 crore. In addition, some HFCs that obtain the necessary equity are unwilling to devote 75 percent of their assets to housing finance instruments because of this sector's slim margins. Also, the NHB is still in the process of obtaining records for many classified firms from the RBI. Finally, due to the NHB's financial liability in the case of HFC bankruptcy, the NHB generally waits for private companies to firmly establish their financial viability before it consents to refinance their loans.

2.2 HFC Branch Types, Growth and Regional Distribution

This section explores the type of outlets HFCs establish, the growth of the HFC branch network and the regional distribution of HFC activities.

2.2.1 Branch Types. HFCs have three main branch types: headquarters offices, branch offices and collection centers. In addition, some HFCs send branch staff to smaller cities surrounding their branch location in order to promote the program and solicit loan applications.

Head offices handle interaction with government agencies, investors and lenders. They undertake resource mobilization, policy formulation, internal audit and inspection. In addition, smaller HFCs still require all branches to present loan applications to the head office for final loan sanctioning. Head offices may also function as branches. Each HFC has one head office.

Branches are involved primarily with customer interaction. They promote the bank's services in the community, solicit deposits, compile and analyze information provided by prospective borrowers and undertake collection efforts. They may or may not have loan sanctioning powers. Branch numbers vary depending on the size of the HFC. Many firms have only one combined head office/branch. HDFC, the largest HFC, has 25 branches and LIC Housing Finance will have 40 branches by March, 1992. As of March, 1991, the 15 recognized HFCs had 136 branches.

Collection centers are one- or two-person branches. Very few firms have this type of facility. They generally collect and process deposits and loan applications and undertake collection in small cities and then forward money and documents to nearby branches. They do not have loan sanctioning power. Very few firms have this type of facility.

Finally, some HFCs conduct loan promotion efforts known as "camps". In towns near branch locations, HFCs first advertise that they will visit to discuss the firm's loan plans. Several weeks later they conduct an informational meeting at a local hotel. Approximately two weeks after that they return to hand out loan applications. Two weeks later they collect the completed forms, a few weeks after which they return to disburse funds to approved borrowers. Thereafter, it is the borrower's responsibility to make payments to the branch office. If repeated camps generate enough volume, a branch will be established in that location.

2.2.2 Branch Growth. Figures on industry-wide branch growth were not available. Figures on branch growth for recognized HFCs are available and provide some insight into branch expansion for functioning HFCs. For the 16 recognized HFCs, total branches increased from approximately 51 in 1988-1989 to 136 in 1990-1991. Table 2.3 details this growth for public, joint and private recognized HFCs and Figure 2.2 on the following page displays the information graphically.

TABLE 2.3
BRANCH GROWTH OF PUBLIC, JOINT AND PRIVATE RECOGNIZED HFCs

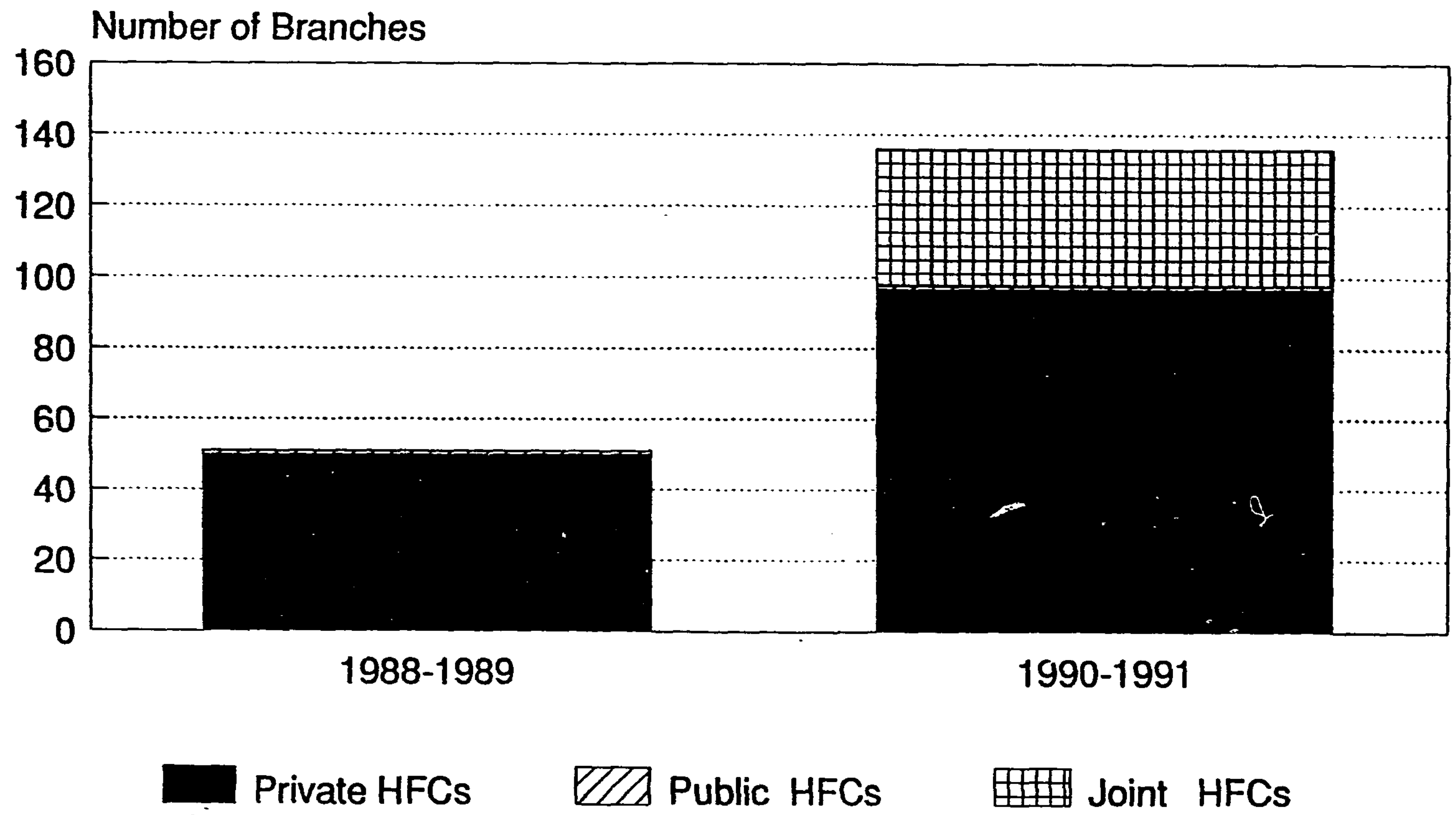
type of HFC	total firms June, 1991	tot branches 1988-1989	tot branches 1990-1991
public*	2	2	2
joint	4	15	73
private	10	34	61
total	16	51	136

* HUDCO is a housing finance wholesaler.
Source: NHB records

2.2.3 Regional Distribution of Branches. There is no industry-wide information on the number of operating HFC branches and their regional distribution. Partial data from recognized HFCs and discussions with the NHB and selected HFCs indicate that as HFCs grow, they expand extensively across regions rather than intensively in a given city or small region. The general pattern is for an HFC to initially establish a branch in one or severallarge cities and then to extend their outlet network into the medium sized and smaller cities[9] surrounding those metropolitan centers. Since the industry is young, most of the

[9] Generally towns with populations from 100 thousand to one million.

Figure 2.2
HFC Branch Growth by Type of Firm
Fiscal 1988-1989 to Fiscal 1990-1991



*HUDCO is excluded
Source: NHB Records

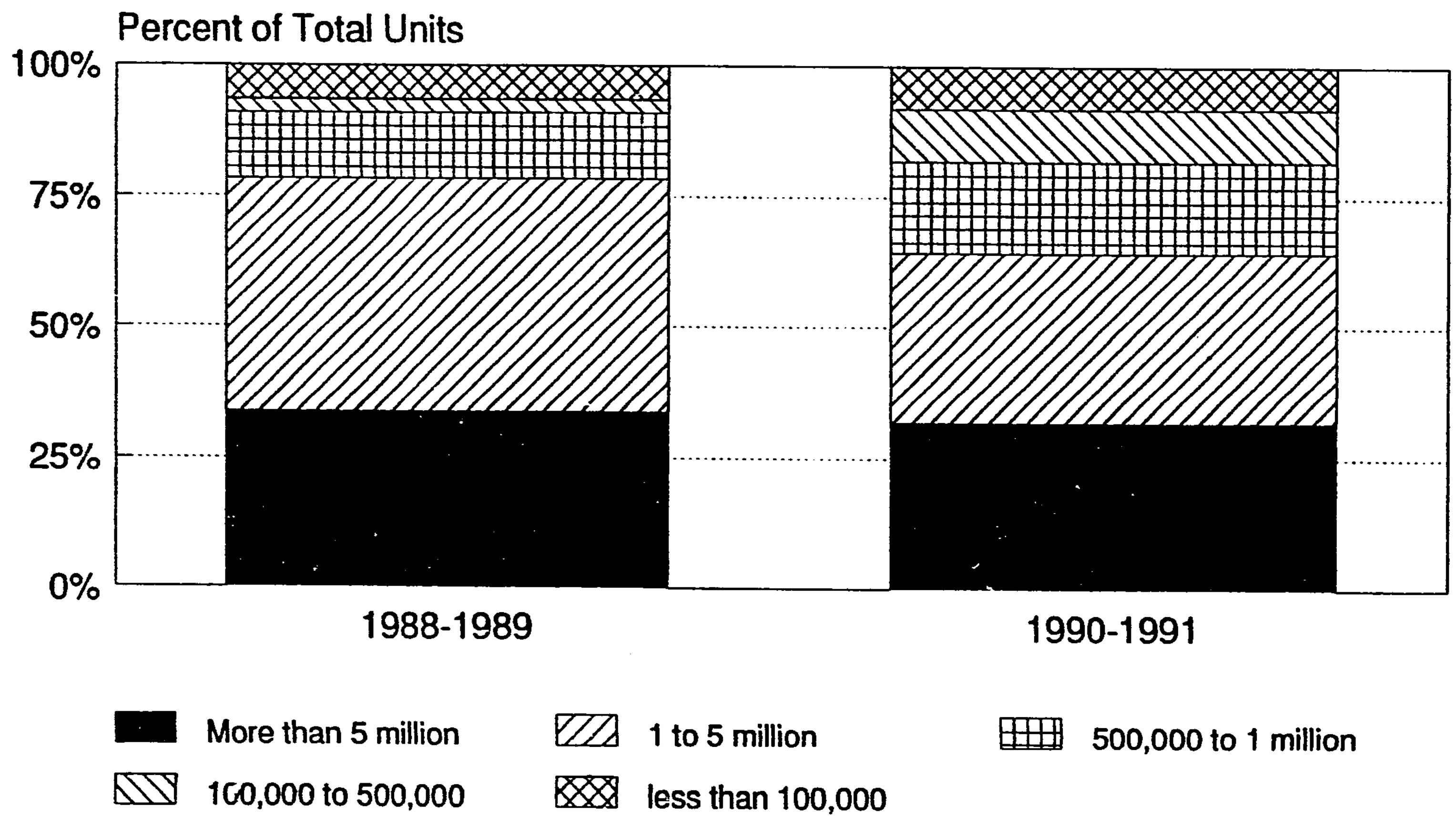
volume is transacted in the major metropolitan centers. However, as individual companies mature, their largest growth occurs in less dense areas. For example, in 1988-1989, of the total number of individual housing loans generated by HDFC, Can Fin Homes (Can Fin), Dewan Housing Finance (Dewan), India Housing Finance Development (IHFD) and SBI Home Finance Ltd. (SBI), 78.5 percent were in cities with populations in excess of one million people. Two years later, that figure had declined to 64.3 percent. The total number of individual housing loans underwritten by these five HFCs grew from 28,218 to 83,572 over the same period. For the five abovementioned HFCs, Table 2.4 details individual housing loans sanctioned by size of city in which mortgaged unit was located and Figure 2.3 presents this information graphically.

TABLE 2.4
HFC INDIVIDUAL HOUSING LOANS FOR 5 HFCS BY SIZE OF CITY WHERE DWELLING UNITS WERE LOCATED

	percent of total units	
city size	1988-1989	1990-1991
more than 5 million	33.8	32.0
1 million to 5 million	44.7	32.3
500,000 to 1 million	12.5	17.5
100,000 to 500,000	2.6	10.0
under 100,000	6.5	8.1

Source: Team analysis based on NHB records and the 1981 Census

Figure 2.3
Financed Units by Size of City
Fiscal 1988-1989 to Fiscal 1990-1991



Source: NHB records and 1981 Census

Despite this decentralizing trend, large cities still account for a substantially larger share of lending volume than national population. In 1990-1991, for example, cities with more than one million inhabitants accounted for 26.8 percent of national population[10] but 64.3 percent of individual home lending by the abovementioned institutions. Areas with populations below 100,000 represent 39.6 percent of national population and only 8.1 percent of individual home loans by the five HFCs.

HFCs set up main offices in metropolitan areas in order to establish a visible presence in the region and to be located near sources of equity and loan funds. However, competition in these large cities is very keen and housing costs are high. Thus firms generally expand into smaller cities where there is still considerable unmet effective demand.

HFCs are relatively evenly distributed throughout the country with the exception of the eastern and northern regions where very few firms have established offices. Table 2.5 on the following page details the number of HFC branches by city and state for recognized firms and Figure 2.4 displays the geographic distribution of HFCs on the map of India.

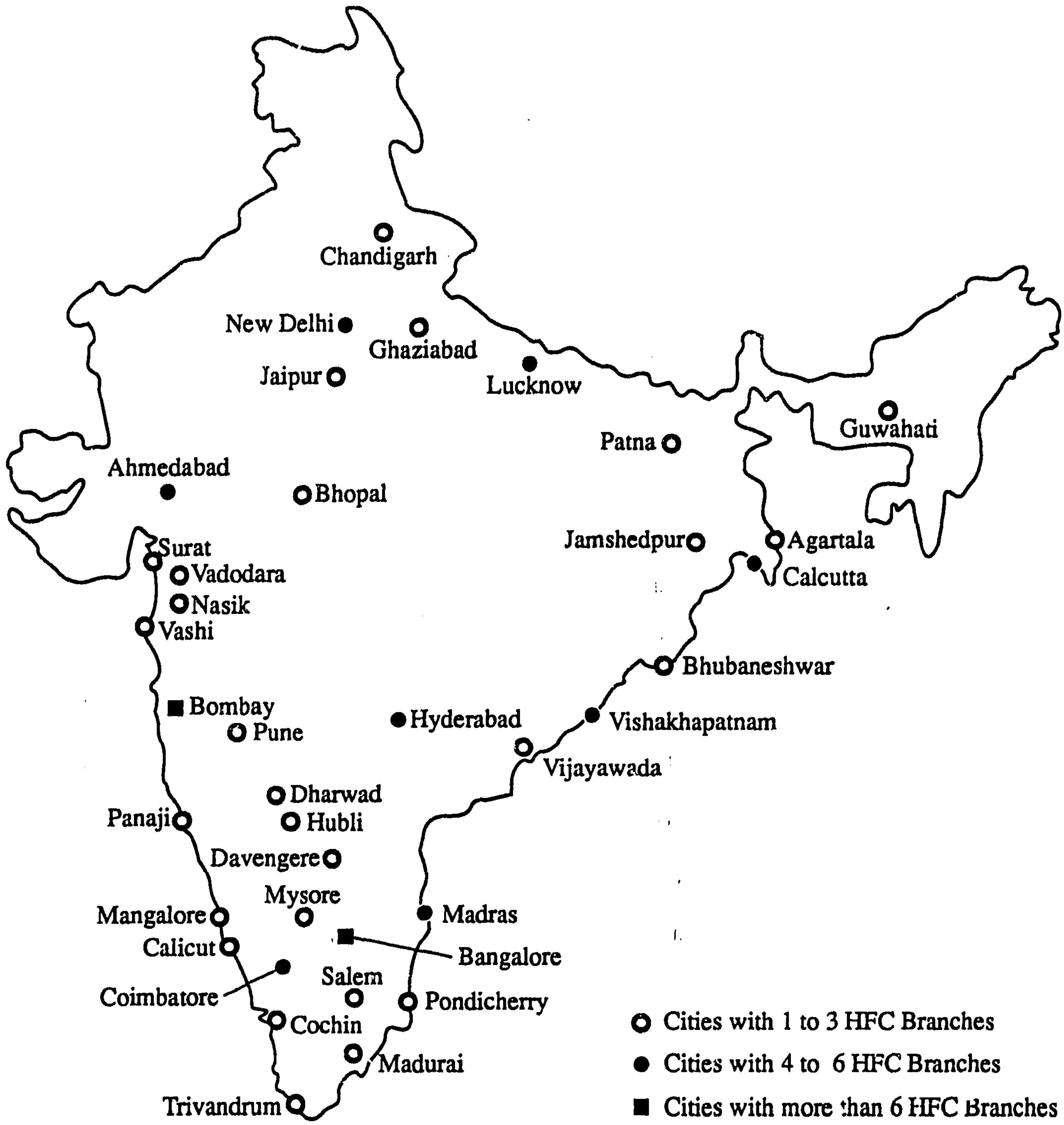
[10] Populations figures are based on the 1981 census and thus underestimate the percentage of the population currently residing in large urban areas.

TABLE 2.5
GEOGRAPHIC DISTRIBUTION OF BRANCHES FOR RECOGNIZED HFCS

state/U.T.I.	city	number of HFCs
Andhra Pradesh	Hyderabad	6
	Vijayawada	2
	Visakhapatnam	5
Assam	Guwahati	2
Bihar	Patna	1
	Jamshedpur	1
Gujarat	Ahmedabad	5
	Vadodara	1
	Surat	1
Karnataka	Bangalore	10
	Mysore	1
	Davengere	1
	Hubli	2
	Dharwad	1
	Mangalore	2
Kerala	Trivandrum	2
	Cochin	2
	Calicut	1
Madhya Pradesh	Bhopal	2
Maharashtra	Bombay	8
	Vashi	1
	Pune	3
	Nashik	1
Rajasthan	Jaipur	4
Tamil Nadu	Madras	6
	Salem	1
	Combatore	4
	Madurai	3
Tripura	Agartala	1
West Bengal	Calcutta	4
Orissa	Bhubaneshwar	3
Uttar Pradesh	Lucknow	4
	Ghaziabad	1
Goa	Panaji	3
Delhi	Delhi	6
Chandigarh	Chandigarh	2
Pondicherry	Pondicherry	1

Source: NHB records
Note: This table is not entirely up to date as it lists only 105 of the 136 branches recognized HFCs operate.

Figure 2.4: Branch Locations for Recognized HFCs



Source: NHB Records

Companies are reluctant to enter the regions in the east and north for several reasons. The transportation and communication systems are frequently poor, which increases transactions costs and decreasing branches' potential geographic scope. These areas have experienced considerable social unrest. Finally, in some areas, clear land tenure is difficult to establish because tribal roots are strong and/or there is a high prevalence of extended families sharing a common dwelling. Even so, the NHB believes that HFCs can operate profitably in these areas and buttresses its argument by pointing to the success SBI HFC has attained serving several medium sized towns in the far east.

The NHB encourages expansion to smaller cities and the northern and eastern regions of the county by educating companies regarding the opportunities in these areas. The NHB has also informed HFCs that it will take equity positions with reputable firms willing to enter neglected areas.

2.3 Conclusion

While the overwhelming majority of formal housing finance continues to be done outside the HFC industry, the HFC market segment is growing extremely rapidly. The number of HFCs has grown from approximately 30 in 1988 to 250 or more in 1991. The majority of these firms are very small and a large number of officially registered HFCs may in fact be defunct or not engaged in long-term housing finance. Nevertheless, powerful financial enterprises are also becoming involved in the field. Over the last several years, eight major commercial banks and the nation's two giant insurance companies have aggressively entered the market.

Since the program began in 1989, the NHB has recognized 16 firms and is in the process of recognizing two more.

The explosive growth this industry has experienced in recent years is attributable to a number of factors. HDFC has definitively proven that HFCs can be extremely profitable, and the GOI has signaled through a variety of direct and indirect means that it wishes to target the housing finance sector. Finally, low barriers to entry and exit make this an easy field for small entrepreneurs to enter.

The same factors that have contributed to industry growth in the past will continue to attract new firms into the field in the near future, * expansion increasingly taking place in smaller cities as the metropolitan markets become saturated. The pace of market growth will be determined primarily by firms' ability to mobilize resources. This issue is discussed in the next chapter of this report.

Firms initially establish branches in one or several metropolitan cities, but most branch expansion is taking place in cities with populations below one million. Firms are moving into smaller cities, because there is less competition there and housing is more affordable for prospective borrowers. HFCs now exist throughout the country, although there are still relatively few in the northern and eastern regions of the country. Overall, branch growth has been very rapid. NHB recognized firms alone have increased their total number of branches from 51 in 1988-1989 to 136 in 1990-1991, an annual increase of 63 percent.

3. HFC Performance

Bank performance involves balancing risk and return. It is also influenced by the social goals government often set for financial institutions. U.S. financial institutions, for example, must meet the social goals of the Community Reinvestment Act, which encourages lending to low-income households and in poor neighborhoods. In India, the NHB regulation and refinancing programs favor "the small man first."

This chapter evaluates HFC performance using data on nine principal HFCs recognized by the NHB to participate in its refinancing program.[1] Not all of the nine provided complete data. Missing data are noted. Four progress indicators are examined: loan growth, increased lending to below median-income households, resource mobilization, and profitability.

3.1 Introduction to Principal HFCs

Data were provided to the NHB from Can Fin Homes (Can Fin), Dewan Housing Finance Company (Dewan), Gujarat Rural Housing Corporation (GRUH), Housing Development Finance Corporation (HDFC), India Housing Finance Development Ltd. (IHFD), Life Insurance Corporation Housing Finance Ltd. (LIC HFC), Parshwanath Housing Finance Corporation (PHFC), Saya Housing Finance Company (Saya) and Sate Bank of India Housing Finance Ltd. (SBI HFC). Table 3.1 Provides some basic information about these firms.

[1] The evaluation team accepted that the HFCs' representations were accurate and did not attempt to verify information by directly reviewing accounting records or loan files.

TABLE 3.1
BASIC FACTS ABOUT HFCs EVALUATED

name	number branches	year founded	loans originated fiscal 1990-1991	affiliate
CAN FIN	24	1987	21,400	Can Fin Bank
DEWAN	12	1984	3,911	none
GRUH	2	1986	3,051	HDFC
HDFC	25	1979	115,906	none
IHFD	16	1986	1,256	none
LIC HFC	16	1989	18,245	LIC Insurance
PHFC	1	1986	1,119	none
SAYA	1	1985	3	none
SBI HFC	10	1988	6,878	SBI Bank

Source: NHB records

Dewan, GRUH, HDFC, IHFD, PHFC and Saya are independent firms without "parent" companies in other financial sectors. HDFC is by far the oldest and largest HFC. In fiscal 1990-1991, it originated 64 percent of the total loans sanctioned by the nine HFCs listed in Table 3.1. In 1986, HDFC helped establish GRUH and GRUH's general manager is secunded from HDFC. GRUH, designed as a model to prove the viability of undertaking housing lending in rural areas, operates almost exclusively in rural Gujarat. Founded in 1984, Dewan is the second oldest major HFC. It is owned and operated by the Wadhawan family. Saya is suffering from a critical lack of capital and originated only three loans in 1990-1991. The firm plans to obtain loan capital through the NHB refinancing program and use these funds to greatly increase its lending in the coming fiscal year. PHFC is affiliated with a developer group which specializes in projects for group housing societies. IHFD is also linked to a construction firm. Both PHFC and IHFD cater almost exclusively to middle- and low-income families.

In contrast to these firms, Can Fin Homes, SBI HFC and LIC HFC have very close ties to huge financial institutions. Can Fin and SBI are subsidiaries of banks bearing the same name. LIC HFC is the subsidiary of India's huge Life Insurance Company. These three HFCs are able to draw heavily on their parent companies for personnel, facilities and low-cost capital.

3.2. Loan Growth and Industry Concentration

Lending by the nine principal NHB-recognized HFCs has increased rapidly since 1988. Concurrently, the industry has become less concentrated. Average loan sizes have increased but at a level somewhat below the inflation rate. This section examines these trends in more detail.

<u>3.2.1 Growth of Sanctioned Loans</u>. For eight of the HFCs reviewed, sanctioned loans have increased at a very rapid rate over the last several years.[2] Table 3.2 details these firms'

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[2] Analysis of loan growth over the period excludes LIC HFC because it was not operating in 1988-1989. LIC Insurance was involved in housing finance at that time, and information on the volume of lending through the parent company is available. However, since not all parent company lending is currently being channeled through the HFC, it is not possible to compare housing lending by the parent company in 1988-1989 to lending by the HFC affiliate in 1990-1991. It would also be misleading to assume that LIC HFC had no loan volume in 1988-1989.

When interpreting the growth statistics, readers should bear in mind that LIC HFC is lending growth rates.

TABLE 3.2
GROWTH OF SANCTIONED LOANS FOR EIGHT HFCs: 1988-1989 TO 1990-1991

compound annual growth rate (percent)

	number of loans	volume of loans
including HDFC	44	47
excluding HDFC	113	116

Source: NHB Records

In all, these firms sanctioned 74,554 loans in 1988-1989. Lending grew at an annual rate of 44 percent over the period such that in 1990-1991 the group approved a total of 153,524 loans. If HDFC is excluded from this analysis, total loans increased from 8,311 in 1988-1989 to 37,669 in 1990-1991.

3.2.2 Growth in Loan Disbursals. Growth in the volume of loans disbursed has been slightly faster than growth in loans sanctioned. However, in 1990-1991, volume of loans disbursed for seven recognized HFCs represented only 83% of the volume sanctioned. Table 3.3 delineates the growth of loans disbursed and sanctioned from 1988-1989 to 1990-1991.

currently an important player in the HFC industry. In 1990-1991, the company sanctioned 18,245 loans. For the nine principal HFCs evaluated in this represented 13.6 percent of total loans underwritten and 38.8 percent of all non-HDFC loans sanctioned.

TABLE 3.3
LOANS SANCTIONED VERSUS LOANS DISBURSED FOR SEVEN RECOGNIZED HFCs

	compound annual growth rate 1989-1990 to 1990-1991		Ratio of volume disbursed to volume sanctioned	
	volume sanctioned	volume disbursed	1988-89	1990-91
including HDFC	47	53	75	83
excluding HDFC	116	148	63	84

Source: NHB records

There are several reasons why volume of loans disbursed is significantly below volume sanctioned. There is always some time gap between loan approval and disbursement. Thus, when finance companies are growing rapidly, it is natural that their volume of sanctioned loans will consistently exceed their volume of dispensed funds. Furthermore, in contrast to customary U.S. practices, loans in India are generally approved early in the loan process based on credit and income information, and disbursed later when clear title and other security is obtained. Finally, operating procedures generally become more efficient as a company matures. Thus, as companies gain more experience, their ability to disburse funds in a timely way improves. The fact that the ratio of disbursed to sanctioned funds has grown over the last several years suggests that this is happening to HFCs.

64

3.2.3 Industry Concentration. Over the past three years, industry concentration has declined rapidly. HDFC is not only the oldest HFC. It is also by far the largest. In 1988-1989 it had an 89 percent share of the total volume of loans sanctioned by the eight recognized HFCs for which data were available. This share had fallen to 75 percent by fiscal 1990-1991. When HDFC is excluded, the share of the next largest HFC--Can Fin--declined from 72 percent to 65 percent over the same period.

3.2.4 Factors Driving Industry Growth and Deconcentration. Multiple forces have contributed to these spectacular growth rates and to the deconcentration of the housing finance industry. These include incentives for new firms to enter the field and, for existing firms, resource mobilization efforts, aggressive geographic expansion and some marketing innovations.

Chapter 2 contains a detailed analysis of factors contributing to growth in the number of HFC industry participants. To summarize briefly, HDFC's returns on equity above 30 percent have proven that housing finance can be lucrative. The HDFC demonstration effect has inspired many banks and large financial groups to form HFC subsidiaries. The ease of creating an HFC has also facilitated entry into this industry. And financial players viewed GOI's founding of the NHB as a signal that the housing finance sector would be given special attention in the future.

In the past, Indians have had severely limited access to formal housing finance; yet homeownership is highly valued. Not surprisingly, HFCs report that the effective demand for their loans is great and increasing, despite economic uncertainties and rapidly escalating housing and land prices. In this context of great demand, the key to HFC growth is their ability to mobilize resources. As the next section details, HFCs have succeeded in mobilizing funds from a variety of sources in the past three years.

Some HFCs have displayed considerable energy and ingenuity in marketing their loans, and the expansion of HFCs into new geographic regions has greatly broadened their market. Creativity in finding new financing options has also played a role. For example, several HFCs use the tactic of approaching large companies accustomed to using operating funds to finance subsidized housing loans for their employees. The HFCs offer to take over the financing of these loans. This allows the companies to use a much smaller portion of their capital to write down the interest rate on these loans. Such offers have proven very attractive to firms.

It should be kept in mind that HFC growth started from a small base. The eight HFCs discussed above sanctioned only 74,554 loans in 1988-1989, compared to 153,524 in 1990-1991.

3.2.5 Trends in Average Loan Sizes. Average loan sizes have been increasing over the last several years. Nevertheless, their growth rate has been substantially below the inflation rate, and loans under Rs. 50,000 still account for more than one-third of the total number of loans sanctioned. From 1988-1989 to 1990-1991, average loan size for the nine surveyed HFCs grew at an average annual rate of 4.2 percent. This compares with inflation rates of 8 to 11 percent.

The factors accounting for slow growth in average loan size are essentially a subset of those accounting for lending to below median income families. These are detailed in chapter 4 of this report. To briefly summarize, these factors include market and NHB-generated incentives. Market incentives stem from the fact that formal housing finance has been geared historically towards making relatively large loans to affluent families in the largest cities. Thus, the greatest potential for market expansion lies in serving middle-income families in mid-sized and smaller towns, where housing is relatively affordable for this group. NHB-provided incentives to make relatively small loans include concentrating the benefits of its refinancing program on loans for smaller units and loans for under Rs. 150,000, and inducing firms to expand geographically into mid-sized and smaller towns, where there is considerable demand for small loans.

3.3 Increased Lending to Below-Median Income Households.

Chapter 4 details the experience of the HFCs in lending to below-median income households. To briefly summarize, the limited data available indicate that the HFCs have increased their lending to households with incomes below the median level somewhat faster than total lending has grown over the last three years. As total lending by eight of the nine surveyed HFCs has grown at a rate of 44 percent per year since 1988-1989, exceeding this pace is a considerable accomplishment. (LIC HFC is excluded because of incomplete data as explained in footnote 2 of this chapter). While lower income families have been increasingly priced out of the market in metropolitan areas, the HFCs have augmented their share of total loans going to this group by opening branches in smaller cities and marketing loans in rural areas.

3.4 Resource Mobilization

HFCs have raised liabilities in five main forms: equity, deposits, term loans, capital market issues, NHB refinancing, and loans from extra-national bodies. Table 3.4 details the distribution of these liabilities for eight HFCs and Figure 3.1 displays this distribution graphically.

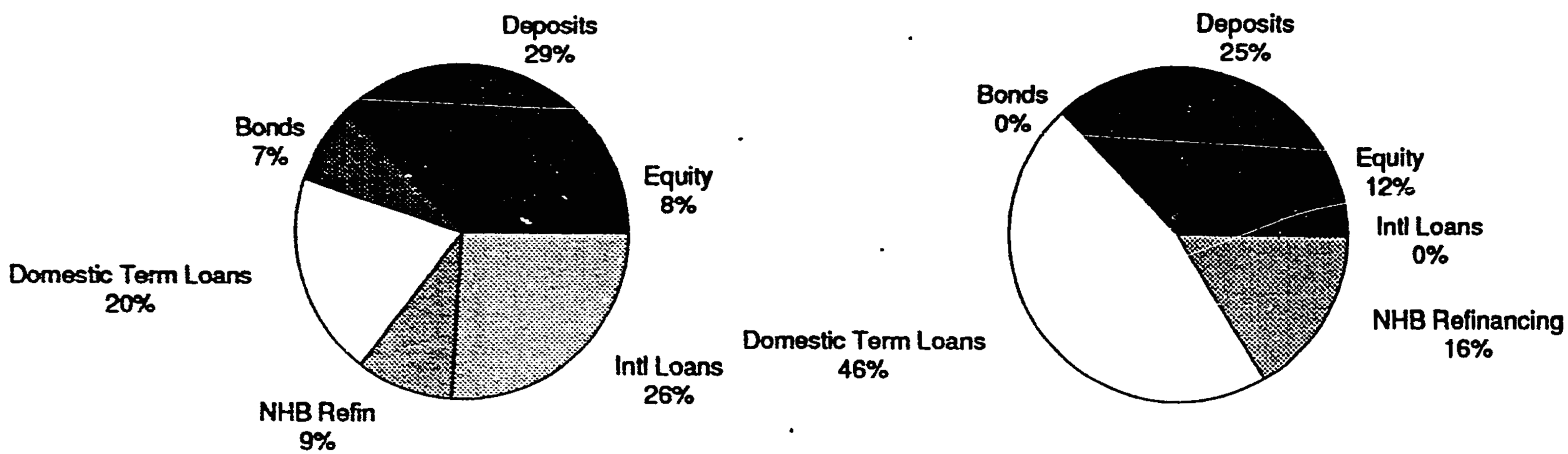
TABLE 3.4
COMPOSITION OF LIABILITIES OF EIGHT RECOGNIZED HFCs, 1990-91
(PERCENT DISTRIBUTION)

type of liability	share including HDFC	share excluding HDFC
equity	8.5	12.5
deposits	29.0	24.6
bonds	7.4	0.0
domestic term loans	19.7	46.6
NHB refinancing	8.4	16.4
extra-national loans	26.0	0.0

Source: NHB Records

The above distribution shows that for the eight HFCs included in the table, deposits, domestic term loans and international borrowings have each supplied 20 to 30 percent of the firms' capital. Individual firms have relied on very different strategies for funds mobilizing however. Can Fin, which has close connections through its parent company to many large corporations, has mobilized 57 percent of its funds through corporate deposits. LIC-HFC and

Figure 3.1
Recognized HFCs' Capital Composition
Fiscal 1990-1991



Share Including HDFC

Share Excluding HDFC

Source: NHB Records

SBI are joint sector HFCs with powerful parent companies. These firms have respectively raised 85 percent and 70 percent of their capital through relatively low cost term loans from their affiliates. Dewan, GRUH, IHFD and PHFC, are small, private HFCs with little or no access to corporate deposits or affiliate company term loans. They have become extremely dependent on NHB refinancing and currently NHB's refinancing program accounts for more than 50 percent of total resources for each of these firms. Since HDFC is by far the oldest, largest and most respected of the eight HFCs surveyed, it is not surprising that this firm has been most successful at diversifying its resource base. HDFC is the only HFC to have floated a bond offering or accessed international capital markets. Deposits and international loans each account for approximately one-third of HDFC's total funds, domestic loans account for 14 percent of funds. The capital composition of eight of the surveyed HFCs is shown in Table 3.5 and discussed in more detail in the rest of this section.

3.4.1 Deposits. In most countries, deposits, particularly household deposits, are the major source of the housing finance industry's low-cost, stable funds. Household and organizational deposits represented 29 percent of the capital of the eight principal HFCs approved for the NHB refinancing program in 1991. Without HDFC, this share drops to 25 percent.

Thus, for the HFCs surveyed, the average share of deposits in liabilities and equity is relatively low by international standards. However, the share of deposits in the total liabilities of individual HFCs varies greatly, as Table 3.5 indicates.

70

TABLE 3.5
CAPITAL COMPOSITION
OF EIGHT RECOGNIZED HFCs, 1990-1991

company	equity % funds	deposit % funds	bonds % funds	domestic term loans % funds	external sources % funds	NHB refinance % funds
CAN FIN	7.5	57.0	0.0	16.1	0.0	19.4
DEWAN	15.8	8.0	0.0	8.4	0.0	67.8
GRUH	13.4	0.0	0.0	35.1	0.0	51.6
HDFC	7.6	30.0	9.0	13.7	31.8	7.8
IHFD	26.4	2.9	0.0	14.1	0.0	56.6
LIC	14.9	0.0	0.0	85.1	0.0	0.0
PHFC	31.0	0.0	0.0	5.2	0.0	63.8
SAYA	NA	NA	NA	NA	NA	NA
SBI	19.8	0.0	0.0	74.0	0.0	6.3
TOT W/ HDFC	8.5	29.0	7.4	19.7	26.0	9.4
TOT W/O HDFC	12.5	24.6	0.0	46.6	0.0	16.4

Source: NHB Records

The two largest HFCs--HDFC and Can Fin--raised 57 percent and 30 percent of their liabilities in deposits respectively. Yet, Can Fin projects that its share of deposits in total liabilities will drop by 10 percent in 1991-92. Of Can Fin's and HDFC's total deposits, roughly 75 percent are organizational deposits and only 25 percent are from households. (Leaving aside Can Fin and HDFC, the picture changes dramatically--the share of deposits in total liabilities for the other HFCs averaged only 0.8 percent. Four of these firms collected no deposits at all.)

A number of factors help explain this extremely low figure. Some of these HFCs, such as LIC HFC and SBI HFC have had easy access to subsidized loans from parent companies and so have had no incentive to attempt to mobilize funds from other sources. As the organizations grow, however, they will not be able to continue to rely on affiliate term loans to cover all their capital needs. Indeed, both LIC HFC and SBI are now beginning to seek other sources of funds. Branches, which take time to develop, are also necessary to secure household deposits. The low share of deposits in total liabilities represents a serious resource mobilization problem for HFCs which requires examination.

On the surface, India would appear to have great potential to fund shelter through household savings. India has a savings rate equal to 22 percent of GDP--far above that of other developing countries and well above that of all but a few industrialized nations (Buckley, 1990). As the Indian population is still predominantly rural, a large proportion of these funds is held in rural areas, where cultural and communications barriers have tended to block access. India's Post Office savings system has succeeded in mobilizing some of these funds, holding about one-third of total national savings at interest rates of approximately 5 percent. In contrast, the competition for savings in urban areas, where people are accustomed to participating in the commercial economy, is fierce. The two overall strategies available to HFCs for mobilizing household deposits are to compete in the urban and commercial economy at higher rates, or to extend their reach to rural areas and to the informal economy.[3]

All HFCs interviewed felt the following were significant barriers inhibiting their ability to secure deposits: 1) differential tax treatment between deposits with HFCs and those

[3] Tapoban, a company that has had considerable success with the latter strategy, is discussed later in this chapter.

12

with banks,[4] 2) the RBI-mandated maximum interest rate, currently 14 percent, 3) the RBI-mandated 24-84 month term on deposits and 4) the NHB requirement of a maximum 2 percent commission to be paid for securing deposits.

Some barriers affect joint and private HFCs to different degrees. HFCs in general, but particularly private firms, lack public trust. Various well-publicized scams and bankruptcies have made the investing public leery of trusting their savings to private investment companies. Joint HFCs linked with scheduled banks are able to partly allay this mistrust through their association with parent companies. The joint HFCs typically bear the name of their parent bank and often operate out of the same building or use the facilities of the bank to accept deposits. These joint HFCs can potentially attract considerable deposits, which have a minimum term of 3 months under RBI regulations, from organizations such as universities, public authorities, and labor boards: Can Fin's ability to raise 57 percent of its funds in deposits largely from such organizations is noteworthy. In addition to competitive interest returns, personal and business contacts are important in securing these organizational funds (Diamond, 1989). Private HFCs can attempt to tap the same capital sources; in practice however, public mistrust and a lack of business contacts stymie many private HFCs' efforts to attract deposits of any type. As many private HFCs lack the track record necessary to issue debt and access external sources, their only other potentially significant sources of funds are NHB refinancing and equity infusions from their promoters.

On July 1, 1989, the NHB launched a program, the Home Loan Account Scheme

[4] Tax on interest revenues earned from HFC deposits is automatically deducted and individuals must apply for a refund in order to recover it. Tax is not automatically deducted from interest received on bank deposits.

(HLA), with the potential to assist financial institutions in mobilizing deposits for housing. If a participant in this scheme saves for five years, he or she is entitled to a housing loan several times the size of the accumulated savings. Initially, NHB extended the right to use the HLA only to commercial banks. Recently, however, six HFCs have been authorized to accept HLA deposits. The results have been unimpressive for commercial banks partly because these institutions lack an incentive to market the scheme. The HLA program has more potential for HFCs because it fits their business of housing lending. Yet the narrow focus on households willing to save and wait five years for a home loan limits its market.

The experience of a small number of HFCs not approved by NHB for refinancing contrasts with HFC difficulty in mobilizing household deposits. Since its inception one year ago, one of these organizations, Tapoban Housing Finance Limited, has mobilized Rs. 40 crore from the public. These funds total 66 times its equity, far exceeding the legal maximum. The company circumvents this regulation by considering these funds "security deposits" for future home loans. The organization has 30,000 field representatives, mostly in rural areas, who are paid substantial commissions to raise funds, usually based on their personal relationship with potential depositors. The company pays rates on these funds below those available in urban areas, although above those available on the postal savings accounts that rural savers often use. The financial viability of this company is untested and some of its financing schemes, such as a "no-interest" loan, are suspect. They may have found a solution to the problem of resource mobilization, but such companies represent a critical regulatory challenge to NHB.

3.4.2 Domestic Term Loans. Domestic term loans, which typically have a maturity of at least a year, represent 20 percent of recognized HFCs' capital overall. Without HDFC, this share rises to 47 percent. As Table 3.5 indicates, share ranges from 5 percent for PHFC to 85 percent for LIC HFC, whose liabilities derive almost entirely from term loans from its parent life insurance company.[5] Joint HFCs often receive term loans at concessionary interest rates from their parent organizations. For example, two joint HFCs are currently paying 12.8 percent on loans from their parent banks, although HDFC must pay 16 to 17 percent on term loans and HFC management maintains that market rates have fluctuated between 15.5 to 18 percent in the recent past.

HFCs with access to these low cost funds use them extensively. However, the HFCs that must pay the market rate of return for these funds are limited in their ability to undertake term loans, because the cost of these funds exceeds the interest rate on loans below Rs. 200,000 in size.

3.4.3 Capital Markets. HDFC is the only HFC to issue bonds to finance housing. As Table 3.5 indicates, this source of funds constitutes 9 percent of the organization's total funds. A number of other HFCs are now considering bond issues. Various problems surround bond underwriting, however, including a three percent stamp duty. Even if these problems are solved by legislation, the difficulty of finding a market niche at rates that bear a reasonable relation to HFC lending rates remains.

3.4.4 Equity. A number of newly established HFCs have depended on the equity contributions of their promoters to start lending. However, this dependence has decreased as

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[5] LIC HFC has recently begun to make use of the NHB refinancing program.

most of the HFCs have succeeded in leveraging their funds. Indeed, equity currently accounts for only 8.5 percent of the total capital of the eight surveyed HFCs, 12.5 percent if HDFC is excluded from consideration. As Table 3.5 demonstrates, equity accounts for no more than 31 percent of any individual firm's capital.

Overall, the weighted[6] average debt-to-equity ratio of seven of the HFCs for which data are available[7] increased from 2.5 in 1989-90 to 6.6 in 1990-91 if NHB refinancing is not counted as debt. If NHB refinancing is counted, their average leverage increased to 8.2 in 1990-91. HDFC had a debt-to-equity ratio of approximately 15.4 from 1988 to 1991. However, the company recently issued a large equity offering, reducing its current ratio to 12.2.

3.4.5 External Sources. As Table 3.5 indicates, HDFC is the only firm that has been able to secure international loans. The firm has obtained disbursements or commitments to date of over $415 million in international credit. However, the potential for other HFCs to access international capital markets is limited. HDFC was initially able to obtain its international funds due to its pioneering role as India's first financial institution dedicated to the provision of housing credit. It was subsequently able to mobilize overseas capital based on its outstanding track record, large size and internationally respected management team. Other HFCs cannot position themselves as worthy experiments; and, they lack HDFC's international recognition and sterling operating history.

[6] Each firm's debt to equity ratio weighted by its volume of lending.

[7] Can Fin, Dewan, GRUH, IHFD, LIC, PHFC, and SBI.

3.4.6 NHB Refinancing. As of March 1991, NHB had provided 16.4 percent of capital for surveyed HFCs excluding HDFC. Although a modest share of the overall total, NHB refinancing has been instrumental to the growth of a number of smaller, private HFCs, allowing them to leverage their equity and attain a minimum level of profitability. As Table 3.5 illustrates, generally, NHB has been the only substantial source of non-equity funds for the private HFCs excluding HDFC, and now accounts for from 52 to 68 percent of total capital for four firms. Dewan's 800 percent growth in loans over the past two years has been funded almost entirely by NHB refinancing and "ad hoc" finance. For the joint HFCs more able to raise funds from other sources, the NHB has so far contributed only modestly to total funds--6.3 percent for SBI and 19.4 percent for Can Fin. Yet, as the competition for other sources of funds increases, joint HFCs are turning increasingly to the NHB. For example, Can Fin, which has had the best record of independently mobilizing resources after HDFC, expects to increase its dependence on NHB to 32 percent in 1991-92. Other joint HFCs project a much higher degree of dependence on the NHB.

3.5 Profitability

Rate of return on equity (ROE) is the most commonly used overall measure of banks' profitability. If HDFC is excluded, the weighted average after-tax ROE for surveyed HFCs with data[8] has increased from 3.9 percent in 1988-89 to 22 percent in 1990-91 primarily because these HFCs have succeeded in leveraging their capital. With inflation running at 11.7 percent in 1990-91, 15-20 percent is the minimum long-term return acceptable to

[8] Can Fin, Dewan, GRUH, IHFD, PHFC, and SBI.

investors. Thus, as a group, the HFCs surveyed have surpassed the minimum acceptable level of profitability. However, the after-tax ROE of these companies ranges widely - from 9.9% for PHFC to 26.4% for Can Fin. For established firms to maintain their profitability and for new companies to improve theirs, HFCs must continue to leverage their equity. Yet, the rapidly escalating cost of funds limits firms' ability to access capital on terms that permit a survivable spread between borrowing and lending rates.

3.6 Risk Indicators

Lending involves four types of risk: underwriting and credit risk, interest rate risk, liquidity risk, and capital risk. The ability of HFCs to deal with these risks depends largely on the quality of management.

The managing directors and some other management staff in joint HFCs customarily are seconded from the HFCs' parent organizations. While this practice generally insures that senior staff have substantial experience in bank management, it also creates potential problems. If management know that tenure with an HFC will be short, they may be tempted to employ strategies that yield short-term gains but have negative long-run implications for their firm. Furthermore, anecdotal evidence indicates that at least one joint sector financial institution may be using their HFC affiliates as a "dumping ground" for senior staff they consider inadequate. If HFC management perceive their positions as evidence of corporate disfavor, they are unlikely to be motivated in their work.

The managing directors of the private HFCs have a much more varied background, ranging from construction companies to investment firms. They often have little or no

18

experience in lending aside from that garnered on the job in their own HFC.

3.6.1 Credit Risk. HFCs underwrite two types of loans: individual loans and developer and organizational loans. The credit risk firms face on each is different.

(a) Credit Risk on Individual Loans. Overall, the credit risk on individual loans is low, despite the lack of an effective foreclosure procedure (Urban Institute, 1989). HFCs operate on very slim profit margins, which are currently declining. Even a relatively modest delinquency rate can decimate company earnings. Furthermore, India lacks an effective foreclosure procedure. HFC management is very aware of the risk these factors pose and attempt to compensate by employing conservative underwriting and loan processing procedures. The factors affecting risk on individual loans are summarized below--for details, see Annex 3.1.

The average loan-to-value ratio used by the HFCs visited ranged from 51 to 75 percent. For the remaining equity in the property, HFCs verify the physical value-added in the case of construction projects and the borrower's sources of cash equity (downpayment). The maximum debt-service-to-net-income ratio ranges from 30 to 40 percent. Guarantors are required on 70 to 100 percent of loans, depending on the company. The loan term is short, varying with the age of the borrower from 7 to 20 years. Loans over a certain size require approval from higher levels in the company.

These conservative procedures have kept arrearage rates low. The Office of Thrift Supervision defines the non-current loan rate for Savings and Loans as the volume of loans past due 90 days or more divided by the volume of total loans outstanding. In the United States over the past year, the non-current loan rate for the Savings and Loan industry has

19

ranged from 1.6 to 1.9 percent.[9] Of the seven HFCs for which data were available,[10] all expect GRUH had non-current loan rates substantially below the U.S. average,[11] ranging from 0.01 to 0.4 percent.

This repayment record is very strong by U.S. standards. Also, it compares favorably with rates from housing finance systems in other developing countries and contrasts with the dismal record of widespread defaults in other sectors in India, such as agriculture. Delinquency rates may rise as the industry ages. Many companies are so new that there has not been time for a significant percentage of their loans to become seriously overdue. Furthermore, even older firms have been growing so rapidly that loans old enough to develop serious delinquency problems represent only a small portion of their total portfolio.

HFC management feel that the main credit risk on individual loans in the future is a systemic one--that poor underwriting or collection procedures of one or a few HFCs will prompt their borrowers to default, and that this contagion will spread to other HFCs as borrowers come to believe that housing loans, like agricultural loans, need not be taken seriously. This risk is essentially a regulatory issue.

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[9] Source: June 12, 1991 news release by the Office of Thrift Supervision.

[10] Can Fin HFC, Dewan, GRUH, HDFC, IHFD, LIC HFC and SBI HFC.

[11] For GRUH this figure is 2.36 percent. There are a number of reasons why GRUH has late payment rates in excess of the HFC average. Since many GRUH borrowers are farmers, they sometimes delay payment until crops have been harvested. In addition, for many borrowers, making repayments involves considerable transactions costs. Thus, they often prefer to pay larger amounts at less frequent intervals. Finally, in comparison to customers of other HFCs, GRUH borrowers are less likely to have telephones and more likely to live a considerable distance from the HFC office. Thus, making contact with delinquent customers and bringing pressure to bear on them is more difficult and time-consuming. Even so, the firm has only one account overdue by more than one year.

(b) Credit Risk on Developer Loans. Although credit risk is low on individual loans, HFCs are allowed to invest 25 percent of their assets in investments that do not qualify under NHB guidelines. These funds are often invested in high-yield bridge loans to developers. In addition, NHB has recently initiated a program to refinance land development loans made by HFCs. To date, public agencies have accounted for most of the demand for these land development loans. Nevertheless, private developers have recently submitted to the NHB proposals for a considerable volume of these credits. The NHB land development program provides 100 percent financing for public agencies and cooperative housing societies, and 80 percent financing for private developers.

In the United States, developer loans almost invariably carry a much higher risk than loans to individuals since there is always the risk that by the time homes are constructed demand will have temporarily declined, making it difficult for the borrower to find a market for his or her units. It is largely for this reason that so many U.S. savings and loans associations (S&Ls) are in considerable financial distress. To date, the Indian housing market has been considerably less volatile than its U.S. counterpart. Nevertheless, management at SBI HFC and Can Fin HFC agree that developer loans are riskier than loans made for single family dwellings. An additional risk in the underwriting of developer loans is that many HFCs lack the technical staff to evaluate large infrastructure projects.

The land development program potentially serves low-income households. But this benefit must be weighed against the added risks. The borrowers would often be public agencies; but local authorities have frequently fallen behind on obligations to other public bodies and may well do so on loans from HFCs. Local infrastructure and land development credit is a difficult business, usually handled in developing countries by institutions dedicated to this purpose. In India, HUDCO performs this role. Despite such specialization, these organizations customarily have an unsatisfactory record of cost recovery, seldom operate on a market basis, and continually require subsidy injections from government. The NHB can help HFCs reduce the risk of undertaking these loans by providing technical assistance and training in this area.

3.6.2 Interest Rate Risk. Maturity mismatch between assets and liabilities afflicts many housing finance systems. This problem continues in the United States, for example, even after the housing finance traumas of the 1980s.

In India, interest rate risk has not been a problem in the past, mainly because the RBI has maintained relatively stable interest rates (Wilson, 1988). However, financial liberalization will bring greater swings in both the cost of liabilities and the return on assets.

As interest rates have risen in 1990-91, interest rate risk has fast become a major concern for HFCs. The management of the joint HFCs visited, approach the interest rate risk problem by making annual projections of the interest spread between the cost of resources and the return on assets. The spread is then recalculated on a quarterly or monthly basis, sometimes for the different regions of the HFC's operation, and used to correct funds mobilization and lending strategies as needed. None of the mathematical tools used to measure interest rate risk (such as interest gap or duration) are applied. Rather, management looks at the figures and makes its decision on "hunches", as one managing director of a joint HFC put it. Some private HFCs employ interest rate exposure analyses similar to those used by the joint HFCs; however, one private HFC's managing director interviewed said that his

8V

organization did no interest rate risk analysis whatsoever.

The managers of joint HFCs are in close touch with the organizations that hold their major liabilities, and often have some control over the cost of those liabilities. For example, Can Fin and SBI have been able to hold down the cost of term loans from their parent bank to 12.75 percent in an environment that now demands from 15.5 to 18 percent. However, as financial liberalization continues, their ability to influence the cost of their liabilities will decrease. Furthermore, private HFCs have no ability to influence the cost of funds.

On the asset side, the problem of managing interest rates is different for existing and new loans. The bulk of existing assets are individual housing loans whose interest rates are mandated by the NHB. Although these loans have a provision for the interest rate to be raised if the NHB so authorizes, this has yet to be done. Furthermore, the consequences of raising the interest rate on outstanding loans are unpredictable. Individual borrowers are unprepared for such an increase, which may be widely ignored or prompt defaults. Squeezed by the increasing cost of their resources, some HFCs are exercising the option to raise interest rates on existing loans to developers and companies; however, they are reluctant to employ this strategy for extant housing loans to individuals.

For new loans, the main option for dealing with rising costs is to stop extending credit that can neither be sold to NHB nor made at suitably high interest rates--these are predominantly the loans for units larger than 40 square meters but for amounts smaller than Rs. 200,000. Loans financing small units can be sold to NHB and larger loans carry competitive rates. Particularly because the demand for larger loans is limited, HFCs are increasing their reliance on NHB refinancing to fund smaller loans.

97

Overall, interest rate risk is manageable under current conditions. The principal danger is that term mismatches combined with rising resource costs will force HFCs to adjust the interest rate on existing individual housing loans. This step could possibly spark a rash of defaults which, once started, could spread rapidly given the lack of an effective foreclosure procedure. Currently this scenario is remote, although the danger concerns top management of some of the HFCs visited.

Given that interest rate risk is a relatively new and increasingly important area of concern for the Indian financial community, the NHB could provide technical assistance and training to HFCs in order to increase management awareness of this risk and illustrate ways in which firms can minimize their exposure.

3.6.3 Liquidity Risk. Liquidity is important to meet the demands of depositors and other commitments. The NHB imposes a liquidity requirement of 10 percent of deposits on HFCs. HFCs can meet this requirement through holding either cash or approved liquid assets, such as UTI investments, which currently yield 13 percent--equivalent to the average paid on deposits. HFCs have little difficulty meeting this liquidity requirement. The percentage of liquid assets for the HFCs for which data are available ranges from 16.6 to 28 percent. In comparison, the U.S. Federal Home Loan Bank, which regulates S&Ls, requires these institutions to maintain 5 percent of deposit accounts plus borrowings in liquid assets (Wilson, 1988).

3.6.4 Capital Risk. Capital serves to assure public confidence in the stability of a company and protects depositors and creditors against loss. To date, HFCs have been faced with too little debt to adequately leverage their equity rather than excessive liabilities.

84

However, debt-to-equity ratios for most surveyed HFCs have increased rapidly over the last several years. The weighted average ratio for all surveyed firms with data (excluding HDFC)[12] increased from 2.5 in 1989-90 to 6.6 in 1990-91, if NHB refinancing is not counted as debt. If NHB refinancing is included in the analysis, their average leverage increased to 8.2 in 1990-91. HDFC had a debt-to-equity ratio of approximately 15.4 from 1988 to 1991. However, as noted earlier, the company recently issued a large equity offering and its current ratio is 12.2. Table 3.6 details the 1990-1991 debt-to-equity ratios for eight recognized HFCs.

TABLE 3.6
DEBT TO EQUITY RATIO
FOR EIGHT RECOGNIZED HFCs, 1990-1991

HFC	ratio of equity to total assets
CAN FIN	12.4
DEWAN	5.4
GRUH	6.8
HDFC	12.1
IHFD	2.8
LIC	5.7
PHFC	2.2
SBI	4.1

Source: NHB Records

Most HFCs have not yet had the opportunity to establish the level of financial stability and dependability HDFC has displayed over the last 10 years. Thus, they should probably not attempt to match HDFC's leverage ratio. Nevertheless, many firms can significantly increase

[12] Can Fin, Dewan, GRUH, IHFD, LIC HFC, PHFC, and SBI.

their debt without jeopardizing the financial health of their firms.

Furthermore, none of the firms surveyed are currently over-leveraged by U.S. standards. An equity-to-assets ratio of 6 percent is considered the minimum acceptable for banks and credit unions in the United States. The equity-to-total-assets ratio of the eight surveyed HFCs ranges from 7.5 to 31 percent.

Top management in most surveyed HFCs has a conservative attitude towards capital requirements. For example, Can Fin Homes, which has the highest debt-to-equity ratio of all HFCs, plans to double its equity soon.

3.7 Conclusion on Performance

The HFCs' record of loan growth and lending to below-median income households is impressive. Maintenance of this solid performance depends critically on the industry's ability to mobilize greater resources in the future.

Over the last three years, the HFCs reviewed have performed well overall in raising funds, leveraging equity, and reaching minimum profitability. Nevertheless, performance in these areas varies widely across companies. Currently, the increasing interest rates accompanying financial deregulation are constricting HFC access to affordable capital and are forcing the firms to rely more heavily on NHB refinancing.

Credit risk on HFCs' individual loans is relatively low. The industry's repayment record is excellent and should be guarded carefully in order to minimize the systemic risk of a chain reaction of defaults.

The credit risk on developer loans, including those under the NHB land development

96

program, is probably higher than that for individual home loans, and should be approached with caution. The NHB could help firms reduce the risk for HFCs of undertaking developer loans by providing the firms with technical advice and training regarding the underwriting and monitoring of these credits.

Interest rate risk is manageable at this time. Nevertheless, interest rate exposure is likely to become more dangerous over time, as India's capital market becomes more vulnerable to market conditions. Some HFCs could benefit from education regarding the dangers of interest rate exposure in a volatile capital market and possible techniques to measure a firm's vulnerability. Currently, the HFCs' main interest rate risk problem is the danger of having to raise rates on existing individual housing loans, which might provoke widespread defaults.

HFCs' liquidity and capital risks are low.

4. Participation by Households Below the Median Income[1]

This chapter examines HFC lending to below-median-income households over the last three years. It explores the causes for loan volume growth, the problems encountered in lending to this group, what the NHB has done to alleviate these difficulties and the effectiveness of NHB and USAID targeting of these households.

4.1 Growth of Loans to Below-Median-Income Households

Comprehensive data on lending to families earning below the median income were not available. Although most HFCs now tabulate this information, LIC Housing Finance still does not and Can Fin only began to do so as of October, 1990, and was not able to provide the data to the team in time to include it in this analysis. These two HFCs account for 27 percent of industry volume if HDFC is included and 76 percent of volume if HDFC is excluded. The team used loan size as a proxy for income for LIC HFC as this firm estimated that at least 90 percent of its loans under Rs. 50,000 were to borrowers whose monthly income did not exceed Rs. 2,200 per month. Yet even this information was available only for 1989-1990. The incompleteness of the data on lending to this market segment renders the following analysis only suggestive of actual lending patterns.[2]

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[1] For the period this report covers, urban median income ranged from Rs.2,000 to Rs. 2,200 per family per month.

[2] Annex 4.1 is a survey design that would enable AID to examine in a statistically reliable manner what percent of HFC loans for less than Rs. 50,000 have gone to below-urban median income households.

The limited data indicate that recognized firms have increased their lending to households whose income is below the median urban level at a somewhat faster rate than they have increased total lending over the last three years. This implies very rapid loan growth for this sector, as the total number of loans HFCs have made has increased by an average annual rate of 44 percent from 1988-1989 to 1990-1991. Total volume has increased by approximately 47 percent annually over the period. If HDFC data are included, loans to below-median-income households accounted for 21 percent of total loans sanctioned in 1988-1989 and 26 percent of sanctioned loans in 1990-1991. The volume of loans to this group grew from 18 percent to 20 percent of total volume over the same period. If HDFC data are excluded, the target group's share of total loans was approximately 35 percent in 1989-1990, and its share of total volume was approximately 21 percent. Table 4.1 summarizes available data on share of total loans to low-income households by recognized HFCs:

TABLE 4.1:
PERCENT OF TOTAL LOANS TO LOW-INCOME HOUSEHOLDS

loans to low-income as percent of total		
year	# loans	volume loans
1989-1990	21	17
1990-1991	26	20

Note: Data excludes Can Fin
Source: NHB Records

Thus, it would appear that the share of HFC loans to low-income borrowers is approximately one-quarter of total loans and that it has probably increased over the last few years. Discussions with HFC directors indicate that while low-income families have been

89

increasingly priced out of the market in metropolitan areas, firms have maintained or increased the share of their total loans going to this market segment because they have opened branches in smaller cities where homes are still relatively affordable to this group.

4.2 Incentives and Disincentives for Lending to Below-Median-Income Households

Firms' primary inducement to lend to below-median-income households is that these families represent the majority of India's unserved housing finance market. NHB incentives also encourage lending to this group, although some NHB regulations actually discourage firms from serving these families.

4.2.1 Market Incentives. HFC management at Can Fin Homes, Dewan, GRUH, LIC HFC and SBI HFC all stated that the primary reason target households account for a significant share of HFC loans is that these families represent an important share of the firms' effective demand. Historically, formal housing finance has served relatively affluent families. Thus, the greatest potential for market expansion lies in serving middle-income families - who have been excluded from the market in the past--in mid-sized and smaller towns--where housing is relatively affordable for this group. This point is substantiated by the fact that HFC branch growth over the last several years has been much faster in cities with populations below one million than in the metropolitan areas, but average loan sizes have been relatively constant.

4.2.2 NHB Incentives. The NHB has also played a role in encouraging lending to below-median-income families by providing HFCs incentives to make relatively small loans and loans for units under 40 square meters in size, and by instituting the Home Loan Account

90

Scheme.

(a) Restrictions on Loan Amount and Unit Size. The NHB's initial strategy concentrated benefits on loans of Rs. 50,000 or less. Specifically, the NHB originally provided 100 percent refinancing for loans up to Rs. 50,000 made for the purchase or construction of units under 40 square meters and loans up to Rs. 30,000 for upgrading and/or major repairs. Loans for semi-urban and rural homes were exempt from the 40 square meter requirement provided that the cost of the unit including land did not exceed Rs. 65,000. Urban loans for up to Rs. 100,000 were eligible for refinancing up to Rs. 50,000, provided that the unit's built up area was under 40 square meters.

Under the interest rate structure prevailing in the HFC market, families earning the median income (Rs. 2,200 per month) can afford to borrow Rs. 50,000 provided that they devote 30 percent of their gross income to housing payments and undertake a 20 year mortgage. Thus, the maximum refinancing amount under the program was only slightly higher than the maximum loan families with incomes below the median could afford. Requiring all units to either be less than 40 square meters in size or cost under Rs. 55,000 was intended to help prevent more affluent families from putting several small loans together to purchase a unit.

Since March 1990, the NHB has relaxed its refinancing requirements considerably. Currently, the NHB will refinance 100 percent of loans up to Rs. 200,000 for units under 40 square meters in size. Refinancing for units larger than 40 square meters is available up to Rs. 100,000, for units whose cost (including land) does not exceed Rs.150,000.

The NHB believes that relaxation of refinancing criteria was necessary. Staff maintain that housing costs were considerably higher than the maximum loan size eligible for refinancing when the program was initially implemented, and that since that time rapid housing cost inflation (especially in metropolitan areas) has further widened the gap. This conclusion appears accurate, but does not change the fact that median-income households can still only afford loans of Rs.55,000 or less.

Despite this relaxation of refinancing criteria, several of the smaller HFCs interviewed felt that the NHB program was a significant motivating factor behind their decisions to direct branch growth to areas where below-median-income households could afford to purchase units. Furthermore, one larger firm indicated that, as it became more dependent on the refinancing program, it too would find its lending decisions influenced by NHB targeting efforts.

(b) Home Loan Account (HLA) Scheme. While the HLA scheme is open to everyone, the NHB believes that it will prove particularly beneficial to households employed in the informal sector. The scheme requires households to save consistently over a period of several years. The NHB has pledged that, at the end of this period, it will refinance loans to these households based on a multiple of the amount they have saved.[3] The NHB does not require firms to lend to families who have participated in this program. But HLA participation will certainly increase the chances of informal-sector families receiving a mortgage loan. The primary impediments to HFCs' lending to this group are that these households' incomes cannot be definitively verified and that family earnings may be extremely variable. The HLA program provides a means whereby these families can demonstrate that they are capable of

[3] See Annex 1.4 for a complete description of this program.

qv

mobilizing a fixed amount of resources on a consistent basis.

The scheme creates substantial contingent liabilities for the NHB (see chapter 6 of this report). Thus, it would be useful for the NHB to collect demographic data on program participants in order to assess whether the program is serving intended beneficiaries.

4.2.3 NHB Disincentives. Unfortunately, NHB regulations also create two disincentives for lending to lower-income households.

(a) Interest Rate Spreads. The NHB maintains that the interest rate spreads between the rates HFCs may charge borrowers and the rates at which the NHB will provide refinance provides an incentive for lenders to make small loans because this spread declines as loan size increases. Nevertheless, the system actually encourages HFCs to make loans for larger amounts (up to Rs. 200,000). While the spreads decline as loan size rises, the total profit HFCs make on the loan increases with size. Thus, a 1.5 percent spread on a loan for Rs. 50,000 will be more profitable than a 2 percent spread on a loan for Rs. 25,000. A loan of Rs. 200,000 will be considerably more profitable than a loan of any smaller size. Table 4.2 illustrates this point:

TABLE 4.2:
HFC PROFITS FROM REFINANCING BY LOAN SIZE

loan size (Rs.)	spread (%)	maximum profit (Rs.)
up to 25,000	2.0	500
25,001 to 50,000	1.5	750
50,001 to 200,000	1.0	2,000

Source: NHB Guidelines

93

(b) Front End Loan Fees as a Fixed Percent of Loan Size. NHB's Guidelines to all HFCs require that front end fees be less than or equal to two percent of the loan amount. Yet, the front end costs HFCs incur are relatively fixed over loan size. Thus, HFCs will recover more of their fixed costs from fees when loan sizes are larger. While this is a clear incentive for HFCs to make larger loans, HFCs interviewed differed in their opinions as to the seriousness of this problem. One maintained that it was a significant deterrent to lending to low-income families, while several others said that it did not significantly impact their lending decisions.

4.3 NHB Promotion of Affordable Loans to Below-Median-Income Households

It is not enough for firms to be willing to lend to low-income families. These households must also be able to afford loans. The NHB encourages HFCs to make their loan products affordable to lower-income households by creating a refinancing program and limiting access to firms that follow NHB's guidelines for allowable interest rates on loans. Table 4.3 details the rate structure firms must comply with in order to participate.

**TABLE 4.3:
INTEREST RATE GUIDELINES FOR FIRMS PARTICIPATING IN NHB'S REFINANCING PROGRAM**

loan size (Rs.)	interest (%)
up to 7,500	8.0
7,501 to 15,000	9.5
15,001 to 25,000	10.0
25,001 to 50,000	12.5
50,001 to 200,000	14.0

Source: NHB Guidelines

94

Furthermore, participating firms must charge total front end fees of two percent or less of loan amounts. If firms were free to set these fees they would incline towards fixing their absolute size regardless of loan amount--making these expenses more burdensome for lower income people than more affluent borrowers.

By inducing firms that control a large share of the market to conform to this interest rate and fee structure, NHB effectively sets the rates for the entire industry, since even firms not participating in the refinancing program must compete against participating firms for customers. However, the NHB's ability to control industry-wide rates is weakened by the fact that in most areas demand for loans far outstrips supply.

4.4 Difficulties Encountered in Lending to Below-Median-Income Households

HFC managers interviewed emphasized several major problems they face in lending to below-median-income households. The following is a description of these difficulties and a brief discussion of NHB actions that should play some role in mitigating them.

4.4.1 Repayment capacity is below the amount necessary to purchase a unit. A median-income family can currently afford to take out a loan for approximately Rs. 55,000.[4] There appears to be some discrepancy between HFC management reports on home prices and information in Buckley et. al (1989). The former claim that a loan for Rs. 55,000 is entirely insufficient to purchase a unit, even if the borrower is capable of making a very significant

[4] Assuming the household took out a 20-year mortgage loan and devoted 30 percent of gross income to monthly payments.

downpayment. However, even assuming that home prices have increased by 30 percent over the two years since the Buckley report was published, Buckley's findings imply that a loan of Rs. 55,000 in combination with a downpayment of 30 to 50 percent would be adequate to purchase a modest home in any of India's largest cities. On balance, it is likely that median income families can still afford to purchase basic units if they are able to amass very significant downpayments. Nevertheless, home prices are rising faster than incomes in India's largest cities, such that median-income families in large cities, will probably be increasingly priced out of the market.

The NHB is attempting to address this affordability issue via its relatively new Land Development and Shelter Scheme - which makes serviced plots and core units available to low-income families at affordable prices.

4.4.2 Increased Frequency of Late Payment and Default. Most HFC managers interviewed said that low-income households are more likely than other households to be in arrears on loans. One HFC had actually calculated that below-median-income households had a 10 percent higher late payment rate than households with higher incomes. For several HFCs, the percentage of total loans that was in arrears was significantly higher than the percentage of loan volume which was late in making payments. To the extent that loan size and income are correlated, this implies that low-income families have poorer payment records. Nevertheless, in their evaluation of the Housing Guaranty 002 program, Buckley et. al (1989) did not find higher arrearage rates for HDFC borrowers.

Although there is little the NHB can do to induce low-income borrowers to pay promptly, it is working to reduce the cost of delinquency to lenders by attempting to instigate an effective foreclosure law. Lenders expressed the belief that enactment of such a law would significantly increase their willingness to lend to low-income households.[5]

4.4.3 Clear title is often difficult to establish. Low-income families are more likely to have informal land for which it is difficult to establish a clear title. Furthermore, this group often lives in extended families making it complex to establish who should hold the mortgage and assume repayment responsibility. In situations where land title and repayment responsibility are difficult to determine, HFCs generally refuse to issue credit.

4.4.4 Lack of Credit Record and Bank Experience. Low-income households generally do not have prior experience borrowing or interacting with formal financial institutions. Thus, they lack a proven commitment to loan repayment and some HFCs fear they will not take their obligation seriously.

NHB's HLA scheme provides a vehicle whereby families can demonstrate their ability and willingness to make regular financial contributions for the purpose of housing acquisition. Tapoban's program described in footnote 4 mitigates HFC risk from these factors.

[5] Tapoban Housing Finance (an unrecognized HFC) employs an interesting strategy for reducing the default risk associated with low-income lending. This HFC requires prospective borrowers to maintain a deposit account with the organization equal to 25 percent of the cost of the loan needed. This "security deposit" earns interest and is slowly devolved to the borrower from the seventh to the twentieth year of the loan repayment period. In this way the organization reduces both the risk of default and its loss in the event that default occurs.

97

4.5 Lending to Special Groups

In addition to the difficulties discussed above, which banks face when they lend to all low-income groups, other problems arise when financial institutions attempt to service particular low-income sub-markets. This section discusses the problems HFCs encounter in lending to these groups and, where possible, estimates the share of HFC loans going to these sub-markets.[6]

4.5.1 Informally Employed Households. Lenders maintain that issuing credit to informally employed households is a problem because it is difficult for HFCs to verify family income, and firms worry that these families will experience larger income variations than families who have more stable work. Indeed, some firms simply refuse to make loans to individuals who do not have either a "permanent" job or their own business. HFCs' estimates of the share of their urban borrowers who were informally employed varied from one to twenty percent. Based on data from EIU (1990), the team very roughly estimates that informally employed persons account for from 60 to 75 percent of the economically active population in urban areas.

As mentioned above, the NHB's HLA program provides a means whereby households

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[6] The following discussion is based on interviews conducted with management of Can Fin Homes, Dewan, GRUH, LIC HFC and SBI HFC.

Most lenders do not store data in a way that allows them to easily determine lending volumes by the sub-markets discussed below. Thus, information on these groups' participation in the credit market and the risks this type of lending poses is highly impressionistic. It is the team's understanding that the NHB has agreed to collect more information on the prevalence of lending to specific submarkets. It would also be very useful to compare the arrearage rates of these loans to those of more conventional borrowers.

98

in this group can demonstrate their credit-worthiness and reliability. LIC Housing Finance, which claims to have had significant success lending to this group, says that it sends underwriters out to observe micro-entrepreneur applicants at their workplace in order to obtain an impression of the viability of applicants' informal businesses.

4.5.2 Female Headed Households. Only one HFC was able to estimate the percent of loans it makes to female-headed households. Dewan calculated that approximately 7 percent of its loans were made to this group. Information on HLA account holders provides an indication of the number of women who are actively saving for the purchase of a home: 20 percent are women. However, housewives account for 8 percent of all account holders, so we can conclude that these unemployed women have opened accounts on behalf of their families with their husbands' resources. Thus, approximately 12 percent of HLA account holders appear to be women saving from their own incomes. Estimates of the number of female-headed households in Indian society vary widely from 10 to 33 percent of all households. [7]

In sum, we lack clear data on both the number of female-headed households in India who would potentially require a mortgage and the number of these families which have access to housing finance. However, it appears that from 7 to 15 percent of housing borrowers are women without husbands, compared with 10 to 33 percent of all Indian families.

[7] According to information provided to the evaluation team by USAID, the 1971 census estimated that approximately 10 percent of all Indian households were female headed. However, additional AID-furnished information referred to other, unspecified, studies estimating that female-headed households account for approximately 33 percent of rural households and 20 to 25 percent of urban households. Because this report is concerned with housing finance, it would be useful to know what percent of female-headed households are older widows, since very few of these women will require housing finance. Unfortunately, this information was not available.

Senior management at all the HFCs interviewed said that there are no disadvantages in lending to female-headed households, provided that these families have adequate incomes to meet repayment requirements. Several HFCs said that when mortgages were made out jointly to husbands and wives, repayment rates were better than when the loan was in the man's name only. Dewan Housing Finance and SBI Housing Finance, for example, actually require wives to be co-borrowers even if they do not work outside the home, in order to promote prompt payments.

4.5.3 Older Household Heads. The HFCs interviewed do not lend to families whose income earners are older than 55; or if they do, these loans amount to a minute fraction of their total loans. Most require complete repayment by the time the borrower turns 60 or retires--whichever is earlier. Several HFCs' mortgage plans include free life insurance up to the amount of the outstanding balance at the time of the borrower's death. Thus, for these companies, lending to older families is particularly risky.

Several of the companies surveyed have attempted to court middle-aged borrowers via a special mortgage instrument. Under this scheme, payments start relatively high and then decline over time, so that if the borrower retires or dies before repayment is complete, he or his family will have a relatively small outstanding loan balance.

4.5.4 Rural Households. Five companies--Can Fin, Dewan, Gujarat Rural Housing Corporation (GRUH), HDFC and IHFD--provided information on the share of their loans going to families in cities of various sizes.[8] In 1990-1991, approximately 9 percent of this group's loans went to families in cities smaller than 100,000 people. This figure is up from

[8] Note that one source questions the reliability of GRUH's information on this subject.

6.7 percent just two years earlier and represents very rapid growth given the explosive expansion of the entire industry over the same period. Nevertheless, only GRUH is doing significant underwriting in truly rural areas. Over the last two years, approximately 73 percent of GRUH's loans have gone to families in villages with populations below 10,000. EIU (1990) states that India's population was about 75 percent rural in 1981. While the report does not define rural, in India the term is generally reserved for villages with less than 5,000 inhabitants.

All companies surveyed highlighted the same two difficulties with rural lending: (1) Rural areas are relatively more expensive to service because population densities are low and infrastructure systems are often poor; and, (2) Rural areas have a much higher late payment rate and presumed default risk than semi-urban and urban regions. Late payments are higher due to poor infrastructure facilities, and many lenders worry that defaults would be higher because rural families have been "spoilt" through years of loan forgiveness on agriculture-related debt. Indeed, GRUH's late payment rate is significantly greater than rates currently experienced by its counterparts. Nevertheless, as noted earlier, GRUH has only one loan overdue by more than one year, is lending profitably to households in rural areas[9] and plans rapid expansion. The company's success in this market niche may well engender imitation and GRUH itself hopes to help establish rural-focused HFCs in other states.

Although exact figures were not available, Tapoban Housing Finance claims that it does a significant amount of lending in rural areas as well. Its "security deposit" scheme

[9] GRUH's after-tax return on average equity (ROE) was 12.5 percent in 1990-1991, up from 6 percent in 1988-1989. The company anticipates steady ROE growth for the next several years.

discussed above significantly reduces its exposure to default risk, and could possibly be useful to other HFCs considering entering this market. GRUH attempts to minimize defaults by allowing farmers to make payments that coincide with this group's cash flow rather than requiring equal monthly installments.

4.6 Note on Loan Size as a Proxy for Income

NHB-mandated interest rates range from 8 percent on loans of Rs. 7,500 or less to 14 percent on loans from Rs. 50,000 to Rs. 200,000. Rough team calculations imply that a free-market mortgage interest rate would probably approach 16.25 percent.[10] Thus, the NHB has fostered a system in which interest rates are approximately from 2.25 to 8.25 percentage points below free-market rates. Given that homebuyers are thereby receiving a significant subsidy,[11] it is important for the NHB to determine that these lower-interest loans are benefiting the organization's target group.

Most NHB incentives for lending to low-income households and efforts to improve affordability for this group actually are targeted at small loans rather than directly at families with modest incomes. Similarly, the USAID HG-003 program provides refinancing for all

[10] This figure is arrived at via the following simplifying assumptions. Suppose a hypothetical HFC's funds consists half of deposits and half of term loans from commercial banks. The firm pays a 14 percent interest rate on the former and a 15.5 percent rate on the latter. Thus, its average cost of funds is 14.75 percent. The HFC lends with a spread of 1.5 percent. Thus, in this simple scenario, the firm would make loans at a rate of 16.25 percent.

[11] For example, a family that takes out a 20-year loan for Rs.100,000 at a 14 percent interest rate will return Rs.11,810 less in present value rupees than a family that takes out the same loan and faces a 16.25 percent interest rate. Thus, under the conditions outlined above, the subsidy on the 14 percent interest loan is approximately 12 percent of the loan value.

loans under Rs.55,000, on the rationale that a loan of this size is affordable to below-median-income families. The NHB has targeted small loans rather than lower-income families on the apprehension that, if it provided benefits based on income, households would have an incentive to underestimate their earnings. This is a significant risk as income is frequently difficult to verify. USAID accepted loan size as a proxy for income since this system was easier for both HFCs and NHB to administer.

While low-income people are definitely restricted to small loans, it is nevertheless true that more affluent families make use of small loans as well. Can Fin estimated, for example, that virtually all of its upgrading loans (which are for Rs. 30,000 or less) went to families earning significantly above the median income. When asked to estimate the percent of their loans below Rs. 50,000 that went to families earning below-median income, firms' estimates ranged from 25 percent to 90 percent. Dewan, LIC HFC, and GRUH placed the figure at over 90 percent. Can Fin Homes felt that possibly fewer than 25 percent of its under Rs. 50,000 loans went to target group households; SBI HFC estimated this figure to be "somewhat over half" of its small loans. Information provided by HDFC indicates that approximately 67 percent of its small loans were for below-median-income households. HFC management interviewed felt that the principal reason accounting for this wide range is that some companies make "wholesale" loans to employers who, in turn, "retail" them to their employees. These loans are virtually never designed to cover the majority of the cost of a home. Rather, they are used to supplement companies' lending of their own resources and employee savings.

NHB-mandated interest rates are subsidized for all loans below Rs. 200,000. If a significant percentage of these loans are going to families who could afford to pay market rates, this system is not efficiently targeting its limited resources and the NHB may wish to consider modifying it. Virtually all firms surveyed now have the ability to compile information on the share of their loans, by loan size, going to below-median-income households. This information could be very useful to the NHB as it continues to design policies and programs to promote lending to this group, and the NHB might consider monitoring it on an ongoing basis. Further, it is this team's understanding that USAID plans to conduct a statistically reliable survey of HFCs that have received HG-003 funds, in order to determine what share of the loans refinanced went to households in the program's target group. A protocol for this survey is outlined in Annex 4.1.

4.7 Conclusion

Although data are not entirely reliable, information available indicates that below-median-income households probably account for one-quarter of all HFC borrowers and one-fifth of total HFC loan volume. Their share of total loans will probably at least remain constant and may, in fact, increase over the next years. Over time, loans to these households will be increasingly concentrated in non-metropolitan cities.

The growth in lending to these families is largely market-driven. However, the NHB has played a role in encouraging firms to direct their resources to this market segment. As the NHB's refinancing program expands, its ability to influence firms' lending patterns will grow. The NHB's unit and loan size restrictions for refinanceable loans encourage lending to this group, as does the organization's efforts to promote the establishment of HFC branches in smaller cities. Finally, the organization's HLA program may be beneficial to this target group in the future. The NHB also increases loan affordability for the target group by essentially setting industry-wide interest rates which are quite low for small loans and increase as loan size grows.

Firms interviewed felt they faced a number of problems when they attempt to loan to low-income families. These include low repayment capacity, higher risk of late payment and default, unclear land titles and the lack of an established credit record. The NHB has taken some steps to address these issues, although it is still too new to have made significant gains.

The scarce data suggest that informally employed families, older households, families without secure land title, and households in small towns and rural areas have had relatively little access to the HFC system, and that HFCs feel these sub-markets are significantly riskier than other sub-markets. Lenders do not perceive any special impediments to lending to women. A thorough analysis of the issues involved in lending to these groups would require much more complete data on these sub-markets' demand for housing finance and the share of housing credit they receive.

The NHB and USAID have concentrated their low-income housing finance promotion efforts on borrowers who take small loans, rather than on borrowers with below-median incomes. The degree to which these two groups overlap appears to vary widely across HFCs. Most recognized HFCs now have the ability to track the share of loans going to low-income families and NHB might improve its program targeting by compiling this information.

5. Demand for Additional Refinancing

Initially, US $50 million dollars was available in the HG-003 loan. Twenty-five million dollars of the total remains to be disbursed. Furthermore, USAID is considering the authorization of an additional US $50 million in housing guarantee funds to finance NHB purchase of HFC loans to below-median-income households. This chapter considers whether effective demand from households below the median-income is sufficient to absorb these funds.

There is a widespread perception that below-median-income households have trouble affording formal housing finance. HFC management were unanimous in their belief that land and construction prices have increased very rapidly in recent years and that a loan of Rs. 55,000, currently deemed to be the maximum that a household at the median income can afford, is adequate to cover the cost of the construction or major repair or extension of a house only if families are able to make very significant downpayments. However, the increase in the share of loans to below-median income borrowers by the nine recognized HFCs for which data were available indicates that some households are able to take advantage of small loans for housing purposes. HFC managing directors also report that below-median-income households are saving increasing amounts and making extra efforts to bridge the difference between the loan amount they can afford and the cost of their project.

The main question is the desire and ability of recognized HFCs to lend to below-median income people. An important determinant of the ability of these HFCs to meet this demand is their network of branches. India is predominantly rural. Unsatisfied effective demand lies disproportionately in rural areas and smaller towns. Encouragingly, as described in Chapter 2, HFCs have greatly expanded their branch network to smaller cities.

Another determinant, of course, is whether HFCs want to meet this effective demand for households eligible for NHB refinancing and for HG loans. As Chapters 3 and 4 indicate, the record so far is good. In addition, the recent rise in the cost of HFCs' funds has narrowed the options for resources suitable for these firms and, hence, focused their attention on NHB refinancing. One company, for example, projects its average cost of funds for 1991-92 at 14.1 percent. This rate is <u>above</u> the NHB regulated rate of 14 percent for loans below Rs. 50,000. Thus, HFCs increasingly must use their own funds to make larger loans, which carry rates above the cost of these funds, and utilize NHB refinancing to fund smaller loans. For these reasons, the problem facing the HFC industry in the medium term is likely to be an insatiable demand for NHB refinancing, and with it HG funds, rather than a lack of demand.

Estimates based on the projections of the seven[1] recognized HFCs with data for NHB refinancing bear out this conclusion. Table 5.1 details the HFCs' refinancing projections. Loans for up to Rs. 50,000 are eligible for refinance under the HG program. These figures shown in Table 5.1 are considerable underestimates of likely future demand because data were unavailable for Can Fin and LIC HFC, the second and third largest HFCs. Perhaps partly for this reason, the compound annual growth rate (CAGR) of 22 percent is less than half that of total loan volume and loans to below-median-income households from 1988-1989 to 1990-1991.

[1] Dewan, Gruh, HDFC, IHFD, PHFC, Saya, and SBI.

TABLE 5.1
REFINANCING PROJECTION BY SEVERAL RECOGNIZED HFCS FOR NHB REFINANCING
(IN LAKHS)

year	loans up to RS. 50,000	total loans
1991-92	11,200	31,357
1995-96	24,472	82,862
compound annual growth rate for 1991-92 to 1995-96	21.6%	27.5%

Source: NHB Records

Yet even based on this conservative CAGR, refinancing eligible under the HG program substantially exceeds available funds. USAID regulations currently specify that no more than 25 percent of HG funds go to one HFC. HDFC, whose loan volume far exceeds the other recognized HFCs, has already used this amount and therefore is unable to draw from the remaining US $25 million. On the assumption that an 11 percent devaluation in the rupee relative to the dollar in the next year, six other HFCs project a demand of US $22,680,327 for the refinancing of loans up to Rs. 50,000. This amount is US $2.2 million short of the total US $25 million remaining to be disbursed. Yet, as noted, the two HFCs for which refinance projections are unavailable, Can Fin and LIC HFC, have been the largest lenders of the group of eight by far, accounting for a total of 76 percent of loans sanctioned of these eight HFCs in 1990-91.

AID plans to exclude LIC from HG refinancing because that HFC has access to funds from its parent company. But, Can Fin alone will almost surely ask for more than US $2 million in HG-eligible refinancing next year. Indeed, the HFC issued a total of Rs. 299,100,000 (approximately US $15 million) in credits under Rs. 50,000 in 1990-1991 alone and can seek approximately an additional US $4.7 million in refinancing while remaining under the stipulated 25 percent maximum. Thus, absorbing the second US $25 million in 1991-92 is highly likely.

The HG-eligible refinancing demand estimate for 1991-92 is generally based on the HFCs' operating budgets for next year, and therefore should be relatively reliable. The plausibility of this demand estimate is further reinforced given the companies' 1990-1991 volume of loans under Rs. 50,000. Table 5.2 compares 1990-1991 volume of loans under Rs. 50,000 to 1991-1992 refinancing requirements for loans of the same size.

TABLE 5.2
1990-1991 LOAN VOLUME VERSUS
1991-1992 REFINANCING PROJECTIONS

company	1990-1991 vol loans < Rs. 50,000 (in Rs. lakhs)	1991-1992 refinancing vol < Rs. 50,000 (in Rs. lakhs)	refinancing % previous year volume
DEWAN	1,643	1,330	81%
GRUH	1,957	1,054	54%
HDFC	16,783	5,666	1,558%
IHFD	77	1,200	100%
PHFC	1,195	1,200	3,000%
SAYA	1	300	70%
SBI	664	400	50%
TOTAL	22,300	11,200	50%
TOT W/O HDFC	5,517	5,534	100%

Source: NHB Records

As the table indicates, most companies' projections call for them to refinance fewer loans under Rs. 50,000 in 1991-1992 than they sanctioned the year before. Only IHFD and Saya expect to refinance significantly more loans in this size bracket next year than they underwrote this year, and both companies are projecting this rapid growth from a very small base. Excluding HDFC, companies overall expect to refinance next year the same volume of loans under Rs. 50,000 as they made this year. Given that these companies have a combined growth rate in lending volume of over 100 percent per year for the last two years, these projections seem obtainable.

Thus, it seems clear that there currently exists sufficient demand to utilize US $25 million of HG-003 refinancing in 1991-1992.

Evaluating the NHB program's potential to absorb an addition US $50 million in the following three years is a somewhat more complex undertaking. In order to gauge this demand, we have evaluated the situation under several scenarios. Table 5.3 projects the growth in loans below Rs. 50,000 in 1991 US dollars based on an overall CAGR of 22 percent in loan volume and a depreciation in the rupee relative to the dollar of 11 percent per year. The projection is for the three years when the proposed HG funds of US $50 million would be used: 1992-93, 1993-94, and 1994-95.

TABLE 5.3
PROJECTION OF HG-ELIGIBLE REFINANCING DEMANDED BY SEVEN RECOGNIZED HFCS

year	amount (1991 US $)
1992-93	50,457,902
1993-94	55,474,209
1994-95	60,822,630
total	166,822,530

Source: Team's calculations based on NHB Records

According to this projection, total financing demanded is US $166 million. This figure is low in that it excludes demand from two important HFCs, Can Fin and LIC HFCs, seven additional recognized HFCs and HFCs that may become recognized during this period. But a consistent 22 percent CAGR might be considered high, even though the recognized

\\\

HFCs have expanded at nearly twice that rate over the last three years. In addition, entrepreneurs sometimes overestimate future growth. For this reason, Table 5.4 delineates demand for refinancing for loans less than Rs. 50,000 assuming no expansion in HFC demand for loans of this size beyond that projected for the 1991-1992.

TABLE 5.4
PROJECTION OF HG-ELIGIBLE REFINANCING DEMANDED FROM SEVEN RECOGNIZED HFCS, ASSUMING NO GROWTH BEYOND 1991-92

year	amount (1991 US $)
1991-93	41,358,936
1993-94	37,271,214
1994-95	33,532,934
total	112,163,084

Source: Team's calculations based on NHB records

Finally, USAID regulations currently specify that no more than 25 percent of total HG funds should go to one HFC. Currently, HDFC has exceeded this 25 percent. Despite the growth of other HFCs, it might do so again under the proposed additional US $50 million in HG funds. Table 5.5 assumes both that HDFC is limited to 25 percent of the total and that no growth in demand will occur beyond 1991-92 for any of the HFCs.

TABLE 5.5
PROJECTION OF HG-ELIGIBLE REFINANCING ASSUMING HDFC DOES NOT EXCEED THE 25% LIMIT AND NO GROWTH BEYOND 1991-92

year	amount (1991 US $)
1992-93	27,267,799
1993-94	24,552,412
1994-95	22,089,820
total	73,910,031

Source: Team's calculations based on NHB records

In this most conservative scenario, lending for HG-eligible loans levels off. This could be caused by a shortage of affordable housing with legal title on which loans could be made or competition from other lenders, i.e., commercial banks or state bodies. Even then, the recognized HFC requirements for HG-eligible funds still significantly exceed the proposed US $50 million.[2]

In sum, the demand for HG-eligible funds is likely to exceed the $50 million currently proposed. Even if no growth in demand for refinancing occurs after 1991-1992 and HDFC is limited to 25% of total refinancing, demand still substantially exceeds supply.

[2] This conclusion is based on the assumption that the rules governing the eligibility of loans for HG refinancing are not modified.

6. NHB's Promotion of the Housing Finance System

Since its creation the National Housing Bank has perforce been the lead institution for the development of the housing finance system in India. This chapter discusses three aspects of NHB's performance: its work as a regulator for housing finance companies; its role as a mobilizer of additional funds for the housing finance system, and how this mobilization compares with the expectations for additional funds it has created; and, its operations as the institution charged with promotion of the general development of the housing finance system. Note that these tasks are closely related. The perception that HFCs are financially strong and adequately supervised by a regulatory agency has a very strong impact on the HFCs ability to raise funds and the cost of those funds; this in turn affects the volume of funds the NHB will be required to mobilize using its status as a government sponsored enterprise.

6.1 Regulation and Supervision

Fundamental to successful expansion of the housing finance system is careful and adequate, but not overly restrictive, regulation of the HFCs. Regulation and supervision begins at the point at which a firm registers as a housing finance company, and the HFC becomes subject to increasing degrees of oversight as it avails itself of NHB's loan refinancing scheme. Our discussion begins with an overview of degree of regulation to which HFCs with different status are subject. Finally, we describe NHB's response to date to suggestions for a number of improvements in its regulatory powers and activities.

<u>6.1.1 Extent of Supervision to HFCs with Different Privileges</u>. For the purpose of supervision, the HFCs have been divide into two groups--those that have merely been

registered as HFCs and those registered HFCs which have been recognized by NHB as being eligible to obtain refinancing.

The registered, but not recognized companies, as discussed in Chapter 2, include two groups of HFCs. First are those companies with which NHB has little contact, either because of some error in transferring information between the Registrar of Companies and NHB or because they did not respond to NHB's initial letter of inquiry. NHB has no supervisory contact with them. Second are those companies that have registered as housing finance companies, have responded to NHB's letter of inquiry about their business, and been confirmed by NHB as an HFC. Each HFC passing through this screen is sent the "Housing Finance Company Directions," which informs the institution of deposit-taking regulations and requires it to submit substantial financial information. At the end of each year, the institution is required (under the NHB statute) to submit similar information to HFC, including audited financial statements. NHB staff report that only about half of the required annual reports are received. At present there is no scheduled supervisory visits to these HFC; NHB examiners have made visits ("4 or 5" in the last six months) in response to complaints received about the companies.

In short, these HFCs are essentially unsupervised; and it would be surprising if one or more does not fail, possibly undermining public confidence in the housing finance system in general. NHB staff are aware of the problem and are now beginning to make plans for regular supervisory visits.

Much greater supervision is given to the 16 recognized HFCs, especially private HFCs. They are subject to five different types of supervision, either during the process of being recognized or thereafter.

-- Like the registered HFCs, they must file annual financial information with NHB. Response has been good.

-- At the time an HFC applies for recognition, it is subject to a supervisory visit, which is apparently quite thorough.

-- Any HFC using the refinance facility (plus LIC Housing Finance which until very recently did not use the facility) must file half-yearly reports (a requirement under HG-003). Response to this requirement has been weak. Note that recognized HFCs not using the finance facility are not subject to this requirement.

-- HFCs using the refinance facility may be subject to supervisory visits either prior to or after each refinancing transaction. To date several private HFCs have been subject to a supervisory visit for each transaction; joint sector HFCs are less frequently monitored generally. While the primary purpose of the visit is to insure that only eligible loans are being refinanced, NHB also takes the opportunity to look at the financial conditions in general.

-- NHB has just begun a program of regular supervisory visits to all recognized HFCs, which are to include a rigorous examination of asset quality, particularly for the 25 percent of assets not held in long term housing loans. Private HFCs are to be visited annually; joint sector HFCs every two years.

NHB plans to improve the reporting from the recognized HFCs in the near term by arranging for each to provide NHB figures from its management information system on a bi-monthly basis in a format provided by NHB. A Director from each company will be made responsible for seeing to it that the data are provided in a timely way.

A theme running through the current supervision program is that private HFCs are subject to significantly more scrutiny than their joint sector counterparts. NHB strongly believes this differential is justified by the fact that "parent organizations" will be watching the subsidiaries closely. Against this one can raise several points: lack of experience of the new joint companies in housing finance; apparent poor business practices of some;[1] and adverse incentives for the long-run health of the HFC that may be operating when senior management is temporarily transferred to the subsidiary from the parent organization, rather than permanently associated with it (such detailing of senior staff is now common). These points suggest the need for similar supervision for both private and joint sector HFCs, with those in either sector, which need more than routine attention, receiving it.

NHB clearly needs to strengthen its supervision operation. Staff estimate that it would require between 10 and 15 full-time examiners to carry out an annual program of on-site inspections at all registered and recognized HFCs. This contrasts with a current staff complement of five, which both do supervision and verify that the loans refinanced by NHB qualify for the program. At the moment NHB does not have a schedule for hiring and training the additional staff. Additionally, the NHB's department of supervision badly needs to be computerized so that it can more easily analyze the data submitted to it.

NHB should also carry out the function of compiling statistics on the entire housing finance sector, not just the HFCs to which it provide refinancing. At present no agency is preparing these data on a regular basis.

It appears quite clear that the requirements for the Housing Guaranty Program have had important impacts on NHB's supervisory function, even as undeveloped as it is. First, it is doubtful that the half-yearly reports from recognized HFCs would have been required; and,

[1] Senior management interviewed by the team at a HFC which is a subsidiary of a commercial bank reported that its underwriting (loan appraisal) standards were not written down and that there was no special training for loan underwriters, but rather only on-the-job training. Moreover, he reported that the procedures to be followed in pursuing payment of overdue loans were not written down.

117

indeed, even with the requirement, they were not instituted until the time at which NHB had to satisfy this condition in order to draw the HG funds. Second, the financial standards (e.g., regarding level of arrears) for a HFC to be included as a sub-borrower under the HG have been adopted for general use by NHB.[2] In this regard it appears clear that the norm for overdue loans should be revised. In fact, a review is underway and the level of arrears will be revised from less than 7 percent after 30 days to somewhat less than that level after 90 days.

6.1.2 Strengthening Regulatory Powers. As part of USAID's technical assistance to NHB, James Croft did a thorough examination of NHB's regulatory powers. Croft (1990) identified a number of areas which could be strengthened, and the summary table of his recommendations is reproduced as Table 6.1. NHB management is in substantial sympathy with most of the recommendations.

TABLE 6.1
SUMMARY OF RECOMMENDATIONS EXCERPT FROM CROFT'S LETTER

recommended changes	type of action	timing
Require one or two years of operating history before an institution becomes NHB-qualified	G	Imm
Allow HFCs to advertise their NHB-qualified status (with a disclaimer about any NHB guarantee of repayment)	G	Imm

[2] NHB had already been gathering similar data as part of its review of HFCs who were applying to receive refinancing, but the setting and enforcement of the norms seems attributable to the HG-loan provisions.

118

recommended changes	type of action	timing
Seek authority to issue both general and specific directions concerning loan and investment activities for HFCs.	L	(Begin) Imm
Establish guidelines for investment in nonhousing loans for 25% of portfolio.	G	Imm
Develop portfolio diversification rules.	D	Int
Establish limits for the amount of refinancing an HFC can have outstanding.	G	Int
Allow HFCs to leverage capital more highly if their loans comply with the most conservative underwriting and documentations standards.	D	L-T
Propose legislation to establish a secondary mortgage market.	L	L-T
Study feasibility of offering better loan refinancing terms on the most conservatively underwritten loans with standard documents.	G	Int
Develop underwriting criteria to use as equity trade-offs (only after Parliament approves legislation allowing rapid foreclosure and sale and after these new provisions have been tested).	D	L-T
Modify reports to NHB to allow measurement of interest rate risk exposure.	D	Imm
Develop rules for limiting interest rate risk exposure	D	Int
Seek authority to apply remedies against institutions engaged in unsafe and unsound practices--up to an including conservatorship.	L	Int
Obtain authority to prohibit deposit taking for unsafe and unsound operations at an HFC.	L	Int

recommended changes	action	timing
Seek authority for NHB to:		
* Encourage mergers of weak with strong institutions.	L	Int
* Establish receivership at an HFC's insolvency	L	Int
* Establish receivership prior to insolvency.	L	L-T
Develop a position on the feasibility of deposit insurance for HFCs and present it to Parliament.	L	Int

Legend	G = Guidelines	D = Directives	L = Legislative
	Imm = Immediate (next year)	Int = Intermediate (1 to 3 years)	L-T = Long Term (3 to 5 years)

Source: Croft (1990)

The greatest deficiency identified by Croft is NHB's present lack of regulatory power on the asset side of the balance sheet. The amendments that have been drafted to the NHB Act will give NHB the necessary authority to regulate HFCs comprehensively. NHB senior management, however, prefers not to establish too many norms in the near term, but rather to give informal guidance and to learn more about HFC operations as more HFCs mature before considering specific norms. Without attempting to give a complete rendition of NHB's response to each recommendation, the following points are noted.[3]

> -- NHB is sensitive to individual HFCs becoming too dependent on it for financing. Since debt from NHB refinancing does not count in the calculation of an HFCs debt-to-equity ratio, excessive dependence could imply excessive leveraging. NHB management has recently sought guidance from its advisory committee on this point, and may take action to address this problem.

[3]It may be worth noting that NHB believes it was never asked by USAID for its "policy response" to Croft's recommendations.

120

-- NHB will modify the reports it receives so as to be able to measure interest rate risk. This sets the stage for possibly allowing HFCs to accept shorter-term deposits and still avoid an excessive maturity mismatch between assets and liabilities.[4]

-- NHB believes that it has adequate powers under the Companies Act to apply remedies--including closure or merger--against institutions engaged in unsound and unsafe practices. Under its own Act, NHB could only prohibit an HFC from continuing to take deposits. NHB believes that it could go to the courts and have a receiver appointed in a several-week period. The team's view, given the general ponderousness of the Indian courts, is that this may be excessively optimistic.

-- NHB believes that deposit insurance is a poor idea for India, in that it could encourage excessive risk taking by the HFCs. (Everyone in the financial community with whom the team spoke agreed with this position.)

In short, NHB is in the process of substantially strengthening its regulatory powers through the proposed amendments to its Act, although more might be done with respect to dealing with unsound companies. It is also taking steps to develop more information as a foundation for possible future regulatory action.

6.2 NHB's Funds Mobilization Strategy

A strategy for mobilizing resources must be viewed against the organization's commitments and other requirements. Accordingly, this discussion first reviews the National Housing Bank's commitments and then analyzes the way in which it has generated resources to date and its plans for the future.

[4] See Chapter 7 for a discussion of HFCs deposit taking powers.

The NHB has three types of outstanding commitments under which it has agreed to refinance qualifying housing loans:

1. Regular refinance program. The NHB has an open-ended commitment to refinance qualifying loans presented to it by HFCs it has recognized. This appears to be a very substantial commitment indeed, based on the explosive growth of the housing finance system and of the volume of loans presented to NHB for refinancing in the past two years, and on the plans of the HFCs whose projections for refinancing reviewed in Chapter 2. The seven HFCs that provided estimates of their 1995-96 refinancing needs indicated a need for Rs. 828 crores. Given the overall growth in the number of HFCs in the past two years, the fact that LIC Housing Finance is planning to make major requests for funding beginning in the near future, and the suggestion that all the commercial banks may have HFC subsidiaries shortly, this must be viewed as a highly conservative figure.

2. Home Loan Account Scheme. To encourage commercial banks to promote the HLA scheme, NHB has promised to refinance any loan made to households who have fulfilled their savings account. It is very difficult indeed to know how large this liability really is, since it depends both on the number of HLA account holders who become borrowers (as opposed to participating solely for the tax advantages) and on the share of loans originating in institutions elected to hold in their own portfolios. These financing demands are not likely to be very large over the next several years. Through March 1991, accumulated deposits totaled at least Rs. 80 crores.

122

One can obtain an idea of the upper limit of the possible financing if one assumes that these were the final balances coming due each year in the future, that the average loan-to-savings ratio is three, and that NHB has to finance all of the loans originated; then the total annual requirements would be Rs. 240 crores in 1995-96. Because the HLA was offered only by commercial banks until 1991, and even now it is offered only by a few HFCs, likely commitments are beyond those just indicated.

3. Land Development and Shelter Projects. To reduce the risk to developers of undertaking such projects, NHB has promised to refinance mortgage loans originated by commercial banks and recognized HFCs that result from project development. This program is just getting underway; NHB has made commitments to some 45 projects but only Rs. 75 crores in refinancing had been disbursed by mid-June, 1991. Hence, it is impossible to make an assessment of possible volume. Given the general shortage of construction period financing, this could be a high volume program.[5]

To date NHB has not made systematic estimates of the total funds it will require under differing assumptions about the rate of development of the housing finance system.[6]

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[5] NHB also has a residual liability from its principal refinance program. This liability is different from the preceding. It arises from the possibility that an HFC fails, leaving NHB with assets in the form of the loans NHB has refinanced. Because it is likely that the failing HFC will have experienced high rates of loan delinquency and default, NHB may suffer a liquidity problem as the cash flow due on these loans does will not materialize. NHB has not established an explicit reserve account against the losses that would be incurred from such bad loans.

[6] NHB has made estimates of its future funding needs but has done so on the basis of targets for the number of units it "should" be financing in light of the growth in urban housing needs. These funding requirements may or may not correspond to those arising from

Thus far, how has NHB been financing its activities and what are its prospects for the future? Table 6.2 shows NHB's sources of incremental funds for the first nine months of the current fiscal year. A quick review reveals that these funds come exclusively from either directed sources (RBI, LIC) or from bond issues carrying special tax advantages. The average cost of funds is only 8.5 percent, and 10.5 percent on borrowings. The team found general agreement both within NHB and elsewhere in the financial community that these sources could not be relied upon for a volume of funds sufficient to meet NHB's burgeoning funding requirements.

the four sources enumerated in the text. For details see National Housing Bank (1990a), para 80-82 and annexure 6.

TABLE 6.2:
SYNOPSIS OF NHB'S SOURCES OF INCREMENTAL FUNDS
JULY 1990 - MARCH 1991

source	interest rate (annual)	Rs. (crores)	percent of total
capital (RBI)	--	50.0	11.9
profit	--	21.6	5.1
borrowings RBI-long term operations fund	6.0	50.0	11.9
bonds (GOI) guarantee	11.5	80.0	19.0
bonds (Cap Gains)	9.0	43.2	10.3
LIC	12.0	171.0	40.6
miscellaneous	*	4.8	1.1
total		420.6	99.9**

* interest rate not known
** does not add to 100 due to rounding.

Note: The Rs. 50 crores from the Housing Guaranty Loan was received after March 1991.

Source: NHB Records

Aside from a plan to increase the share of non borrowers participating in the Home Loan Account scheme,[7] NHB has three ideas for tapping the broader financial market for

[7] The specific proposal is to make households who currently own their home eligible to participate. These households would be attracted by the tax advantages associated with the scheme but very likely would not be borrowers.

125

funds. All of these are in the early planning stages, but under active discussion with the relevant authorities.

The first idea is establishment of a mutual fund, which would be marketed through the banking system, as are the UTI mutual funds. Mutual funds have done extraordinarily well in the past two years in garnering funds, especially the new funds which have been offered by commercial banks. They have now caught the imagination of the public and marketing a new fund appears feasible. The judgement of NHB's chairman--the former chairman of UTI--on marketability of a new fund is to be trusted.

The envisioned fund would be a closed-end, monthly assured income fund, which would probably have to pay 13 percent or somewhat more to be attractive. The plan is to pay for these funds with income from refinancing larger loans. Note, however, that NHB's highest return is 14 percent on loans of Rs 50,000 to Rs 200,000. It may well be that for this scheme to work, and if NHB holds the mortgage interest rates and its refinancing rates fixed, NHB will have to refinance larger loans to earn a higher rate of interest. If this is the case, then the funds raised through the mutual fund will finance these new loan purchases, but not the funding requirements reviewed above.

The second idea is for NHB to establish a pension fund to which anyone could subscribe but which would be aimed at the self-employed. The balance of pension maturities with housing loan maturities is obviously attractive. Moreover, the 12 percent interest necessary to investors (plus another 50 to 70 basis points for administrative cost and front end commissions) makes the cost reasonably attractive to NHB. Again, though, these costs are at

126

the upper end of the interest on NHB-refinanced loans.

While one can applaud the creativity of the pension fund scheme, one might also question whether a pension fund should be operated by an entity with an investment portfolio dedicated to a single type of asset. Concerns here are both adequate diversification of risk and the related question of the overall future rate of return if the assets are composed exclusively on long-term investments when the structure of interest rates may change.

The final idea is to sell mortgage-backed securities (MBS) in the capital market. In this case NHB will observe HDFC's maiden offering of an MBS and likely follow this lead. Once more, however, the rate of return required to sell these securities will be at the upper end of NHB's assets.

Overall, NHB is clearly aware of its need to raise funds beyond the "favored sources" to which it has had access, since these are unlikely to be provided in adequate volume to meet its future financing requirements. Its broad strategy of moving to a blend of market-rate and favored funds and concentrating the use of its "favored sources" on the small, lower interest rates loans also is correct. The real question is whether it can match the rate of return on the upper end of its portfolio with the cost of funds in the open market. NHB management has identified the spots in the market where it has the best chance of doing so. But at the moment rigorous analysis of the schemes and the balance of costs and revenues is lacking.

6.3 System Promotion

The data on the growth of the housing finance system reviewed in Chapter 2 made clear that the very creation of the National Housing Bank produced an enormous increase in interest in housing finance in the financial community, by signaling Government's interest in the sector and that associated support would be forthcoming. The main NHB initiatives to promote the housing finance system have already been noted, i.e., creation of the Home Loan Account Scheme and its refinancing schemes for individual loans and for land development and shelter projects. This section examines other actions taken by the NHB to promote the expansion and maturation of a market-oriented housing finance system, such as training programs, assisting selected HFCs with equity participation and meeting with officers of principal HFCs to resolve various problems.[8]

NHB has undertaken promotional activities alone and in conjunction with USAID. In the following, NHB's own activities are discussed first and then the USAID-assisted activities are covered. Each of the actions taken is discussed in turn.

6.3.1 National Housing Bank Activities. The team has identified eight areas in which NHB actions have affected the development of the housing finance system in the past two years. These are briefly reviewed below.

(a) Meetings with Officers of Recognized HFCs. The NHB has, with modest exceptions, kept to its schedule of quarterly meetings with the officers of those HFCs eligible

[8] This discussion complements that in Chapter 7 on NHB actions (or lack of action) to address specific constraints to the growth of the system and its ability to serve lower-income families effectively.

128

for NHB loan refinancing. These meetings are reported to be productive by both NHB and the HFCs.

(b) Modification of Refinancing Terms. When it was determined that the initial definition of the loans NHB would refinance were unrealistically restricted, NHB liberalized them as needed, beginning in March 1990. It can be argued the NHB's strategy in this matter was correct: set severe standards at the start, because liberalization is much easier than increasing restrictiveness.

(c) Liberalization of Terms for Commercial Bank Lending to HFCs. After consultation with the NHB, the RBI increased the amount of term lending permitted by commercial banks to an HFC from one to three times the HFCs net owned funds (i.e., paid up capital and free reserves less cumulative allowance for losses and other intangible assets).[9] In addition, over the period the interest rates permitted on these loans were raised twice, to a maximum of 17 percent, and very recently they have been reduced to 15.5 percent on the basis of NHB's discussions with the RBI. While these rates make the term loans costly to the HFCs, it also makes commercial banks more ready to lend.

(d) Realignment of Mortgage Interest Rates. After the RBI made a general upward adjustment in the interest rate structure, the NHB obtained permission for parallel adjustments to interest rates on mortgage loans, effective from January 1, 1991. Note that the interest rate schedule adopted dictates the precise rate to be charged on loans of each size, up to those of

[9] If the HFC is a subsidiary of a commercial bank, the leveraging in increased from 3 to 5.

124

Rs. 2 lakhs or more. In other words, HFCs have no flexibility in setting rates. This denies those HFCs--particularly the new, private ones--the chance to charge higher rates in line with their higher costs of funds in certain market niches. Moreover, even the large HFCs lack the ability to charge differential rates with the anticipated degree of risk and servicing costs.

(e) Equity Participation. NHB has made commitments to a half dozen new HFCs that it will take an equity position of between 10 and 20 percent of total subscribed capital. Two of these participations have been disbursed. In all but one case the HFCs involved are subsidiaries of commercial banks; in the other case it is a private company.

In none of these cases is NHB's contribution necessary for the paid-in capital to reach the Rs 1 crore minimum necessary to qualify a HFC eventually for NHB's refinancing program. Rather, the motivation of the HFCs in requesting participation is to give them greater credibility in the market, thereby facilitating the mobilization of term loans in the short term and over the longer term possibly entering the capital markets to raise funds.

(f) Selling of Debt by HFCs. Thus far, as noted, only HDFC has sold bonds to the public. Within the past two years the Securities and Exchange Board of India has stated that a finance company must have a track record of at least three years before they could have access to funds through the capital market. Hence, few HFCs now qualify. Can Fin Homes, however, is reportedly preparing a bond offering. HFCs are required to discuss the possibility of an offering with NHB. NHB reviews proposals, but it has not and does not plan to provide any advice or assistance to HFCs in structuring bond offerings.

130

(g) Dissemination of Research Reports, etc. NHB has distributed copies of reports generated by USAID consultants. The Croft (1990) report on supervision was cited as an example. The HFCs visited by the team were well acquainted with the content of several of the studies. However, NHB's dissemination procedures are clearly quite ad hoc and appear not to go beyond the HFCs recognized for the refinance program and selected government officials. The NHB does not publish a regular newsletter or bulletin to HFCs that would be a natural vehicle for sharing the results of studies, trends in the industry, and information on dates for relevant conferences and the like.

(h) Training. NHB has undertaken a limited amount of training for HFCs, scheduled state cooperative banks, and commercial banks. Its major initiative to date was a program in which about 200 faculty members of the Bankers Training Colleges (the training arm of the commercial banks) were given instruction in five-day courses on housing finance and the operations of NHB. The course was offered eleven times beginning in mid-1989. The faculty are to integrate this information into the colleges' training programs.

NHB also provided input and lecturers to a series of two-day workshops for the technical staff and officers to various lending institutions. Lastly, NHB requested USAID to help finance the Association of Metropolitan Development Authorities in presenting a training program for authorities on NHB's Land Development Program.

The NHB has been less active in promoting training for HFCs, particularly those which are not subsidiaries of commercial banks. Its only direct action appears to have been co-sponsoring a five-day training program with HDFC for officers and middle managers in May 1991.

The National Housing Bank has the idea of establishing its own training and research institute. In this respect it is following the pattern established by its parent organization, the RBI. The necessity for creating yet another institute seems questionable, given the existence of one specialized institute for training in housing finance--the Centre for Housing Finance (a subsidiary of HDFC)--and the small size of the market for training. On the grounds of efficiency and expediency NHB would appear well advised to pursue developing a working relation with the Centre and other existing training institutions rather than initiating the demanding task of creating a high quality training institute from scratch. The Centre itself should draw on the expertise of the other major HFCs, particularly LIC Housing Finance and CanFin Homes, as well as HDFC in offering its courses.

6.3.2 USAID-Sponsored Activities. Table 6.3 summarizes the training, technical assistance and studies sponsored by USAID from the fall of 1988 through May 1991. USAID expenditures in those areas has totaled about $1.7 million. The list indicates substantial accomplishments in this area.

In terms of the participants in the training activities, the majority--perhaps 60 percent overall--have been from public sector institutions (including the NHB itself and central government officials), with the balance coming from private HFCs. USAID staff believe that, without the active support of training by USAID, few if any of the participants in training of this type would have been drawn from the private sector. The training has apparently been effective--several HFCs told the team they were anxious to participate in the course offered by the Fels Center and other activities.

The studies listed have been of consistent high technical quality, reflecting well on the care with which both the terms of reference were drafted and the selection of and support to the consultants to prepare them. Interviews with NHB senior management and senior management at the largest HFCs revealed that they were quite familiar with the studies and that the studies had proven to be a rich source of ideas for them. In particular, the studies on the regulatory framework (by Wilson, by Madway, and by Croft), and the possibility for a secondary mortgage market in India (Struyk) were particularly well received. Croft's analysis led fairly directly to the proposed amendments to the NHB Act to strengthen NHB's regulatory powers. Struyk's paper has stimulated wide discussion of a secondary market and has been instrumental in helping HDFC structure its proposed offering of mortgage-backed securities.

Two attempts to establish on-going relationships between Indian and American institutions--HMSI with the Fels Center, and NHB with the Federal National Mortgage Association (FNMA)--did not produce positive results. In discussing the problems encountered with those involved, it appears that the lack of success is attributable more to the general difficulty of making such arrangements than particular failings by those involved. It may be worth noting that during the same period a successful relationship was established between the National Institute of Urban Affairs (India) and the Research Triangle Institute with the assistance of the same USAID staff.

6.4 Conclusions

NHB's record with respect to the supervision of HFCs is weak overall. It is particularly poor for those HFCs which are registered but not recognized as being able to obtain refinance from NHB. Even for the recognized companies, however, much improvement is needed. NHB appears to understand this and some action may be taken soon. But NHB has been more aware of the limitations in its regulatory authority, and has taken steps in the form of preparing and vetting amendments to the NHB Act to provide it with most of the powers outside observers believe it needs.

NHB has very large implicit outstanding commitments for providing refinance to the HFCs. It has not made any systematic estimate of the size of these commitments, and this should be done. Nevertheless, the NHB is aware that its commitments probably exceed the volume of funds it will be able to obtain from "favored sources," i.e., low-cost funds allocated by government bodies. It has, therefore, begun exploring options for obtaining funds from the market. These ideas have not yet been converted to plans. A sound strategy is obviously required.

Over the past two years NHB has been very active in promoting the development of the housing finance system. Eight separate areas of positive intervention have been reviewed in the previous section. While more could be done in several areas, there is a solid record of accomplishment. Similarly, USAID, working with NHB, has executed a substantial complementary program of training, studies, and technical assistance, over the period.

Table 6.3
TRAINING, TECHNICAL ASSISTANCE, AND STUDIES IN URBAN HOUSING FINANCE PROGRAM, FALL 1988-MAY 1991

timing	activity
	A. TRAINING
spring 1991	Five Indian professionals completed the Fels Housing Finance Course.
spring 1991	Four Indian professionals participated in the seminar on Effective Housing Finance held in Bangkok.
winter 1990	NHB training was given for local officials, i.e., members of Association of Metropolitan Development Authorities, on borrowing under the Land Development and Shelter Projects Program (AID part-financing).
spring 1990	Seven Indian professionals completed the Fels Housing Finance Course.
spring 1990	Three Indian participants completed the UC (Berkeley) Course in Land Management.
spring 1990	One Indian participant completed the International Shelter Workshop held at MIT.
fall 1989	Three India participants completed the seminar on Public/Private Ventures in Urban Development and Shelter, followed by a study visit to U.S. regulatory institutions.
	B. STUDIES, TECHNICAL ASSISTANCE[10]
fall 1990	Three senior professionals, nominated by NHB, completed a three-week study tour to five Latin American countries.
early 1990	Study of financial viability of housing finance companies was completed.

[10] Unless otherwise noted, all studies were executed by expatriate consultants or U.S. firms.

timing	activity
fall 1990	Study on Options for the Supervision and Regulation of Housing Finance Companies was completed.
fall 1990	Study on the Indian housing finance system was completed by the Ahmedabad School of Planning.
spring 1990	Study tour for two participants of the Fels course was arranged to mortgage and regulatory agencies in the USA.
spring 1990	Several Indians attended Third International Shelter Conference in Washington and participated in presentation of Indian case study.
spring 1990	NHB Chairman and others attended RHUDO policy seminar on housing finance in Thailand.
1990-1991	Intensive analysis was undertaken of the possibility for establishing a collaborative relationship in housing finance between the Fels Institute and the Human Settlements Management Institute (HUDCO), including exploratory visit by Fels staff. Ultimately the initiative proved unworkable.
1990-1991	Intensive analysis of the possibility of ongoing program of technical assistance from FNMA to NHB. Ultimately initiative proved unworkable.
December 1989	Final evaluation of the HG-002 Program (loan to HDFC) was completed.
fall 1989	Study on eventual feasibility of a secondary mortgage market in India was completed.
fall 1989	Information on the Torrens system of title registration was provided to NHB at its request. NHB is pursuing with Indian academic and state government officials.
February 1989	Study on options for expediting mortgage foreclosure was completed.
1988-1991	USAID urban advisors, both resident and local national, gave lectures on housing finance topics at several institutions.

7. Sectoral Constraints

Development of the Indian housing finance system is thwarted by numerous constraints, some legal, some regulatory, some simply attributable to an absence of information available to housing lenders. The NHB was created explicitly to deal with some of these--most prominently to assist HFCs in obtaining funds for housing lending and to meet the necessity for stronger supervision of housing finance institutions. In addition, however, in its capacity as the central government agency for housing finance, the NHB was expected to help address other constraints. This chapter reviews its actions with regard to a number of these constraints.

7.1 Mob 'zing Savings from Households

Throughout the world, housing finance institutions have traditionally raised funds by accepting deposits from households. The NHB is aware of this, and set the mobilization of household savings for housing lending as one of its primary objectives. To this end it originated the Home Loan Account Scheme (HLA), which has the potential to achieve this objective and at the same time to permit households who would not otherwise qualify for formal sector financing to do so.[1] However, until January 1991 only commercial banks were permitted to offer these accounts: after that date selected HFCs have been permitted to do so, but to date the number is only six--HDFC and five HFCs associated with commercial banks.

The restriction in favor of commercial banks was based on NHB's lack of confidence

[1] For a discussion based on the housing-linked contract-savings scheme offered by HDFC, see Struyk (1990).

in the financial strength of most HFCs and NHB's desire to have the HLA scheme offered quickly on a wide spread basis. The appropriate response to this belief should have been more careful supervision of the HFCs rather than the blanket prohibition. If NHB believes its supervisory capacity is not sufficient for such monitoring, as was expressed in our interviews, then a schedule for expanding this capacity should have been developed and implemented. The effect of allowing only commercial banks to offer the HLA may have been to have the HLA promoted by those least interested in promoting it and simultaneously to deny it to those institutions that most needed the incremental deposits.[2] One can make a strong argument that NHB should have moved more quickly to permit HFCs to participate in this program.

Beginning in 1989, HFCs lost the ability to take deposits from individuals for a term less than 24 months.[3] This action was taken by the Reserve Bank of India in part to protect the weak commercial banking system from competition, and in part to force HFCs to reduce possible interest rate risk from term mismatch on their assets and liabilities. The effect was to badly undercut the NHB's mobilization strategy and to set the stage for some HFCs to become overly dependent on the NHB refinancing program for obtaining funds (see Chapter 3). Commercial banks are paying 10 percent for two-year deposits. While HFCs could offer up to 14 percent, they are presently offering 12.5 to 14 percent, plus payment of commission

[2] Among the commercial banks, six have performed well and one has excelled in marketing the HLA, the others have not marketed it effectively. NHB staff argue that this poor performance was due in large part to the tardiness with which the RBI issued the circular explaining how such deposits would be treated in terms of the various reserves requirements to which deposits can be subjected. The circular was issued in February 1990 and NHB believes that the deposits will soon increase significantly.

[3] This restriction does not apply to deposits from corporations and foundations.

138

to agents, some of which may be returned to the saver. The ostensible interest rate advantage enjoyed by HFCs is, however, offset by restrictions on advertizing for funds and the fact that income tax on interest earnings is collected at source for HFCs but not for commercial banks. For the saver with an HFC account to take the income tax advantage permitted on these savings he or she must apply for a tax refund; savers at commercial banks take the deduction on their income tax.[4] As to advertizing, the NHB must approve advertisements, and the HFCs feel they are being unduly restricted in what is permitted.[5]

Many in the Indian financial world have argued that the inability of the HFCs to accept shorter term deposits is a fundamental handicap to development of the system.[6] Thus far, NHB has worked quietly behind the scenes without effect to get this provision changed. The RBI's position is that HFCs have been granted a major advantage in competing for longer term deposits because deposits held by HFCs are subject to much lower reserve requirements than are those held by commercial banks: in effect the RBI argues that the advantage to HFCs for longer term deposits is appropriately balanced by the prohibition on accepting short-term deposits.

In short, the entire issue of the range of savings accounts HFCs can offer must be revisited. In doing so, a clear distinction must be made between the two reasons given in the past for the limitation imposed. The first argument--that commercial banks should be

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[4] This is the tax advantage under Section 80L of the Income Tax Act under which up to Rs. 10,000 in interest is deductible.

[5] See Parekh (1991), p.7.

[6] See, for example, the "Directors' Report" in HDFC's 1989-1990 Annual Report (p.18), and "Housing Finance: Structural Changes Required," <u>The Economic Times</u>, July 26, 1990.

139

protected from competition--is without merit. But at the same time HFCs should not be granted blanket advantage--a "level playing field" should be created. The creation of this condition may be possible as liberalization of the financial system continues, and reserve requirements applicable to commercial banks are reduced. Equally important in leveling the playing field is elimination of the tax deduction at source for savers at HFCs. As to the second argument--that HFCs, especially private HFCs, need greater supervision--the NHB should respond with greater supervisory resources and the appropriate amendments to its Act to insure that it has the necessary regulatory powers.[7] The present unfavorable treatment of HFCs gives at least the appearance of a bias against them on the part of NHB.

7.2 Low Interest Rates on Small Loans

The interest rate structure on mortgage loans imposed by the NHB, following the pattern set by HDFC, is one under which the interest income from larger loans that carry relatively high interest rates cross-subsidizes the lower rates on smaller loans.[8] Many believed that this structure was too restrictive and would retard the growth of HFCs. In fact, Diamond (1990) in a technically strong analysis shows that NHB's refinancing program for the small loans offsets this problem effectively.

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[7] See Chapter 6 on NHB's regulatory program.

[8] In fact from the borrower's perspective, in after-tax concession terms, the rates on small and large loans are essentially equivalent.

7.3 Mortgage Instrument Standardization

A number of analysts have observed the need for standardizing the mortgage instruments in use, as a way to increase investor interest in mortgage-backed debt (by decreasing the amount of research potential investors would have to do in assessing each new issue) and as a necessary precursor to the establishment of a secondary mortgage market.[9] NHB has had the natural opportunity to accomplish this by requiring that a standard instrument be used for the loans it refinances. This has not been done, and NHB staff make no argument for why it should not be done. They do, however, point out that legally the regulation of mortgage instruments is at the State level; they also report that amendments to the NHB Act could give NHB this power.

7.4 Strengthening the Mortgage Instrument

All HFCs are now issuing an "equitable mortgage" under which the title deed is held in deposit by the mortgagee. This instrument has two advantages: (1) in case of default, the HFC can be given the power of sale without intervention of the courts; and, (2) it avoids the formal registration process and the accompanying Stamp Tax, which can be 10 percent and more of the price of the unit.[10] While the lack of registration increases affordability, it restricts use of the property for collateral for other loans and may lead to confused title

[9] See, for example, Struyk (1990).

[10] Actually, the equitable mortgage is subject to small stamp tax payments in two states, Maharastra and Gujarat.

141

claims. The NHB has taken the leadership in working on this issue and has designed a simple procedure for households to use after taking the mortgage loan, which in effect would register the property without having to pay the stamp duties. The procedure has been proposed as an amendment to the National Housing Bank Act. The several amendments to the Act are now under review by the Ministry of Law.

7.5 Limited Array of Mortgage Instruments

Many countries with inflation rates at 10 percent or higher have considered increasing affordability for potential homeowners through adopting mortgage instruments that deal effectively with the "tilt" problem of the standard fixed rate mortgage (FRM) of the type offered in India. Under the FRM, payments as a percentage of income are high as a percent of income in the early years of the mortgage and decrease steadily over time as the borrower's income increases. Other instruments--such as the Graduated Payment Mortgage (GPM) or the Price Level Adjusted Mortgage (PLAM)--increase the size of the loan the household can take using the same share of his income for mortgage payments, by rearranging the mortgage payment stream so that payments are larger in nominal terms (although at least close to constant in real terms) in later years.[11]

In principle, NHB should take the lead in educating the industry about the strengths and weaknesses of such instruments and advising them on when their use is appropriate.

[11] Additionally, introduction of adjustable rate mortgages (ARMs) should be considered as a way for HFCs to minimize their interest rate risk, a risk that will become more important if HFCs are permitted to take shorter term deposits and if inflation become more volatile.

However, thus far the only actions taken by NHB were a brief notice about the GPM in its 1990 "Concept Paper" (p.30) and a 1988 RBI circular on advising GPMs.[12] Independently, HDFC and few other HFCs it helped establish have been offering GPMs and other non-FRM instruments to selected borrowers for several years. Also, in November 1988, the RBI advised banks that they could consider use of the Graduated Payment Mortgage in response to customer requests. Thus, some "ground preparing" steps have occurred, and the time is ripe for NHB to provide the necessary information and guidance.

7.6 Creative Underwriting of Loans for Low-Income Borrowers

NHB's motto is "Small Man First." Acting on it, the NHB designed its refinancing program so as to concentrate its lending resources on low- and middle-income families. The HLA scheme, by establishing the creditworthiness of non-salaried workers through the record of their regular savings, should open formal housing finance to households who would not otherwise be served. NHB has not been active in another area however: helping the HFCs to develop flexible underwriting standards for loans to low-income, especially self-employed, borrowers who are not HLA participants. While it would be unwise to set targets for HFCs to reach these households, the HFCs are certainly more likely to consider lending to them if they understand alternatives for minimizing the risk of payment delinquency or default.

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[12] NHB indicates that this November 2, 1988 circular was issued at its behest.

7.7 Mortgage Foreclosure

The difficulties of foreclosing on a defaulted mortgagor in India are legend. A direct consequence of these difficulties is that lenders must be highly conservative in underwriting loans--meaning that marginal borrowers are denied credit. If foreclosure were less costly and time consuming, the size of loss associated with default would be less, and lenders would be more willing to make loans to less qualified households or to demand less collateral of current borrowers. An indirect consequence of the difficulties in foreclosing is to raise questions about the quality of assets held by HFCs, which makes it more difficult for them to raise funds by equity or debt offerings. Other things equal, successfully dealing with the foreclosure issue would increase the loan-to-value ratios offered by HFCs to borrowers of the types now receiving loans, permit HFCs to loan to groups presently viewed as high risk, and facilitate HFCs efforts to raise funds.

In the past few years, alternatives for expediting the foreclosure procedure have been advanced, and legislation for adoption of two options was formulated and began moving through the review and legislative process.[13] One of these procedures would be created in conjunction with a mortgage insurance scheme to be offered by the General Insurance Corporation. Although the legality of the scheme has been approved by the Ministry of Law, opinion remains divided among various ministries as to whether to proceed; and the scheme has not been presented to Cabinet.

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[13] Madway's (1989) analysis gave substantial impetus to developing these options; see Struyk (1990, pp.9-13) for the status of the initiatives as of the fall of 1989.

The alternative, formulated primarily by the NHB, would be created through an amendment of the National Housing Bank Act, under which financial institutions with a "nexus of interest" with the NHB could use the expedited procedure. The nexus would be established by the institution's participation in NHB's refinancing program. Two versions of the proposed amendment to the National Housing Bank Act are now under review. The versions differ on the extent to which access to the expedited procedure is provided directly to HFCs. Under the version with more limited access, NHB would have to access the expedited procedure on behalf of the HFCs--a role NHB hopes to avoid.

7.8 Simplification of Title Investigation

In India the process of investigating a property's title as part of the mortgage origination process, to insure that is free of impediment, is expensive. For some time Indian housing lawyers have been considering alternatives to the present system. NHB has been active in this effort in the past years. However, because title registration is a state subject, action must come at that level. NHB has participated actively in a committee investigating the possibility of implementing the Torrens system of title registration.[14] At the present time it appears that the government of Tamil Nadu has agreed to revise its registration system to move it as close as possible to the Torrens system. This would demonstrate a potentially

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[14] Under the Torrens system, on the first occasion that an existing or new property is transferred, the competent authority issues a certificate stating that the new owner is indeed the owner. This certification is based on a thorough search of the title history. However, in subsequent transactions involving the property, reference to the certification is all that is necessary by way of title search. Importantly, if a defect in the title is subsequently alleged, the state bears the responsibility, not the new owner.

important cost-cutting measure in the home acquisition process.

7.9 Conclusion

In the comparatively brief period of two years, the NHB has moved with some effect in a large number of areas to reduce the constraints to the development of the housing finance system. Of course, much remains to be done.

In summarizing the record it is useful to divide the eight areas reviewed above into two groups: those posing the more serious and immediate constraints to system development and those whose resolution is important to longer-term development. Those in the first group include:

-- mobilizing savings from households
-- raising the low interest rates on small housing loans
-- strengthening the mortgage instrument
-- expediting foreclosure procedures.

In the latter three areas, NHB has made significant progress: it has dealt directly with the low interest rate on small loans through its refinancing program, and the proposed amendments to its Act will result in very substantial progress in strengthening the instruments and expediting foreclosures. As to the mobilization of savings from households, the record is more mixed and the situation more complex. The HLA scheme certainly should be a help to HFCs, but it has been withheld from most of them on what appear to be questionable grounds. Also, HFCs feel themselves badly disadvantaged by the RBI's prohibition of their accepting deposits for less than 24 months, although the extent of the handicap is not clear.

NHB has been notably less active in the other four areas:

-- mortgage instrument standardization
-- introduction of additional types of mortgages
-- creative underwriting of loans for low-income borrowers
-- simplification of title investigation.

While it is easy to point to the middle two items in the foregoing list as evidence of lack of concern for the low-income borrower, immediate progress on them may not be the most important factor. NHB's targeted refinance program and improved foreclosure procedures may be more important to delivering loans to this group. Of course, progress in all of these areas will be important to future system development and to determining the extent to which low-income households are served by the housing finance system.

8. Program Management

This chapter discusses the way in which the HG-003 loan program was managed by the combination of USAID and the NHB. Three aspects are considered: how the program of technical assistance and training was executed, the extent to which the Master Program Implementation Plan was carried out, and the degree to which the project was implemented in line with the schedule defined for it in the Project Paper.

8.1 Technical Assistance and Training[1]

The specific contents of the technical assistance and training program are reviewed in Chapter 6. An implementation plan for the program (the MPIP) was carefully and thoughtfully laid out by USAID staff near the beginning of the projects.[2] It has been executed quite efficiently and essentially on schedule. As noted previously, the major problems in execution were the two efforts to establish on-going working relationships between U.S. and Indian institutions--FNMA with the NHB, and the Fels Center with HMSI. In both instances, lack of success in achieving the desired working relationship does not appear attributable to USAID.

It is worth noting that the technical assistance and training was highly concentrated on the NHB with much less attention to other government agencies. And little was directed to

[1] This description is of technical assistance provided <u>in addition to</u> the long-term resident and local national advisors for urban projects stationed at USAID.

[2] The internal USAID document is "Urban Strategy Resource Requirements."

increasing the capabilities of HFCs. It seems desirable to redress this imbalance.[3]

8.2 The Master Program Implementation Plan

The MPIP lists a large number of actions to be taken by the NHB as part of the loan agreement. Overall, the NHB receives a mixed review for its performance in this area; likewise, USAID staff bear some responsibility for not monitoring progress and encouraging more timely action by NHB in some of these areas.

Performance for selected provisions of the MPIP is briefly inventoried below; the substance of nearly all of these provisions receives more complete treatment in earlier chapters.

Selection criteria and procedure for selecting HFCs. (MPIP, section A) Successfully executed.

Reports and statements to be submitted by HFCs. (MPIP, section B.v) Performance in this area has been poor, as evidenced by the lack of reports found when USAID staff visited NHB to examine them in the spring of 1991.[4]

Development of plan of technical assistance to HFCs. (MPIP, section E) Draft plan prepared.[5]

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[3] the NHB reports the following allocation for the 23 persons sent abroad for training: NHB, 11; commercial banks, 5; HFCs, 4; state government, 2; and GOI,1.

[4] "Do-Diligence [sic] on conditions precedent to Disbursement of HG-003 first tranche," memo prepared by C. J. Billand, based on visit to NHB Bombay on 13 and 14 March 1991.

[5] This very abbreviated plan is a combined technical assistance and training program. It was handed to the team but it has not yet been submitted to USAID.

Development of comprehensive training program. (MPIP, section E) Draft plan prepared. However, little training activities have been undertaken (see Chapter 6).

Holding of quarterly meetings with Chief Officers of the Principal Housing Finance Companies. (MPIP, section E) Meetings have been held on a regular basis.

Appropriation of a portion of NHB's profits for rendering technical/training assistance to HFCs. (MPIP, section E) Rs. 20 million has been appropriated but not yet used for this purpose.

Program of regular inspection of HFCs obtaining refinance under the HG loan. (MPIP, section G) In March 1991, NHB provided a statement about the inspection program, which is now being implemented. Under it, inspections of private HFCs will be made annually and of all HFCs every two years.

General program for strengthening framework for overseeing the functions of HFCs. Plan still under preparation.

Procedure to monitor end-use of subloan. (MPIP, section F) As noted in Chapter 4, a rule-of-thumb is being used to identify loans qualifying for refinancing under the HG loan. However, NHB examiners are making separate visits to perform a sample checking of the documents for 10 to 20 percent of loans refinanced under the HG loan program.

Assisting HFCs in mobilizing additional resources. (MPIP, p.13) This is for mobilization of funds in addition to those provided through refinancing. Only action to date is a program of advertisements by NHB announcing recognized HFCs, which is designed to increase public confidence in the institutions and help the HFCs attract deposits and term loans.

The project file and discussions with NHB staff make clear that the presence of the Conditions Precedent certainly caused NHB to devote more energy to technical assistance, training issues and regulatory issues than it would have otherwise. However, not all the conditions were met before the first loan disbursement, and USAID staff should insure that they are met before the next disbursement.

8.3 Adherence to the Project Schedule

The Project Paper (PP) contains the Program Implementation Schedule (pp.53-4). This schedule with the projected dates and actual dates when various tasks were accomplished is shown in Table 8.1. If the date of the disbursement of the first $25 million in HG-loan funds is taken as a benchmark, the project was at that point running approximately fifteen months behind the schedule indicated in the PP. However, the second disbursement was not scheduled to be completed until December 1992, and this may now occur even before the end of December, 1991. Hence, while the project began slowly, its execution is accelerating.

The initial delay was entirely because preparation of the Implementation Plan was more than a year behind schedule due to NHB's preoccupation with launching its programs and its lack of need for the funds available under the HG. With hindsight, the original target dates look inappropriately optimistic. Once the Implementation Agreement was drafted, the program experienced no further slippage.

Assistance from USAID to NHB in carrying out some technical assistance and training tasks was hampered by the delay in being able to recruit a local professional to work on the program for USAID. This delay is attributable to GOI procedures under which five ministries had to approve the hiring.

8.4 Conclusions

Overall, program management appears to have been effective. The thoughtful training and technical assistance program designed by USAID at the beginning of the program was

151

largely executed; those planned activities that were not completed were not due to lack of diligence by USAID or the NHB. NHB succeeded in meeting the Conditions Precedent in the loan agreement. However, USAID staff might have been more diligent in pursuing some areas, and should require NHB to more fully comply with the MPIP prior to the next disbursement. Overall, the presence of the Conditions Precedent clearly caused NHB to devote more energy to technical assistance, training and regulatory issues than it would have otherwise. The project, while initially off to a slow start compared with a perhaps unrealistically optimistic schedule, has now "caught up"; and the second tranche of funds may well be disbursed ahead of the original schedule.

TABLE 8.1
PROJECTED AND ACTUAL PROGRAM IMPLEMENTATION SCHEDULE

projected date by which action would be complete	actual date when action was completed	action
Sep 30 1988	Sep 1988	US $50 million project paper was approved; authorization for US $25 million was signed.
Sep 30, 1988	Sep 1988	Mission issued Letter of Advice.
Dec 31, 1988	Dec 1988	NHB technical staff received short-term orientation training.
Nov 30, 1988	Dec 1989	Draft Implementation Agreement was prepared by USAID and sent to NHB.
Dec 31,1988	Dec 1988	NHB initiated consultations with HFCs.
Dec 31, 1988	Sep 1989	USAID recruited local professional for program support.
Mar 31, 1989	Mar 1990	Implementation Agreement was signed by USAID and NHB.
Jun 30, 1989	Mar 1990	Loan Agreements between NHB and individual HFCs were negotiated and signed.
Jul 15, 1989	Jun 1990	NHB processes first disbursement to HFC.
Sep 30, 1989	Dec 1990	Legal opinions, MPIP and other Cps to Investor Selection were completed.
Oct 31, 1989	Jan 1991	NHB, or approved designee, sought US Investor.
Dec 31, 1989	Apr 1991	HG Loan and Guaranty Agreements were negotiated and signed.

153

projected date by which action would be complete	actual date when action was completed	action
Dec 31, 1989	Apr 1991	NHB drew down authorized disbursement of HG loan (US $25 million).
Dec 31, 1989	Mar 1991	NHB prepared short-term training plan (draft).
Jun 30, 1990	Jun 1991	Mid-term evaluation was completed.
Aug 31, 1990	Dec 1990	MPIP was updated.
Sep 30, 1990		Second tranche (US $25 million) was authorized.
	Sep 1989 Jul 1990 Jun 1991	US $13.75 million US $ 5.00 million US $ 6.25 million
Dec 31, 1991	Apr 1991	NHB drew down and disbursed remainder of the first tranche US $25 million.
Dec 31, 1991	(end 1991)	Draw-down of second tranche to be completed.
Jun 1991		Final evaluation of program to be completed.

154

9. Principal Conclusions and Recommendations

Numerous conclusions and recommendations have been presented in specific chapters of the report. Here attention is concentrated first on the highest priority recommendations and conclusions. The chapter closes with a brief section on the impact of USAID's assistance.

Supervision and Regulation. The team recommends that NHB give its highest priority to strengthening the system for supervising housing finance companies before one or more HFCs fail and damage the reputation of the entire system. Such an outcome would undo much of NHB's laudable and effective work in promoting the housing finance system. An adequate number of staff, well-trained and dedicated full-time to supervision under a managing director charged solely with this responsibility, is essential.

It is important to note in this context that NHB has already recognized important limitations in its regulatory powers, in part because of cogent outside analysis. And it has moved with dispatch to draft the amendments to the National Housing Bank Act that are necessary to deal with the most serious of these limitations. The draft amendments are under review.

Promotion. By nearly any standard NHB has been highly successful in producing a surge in the number of housing finance companies and the volume of formal lending for housing. It has accomplished this through both its specific programs for refinancing and a number of smaller, less dramatic actions aimed at garnering privileges for the sector, usually increasing its efficiency.

The team believes that the next logical step in enhancing the development and competition of the sector will involve giving the HFCs some latitude in setting the interest rates on their loans. This could be accomplished by NHB establishing substantial ranges within which lenders could set their rates, or by establishing minimum or floor rates for loans of different sizes. The rate on large loans, i.e., those above Rs. 2 lakhs, would in any case be completely market determined--through NHB's setting a floor rate for these loans. NHB can in effect control the minimum rates on small loans through its refinancing rates.

With this flexibility, all HFCs could vary interest rates (even for the same loan) with perceived riskiness or ease of servicing (e.g., payroll deduction or not). Moreover, it would give HFCs more flexibility in raising funds from high cost sources. Individual HFCs should be able to identify "market niches" in which to work successfully. The team believes that the newer HFCs need not fear cut throat competition from the larger or more established companies. Lastly, in light of the large interest rate increases on loans recently granted to the urban cooperative banks, an NHB request to the Reserve Bank of India for such a change may well be accepted.

Lending to Low-Income Households. Given use of the rule-of-thumb that loans of Rs. 50,000 refinanced by NHB were taken by households below the urban median income level, and the fact that most reporting is on this basis, it is not possible to know the extent to which low-income households are being served. Consequently, the team's first recommendation on this score is that the necessary data be assembled to determine the share with precision.

The incentives NHB has established to encourage lending to low-income families seem reasonable. If at any time NHB decides to limit the volume of refinancing any one HFC can take for any reason, the team recommends that loans to low-income households be exempted from the limit. This should provide a significant increase over the present incentives to do such lending.

Funds Mobilization by NHB. NHB has very large implicit outstanding commitments for providing refinance to the HFCs. It has not made any systematic estimate of the size of these commitments, and the team strongly recommends that this be done as soon as possible after further discussions with the principal HFCs. These projections will provide the targets essential for future planning.

Even in the absence of these targets, the NHB is aware that its commitments probably exceed the volume of funds it will be able to obtain from the "favored sources" --i.e., low-cost funds allocated by government bodies--upon which it has relied exclusively to date. It has, therefore, begun exploring options for obtaining funds from the market. These ideas have not yet been converted to plans. A sound strategy is obviously required.

The team recommends that in future loans from USAID to NHB particular attention be given to NHB's success in mobilizing an increasing percentage of its total resources from the more open financial markets. The team is aware that implementation of this recommendation may require that refinancing rates (and therefore mortgage interest rates) be increased. Nevertheless, without turning to the market, NHB will probably soon have to begin rationing the amount of financing it can provide to HFCs.

The USAID Role. The team's overall assessment is that USAID's involvement has been highly constructive in this stage of development of the Indian housing finance system. Both capital and technical assistance have been productive.

With respect to the capital assistance, several of the conditions in the Master Program Implementation Plan (MPIP) were effective. The norms set in the MPIP for sub-borrowing

157

HFCs have been adopted for general use by NHB. The half-yearly reports and other monitoring required in the MPIP have been the core of NHB's supervisory activity, and the poor performance in gathering data from even the recognized HFCs has alerted senior management to the larger supervision problems. Similarly, the conditions in the MPIP requiring technical assistance and training plans caused NHB to turn to these activities. The impact of the MPIP becomes clear when it is observed that work began in these areas only at the point NHB wished to draw on the HG loan funds. NHB management now admits these areas were neglected during its "start up phase" and that more needs to be done.

The team also believes that NHB has treated the requirement to loan to low-income families seriously, and has tried to steer HFCs to open offices in smaller cities as one way of increasing lending to qualifying households. Nevertheless, USAID has not insisted on full compliance with all of the terms beyond the financial conditions in the MPIP for dispersal of HG loan funds in the past; the team recommends greater attention to all the conditions in the MPIP in the future.

The technical assistance components have also proven valuable. Three of the studies had demonstrable impacts on NHB thinking: Croft's on regulation (which built on Wilson's earlier paper); Madway's on foreclosure; and Struyk's on possibilities for a secondary mortgage market. In addition, the team's sense is that those who participated in the training courses profited from them--not simply in acquiring technical knowledge but in becoming more receptive to new ideas for development of the Indian housing finance system.

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159

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160

ANNEX 1.1:
SCOPE OF WORK FOR THE EVALUATION

STATEMENT OF WORK
Housing Finance System Program: Interim Evaluation
and Preparation of a Project Paper Supplement

BACKGROUND

The long term goal of the Housing Guaranty (HG) Program in India is the development of a financially-sound housing finance system which is market-oriented, capable of raising its capital from domestic resources, and provides long term shelter finance to a wide range of households, including those below the median income.

Beginning in 1981, A.I.D.'s objective was to assist the Housing Development Finance Corporation (HDFC) to demonstrate the commercial feasibility of market-oriented loans to lower income households, and to improve HDFC's ability to respond to increasing market demand. Through 1989, $125 million of HG funds were directed to HDFC.

The expansion of HDFC under HG-001 was the first building block in developing the system. HG-002 was designed to support HDFC's transition to a more active pursuit of its low income client group, and to support the institution's stable financial growth through the provision of additional long term capital. With the support of HG-002, HDFC expanded its operations geographically by opening new branch offices, and increased efforts to finance homes for lower income households. Later tranches of the program were designed to give institutional support for the development of new housing finance companies.

The final evaluation of HG-002 was completed in December of 1989, found that

> "To sum up, HDFC has made great headway in demonstrating the effectiveness of a market-oriented approach to housing finance—in particular, the level and share of market-oriented investment in and finance for housing has very clearly increased due to HDFC's operations. These levels and shares are likely to increase further in coming years as the activities of imitators come on line. The availability of financing for lower-income households has also increased, even though the affordability of housing within many cities has declined over the same period. Finally, HDFC's record of risk management is good, in spite of the continuing lack of a viable foreclosure law."

162

The third phase of the program, which began in September 1988 and will continue into 1993, HG-003, seeks to expand the market-oriented housing finance system by directing HG support to a group of emerging private and joint sector housing finance companies (HFCs). HG loan authority of $50 million was provided for capital support, and technical assistance and training funds were allocated for support through the mission's Development & Management Training (D&MT) and Technical Assistance Support Program (TASP).

The program seeks to achieve the expansion objective by (1) providing critically-needed lending capital to meet the near- and mid-term needs of eligible companies serving a number of geographic areas; (2) fostering a relationship between recent entrants to the sector and the National Housing Bank (NHB) in order to improve the new firms' abilities to mobilize resources, manage their portfolios, increase lending to low-income households, and to operate effectively within the existing public policy environment; and (3) addressing a number of sectoral constraints on expanding the system, through technical assistance and training.

The program channels funds through NHB, which provides refinancing of mortgage loans originated by HFCs that meet the following Program eligibility requirements:

(a) Adherence to sound underwriting practices;
(b) Usage of market principals in their operations;
(c) Implementation of adequate collection procedures; and
(d) Lending to households below the median income.

As of June 30, 1990, NHB has refinanced $150 million of lending by primary mortgage lenders. This facility is a major incentive for encouraging the formation of new HFCs because of on-lending resource constraints. To qualify for refinance, companies must apply to NHB and meet eligibility criteria–including financial fitness. Thus far, there have been forty applicants to NHB. Of these, NHB has recognized eleven, and twenty-two others have partially met the criteria for full-fledged recognition.

There is now an opportunity to expand the program by providing an additional $50 million in HG loan authority, to be supported by a new Program specific supplemental bilateral grant of $3.2 million.

The current technical assistance activities are supported by two mission programs: D&MT, and TASP. The PACD for the D&MT program is June of

1992. Therefore, this resource will no longer be available to fund technical assistance and training activities. As an alternative source, the TASP program poses impediments in the form of restrictions on the use of funds for training activities. Therefore, there is a need for a new DA funded Program specific grant.

Based upon anecdotal evidence, it appears that additional capital in the form of a HG loan add-on to support NHB's refinance program can result in additional programmatic and policy dialogue accomplishments. These are more particularly described in the attached Draft Project Identification Document (PID).

In February of this year, a Concept Paper which outlined the purpose for a new grant program and additional HG loan authority, was approved by the Mission Review Committee (MRC). Subsequently, a Project Identification Document (PID) was prepared, and is currently being reviewed by the Mission, before being forwarded to A.I.D. Washington for approval.

ARTICLE I: TITLE

Housing Finance System Program: Interim Evaluation and Preparation of a Project paper Supplement.

ARTICLE II. OBJECTIVES OF THE INTERIM EVALUATION AND PROJECT PAPER SUPPLEMENT ACTIVITY

This activity consists of two separate but linked components: an interim evaluation of HG-003, and the preparation of the HG-003A PP supplement. In principle, the objective of this two-part activity is a "look backward/look forward" exercise. The interim evaluation provides an opportunity to measure the accomplishments, and recommend alterations in program direction. The preparation of the PP supplement provides an opportunity to incorporate these recommendations into a new grant program for technical assistance and training activities to support additional HG loan resources.

The primary objective of the interim evaluation component, described in the following Statement of Work Interim Evaluation, is to appraise progress made towards achieving the objectives of the Housing Finance System Program (Program), especially improvement of the management performance of joint and private sector HFCs. The evaluation will identify and quantify major accomplishments of the Program to date, and obstacles to Program implementation.

164

A subsidiary purpose of the evaluation is to assess the role and contribution of the NHB to promotion of HFCs as integral part of the housing finance system.

In addition, the analysis is designed to provide guidance for the implementation of the remaining part of HG-003; and for the design of the proposed add-on program, HG-003A, and new grant program to support additional technical assistance and training activities, which would be intended to strengthen and extend the coverage of private and joint sector HFCs.

The objectives of the PP supplement component, described in the Project Paper Supplement Statement of Work, are to prepare an amendment to the current HG-003 PP to incorporate a new grant Program estimated at $3.5 million , and authorize additional HG loan funds estimated at $50 million. The PP supplement will incorporate the findings and recommendations of the interim evaluation by revisiting as appropriate, the Program's background, description, implementation plan, project analysis, conditions precedent and annexes. The PP Supplement will provide an agenda for technical assistance and training to support expanded programmatic and policy dialogue objectives. Based on an analysis of demand for refinancing undertaken in the interim evaluation, the PP Supplement will substantiate the amount of additional HG loan funds and DA grant funds to be authorized in the HG-003A add-on.

ARTICLE III: STATEMENT OF WORK

A. INTERIM EVALUATION

The contractor shall conduct an evaluation which addresses the following:

1. How was the performance of private and joint sector HFCs changed since the introduction of the NHB's refinancing program? How successful have the emerging HFCs been in mobilizing resources for lending? Is it possible to attribute any changes to actions by NHB?

2. To what extent has the network of financially-sound, market-oriented HFCs grown since the inception of the Program?

3. How successful have emerging HFCs been in lending to below-median income households? What problems have they encountered? Are there specific low-income groups that are substantially not being reached by the present HFC lending products?

4. What support has been given by NHB to primary lenders in pursuit of the program objectives? Have the NHB's plans and policies to exercise a regulatory function been developed and exercised in such a way as to promote sound development of the housing finance system.

5. To what extent have sectoral constraints on expanding the system been addressed since the start of the program? How effective have the technical assistance and training activities been to date, in promoting the Program's objectives? How can further technical assistance and training best help to address these constraints?

6. What is the capacity of the housing finance system to generate additional financing which meets the existing criteria for eligibility?

The Contractor will provide USAID/India and NHB with a list of subsidiary questions and issues to be discussed with the HFCs, and the data to be made available for examination by the HFCs. These lists will be provided to USAID/India on or before the date of arrival of the team in India.

Since the focus of HG-003 is the performance of HFCs in the joint and private sectors, the analysis will focus on this group of primary lenders. Where required by the context, however, the statistical analysis and text will describe the broader housing finance system, including all HFCs, or all primary lenders as appropriate.

In order to best answer the questions presented above, the Contractor shall follow the methodology outlined below:

1. Performance of HFCs

A major objective of the Program is to "foster a relationship between recent entrants to the sector and NHB in order to improve the new firms' ability to mobilize resources, manage their portfolios, increase lending to low-income households, and operate more effectively within the existing public policy environment". The Contractor will determine the extent to which HFCs have improved their performance in these specific areas, and the extent to which the NHB has assisted in supporting these achievements.

The Contractor will make quantitative estimates of output, purpose and goal achievement according to the indicators listed in the Logical Framework (Annex C), so far as readily available data permits.

166

Particular attention will be paid to the issue of resource mobilization, documenting the record of HFCs in mobilizing resources from different sources and the mechanisms used to do so. The Contractor shall report on the success of HFCs in mobilizing households deposits. Several reports by and for A.I.D. have identified constraints on resource mobilization. The Contractor will re-examine these lists, and state the extent to which changes have occurred in the environment for resource mobilization over the past three years.

Other data to be reported will include default rates and arrearages, and, to, the extent possible, rates of disbursement of private versus joint and public sector firms.

Measurement of outputs will be made on the basis of comparison of data provided for all HFCs eligible to participate in the HG program, over a period covering about the last three years. Because of expected dominance of the statistics by HDFC, data for th company will be treated separately. The statistical data will have been collected in advance by NHB and will be made available to the Contractor in the proforma attached as Annex D. The data will be provided to the Contractor by USAID/India one week before the arrival of the Contractor in New Delhi. Information on HDFC will be obtained from the recent evaluation report of the HG-002 project. Additional data on HFCs will be obtained from annual reports and other published sources. The Contractor will visit a sample of eligible HFCs to supplement the information provided by those companies to NHB, and make an assessment of the management practices of those companies.

The HFCs sampled will be selected by USAID/India and NHB in advance of the arrival of the Contractor. They are likely to comprise one HFC based in Delhi, and three based in other cities. USAID/India and NHB will have determined that the selected HFCs will give appropriate assistance to the Contractor, including agreement to make senior management available for interview, permitting the Contractor to examine the HFCs' records, and seconding a staff member to work with the Contractor during the period of the visit.

Determining the role of NHB in facilitating the changes will be made on the basis of interviews with senior staff of NHB, of HFCs participating in the NHB refinance program, appropriate GOI and A.I.D. officials and others involved with the housing finance sector in India.

2. Growth of the HFC network

The Contractor will record changes in the number of HFCs over time, both those classified by the Registrar of Companies, and those recognized by NHB as qualifying to participate in NHBs refinance program. The Contractor will offer opinions on the reasons for the increase, or lack of increase in the number of companies.

The Contractor will examine the issue of classified HFCs. As best as possible, the Contractor shall attempt to quantify the number of HFCs classified by the Registrar of Companies. An examination of NHB's attempts to contact, evaluate and oversee the activities of classified but not recognized HFCs shall be undertaken. The Contractor shall offer opinions on NHB's success or lack thereof, to extend oversight and regulation authority to classified HFCs.

The Contractor will evaluate changes over time in the number and loan volume by size of loan, for recognized HFCs. The Contractor will examine NHB's process for recognizing HFCs. The Contractor will offer opinions on the reasons for the increase, or lack of increase, in number and volume of loans, and the appropriateness of NHB's process for recognition.

The Contractor will identify changes in the network of HFC outlets over the three previous years. "Outlets" will be taken to include both head and branch offices, and other offices and agencies used by the HFCs to raise household savings or make loans. The Contractor shall identify any changes in the type and distribution of outlets, and will identify ways in which physical access by households to HFCs has changed and, correspondingly, groups for whom access is still difficult.

Data for this question will be obtained from the same sources as for question 1: annual reports and statistical returns provided to the Contractor prior to arrival in India; and addition information collected in India including visits to sample HFCs.

3. Low-income household participation

The Contractor shall report, for all eligible HFCs, changes in the volume, both absolute and relative, of lending to below-median income households, over the past three years. The Contractor will also assess for the sample HFCs and for other HFCs as permitted by their published accounts, their implementation plans, policies and practices related to low income households.

Insofar as data are made available to the Contractor regarding the income distribution of HFC borrowers, the Contractor will record the degree to which companies' programs are reaching low-income households. So far as data permit, the Contractor shall identify different low-income beneficiary groups that are being reached, or not, by the lending programs of each HFC: i.e., formal sector employed borrowers versus other informal sector employed borrowers; women-headed households versus total households; households in large cities versus total households; households with older heads versus total households.

The Contractor shall attempt to assess the degree to which HFCs have assimilated the objectives articulated in the HG-003 Project Paper. With respect to lending to low-income households, the Contractor shall report on their success (or failure) in meeting these objectives, and document the problems that have been encountered in this area.

Statistical data for this assessment will be collected and supplied to the Contractor by USAID/India in advance of the Contractor's arrival in India. It will be supplemented by the visits to sampled HFCs.

4. NHB Support for System Development

A major objective of HG-003 is the provision of programmatic support to primary housing finance companies. Support was envisaged to include the provision of technical assistance and training–interpreted in a broad sense–and the establishment of an appropriate regulatory framework within which the development of HFCs would be promoted. In this context, support would include activities such as regularization of procedure for advertising, provision of a forum for discussion of common problems and dissemination of research relating to fund mobilization, and similar matters.

Many steps have been taken by the NHB and others to provide such support, often with the assistance of USAID/India. A number of other activities have been initiated, but not yet completed. The Contractor is requested to list activities that have already been taken in this regard, and activities that have been initiated, together with the expected outcome of each activity. The Contractor will assess the quality and appropriateness of the developmental activities to reach the stated objectives. The Contractor will assess the current and future role of Indian institutions (other than NHB and the HFCs) which have participated in technical assistance and training activities.

As part of its implementation planning for the program, NHB prepared a Master Program Implementation Plan (MPIP). The Contractor will review and evaluate the progress made by the NHB on the MPIP.

5. Sectoral Constraints

The Project Paper for HG-003 identified a number of constraints to development of the housing finance system, and subsequent papers prepared by and for A.I.D. have listed other constraints. Some of those are directly addressed by the main thrust of this Program, such as the shortage of lending capital available to primary lenders. The Project Paper explicitly stated that certain other constraints could not be addressed by this program, including urban land prices, tenure and titling problems and inadequate urban infrastructure. It was, however, intended that a further group of policy-related constraints to expanding the housing finance system could be addressed through technical assistance and training

By reviewing technical papers relating to India's housing finance system which have been written in the past three years, the Contractor will identify these constraints (but need not describe them at any length). The Contractor will make a concise statement of steps to be taken to address these constraints. It is likely that the presentation of these findings will be in simple tabular form.

The Contractor will also state what measures, if any, have been taken to address these constraints over the past three years.

The analysis of constraints will be undertaken from a review of recent literature, some of which will be supplied to the Contractor by USAID/India. The statement of measures taken will derive from interviews with officials and representatives of housing finance institutions in India, and from documentary evidence.

6. Demand for Additional Refinancing

The conditions precedent to disbursement of loan funds under HG-003 describe which categories of rupee-denominated expenditure by the NHB are considered "eligible" for including in the HG loan. NHB must continue to incur eligible expenditures equivalent to an additional $25 million for further borrowings to take place under the HG program. The magnitude and timing of these expenditures is dependent on several factors, not least of which is the ability of HFCs participating in the NHB's refinance scheme to make loans affordable to households below the median income.

The Contractor shall examine the capacity of the housing finance system to generate additional financing which meets the existing criteria for eligibility for HG loans. The Contractor will describe and make projections of the principal factors which influence demand, including the willingness of companies to make lower income loans and the demand by households for such loans. The demand, in turn, will depend on the conditions under which loans are offered. Other factors which may be considered are the supply of and demand for different types of loan instrument.

Based mostly upon information provided prior to arrival in India, the Contractor will make quantitative projections of the demand for NHB refinancing which would be eligible for HG loans, to cover the next three years. Alternative projections will be presented, based on differing assumptions of growth of demand for low income housing loans.

7. Program Management

The Contractor shall assess how USAID/India, RHUDO, and Indian institutions have met their responsibilities for implementing the program, provision of funding, personnel, timeliness of approvals, and coordination. The Contractor will offer opinions on how these can be improved upon.

8. Recommendations

The Contractor will make specific recommendations for the issues described in Sections 1 through 7., to improve the performance of the current program and the add-on. The Contractor shall cite who is responsible for implementing the recommendations to improve the program's performance.

B. PROJECT PAPER SUPPLEMENT

The Contractor shall prepare a PP Supplement which is based in part upon the findings and conclusions of the interim evaluation. In consultation with the representatives of USAID/ New Delhi and RHUDO/Bangkok, the Contractor will review the PP for the Housing Finance System Program (HG-003), and prepare a PP Supplement which amends, as appropriate, the background, description, implementation plan, budgets, project analysis, conditions precedent and annexes as described in the HG-003 PP.

A draft PID has been prepared to amend the HG-003 Program. The original Program goal and purpose will remain unchanged; Program activities will continue to support three principal objectives which are to:

171

- mobilize domestic resources for housing;
- increase private sector participation in housing nance, and
- increase access of middle and low-income famil..s to housing finance.

It is currently anticipated that the expanded Program (HG-003A) will call for approximately $3.5 million in new grant resources, and add an additional $50 million in HG resources. These levels shall be examined, revised as necessary, and justified in the PP Supplement. The HG loan and grant resources will be used to support policy change in the sector, NHB's refinancing window for qualified Housing Finance Companies (HFCs), and to manage the Program.

The following summarizes the main themes as presented in the draft PID for HG-003A:

> The main constraints to developing a healthier and more mature private sector housing finance system are related to the key objectives of the program: a) factors which inhibit mobilization of domestic resources for housing; b) disincentives to private sector participation in housing finance, and c) constraints against access by most middle- and low-income families to housing finance.
>
> India's new private sector housing finance system is at a critical stage in its development. The apex institution, NHB, is developing its role and responsibilities for refinancing, regulating and providing support to HFCs. New HFCs are forming in a broad geographical spread across India.
>
> The expansion of the Housing Finance System Development program will allow continued progress on system development by more carefully focusing on supply and demand issues. Because of resource constraints, new HFCs are starved for on-lending funds. Expanded technical assistance and training resources will be used to mitigate policy and programmatic hurdles to increase HFCs ability to raise savings deposits and borrowings.
>
> Private sector HFCs prefer to lend to the narrow higher income loan market. Higher income borrowers tend to meet more traditional underwriting standards, and are presumed to be lesser risks. The expanded program will offer incentives to HFCs to learn how to safely loan to the largest potential market for housing loans--borrowers with

172

household incomes above and below the median income—by setting aside a certain portion of HG loan proceeds for refinancing home improvement and plot expansion loans originated by HFCs.

Studies and training are an integral part of this policy oriented program. Decision makers have been extremely responsive to information provided through A.I.D. financed studies and consultancies on analysis of constraints and recommendations on options for the housing finance system. The growth of HFCs is a response to changes in the market. These institutions require training and support in their developmental phase.

The PID will be approved prior to starting the work. Copies of the approved documents will be provided to the Contractor at least one week prior to arrival in India.

Using the data, analysis and recommendations developed through the interim evaluation, the Contractor will meet with officials of NHB, the GOI, and joint and private sector HFCs, and USAID, as appropriate, to examine the issues related to amending the HG-003 PP, to incorporate the HG-003A program expansion agenda as described in the approved PID. Particular attention shall be paid to the policy objectives set forth in the approved PID, including the development and negotiation of realistic conditions precedent which will be required to achieve the recommended policy objectives.

The strategies for technical assistance and training shall also be examined, with particular attention on the role of the resident advisor to be placed in NHB offices in Bombay. The PP Supplement shall carefully describe the additional technical and training required to support the expanded programmatic and policy objectives.

ARTICLE IV: REPORTING

1. The Contractor will prepare two documents: a Draft Interim Evaluation (IE) Report which addresses Article III A; and a draft PP Supplement which addresses ARTICLE III B

The IE Report will include an abstract, an executive summary and a section summarizing the conclusions and recommendations of the evaluation, in addition to the main text. Three copies of the draft report will be submitted to USAID/India and one copy to NHB no later than two working days prior to the departure of the Contractor from India.

The PP Supplement will include text to describe changes in the HG-003 PP, as appropriate, in the background, description, budgets, implementation plan, project analysis, and conditions precedent. In addition, revised annexes will be prepared as required. Three copies of the draft PP Supplement will be submitted to USAID/India no later than two working days prior to the departure of the Contractor from India.

2. The Contractor will attend a briefing by A.I.D. shortly after arrival in India. The Contractor shall brief A.I.D. on its findings and recommendations after submission of each Draft Report. The Contractor shall also conduct a separate exit briefing on the findings and conclusions of the IE Report for NHB officials, prior to departure from India.

3. The Contractor shall submit one original copy each of the final IE Report and PP Supplement, within two weeks of receipt of A.I.D. comments on the draft documents. Both original documents shall be submitted to USAID/India along with five bound copies of each; the remaining five copies of each shall be sent to RHUDO/Asia. The originals shall be accompanied by a computer diskette, written on a Wang-compatible word processing program. In addition, the Contractor shall submit printed copies of the final documents to AID/Washington in accordance with the general provisions of the Contract.

4. Simultaneously with submission of the Final IE Report the Contractor will submit a draft of Part II of the "A.I.D. Evaluation Summary Form". A copy of this form, and of the instructions for completing it, are attached as Annex E.

ARTICLE V: RELATIONSHIPS AND RESPONSIBILITIES

The activities described herein shall be carried out by two teams; an IE Team, and a PP Supplement Team. Both Teams will consist of staff supplied by the contractor, along with representatives from USAID/India and RHUDO/Asia.

The IE Team will be directed by the USAID/India Urban Advisor. The USAID/India Evaluation Officer will serve as facilitator to the contractor. The RHUDO Evaluation Officer will provide coordination for RHUDO.

The PP Supplement Team will be directed by the USAID/India Urban Advisor. The RHUDO/Asia representative shall provide coordination for RHUDO.

ARTICLE VI: PERFORMANCE PERIOD

Coordination of the timing for the activities of the Contractor is essential. The field work for both activity components will take place over a five and one-half week period; with field work on each component overlapping during the middle of the period. The Contractor would begin its work on the interim evaluation component in India o/a June 7, with completion of field activities o/a June 27. The Contractor will begin its work on the PP supplement component in India o/a June 25, and complete its field work o/a July 15. The contractor shall coordinate the provision of its field staff to assure that this overlap can be accomplished.

Statistical data from the NHB, as described in Article III, and background reports, will be provided by USAID/India to the Contractor at least one week before departure of the Contractor for India. The interim evaluation analysis will begin on receipt of these data. Field work in India, including visits to a sample of four HFCs to be identified by USAID/India and NHB, will proceed for approximately three weeks. The draft IE Report will be reviewed by NHB, USAID/India, RHUDO/Asia and APRE/H. The consolidated comments from these four agencies will be sent by USAID/India to the Contractor within three weeks of receipt of the Draft IE Report. The Final IE Report will be completed no later than two weeks after receipt of comments on the draft report, o/a August 5, 1991.

Background reports for preparation of the PP Supplement will be provided by USAID/India to the Contractor at least one week before the departure of the Contractor for India. The background analysis shall begin on receipt of these data. Field work in India will proceed for approximately three we[illegible] The draft PP Supplement will be reviewed by USAID/India, RHUDO/Asi[illegible] APRE/H. The consolidated comments from these three agencies will be [illegible] by USAID/India to the Contractor within three weeks of receipt of the D[illegible] PP Supplement. The Final PP Supplement will be completed no later th[illegible] two weeks after receipt of comments on the draft, o/a August 19, 1991.

ARTICLE VII: STAFFING

Each team will consist of representatives from the Contractor, along with representatives from USAID/India and RHUDO/Asia. For the IE Team, th[illegible] Contractor will provide three representatives. For the PP Supplement T[illegible] the Contractor will provide two representatives.

USAID/India will provide logistic support to the Contractor for both components. NHB has agreed to second a senior staff member to assist th[illegible]

Contractor as needed during the field work for the interim evaluation. NHB and USAID/India will work to assemble relevant data which will be sent by USAID/India to the Contractor at the outset of each activity component.

ARTICLE VIII. LOGISTICAL SUPPORT

To supplement the equipment available in the Mission, the Contractor shall provide each of its representatives with portable computer equipment while working in India. The operating system for this equipment shall be IBM compatible.

ARTICLE IX: WORK DAYS ORDERED

For the interim evaluation component:

Housing Finance Specialist/Team Leader	28 Days
Housing Finance Specialist	28 Days
Housing Policy Specialist	28 Days

For the PP Supplement component:

Housing Finance Specialist/Team Leader	28 Days
Housing Policy Specialist	28 Days
TOTAL	140 Days

Project Title & Number:

NARRATIVE SUMMARY	OBJECTIVELY VERIFIABLE INDICATORS	MEANS OF VERIFICATION	IMPORTANT ASSUMPTIONS
Program or Sector Goal: The broader objective to which this project contributes: Sector Goal: To improve housing conditions of low income households. Project Goal: To increase the availability of formal housing finance to low income households nationwide.	Measures of Goal Achievement: Increase in the amount of funds lent for housing by the formal sector. Increased borrowing for housing by low income households.	Special financial sector studies. Project records.	Assumptions for achieving goal targets: That increased availability of formal housing finance will result in increased borrowing by low income households. That increased borrowing will improve housing conditions of low income households.
Project Purpose: To promote the development of a financially-sound, market-oriented housing finance system which makes long-term shelter finance available to a wide range of households, including those below the median income.	Conditions that will indicate purpose has been achieved: End of project status: A network of financially sound market-oriented HFCs serving households below the median income as well as those above.	Monitoring of number and distribution of commercial HFCs and their branches; studies of: financial structure, soundness; market shares; loan collection rates; terms of loans and types of facilities; volume of lending to low income households; etc.	Assumptions for achieving purpose: That the formal financial sector will permit new HFCs to operate in a financially sound manner. That sufficient demand exists in the target population to support system expansion.
Outputs: 1. Increased capital available for unsubsidized home purchase. 2. Increased geographical coverage by HFC branches. 3. New deposit and mortgage facilities. 4. Improved management practices of new and recent entrants to market.	Magnitude of Outputs: 1. Increased loan volume by project HFCs. 2. Substantial increase in branches of eligible HFCs. 3. Introduction of GPMs, ARMs or other creative instruments. 4. Improved compliance with intermediary's criteria; reduced management costs.	1. Project reporting requirements as specified in IA 2,3,4. Mid-term and final evaluations.	Assumptions for achieving outputs: That lack of capital is a major reason for present limited activity of HFCs. That HFCs will be willing and able to adopt sound practices. That HFCs will be willing and able to lend to low income households.
Inputs: 1. HG loan. 2. Grant funds for TA, training and evaluation. 3. Staff time, office and equipment from primary lenders 4. Technical and managerial support from intermediary.	Implementation Target (Type and Quantity) 1. US $50 million guaranty authorization, with disbursements over 3-4 years. 2. $2.9 million in grant funds. 3,4. In-kind contributions from implementing organizations.	1. Project records 2. Project records 3,4. Availability of staff and resources of implementing organizations to absorb TA, training and implement project.	Assumptions for providing inputs: 1. That NHB assigns adequate staff and other resources to program. 2. That necessary agreements between A.I.D. and NHB, and NHB and HFCs are concluded. 3. That HFCs meeting eligibility criteria apply for program participation.

ANNEXURE 'D' TO SOW FOR INTERIM EVALUATION

DATA TO BE COLLECTED BY THE NHB FOR INTERIM EVALUATION
OF HG-003 PROGRAM

(Data to be collected should reflect position as on March 31, 1991)

(1) List of significant regulatory changes and their dates, during the period July 1988 to March 1991.

a) Regulatory changes related to capital markets.
b) Related to operation of Housing Finance Companies (HFCs)
c) Mobilization of Resources

(2) List of NHB activities contributing to Housing Finance System Development during the period July 1988 to March 1991.

e.g. a) guidelines for HFCs
b) acceptance of deposits
c) lending practices of HFCs and interest rates etc.

(3) List of new Public/Joint/Private Sector HFCs formed during the period July 1988 - March 1991.

(4) For Joint/Private sector HFCs - (recognized by the NHB)

dispersion of activities in terms of opening new branches and their locations, during the period July 1988 - March 1991.

(5) List of HFCs classified nd recognised by the NHB (eligible subborrowers) as on March 31, 1991.

(6) For Recognised HFCs (eligible subborrowers)

		Total Loan Sanctions Nos.	Total Loan Sanctions Volume	Total Loan Disbursed Volume
a) Yearwise and according to loan sizes	1988-89 =			
	1989-90 =			
	1990-91 =			

		Loan Sanctions below median income Nos.	Loan Sanctions below median income Volume	Loan Disbursed below median income Volume
b)	1988-89			
	1989-90			
	1990-91			

178

c) 1988-89) i) Number of Units financed by location and income category
1989-90 ii) Average loan size
1990-91 iii) Loan/House Price/Cost ratio according to locat
iv) <u>Loan Terms</u> - Interest rates
- Loan as % of House Price/cost
- Repayment period
- Processing fees etc.

d)	1988-89	1989-90	199
i) Profit after Tax/Average Net Worth			
ii) Debt/Equity Ratio			
iii) Total Assets			
iv) Liquid Assets as % of deposits (10% or more)			
v) Equity Capital as %age of Total Assets (5% or more)			
vi) Interest Coverage Ratio (Interest to Gross Income: 1.2 to 1)			
vii) Household Income to installment ratio (3% or less)			
viii) <u>Sources of funds</u>			
o Own Resources:			
- Share Capital			
- Reserves			
o Borrowings:-			
- Deposits			
- i) Household deposits			
ii) Corporate deposits			
- Bonds			
- Term Loans			
- NHB Refinancing			
- External Sources			

e) Rates of Overdue Loans:

o Volume of Overdue loans to individuals related to outstanding loan portfilios

	Overdue for more than 30 days	Overdue for more than 3 months	Overdue for more than 6 months	More than one year
1988-89				
1989-90				
1990-91				

o Similarly Number of overdue loans to individuals related to outstanding loan portfolio in terms of number of loan.

f) Organizational Chart & copies of Annual Reports (for last 3 years)

(7) Information on yearly and cumulative refinancing made by the NHB to Commercial Banks/HFCs/Cooperative sector for the last 3 years upto March 31, 1991.

180

ANNEX 1.2:
PROTOCOL FOR HFCs

181

PROTOCOL FOR HFCS

Instructions for Completion:

1. Ask the HFC manager questions in sections I.-III.

2. Ask the HFC manager to direct us to other staff to complete sections IV.-V. and for information to fill in any of the gaps let by the answers of the manager to the questions on sections I.-III.

3. Instructions to the interviewer are in capital letters in parentheses.

4. When data is given by the respondent, indicate if it is approximate or exact by using the abbreviations "ap." and "ex."

5. Ask respondents to keep their answers brief, as we have lots to cover.

I. HFC GROWTH AND DEMAND

1. Background on firm
a. Why did your firm's founders decide to form an HFC?
b. How long has your firm been operating?
c. How long have you personally been in the business of housing finance?

2. Branch growth and Loan Growth:
a. What types of outlets do you have (head offices, branches, data collection centers, etc.)
b. How many of each type of outlet did you have 3 years ago and how many do you have today?
c. If the share of each outlet type in your total network has changed over time, why have you made this modification?
d. Has your branch expansion been extensive into new regions or intensive, increasing coverage in given regions? Why?
e. Has your branch expansion been primarily in metropolitan areas or smaller towns and rural areas? Why?
f. In which states and territories do you operate ?
   - Why have you chosen these regions?
g. Data provided to us by NHB indicates that your loan growth has been X% per year over the last three years.
   - Is this correct?
   - What are the major factors contributing to this growth?
h. (IF RESPONDENT UNABLE TO ANSWER THIS QUESTION QUICKLY, SKIP TO I.2.j.): In 1990-91, what percentage of your loans were for

182

- less than 50,000 Rs
- from 50,000 to 100,000 Rs
- more than 100,000 Rs

i. How has this distribution changed over the last three years?
   - What are the major factors explaining these changes?

j. (SHOW RESPONDENT TABLES 14 AND 15): Do these figures for loan size and volume seem accurate to you. If not, please correct.

k.(o) According to the information we received from NHB, your ratio of loans sanctioned to loans disbursed in 1990-1991 was **X%**. What accounts for this ratio?

l. How has the NHB refinancing facility affected your ability to:
   - lend to different income groups?
   - expand your loan volume?

3. Change in Distribution of Borrowers:

a. Annually since inception, or for last three years, whichever is less, what % of total loans have been to:
   - individuals for home ownership
   - individuals for home improvement
   - companies (not involved in construction) for non-housing uses
   - companies (not involved in construction) for rental unit construction
   - companies for repackaging to employees
   - construction firms
   - construction firms with financing tied to promise of permanent take out loan for home purchasers when units completed
   - other entities. Please explain.

b. Which of the above have the greatest potential for growth? Why?

c. Which are the most problematic for you? Why?

d. How has the NHB refinancing facility affected the type of borrowers you have lent to.

4. Demand

a. Has the demand for your loans declined, stayed the same, or increased over the past year, over the past three years? To what do you attribute this?

b. Which income groups currently provide the greatest demand for your loans?

c. Do these income groups differ by geographic area?

d. To which other income groups would you like to lend but have not succeeded? In which geographic areas?

e. Please prioritize the three main problems you have had in meeting this demand and briefly explain.

f. What regulatory or other changes would help you meet this demand?

g. What role might the NHB play in helping you meet this demand?

h. Do you plan to reduce the size of your business, maintain it, or expand it? Why?

i. Do you think that borrowers whose homes are under 40 square meters but which cost significantly more than 1.5 lakhs sometimes obtain more than one loan in order to take

187

advantage of the lower interest rates available on small loans?

j. How do you market your loans?

k. How do your marketing techniques differ for different income groups?

l.(o) How much do you plan to use NHB's new programs to finance land development and shelter project schemes?

m.(o) Under this land development program, do you think the bulk of demand will come from public agencies, private developers, or cooperative housing societies.

5. Going down-market

Home Improvement and Plot Expansion Loans:

a. Are you interested in making home improvement or plot expansion loans to borrowers below the median income? Why or why not?

b. Please prioritize the three most frequent barriers to making such loans and briefly explain.

c. Are conventional underwriting standards a high, medium, or low barrier to financing low-income household?

d.(o) Is the lack of an effective foreclosure law a high, medium, or low barrier to financing low-income households?

e.(o) How could NHB help you in increasing your volume of home improvement and plot expansion loans?

f.(o) What role might community groups and other non-governmental organizations play that would assist you in making such loans?

Apartment Loans:

g. What proportion of your loans volume is currently made for construction of apartments?

h. Please prioritize the three most important barriers to making such loans and briefly explain.

i. How could NHB help in increasing your volume of loans for apartment construction?

Loans to Low-Income Households, Overall:

j. Please prioritize your three most frequent problems in making loans to lower-income people overall and briefly explain.

k.(o) How does the scarcity of serviced land affect your ability to lend to lower-income people?

l. How could NHB help you in increasing your lending volume to low-income people?

6. 25% of Loans Free of NHB Requirements

(SAY TO RESPONDENT: "YOUR COMPANY IS ALLOWED TO LEND 25% OF TOTAL LOANS FOR ACTIVITIES OUTSIDE THOSE SPECIFIED BY NHB)":

a. What do you invest this 25% in?

b. What average rate of return do you get on these investments?

c. How does this rate of return compare with that from housing loans regulated by NHB?

d. Are these loans of high, medium, or low importance to your overall profitability? Please explain.

II. RESOURCE MOBILIZATION AND SUPPLY

1. Composition
a. (IF RESPONDENT UNABLE TO ANSWER THIS QUESTION QUICKLY, SKIP TO II.1.d.):
What is the percentage breakdown of your resources, including the following:
- Household deposits
- Corporate desposits
- Term loans from banks
- Bond issues
- Loans from "external sources" such as international organizations
- HFC refinancing

b. How has this breakdown changed in the last three years? (IF POSSIBLE, GET BREAKDOWNS FOR THESE YEARS).
c. What supply factors explain these changes?
d. (SHOW RESPONDENT TABLE 11): Do these figures for resources seem accurate to you. If not, please correct.
e. Which are the most desirable sources of resources and why?

2. Deposits
a. What interest rate have you paid on household deposits? On corporate deposits?
b. Please prioritize the three most important problems you have had attracting individual deposits and briefly explain.
- Are these problems different for household versus corporate deposits?

c. Have government regulations on term and interest rate of deposits had a high, medium, or low influence on your ability to attract deposits?

d. Have you been approved for participation in the HLA plan?
e Do you think this plan will (would if approved) be of low, medium or high use to you in mobilizing funds? Why?

3. Equity Capital
a. What is the minimum long run ROE your investors expect?
b. What are your plans for achieving this rate?
c. Have you had a low, medium, or high level of difficulty attracting equity capital? Why?
d. What organizations or individuals are the main contributors of equity capital to your business?

4. Borrowings (Debt)
a. What has been the term of borrowing available at different interest rates?
b. Have you been able to tap capital markets? Why or why not?

185

c. Have you had a low, medium, or high level of difficulty borrowing from corporations such as insurance companies? Why?

d. Are you able to borrow funds at below-market interest rates or for unusually long terms? From what sources, and why?

5. NHB refinancing

a. Qualification for participation in refinancing program:

i. Was it difficult for your firm to meet any of the requirements for qualification?
- If so, which ones?

ii. What information did NHB request when you applied for program qualification?

iii. Did NHB conduct a site-visit?
- if so, what type of information did they collect?

iv. How long did it take from the time you submitted your application until you received notice of your approval?

b. Briefly describe the process used for preparing a loan for sale to NHB.

c. How long does this process take?

d. What data do you submit to prove that loans meet value, size and income requirements?

e. How does NHB verify this information?

f. How did you calculate your refinancing requirement projections for 1991-1996 that you gave to NHB?

g. (SHOW RESPONDENT TABLE 12): Do these projections for refinancing seem accurate to you. If not, please correct.

h. What have been the program's main drawbacks?

i. What have been the problems with meeting NHB requirements for house size and loan amount?

j. Please prioritize the three most important means you have used to meet these requirements and briefly explain.

k. Is the NHB facility for financing of low, medium, or high use to you?

l. How has the program's usefulness to you changed as a result of program changes?

6. USAID HG component of NHB refinancing

a. NHB assumes that all loans below Rs. 50,000 are made to households below the median income of Rs 2,200 per month. What percent of your loans under Rs.50,000 are to households below median income?

b. When NHB wishes to lend to below-median income households, would it be more effective to limit loan amounts to below Rs.50,000 or to attempt to limit loans to households earning Rs.2,200 per month or less? Why?

c. Can you estimate the percentage of your borrowers who get more than one loan below Rs.50,000 for construction or purchase of the same house?

7. Effect of capital cost and term on business

a. How has the cost and term of resources changed over the last year, over the last three years?

b. Has the cost or term of resources limited you to a particular market segment? If so, which one?
c. Do you have access to low-cost funds from an affiliate of a large, government-controlled financial institution or similar institution?
d. Are you an independent organization without links to large, government-controlled institutions and without access to low-cost funds.
e. Given your cost of resources, what do you think housing loan interest rates should be? Please explain your thinking.
f. How does access of some but not all housing finance institutions to low-cost funds affect the housing finance system of India?
g. What changes would be necessary to make access to funds more equal?

III. NHB SUPPORT AND MONITORING AND HFC-NHB DIRECTOR MEETINGS

a. NHB Classification:
i. What information did NHB request when you applied for classification?
ii. Did NHB conduct a site-visit?
- if so, what portion of your brances did they visit and what type of information did they collect?

iii. Did NHB assist you in obtaining tax advantages?
- If so, how?

iv. Has the "classified" designation facilitated your efforts to obtain debt and/or equity financing or provided you with other non-tax benefits?
v. Has your recognition for the refinancing program provided indirect benefits in addition to those provided from your classification status?
v. How long did it take from the time you submitted your application for classification until you received notice of approval?
vi. Were any of the requirements for classification difficult to comply with?
- If so, which ones and why?

b. What NHB oversight actions are you subject to because you are classified as an HFC. What additional regulations are you subject to because you are recognized to take part in the refinancing program?
c. Please describe to me what NHB auditors do in their visits here.
d. Do they take any of the following actions:
- examine loan files. how many?
- if yes, do they look at just mortgage files or other types of loans as well.
- check the information in a loan file by calling loan applicants, employers etc.
- audit or examine your financial records
- question you on the cost and terms of your resources
- discuss management with you
- other actions?

e. Do they come annually or at more frequent intervals?
f. Has your submission of quarterly financial statements ever elicited a response from

NHB? What was that response?

g. In its regulatory/monitoring role, has NHB provided advise or guidance regarding your financial situation, underwriting rules, etc?

2. Technical aid and training

a. Have you received any technical aid or training from NHB?

b. If so, in what areas? (planning, resource mobilization, systems etc.)

c. What form has it taken? (documents, seminars, on-site training etc.)

d. Has this training had a low, medium, or high degree of use for you?

e. How has it helped your organization?

f. In what areas do you think you could most benefit from technical aid and/or training?

g. For training in which areas would you be willing to pay? How much would you be willing to pay?

3. Attendance at periodic meetings of HFC executive directors:

a. Have you attended the periodic meetings between NHB and the directors of the HFCs?

b. Are these meetings useful? How?

4. Other contacts with NHB and suggestions:

a. In addition to technical assistance and monitoring visits, and meetings of the directors of HFCs, what other contact do you have with NHB.

b. What suggestions do you have for improving the technical assistance, monitoring, director meetings or other contacts with NHB?

IV. FINANCIAL HEALTH

1. Underwriting Standards

a. Are your standards written down?
- May we have a copy?

b. Who sanctions loans?

c. What education do underwriters have and what training do they receive?

188

d.(o) except at least collect i rate info) For each loan type your firm offers:

(OPTIONAL):	TYPE 1	TYPE 2	TYPE 3	TYPE 4
LTV				
max gross income/repayment				
avg gross income/repayment				
contracted loan maturity				
observed average loan maturity (given that many borrowers prepay)				
interest rate range				
type of payment options				
option for annual interest rate adjustment? (Yes/no)				
collateral requirements				
guarantor required? (yes/no)				
this loan type's % of total loans outstanding				

e. When a borrower defaults, do you expect to repossess his unit?

f. What other actions will you undertake to induce him to repay? (social sanction, guarantor pressure, unit downsizing)

g. Do you have a written policy stating actions collection agents should take when borrowers miss payments?
   - If yes, may we have a copy?

2. What is your interest rate coverage?

3. How do you assess your interest rate risk--that is, the risk of your interest rate coverage worsening in the future because of changes in interest rates? What is your interest rate exposure?

4. Do you have contingency plans in the event that your cost of funds rises sharply and the government does not allow you to significantly increase interest rates on outstanding loans?

4. Have you used non-traditional mortgage instruments?
   - For which income groups do you use these instruments?

189

Loan Quality

What percentage of your loan portfolio (in terms of number of loans and loan volume) is past due by 30 days, 3 months, 6 months and one year:

	(i) % of Total # of Loans	(ii) % of Total Loan Volume
- 30 days		
- 3 months		
- 6 months		
- 1 year		

b. We have seen anecdotal evidence indicating that when women are coborrowers with their husbands, the incidence of late payment is lower. Have you observed such a trend in your lending?

c. What percent of the total volume of loans made since inception have been charged off?

d. How do you decide when to charge off past due loans?

e. Your reserve for bad accounts is what percentage of your total loan volume?

f.(o) To date have you tried to repossess any homes?
- -(o) if yes, what happened?
- -(o) if not, why not?

6. Earnings:
(GET THE FOLLOWING IN FORMATION FOR <u>THE PAST 3 YEARS</u> WITH EXPLANATIONS OF THE CHANGES OVER TIME)

a. What is your after tax ROA? [Net income/avg. assets]

b. What is your after tax ROE? [Net income/avg. equity]

c. What other indicators of return and cost do you use and what are they?

d. How much is your loan origination fee?

e. What percentage of your staff and overhead expenses are covered by fee income?

f. Dividends are what percentage of pre-tax income?

g. What portion of your profits do you retain in your company to fund further growth?

7. Capital

a. What is your equity as a percent of assets when equity excludes reserves for contingencies
   i. When it includes these funds?

b. (ASK QUESTIONS 2A.-2F. IF MANAGER HAS NOT PROVIDED THIS INFORMATION ALREADY OR IF MANAGER'S DATA WERE ESTIMATE)
What percentage of total liabilities are:*
- household deposits?
- Corporate deposits?

- Term loans from Banks?
- Bond issues (if applicable)?
- Loans from International Organizations' (World Bank, AID, etc.)?
- HFC's refinancing loan.

c. What is your firm's Debt to Equity ratio including NHB refinancing?
d. What is your firm's Debt to Equity ratio excluding NHB refinancing?
e. Do you have contingency plans for funds mobilization in the event that NHB is required to significantly reduce its refinancing program in the future.
   - If yes, what are they?

V. LENDING TO LOW-INCOME HOUSEHOLDS AND OTHER GROUPS

1. Quantity of Loans

a. For each of the last three years, what share of your total loans have been to families with incomes below Rs.2200 per month?
   - Why has it changed in this manner? (or why has it remained constant?)

2. Of these loans to low-income households, please estimate what percent were to the categories below and how this figure has changed over time:
a. female-headed households
b. informally employed families
c. rural families (living in towns with populations below 1 lakh and below 0.5 lakhs)
d. families with household heads over 55 years old
e. of the above low-income subgroups which are the hardest to loan to and why?

3. What is your planned increase in number of loans to low-income households?
   - Is the share of loans to low income borrowers in your total portfolio of loans likely to change over time?
4. What problems do you most frequently encounter when you loan to these groups:
a.(o) a low interest rate spread?
b.(o) high fixed costs as % of allowable fees?
c.(o) these families are more likely to make late payments and/or default?
d.(o) others. Please explain.

5. Please prioritize the three most frequent reasons that families in this group are denied credit?
a.(o) They cannot secure a clear title to the land they wish to build on or the home they wish to buy?
b.(o) Their income is too low to be able to afford the necessary repayments?
c.(o) They are informally employed and thus their cash flow is considered too uncertain?

191

d.(o) They live at a level so close to subsistence that even a small emergency will force them to delay their payments?

6.(o) Do low-income families have higher late payment and default rates than families with incomes above the median?

a.(o) If yes, can you estimate how much higher?

7. What are the advantages of loaning to low-income groups:

a.(o) opportunity to obtain NHB refinancing.

b.(o) large potential market

c.(o) other? please explain.

THANK YOUR FOR THIS VERBAL INFORMATION. WRITTEN DOCUMENTS DESCRIBING THE COMPANY, DEPOSIT ACCOUNTS, LOAN PROGRAMS, OR OTHER INVESTMENTS WOULD ALSO BE HELPFUL. THESE INCLUDE ANNUAL REPORTS, DESCRIPTIONS OF DEPOSIT SCHEMES, LOAN BROCHURES, ADVERTISEMENTS, AND NEWSPAPER ARTICLES.

192

ANNEX 1.3:
ORGANIZATIONS VISITED AND PEOPLE INTERVIEWED

Annex 1.3:
Organizations Visited and People Interviewed

The National Housing Bank M.J. Pherwani P.K. Porthrsarathy J.S. Varshneya S.P. Ghosh S.D. Hosangadi P.K. Singh V.K. Garg P.K. Handa M.K. Rakshit Alok Prasad	New Delhi and Bombay
Housing Development Finance Corporation Deepak Satwalekar	Bombay
HUDCO S. Sharma Mulkh Raj	New Delhi
Credit Rating Information Services of India Pradip Shah	Bombay
LIC Housing Finance K.P. Narasimhan S. Subramanyan T. Paul Diamond	Bombay
Infrastructure Leasing and Financial Services Ravi Bhandari	Bombay
Can Fin Homes Ltd. M. D'Souza	Bangalor
SBI Home Finance Limited Ashish Kumar Sen	Calcutta
Dewan Housing Finance Rajesh Kumar Wadhawan	Bombay
Gujarat Rural Housing Corporation N.V. Palany	Ahmedabad

Tapoban Housing Finance Ltd. | New Delhi
Y.A. Shetty

INCAP Housing Development Corp. Ltd. | New Delhi
R.K. Jindal

Peerless Abasan Finance Ltd. | Calcutta
P. Lahiri

USAID | New Delhi
Charles Billand
N. Bhattacharjee
Jeremy Hagger
Michael Lee
Julie Otterbein
B.R. Patil

195

ANNEX 1.4
DESCRIPTION OF PRINCIPAL PROGRAMS OF THE
NATIONAL HOUSING BANK

This description consists of three annexures taken from the document, "The National Housing Bank," published by the bank in October 1990.

Home Loan Account Scheme (annexure 1)

Introduction

1. To progressively meet the colossal housing shortage in the country, it is necessary to build at least one million new housing units per annum. It is proposed to achieve this level of annual addition to housing stock over a period of five years. The financial resources required for the purpose are estimated as under:–

Year	Rs. Crores
1989-90	1,000
1990-91	2,000
1991-92	3,000
1992-93	4,000
1993-94	5,000

2. Commercial banks were to lend Rs.300 crores in 1989* and this is expected to increase over the next five years. Resources will also be available from UTI, LIC and GIC. Even so, the available resources are unlikely to match the requirements referred to above. There is, therefore, need for mobilising additional resources from the public. This is sought to be done by kindling and sustaining the desire to own a house, which is strong in every individual, by encouraging them to save specifically for housing and match it with long term institutional credit support. For this purpose, as announced by the Finance Minister in his Budget speech on 28th February 1989, a scheme called *Home Loan Account Scheme* has been launched from 1st July 1989 by the National Housing Bank with the co-operation of scheduled banks, both commercial banks and co-operative banks participating in the scheme, all over India. The scheme is being gradually extended to all the eligible housing finance institutions.

Home Loan Account (*HLA*)

3.i. Who can open?

Any individual, major or minor, not owning a house anywhere in India, can open a Home Loan Account. The beneficiary will be required to give a declaration to the effect that the account being opened is the only account under the scheme and that she/he does not already own a house anywhere in India. In opening accounts for minors, parents/guardians will be encouraged to open accounts in the names of girls first to provide social security to them. A co-parcener of a Hindu Undivided Family jointly owning a house is also eligible to join the scheme. Non Resident Indians can also open Home Loan Accounts through either direct remittances or transfer from NRE accounts. All the other conditions of the scheme, including the interest rate, will be the same as applicable to resident Indians.

3.ii. Where to open?

The HLA of National Housing Bank can be opened with any branch, in India, of designated scheduled banks. An account opened with a branch of scheduled bank can be transferred to any other branch of the same bank. An account can also be transferred free of cost from one bank to another bank through mutual consent in case the member desires transfer of account to a place where the bank with which the account was opened does not have a branch.

3.iii. Rate of savings

The principle behind HLA is that a member joining it will save as much as she/he can, for a minimum period of 5 years. The scheme is open-ended and a member, including a minor, is

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* *Actual was Rs. 315 crores.*

197

expected to save regularly until she/he decides to acquire a house/flat. The minimum contribution is Rs.30 per month. To facilitate participation in the scheme by all segments of the community, the contemplated contribution can also be made in quarterly, half-yearly or annual instalments subject to a minimum of Rs.90, Rs.180 or Rs.360 respectively. The member will have the option to vary her/his contribution as and when it is convenient for her/him to do so but the contribution will be in multiples of Rs.10.

3. iv. Interest on savings

The savings will earn interest @ **10 per cent per annum** which will be added to the account annually (in the month of March) and treated as reinvested in the account. The interest rate is subject to change in the event of revision of interest rates by the RBI.

3. v. How much to save?

The amount of accumulated savings (including interest) on the basis of regular contributions for a period of five years will be as under :

Amount saved per month *Rupees*	Approximate savings after five years *Rupees*	Amount saved per month *Rupees*	Approximate savings after five years *Rupees*
30	2,300	300	23,200
50	3,900	500	38,600
100	7,700	1,000	77,200
150	11,600	1,500	1,15,800
200	15,400	2,000	1,54,500

The amount to be saved by a member should bear some relationship to the cost of plot/house/flat proposed to be acquired so that together with the loan contemplated under the scheme, the member's desire is fulfilled. This will necessitate the member to assess the cost realistically keeping in view the current trends in prices of land and cost of construction. Banks will also provide guidance on these trends in different parts of the country.

3.vi. Nomination facility

The account is not transferable to others. Nomination facility is available for the purpose of payment of accumulated savings, but not for any other benefit under the scheme.

Defaults / Discontinuance

4. Regular payment on monthly/quarterly/half-yearly/yearly basis is the *sine qua non* of the scheme. If the member fails to make contribution for a continuous period of 12 calendar months, the original date of opening HLA will be shifted forward by the period of default and the minimum period of contribution will be extended correspondingly. In the event of a member discontinuing the contribution, the amount standing to the credit in the account will become payable only after five years from the date of opening the account.

Withdrawal of amount

5. The object of the scheme is to encourage the member to save over a period of years, the amount required to be provided by her/him as margin money for any housing loan. The accumulated savings can thus be set off against any margin requirement for a housing loan either under this scheme or any other housing loan scheme. The amount saved under the

Home Loan Account Scheme (annexure 1)

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2. Commercial banks were to lend Rs.300 crores in 1989* and this is expected to increase over the next five years. Resources will also be available from UTI, LIC and GIC. Even so, the available resources are unlikely to match the requirements referred to above. There is, therefore, need for mobilising additional resources from the public. This is sought to be done by kindling and sustaining the desire to own a house, which is strong in every individual, by encouraging them to save specifically for housing and match it with long term institutional credit support. For this purpose, as announced by the Finance Minister in his Budget speech on 28th February 1989, a scheme called ***Home Loan Account Scheme*** has been launched from 1st July 1989 by the National Housing Bank with the co-operation of scheduled banks, both commercial banks and co-operative banks participating in the scheme, all over India. The scheme is being gradually extended to all the eligible housing finance institutions.

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3.iii. Rate of savings

The principle behind HLA is that a member joining it will save as much as she/he can, for a minimum period of 5 years. The scheme is open-ended and a member, including a minor, is

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* *Actual was Rs. 315 crores.*

expected to save regularly until she/he decides to acquire a house/flat. The minimum contribution is Rs.30 per month. To facilitate participation in the scheme by all segments of the community, the contemplated contribution can also be made in quarterly, half-yearly or annual instalments subject to a minimum of Rs.90, Rs.180 or Rs.360 respectively. The member will have the option to vary her/his contribution as and when it is convenient for her/him to do so but the contribution will be in multiples of Rs.10.

3. iv. Interest on savings

The savings will earn **interest @ 10 per cent per annum** which will be added to the account annually (in the month of March) and treated as reinvested in the account. The interest rate is subject to change in the event of revision of interest rates by the RBI.

3. v. How much to save?

The amount of accumulated savings (including interest) on the basis of regular contributions for a period of five years will be as under :

Amount saved per month *Rupees*	Approximate savings after five years *Rupees*	Amount saved per month *Rupees*	Approximate savings after five years *Rupees*
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3.vi. Nomination facility

The account is **not** transferable to others. Nomination facility is available for the purpose of payment of accumulated savings, but not for any other benefit under the scheme.

Defaults / Discontinuance

4. Regular payment on monthly/quarterly/half-yearly/yearly basis is the *sine qua non* of the scheme. If the member fails to make contribution for a continuous period of 12 calendar months, the original date of opening HLA will be shifted forward by the period of default and the minimum period of contribution will be extended correspondingly. In the event of a member discontinuing the contribution, the amount standing to the credit in the account will become payable only after five years from the date of opening the account.

Withdrawal of amount

5. The object of the scheme is to encourage the member to save over a period of years, the amount required to be provided by her/him as margin money for any housing loan. The accumulated savings can thus be set off against any margin requirement for a housing loan either under this scheme or any other housing loan scheme. The amount saved under the

200

scheme is tied to a housing facility and can be utilised only for building or buying a house or flat. However, part withdrawals will be permitted, for paying registration fees for specific schemes or for purchase of a plot allotted by a public agency or a co-operative housing society or in any project financed by NHB subject to regulations stipulated by the concerned agency for completion of construction of the house or flat within the specified period. Such payments will be made by the bank through cheque/draft in favour of the concerned agency. If for any reason such as the account holder acquiring or inheriting one in the meantime, she/he does not choose to buy/construct a flat/house after five years, she/he may withdraw the accumulated savings on completion of the said period of five years.

Eligibility for loan

6. i. Under the scheme, **after subscribing for a minimum period of five years or any time thereafter,** the member **will be eligible for a loan** from the concerned bank to acquire a new house/flat. However, in the case of a minor, the loan will be admissible only after attaining majority, subject to all other conditions, especially the repaying capacity. In the intervening period of five years from the commencement of the scheme, the bank will give housing loans to members on a preferential basis, but on terms stipulated by the Reserve Bank of India. Members will be permitted to withdraw the accumulated balance in the account after five years, for the purpose of acquiring a house/flat even if they do not avail of the loan facility.

6. ii. The minimum period will be reduced to three years in case the member is allotted a house/flat in any project financed by the NHB. In such a case HLA will be closed and accumulated balance remitted by Cheque/Demand Draft to the authority undertaking the project alongwith loan amount.

Amount of loan & Rate of interest

7. **The maximum amount of loan to be given by a bank under the scheme,** after the member subscribes for a minimum period of five years (or three years, as the case may be), **will be a multiple of the amount of accumulated savings** (including up-to-date interest) as follows:

Loan as a multiple of accumulated savings	*Amount of Loan (Rs.)*	*Rate of interest (%) per annum*
4 times	Upto 50,000	10.5
3 times	50,001 to 1,00,000	12.0
2 times	1,00,001 to 2,00,000	13.5
1.5 times	above 2,00,000	14.5

The amount saved will be allowed to be withdrawn along with the loan. The amount of loan will, however, be limited to the repaying capacity of the beneficiary as assessed by the bank. It may not normally exceed $2\frac{1}{2}$ times the annual income. Otherwise, there will be no ceiling on the amount of loan.

Notes :

1. In order that the benefit of the loan is available to only regular savers banks may, at their discretion, fix a lower amount of loan in case the savings in the later years are disproportionately large as compared to savings in the earlier years.
2. In the case of withdrawals permitted under paragraph 5 above the accumulated savings will be enhanced by the amount withdrawn, for the purpose of fixing the amount of loan.
3. The amount of loan will be related to the accumulated savings upto the time of obtaining a housing loan, not just the balance at the end of five years.

201

8. The rate of interest will be related to the amount of loan and is not on slab basis. Different interest rates are prescribed keeping in view the repaying capacity of the lower income groups and the tax concessions admissible to the higher income groups. These rates of interest are 1.5 to 2.0 percent lower than the present interest rates charged by scheduled banks for housing loans. The interest rates will be subject to change by NHB in the event of revision of interest rates by the RBI.

9. **A loan under this scheme will not bar a loan from any other source** including a loan from a bank on usual terms. Thus, a member can obtain a loan from her/his employer or a co-operative society or any other agency and still avail of a loan under this scheme. Similarly she/he can avail of loan under this scheme and obtain a bank loan on usual terms for the balance requirements. In such cases, the bank will give additional loan on a **priority basis** but subject to usual conditions.

10. To build confidence of the members in the scheme, **NHB will ensure the grant of loan by the bank** subject to the bank satisfying itself with the credit-worthiness of borrower. The scheme envisages an agreement between NHB and each scheduled bank for mobilising savings on behalf of NHB and for providing loans by the bank.

Other conditions

11. *i.* The loan will be subject to all other conditions laid down by the Reserve Bank of India for grant of housing loans by banks. The RBI has recently liberalised credit for housing in respect of margin, security and instalments of repayment so as to make housing loans more affordable by lower income groups. The repayment period has also been extended to 15 years. HLA scheme will be an **additional facility with assured loan at a lower rate of interest.**

11. *ii.* The house/flat either acquired or built with the loan obtained under the scheme cannot be sold for a period of five years after completion or till the entire loan is repaid, whichever is later. Relaxation of this provision may be made by NHB in case of dire distress subject to such conditions as it may deem fit to impose.

12. Loans granted under the scheme are proposed to be covered by a **Group Insurance Scheme** to protect the legal heirs from having to bear the burden of repayment of loan in the event of the death of the borrower. The premium will be borne by the scheduled bank in respect of borrowers who obtain loans upto Rs.50,000 and by the borrowers in respect of larger loans.

Pass book

13. Each member will be given a **pass book** by the concerned bank. The pass book will contain details of monthly savings, interest accumulation, loan disbursement, repayment of instalments etc.

Income Tax concessions

14. **The Government of India issued notification specifying HLA Scheme for the purposes of Section 80 C (now Section 88) of the Income Tax Act, 1961, for the assessment year 1990-91 and the subsequent assessment years.** Accordingly, the savings under the scheme would **qualify for tax concession.** The accrued interest treated as reinvested in the account will also be eligible for the concession. Further, savings made on behalf of a minor child by a parent out of her/his income chargeable

202

to tax will qualify for the same concession. The repayment of principal of the loan will also be a permissible deduction, upto Rs.10,000 per annum, under Section 80 C (now Section 88). Interest on the loan is eligible for deduction in the computation of income from house property under Section 24 of the Income Tax Act.

Similarly, the amount of accumulated savings under the scheme together with interest will be exempt from Wealth Tax under Section 5 of the Wealth Tax Act, subject to the overall ceiling of Rs.5 lakhs.

15. As the scheme is open to all including minors and as withdrawals from the accounts will arise only when the members actually acquire a plot/house/flat, it is expected that there will be continuous accretion of funds adequate to meet the demand for loans under the scheme. However, when lending by a bank exceeds the total savings mobilised under this scheme, NHB will fill the resource gap at the average lending rate of the respective bank under the scheme in the previous year.

16. **The funds available to a bank under the scheme** will be kept separately and will be used only for the purpose of lending to members for housing. Initially, there will be a time-lag between introduction of the scheme and demands made on it for housing loans. In the intervening period, these funds would be utilised by the bank as refinance from NHB under any approved scheme. The intention is that the balance resources will be utilised for giving loans for land development and to industries directly connected with housing such as prefab house plants, tile/brick makers and the like, as per suitable refinance schemes formulated by the NHB. As a consequence, the resources mobilised through this scheme will lead to augmentation/increase in the availability of land and the capacity of industries providing building materials. Surplus funds which cannot be utilised for any refinance scheme of NHB will be lodged with the NHB.

Co-ordination with housing agencies

17. At the time of opening the account, a member is required to indicate the **likely place** where she/he proposes to acquire residential accommodation **and the size** thereof. These intentions will facilitate appropriate **physical planning for land and infrastructure** subject to constraints like congestion, but there is no commitment by NHB to offer a plot/house/flat. Intending members of the scheme will be cautioned that demand for plots/houses/flats in metropolitan areas will take long time to fructify and, in some places, may not be possible at all.

The NHB will endeavour to fund projects of public agencies for acquisition and development of land including on-site infrastructure so as to augment the supply of buildable land. Such funding will be subject to the following conditions:

i. preference will be given for the development of housing in rural areas and small and medium towns.

ii. in the land to be developed, not less than half the area will be earmarked for smaller plots of size less than or equal to 60 sq.m.(100 sq.m. in rural areas). At the same time, not less than 75 per cent of the plots will be of size less than or equal to 60 sq.m. (100 sq.m. in rural areas) and no plot will measure more than 200 sq.m.

iii. of the houses/flats to be built, not less than 75 per cent will have built-up accommodation less than or equal to 40 sq.m. and no house/flat will have built-up accommodation of more than 120 sq.m.

203

HLA scheme is, however, open to any one not owning a house and is not restricted to those seeking the assistance of public agencies. In other words, members can seek dwelling accommodation through any source or by private negotiations and avail of the loan facility under this scheme.

18. After the introduction of the scheme, State Governments will be requested to advise the State Housing Boards and other public agencies engaged in development of housing not to open any general registration scheme, that is, schemes for which land is not identified. As and when specific schemes for development of identified land or construction of houses/flats are taken up, these agencies may open specific registration schemes. Individuals who are registered under the existing general registration schemes may be required to open Home Loan Accounts before they apply for specific registration schemes. NHB will endeavour to evolve guidelines for prescribing eligibility conditions for such specific schemes in consultation with the Central and State Governments. Opening of a HLA may be prescribed as one of the eligibility conditions for allotment of a plot/house/flat by a public agency.

19. State Governments will be requested to give preferential allotment, on the following basis:

i. those who have registered prior to 31.12.1988 and opened HLA ;

ii. others who have registered prior to 31.12.1988 ;

iii. those who have registered on or after 1.1.1989 and opened HLA ; and

iv. others.

If there are reservations for specific classes or categories of persons, preferential allotment will be made on the above basis within each such class or category.

20. Among the members of HLA scheme, allotment will be made strictly on the basis of the month of opening the HLA, that is, those who open accounts in July, 1989 **anywhere in India**, will have precedence over those who open accounts in August, 1989 and so on. A certificate from the concerned bank will be required to be submitted for this purpose.

21. Special efforts will be made to clear the back-log of registration of the public agencies under their existing schemes, with a view to enabling the members to acquire plots/houses/flats as soon as possible after they have saved money for five years.

A national scheme

22. The scheme may eventually **replace all** the existing savings-linked housing loan schemes by banks because the Home Loan Account Scheme will have **nation-wide appeal.** Individuals participating in such savings schemes will have the option to transfer their accumulated savings to this scheme but the date of opening HLA will be the date of priority. Individuals participating in similar savings schemes of Housing Boards or other agencies may also transfer their accumulated savings to HLA on conditions to be decided on the merits of each scheme. The National Housing Bank will thus emerge as a catalyst for stimulating land development and house construction throughout the country though it does not engage itself directly in these activities. The scheme, with the assurance of a loan to the member, has the potential of becoming a **self-financing mechanism for the housing sector.**

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204

Capital Bonds Scheme (annexure 2)

1. These bonds have been notified for investment of a part or whole of the net consideration arising from the transfer of a long term capital asset so as to qualify for exemption of tax under Section 54E(1) of the Income Tax Act, 1961.

2. Net consideration has been defined as the full consideration received or accruing as a result of the transfer of the capital asset as reduced by any expenditure incurred wholly and exclusively in connection with such transfer. The net consideration is required to be invested within six months of the transfer of the asset.

3. All persons who are residents of India can invest in these Bonds. In case of minor applicants, lawful guardian has to sign. Date of birth of the minor has to be furnished invariably. Non-Resident Indians may also invest with prior permission of Reserve Bank of India. An applicant may be an individual, a partnership firm, Hindu Undivided Family or a body corporate. Any one or more persons may apply for these Bonds, provided the number of applicants does not exceed four.

4. Where an application is made by two or more persons, the person first named shall be recognised as bondholder for all purposes and National Housing Bank shall be discharged of its obligations by making payment of the amount under or in respect of the bonds to such person. In case such a person does not survive during the currency of the bond, the second applicant will be recognised as the bondholder.

5. Notwithstanding anything to the contrary in para 4, if two or more individuals applying jointly in their names request in writing that any of them should be permitted to deal with the bonds, then any one or more of the holders shall be entitled to deal with the bonds. In such an event discharge by any one or more of such persons shall discharge NHB as regards receipt of amounts due in respect of such bonds.

6. Applications from corporations, co-operative societies, partnership firms etc., must be signed by person(s) authorised to sign in that behalf. In case of Hindu Undivided Family application shall be made by *Karta* and, if desired, jointly with any adult member(s), but not exceeding four in all.

7. The bonds may be applied for a minimum amount of Rs.1,000 and in multiples thereof. There is no ceiling on the maximum.

8. The Bonds, which carry a rate of interest of 9% and have maturity period of three years, are being issued with two interest modes, as follows —

   i. Interest being payable for the entire period of three years on discounted basis in the beginning itself. On each bond of Rs.1,000, a sum of Rs.240 shall be payable as discounted interest, within three months from the date of investment. Refund of principal shall be made on maturity after completion of three years.

   ii. Interest being paid every six months.

9. The bonds are not transferable, assignable or negotiable, but may pass to the legal heirs subject to the provisions of any law for the time being in force.

10. Nomination facility is available to individual applicants.

11. The bonds will be governed by the NHB(Issue & Management of Bonds) Regulations, 1989 and the provisions of the scheme.

205

12. Apart from the exemption of Tax under Section 54E(1) of the Income Tax Act, following other tax concessions are available –

i. Tax is not deductible at source from the interest paid on bonds.

ii. Interest income on bonds shall be eligible for exemption under Section 80L of the Income Tax Act.

iii. Bonds also qualify for exemption under Section 5(1)(xvie) of the Wealth Tax Act.

13. Following points may be noted in connection with application –

i. Applications should be submitted as per the prescribed format, duly filled in all respects.

ii. Any alteration(s) in the application should be duly authenticated by the applicant with full signature(s).

iii. Full address alongwith Pin Code number should be furnished. Post Box number shall alone not suffice.

iv. If signature is by thumb impression, it must be witnessed by two witnesses. The names and addresses of witnesses should be appended to the signatures.

Other details

i. *Where to buy:* Bonds can be purchased in any of the designated branches of selected scheduled commercial banks and housing finance institutions. **Bonds can also be purchased directly from the offices of NHB at Delhi and Bombay.**

ii. *Payment:* Payment of bonds applied for can be made by crossed account payee cheque/demand draft drawn in favour of NHB. Outstation cheques/drafts are also accepted.

iii. *Brokerage:* Brokerage at the rate of 10 paise per Rs.100 will be paid to the person not being an applicant, whose particulars are given in the application for having acted as broker.

iv. *Acceptance Date:* If the payment is made by cheque, the acceptance date will, subject to such cheque being realised, be the date of the application or the date of the cheque or the date of receipt of application at the branch, which ever is the latest. If the payment is made by demand draft, the date of the draft will be the acceptance date, provided the date of the demand draft and the date of receipt of application at any of the collection centres do not differ by more than 10 days. If they differ by more than 10 days, the date of acceptance will be the date of receipt of the application at the branch.

v. *Repayment:* The bonds, duly discharged, should be submitted for repayment at least two weeks before the date of maturity at the designated office of the Registrar to the Issue i.e. Canbank Financial Services Ltd., "Uma Mahesh", M.M. Chottani Marg, Mahim(West), Bombay - 400016.

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206

Guidelines for Housing Finance Companies (annexure 3)

The National Housing Bank was established on July 9, 1988 under the National Housing Bank Act,1987 as a principal agency to promote housing finance institutions and to provide financial and other support to them. The NHB is keen that not only more housing finance institutions should come up but also that they should be sound, healthy, viable and cost effective. Accordingly, NHB has evolved the following guidelines for promotion of housing finance companies(HFCs) in the private and joint sectors. Only those HFCs which conform to these guidelines would be eligible for financial support from NHB.

eligible for refinancing

Organisation and main activity

2. HFC should be a public limited company formed with the main object of carrying on the business of providing long-term finance for construction or purchase of houses in India for residential purposes. It should be engaged only in financial activity.75 per cent of its lending should be by way of loans for housing.

Minimum paid-up capital requirements

3. HFC should normally have minimum paid-up capital of Rupees one crore to be subscribed in the following proportions and maintained at all times:

	not less than
i. Promoters' contribution	30%
ii. Scheduled banks/public financial institutions/ Government/HFCs approved by the NHB	20%

Notes : *a. If HFC is unable to secure equity participation as stipulated at (ii), promoters' contribution should not be less than 50 per cent of the paid-up capital.*

b. Participation by the scheduled banks is subject to directives issued by RBI.

c. Prior approval of NHB should be obtained before one HFC contributes to the equity of another HFC.

4. On merits of each case, NHB will consider participating in equity of HFC to the extent of 20 per cent of its paid-up capital.

5. i. HFC's name should not bear any resemblance to the name of any construction company with which promoters of HFC may be associated.

ii. HFC should not be a subsidiary of a construction company.

iii. HFC should not have or promote, as its subsidiary, a construction company.

iv. Chairman, Managing Director or any whole-time Director of an HFC should not hold any of these offices in a construction company with which HFC's promoters may be associated or vice versa.

NHB may relax, at its discretion, the conditions stipulated in this paragraph in the case of HFCs which have equity participation by scheduled banks etc. mentioned in para 3 (ii) above.

Board of Directors

6. Normally, the bank/financial institution/HFC/Government having equity participation will have its nominees on the Board of HFC. If for any reason, such Directors are less than two in number, the NHB will have the right to nominate two Directors on the HFC's Board. In the case of HFC which is unable to secure equity participation as stipulated at para 3(ii). NHB will have the right to nominate two Directors on HFC's board. The appointment of HFC's Chief

207

Executive will also be subject to NHB's prior approval. HFC's Memorandum and Articles of Association should contain a provision to this effect.

Borrowings

7. HFC's total external borrowings whether by way of deposits, issue of debentures/ bonds, loans and advances from banks or from financial and other institutions but excluding any loan obtained from NHB, should not exceed 10 to 15 times their net owned funds i.e paid-up capital and free reserves less deferred revenue expenditure and intangible assets. The limits will be as below:

Net owned funds	*Total borrowings*
upto Rs.10 crores	10.0 times
above Rs.10 crores and upto Rs.20 crores	12.5 times
above Rs.20 crores	15.0 times

Credit rating

8. HFC should satisfy such criteria as may be prescribed by NHB.

Acceptance of deposits

9. HFC should mobilise resources mainly by way of deposits from households with minimal reliance on borrowings from institutions. Since housing loans are for relatively long periods, it is also necessary that there is no undue mismatch between the duration of deposits and the lending portfolio. Under the Housing Finance Companies (NHB) Directions, 1989, issued on June 26, 1989 HFCs can accept a deposit of money from the public repayable after a period of more than twenty four months but not later than eighty four months from the date of acceptance or renewal of such deposit at interest rate not exceeding 14 per cent per annum. In the case of a deposit receivable in instalments, its period will be computed from the date of receipt of first instalment.

Loans

10. The main objective of promoting HFCs is to make access to institutional finance for home-seekers easier. The bulk of HFC's lending should, therefore, be directly to individuals or groups of individuals. Their motto should be to render quality service to individual households.

Lending rates

11. HFC's interest rates on housing loans should be as prescribed by the Reserve Bank of India from time to time. Rates of interest w.e.f. 1st January, 1991 are :

Amount of loan *	*Rate of interest (%)*
Upto and inclusive of Rs.7,500	10.0
Over Rs.7,500 and upto Rs.15,000	11.5
Over Rs.15,000 and upto Rs.25,000	12.0
Over Rs.25,000 and upto Rs.50,000	14.0
Over Rs.50,000 and upto Rs.2.00 lakhs	15.0
Over Rs.2.00 lakhs	minimum 16.0

* *The rate of interest will be related to the amount of loan and is not on slab basis.*

208

12. Front-end charges including application or registration fee, processing fee, administrative fee, out-of-pocket expenses in connection with technical inspection and any other fee, charge or expense, under whatsoever name, should not exceed 2 per cent of the loan. There should be no minimum amount prescribed under any head. Document registration charges, stamp duty, etc. are not included in the front-end charges.

Administrative cost

13. HFC should aim at keeping its administrative cost as low as possible. In any case, such cost in the long run should not exceed 1.5 per cent of the outstanding loans.

Prepayment charges

14. Normally, no prepayment charges should be levied except in cases where prepayment of loan is on account of sale of the housing unit financed or there is reason to believe that the prepayment is made to secure some undue advantage.

Auditors

15. HFCs, barring Government companies, should obtain prior approval of the NHB before appointing, re-appointing or removing any Auditor or Auditors.

Security for depositors

16. Every HFC should maintain in the form of liquid assets (with a scheduled bank and/or in unencumbered approved securities) at least 10 per cent of its outstanding deposits, on a day to day basis.

Advertisement rules

17. Issue of advertisements soliciting deposits of money from the public is governed by the Non-Banking Financial Companies and Miscellaneous Non-Banking Companies (Advt.) Rules, 1977 made by the Government of India in consultation with the Reserve Bank of India under Section 58 A of the Companies Act 1956 (1 of 1956).

Financial assistance from NHB

18. NHB extends to eligible HFCs refinance facilities under schemes announced from time to time. At present, NHB provides 100 per cent refinance in respect of housing loans for acquisition/construction of new housing units with built-up area not exceeding 40 sq. m. or cost(including cost of land) not exceeding Rs.1.5 lakhs. 100 per cent refinance is also provided for housing loans upto Rs.30,000 for upgradation and major repairs.Further, the NHB has powers to grant ad-hoc financial assistance to HFCs to meet short-term gaps in resources. NHB will gradually extend the Home Loan Account Scheme to all eligible HFCs. NHB will also refinance Land Development & Shelter Projects financed by HFCs under NHB's guidelines.

Tax concessions

19. In respect of each housing finance company, which is approved by the Central Government for the purpose, the following tax concessions are available:

i. For housing finance companies :

A public company formed and registered in India with the main object of carrying on the business of providing long-term finance for construction or purchase of houses in India for residential purposes, can create a special reserve within an amount not exceeding 40 per cent of the total income and, such a reserve is admissible as a deduction in computing income chargeable to income tax under the head Profits & Gains of Business or Profession vide Section 36-(i)(viii) of the Income Tax Act.

ii. For investment by an individual or person in shares of housing finance company :

a. Investments in the new equity shares of such companies, whose cost of acquisition in the aggregate does not exceed Rs.25,000 is eligible for a tax rebate under Section 88-A under the Income Tax Act. The rebate from the tax payable will be equivalent of 20 per cent of the cost of such shares.

b. Dividend received on shares of housing finance company will qualify for a deduction of upto Rs.13,000 under Section 80-L of the I.T.Act (along with other eligible deductions).

iii. For deposits placed with housing finance companies :

a. Deposits with or investments in any bonds issued by such companies from income derived from property held under trust wholly for charitable or religious purposes, qualify as an eligible mode of investment under Section 11(5) of the I.T. Act.

b. Deposits made with such companies are exempt from Wealth Tax under Section 5(1)(xxvii) of the Wealth Tax Act within the overall ceiling of Rs.5 lakhs specified therein.

c. Interest on deposits by an individual or person with such companies will qualify for deduction of upto Rs.10,000 per annum under Section 80-L of the I.T. Act (along with other eligible deductions).

iv. For loans taken from housing finance companies :

Repayment towards the principal amount of loan taken from any housing finance company for housing purposes is eligible for a tax rebate under Section 88 of the I.T.Act upto a limit of Rs.10,000. Subject to the aforesaid ceiling , the rebate- from the tax payable- will be equivalent to 20 per cent of the amount repaid. The interest payable on the housing loan is a deductible expense under income from house property under Section 24 of I.T.Act.

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210

Guidelines for Land Development & Shelter Projects
Public Agencies

(annexure 4)

Introduction

1. The Draft National Housing Policy postulates that the housing agencies and area development agencies in the public sector would be increasingly reoriented to work more as promoters and facilitators for housing activities rather than as builders of housing units. They are expected to play an increasing role in the development and supply of serviced land. The actual construction of houses would be left to the people who can construct their houses, more economically, suited to their family, social and cultural needs. However, such reorientation of their role will take time and, in the intervening period, the housing and development agencies may have to continue with some construction activity especially to help the low income groups. Certain amount of construction activity may also be necessary while developing new areas, to act as a catalyst for the overall development of new neighbourhoods.

2. The housing and development agencies would, however, be well advised to give up the role of long term housing finance, that is, providing plots/houses on hire purchase basis. The financing role should normally be left to the banks and housing finance institutions. It is desirable that the houses built are sold to the beneficiaries on outright sale basis so that resources of the agencies are not tied up for a long time. Also, mortgage based housing finance system can be developed once primary mortgages are created.

3. The housing and development agencies will require finance for acquisition of land, laying of infrastructure and construction of houses where considered feasible (from the point of view of managerial resources) and desirable (in the absence of any viable alternative for construction). The National Housing Bank proposes to fund through HUDCO, other HFIs and Scheduled Banks such integrated projects subject to the guidelines mentioned in the subsequent paragraphs.

4. The housing and development agencies may undertake projects of land development either for plotted development or for group housing or a mix of both i.e. individual plots and group housing pockets. Integrated projects for land development, which include land acquisition, on-site infrastructure and apportioned cost of off-site infrastructure(where necessary) will be considered. No separate proposal for land acquisition alone will be entertained.

General

5.1 With a view to mobilising large scale financial resources, housing and development agencies should persuade the existing and future registrants with them to open a Home Loan Account(HLA) of the National Housing Bank. The agency will be required to give, in respect of persons qualifying under its eligibility criteria, preferential allotment of plots developed or houses built in the project on the following basis:

i. those who have registered prior to 31.12.1988 and opened HLA ;
ii. others who have registered prior to 31.12.1988 ;
iii. those who have registered on or after 1.1.1989 and opened HLA ; and
iv. others.

If there are reservations for specific classes or categories of persons, preferential allotment will be made on the above basis within each such class or category.

- 211

Among the members of HLA scheme, allotment will be made strictly on the basis of the month of opening the HLA, subject to the member qualifying under eligibility criteria of the agency that is, those who opened accounts in July, 1989 anywhere in India, will have precedence over those who opened accounts in August, 1989 and so on. A certificate from the concerned bank will be required to be submitted for this purpose.

At the time of opening the account, a member is required to indicate the likely place where he/she proposes to acquire residential accommodation and the size thereof. These intentions will be tabulated and the information furnished to the public agencies to facilitate advance planning.

The HLA accumulation will help to meet the margin requirements for obtaining any housing loan. The agency should, therefore, persuade all the potential beneficiaries to join the Home Loan Account Scheme even though some of them may have the facility of obtaining housing loans at lower rates of interest. HLA scheme does not debar members from getting housing loans from other sources or obtain supplementary loan from the HLA scheme.

Notes: *1. A member of HLA is permitted part withdrawal for paying registration fees for specific scheme or purchase of a plot allotted by a public agency or a co-operative society.*

2. In the projects financed by NHB members of HLA are eligible to avail of HLA loans for buying houses/flats after regular saving for a minimum period of three years. If allotment is made to a member before the completion of the said period, she/he can avail of a loan from the bank under normal terms for the interim period, and such loan can be adjusted against the HLA loan obtained subsequently.

5.2 Preference will be given to projects for land development and housing in rural areas and small and medium towns.

5.3 The project proposal should be formulated in consultation with planning and local authorities, wherever applicable, so as to be in line with the proposed development of the area and also be acceptable to the local authorities to ensure proper maintenance of services later. This may be co-ordinated by the State Government through appropriate mechanism.

5.4 Normally, a land development project will be financed only on such land as is in physical possession of the agency without any encumbrance and encroachment. However, projects can be entertained in cases where land acquisition proceedings have advanced to a stage where land compensation award has been made by the competent authority. Projects can also be considered where the land is being procured through negotiations and understanding of sales has been reached. The cost of land, if it has already been paid by the agency, can be included in the project cost.

5.5 The project should be financially viable and should be designed to generate full cost recovery with surpluses wherever possible.

5.6 Appropriate parameters and technology should be adopted to economise in the cost of infrastructure.

5.7 Investment in land development and shelter project should be time bound so as to ensure quick recycling of funds as well as lower costs to the beneficiaries. Normally, a period not exceeding three years is envisaged for developing land and making site available for construction of shelter. If the development cannot be completed during this period, due to unavoidable special circumstances, beyond the control of the housing agencies, a further period not exceeding two years may be considered on

212

merits in each individual case. Construction of houses, where taken up, is expected to commence as soon as possible after the land becomes suitable for the purpose. The project period will be determined at the time of approval on a realistic basis taking into account all relevant facts. Once fixed, however, it is expected to be adhered to through strict monitoring.

5.8 NHB will strive its best to arrange to finance the project to the full extent. The interest rates charged for different components/units of the project will incorporate elements of cross-subsidisation in the prices of the serviced plots as well as in the interest rates (please see para 15 below). The loans will have to be fully secured. Time over-runs beyond the project period will attract a higher rate of interest on the loan. The entire loan along with the accrued interest will be repayable on completion of the project. The agency will, however, have the option to pay the interest annually. However, where the agency opts to continue with hire purchase system in respect of certain units/categories of units in the interim period, the apportioned loan will be repayable in equated quarterly instalments over a period of 15 years from the date of completion of the project.

5.9 The plots developed/houses built under the scheme cannot be sold for a period of five years after taking possession. This provision may be relaxed in case of dire distress subject to such conditions as may be deemed fit to be imposed.

5.10 The proposals for land development and shelter projects may be sent in two stages :

i. *Planning proposal* indicating location, access to infrastructural services, relation with master/development plan if any, development standards, conceptual layout and land use pattern, use of low cost technology, approximate cost and time frame and any other relevant information required for preliminary appraisal of the project.

ii. *Detailed project report* may be sent with detailed layout and designs, design brief, cost estimates, pricing, method of allotment - PERT/CPM chart, organisational structure, cash flow, and other relevant details to enable complete appraisal of the project.

Layout pattern

6.1 In the land to be developed, at least 75% of the plots should be of the size less than or upto to 60 sq.m. per dwelling unit (100 sq.m. in rural areas) and remaining 25% of the plots may be more than 60 sq.m.; however, no plot should normally be more than 200 sq.m. per dwelling unit. At the same time, minimum of 50 per cent of the net residential area should be allocated to plots upto 60 sq.m.

N.B. The plot size of 60 sq.m. can be relaxed marginally so long as the cost of the developed plot does not exceed Rs.50,000. Further, keeping in view the living habits, availability and cost of land, for projects to be taken up in rural, hilly and tribal areas and small and medium towns, the proportion of the small size plots can be relaxed so long as the *average* size of plot in the whole project is not more than 100 sq.m. (relaxable marginally, if the average cost of the plot does not exceed Rs. 75,000).

6.2 The sizes of plots to be provided in any development would have such a composition as to meet the demand pattern of HLA members and other potential beneficiaries having due regard to the composition of various income groups in the population at the city level. When the project involves more than one site in the same area, the overall percentage of plots meant for low income groups should be worked out for all sites together.

23

6.3 The layout should generally conform to the following land ...

		... under each use
	saleable	
i.	residential	50% minimum
ii.	work places, schools, institutions, shops, community places etc.	15 to 20% maximum
	non-saleable	
	roads, pedestrian paths, drains, public and semi-public open spaces.	30 to 35% maximum

Notes: *1. Any neighbourhood development should have provision for basic civic and community facilities; however, where such facilities are available in proximity, the same could be considered and, in that case, the area under residential use could be increased correspondingly.*

2. If the land required under statutory provisions of master plan/development plan is proportionately higher but serves larger city needs, readjustment of the recommended land use pattern can be considered. Such provisions should, however, be carefully reviewed by the planning authorities to keep them to the barest minimum levels.

3. Areas under institutional uses, even if proposed to be allotted free of cost can be included in the saleable component of the land use.

4. Distribution of non-residential saleable area should be preferably as follows :

Community amenities	*25%*
Institutional	*50%*
Commercial	*25%*

Infrastructure provisions (general)

7.1 Minimum acceptable standards should be adopted using appropriate technological development in planning, design and use of materials so as to keep the cost within affordable limits.

7.2 The approach of providing services on incremental basis may also be considered, wherever technically feasible and financially sound. The initial cost of services may be kept low by providing basic minimal level of infrastructure which could be upgraded over a period of time.

7.3 Where off-site infrastructure is required to be provided for servicing the area under development, apportioned cost of such off-site infrastructure may also be included in the project cost.

7.4 Infrastructure provisions should be in conformity with the master plan/interim development plan, if any.

Water supply

8.1 The source of water supply should be clearly indicated along with its location, capacity and quality of water.

8.2 Where water supply is being arranged from external sources, a certificate from appropriate authorities will be required as regards availability of water within the project time frame and the cost involved for supplying water to the project site.

8.3 Where water supply is from a source at site, a certificate of availability of required quantity and of the potability of water, supported with proper test results, will be required. The cost of development of the source and storage/distribution network should be included in the cost of project.

Sanitation

9.1 Where sewage disposal is linked with the existing disposal system of the town, a certificate from the concerned authorities about the linkage with the system within the project time frame and the cost involved will be required.

9.2 Where the sewage disposal system appropriate to the project is proposed to be developed, based upon either low cost sanitation systems or an independent sewerage system along with disposal facility, design parameters and the estimated cost thereof should be furnished.

Drainage

10. The drainage system along with variations in subsoil water level, possibility of flooding and ultimate discharge location should be indicated.

Roads

11. The site should be accessible through existing external road network. The internal road network should be cost effective and should provide access in all weather conditions.

Landscaping

12. The parks, public social facilities, open spaces and roads shall be properly landscaped. The cost of landscaping and plantation of adequate number of trees shall be included in the project.

Electricity

13. For supply of electricity to the project, for street lighting and domestic connections, a certificate will be required from the concerned authorities about the extension of electric supply to the site within the project time frame and the cost involved.

Construction of houses

14.1 Along with area development, shelter component any also be included in the project with the following criteria :

i. Dwelling units should preferably be designed on incremental approach. IS : 8888 as incorporated in the National Building Code may be used as the basis, with emphasis on efficient spatial design of the dwelling unit.

ii. Every dwelling unit should have access to water supply and toilet facilities.

iii. Use of appropriate, innovative and cost effective building materials and construction technology and efficient structural design will be encouraged.

iv. Use of building materials based on agricultural or industrial wastes and those which replace or substantially reduce the use of timber will be preferred.

v. Projects on the concept of group housing will also be accepted.

215

14.2 Of the dwelling units, 75% should have built up accommodation ranging upto 40 sq.m. and no house/flat, will have built-up accommodation of more than 120 sq.m. The size of 40 sq.m. can be relaxed marginally so long as the all inclusive cost is below Rs.1.5 lakhs. At the same time, minimum 50% of the net built-up area should be allocated to the smaller dwelling units.

14.3 Minimum density of 100 dwelling units per hectare (125 dwelling units per hectare in metropolitan cities with population of more than 10 lakhs) will have to be achieved. Low rise high density development will be preferred.

14.4 The above guidelines will be applicable to all land development and shelter projects. However, for land areas measuring less than 2 hectares, the housing agencies can adopt flexible norms, within reasonable limits, to respond to the special needs or potential of the neighbourhoods.

Costs and prices

15.1 The pricing policy should ensure that inflation in land values is avoided. The developed sites may be priced, through appropriate cross-subsidy, in such a manner that the prices of sites for higher income groups and commercial plots are close to market values and the prices of smaller sites are made as affordable as possible for lower income groups. The overall pricing structure for one or more sites in the same area, should ensure full cost recovery with surplus generated wherever possible.

15.2 The basic cost of the project should be arrived at by taking the cost of land, infrastructure and construction cost, including appropriate design, administrative and supervision charges, but excluding interest component.

15.3 To incorporate the element of cross subsidisation in apportioning the cost of the serviced plots, the basic cost of land and infrastructure facilities should be apportioned and the chargeable cost for various types of plots fixed having regard to affordability especially of EWS.

For the purpose of assessing the affordability of the EWS, income norm of Rs.1,150 per month may be adopted, with a sub-group upto Rs.600 p.m. particularly in rural areas. The affordable cost of dwelling units for such categories may be assumed to be about 30 times the monthly income of the families.

If the agency so desires, concessional prices may be adopted for lands earmarked for institutional uses serving a social purpose consistent with the financial viability of the project.

15.4 The individual component/units whether serviced plots, constructed dwelling units, or non-residential units will be charged interest rates in accordance with the interest rate structure prescribed by the Reserve Bank of India from time to time. Rates of interest w.e.f. September 22, 1990 are :

Amount of loan *	*Rate of interest (%)*
Upto and inclusive of Rs.7,500	10.0
Over Rs.7,500 and upto Rs.15,000	11.5
Over Rs.15,000 and upto Rs.25,000	12.0
Over Rs.25,000 and upto Rs.50,000	14.0
Over Rs.50,000 and upto Rs.2.00 lakhs	15.0
Over Rs.2.00 lakhs	minimum 16.0**

* *The lending rate structure relates to the aggregate loan for each unit which the agency avails from HUDCO, other HFIs and scheduled banks. The rate of interest will be related to the amount of loan and is not on slab basis.*

216

** *The actual rate will be worked out in such a manner as to ensure full recovery of the cost of the project.*

15.5 The above interest rates will also apply to cases where the agency prefers to continue with the hire purchase system in respect of certain units/categories of units. However, it shall be ensured that the instalments fixed under the hire purchase system will not carry interest rates lower than those mentioned above.

15.6 In case the agency sells the plots/houses on outright sale basis, the beneficiaries can avail of loans from any agency they like, even at lower rates of interest. For example, in the case of housing loans under HLA scheme, the interest rates chargeable are as under:

Amount of loan	*Rate of Interest (%)*
Upto Rs.50,000	10.5*
Rs.50,001 to Rs.1,00,000	12.0
Rs.1,00,001 to Rs.2,00,000	13.5
more than Rs.2,00,000	14.5

* *Savings under HLA scheme carry interest rate of 10 per cent. The differential is, thus, only half a percent. Further, a concessional rate of 10 per cent will be charged for housing loans upto Rs.7,500 taken by economically weaker sections.*

Operation & maintenance

16. The project report should bring out an appropriate system or methodology for the purpose of maintaining the services either on co-operative basis or through the local authority.

Project implementation

17. The time schedule for the implementation of the project should be carefully worked out and supported with CPM/PERT chart showing the physical progress and investment pattern.

Institutional and management requirements

18. Details of the existing organisation and of managerial capacity and capability should be incorporated in the project report along with proposals, if any required, to strengthen them to undertake the additional responsibility for the proposed project. NHB will insist on continuity in the senior levels of management during the implementation of the project.

Basic parameters for approval

19. Land development and shelter projects will be considered flexibly keeping in view the local conditions, the technical feasibility and the affordability of different income groups subject, however, to three basic parameters, namely,

i. it should be an integrated project (paras 3 and 4).

ii. the agency should agree to give preferential allotment of plots/houses to members of Home Loan Account Scheme of the NHB (para 5.1).

iii. 75 per cent of dwelling units should have built up accommodation ranging upto 40 sq.m. (or within the overall cost of Rs.1.5 lakhs) and no dwelling unit should have more than 120 sq.m. of built-up accommodation (para 14.2).

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- 217 -

Guidelines for Land Development & Shelter Projects
Co-operative Societies

1. One of the objectives of the National Housing Bank is to promote, establish and support the Housing Finance Institutions(HFIs). Among the HFIs operating in the country, the co-operative societies are present in all the states. They are playing an important role in land assembly, development and facilitating construction of houses by its members. The co-operative societies have, so far, largely helped the middle income families. The need now is to help the small man to build his house within his affordability. People living in informal settlements/slums/pavement dwellers should also be helped to organise themselves to form co-operative societies for the development of the area where they live, and construct houses, particularly in such cases where there is a possibility of awarding pattas by the State Governments in favour of the beneficiaries or having access to land by any other means.

2. The primary housing co-operative society is the basic institution to help individuals to own their houses while the Apex co-operative housing finance societies are expected to act as facilitators and provide technical advice, land and financial help to the primary societies for the benefit of their members.

3. NHB has formulated guidelines for land development & shelter projects by public agencies in April, 1989. To meet the overall objectives of increasing the supply of buildable land and construction of houses by the members of the co-operative society, NHB has now formulated guidelines for project finance to be extended to primary co-operative societies.

4. The co-operative societies engaged in building houses/flats for the members, or providing infrastructure thereof, are generally handicapped in timely progress of the construction, due to delay in mobilising resources by the members for payment of their instalments to the society. NHB intends to remove this handicap through provision of project finance to the co-operative societies.

5. Projects will be considered subject to three basic parameters :

   i. It should be an integrated project for land development (including land assembly) and on-site infrastructure and construction of houses.

   ii. All members of the co-operative society shall be the members of the Home Loan Account scheme of the NHB.

   iii. The average size of the dwelling unit shall not have built-up accommodation of more than 60 sq.m.(or within an overall average cost of Rs.2.25 lakhs) and no dwelling shall have a built-up accommodation of more than 120 sq.m.

6. The co-operative societies may undertake projects for construction of houses on plotted development or for group housing or a mix of both. Integrated projects for land development, which include land acquisition, on-site infrastructure,apportioned cost of off-site infrastructure(wherever necessary) and construction of houses will be considered. Projects for plotted development for providing buildable sites to the members may also be considered. However proposals for land acquisition alone will not be entertained.

General

7.1 Any one desiring to own a house needs to save to meet the margin for obtaining a housing loan. In view of the fact that the primary co-operative society is obliged to serve the interests of its members only, they are better placed to motivate people to save. The National Housing Bank has launched the Home Loan Account(HLA) Scheme, precisely

218

to facilitate this kind of self help effort by the citizen to benefit himself, when he decides to acquire a house and, in the meanwhile, help form a pool of resources for the housing sector.

7.2 As a pre-condition for approval of the project for financial assistance, all the members of the co-operative society will be required to become members of the Home Loan Account scheme of the National Housing Bank. It is therefore, necessary that co-operative societies intending to avail of project finance under this scheme should ensure that all their members join the Home Loan Account scheme and open an HLA in a branch of any scheduled bank or any Housing Finance Institution, which may be authorised by National Housing Bank to operate Home Loan Account Scheme. It is however suggested that members may be advised to open an HLA in the branch of the bank/HFI, through which the co-operative society proposes to avail of project finance. In their own interest, members of the society are advised to start saving under HLA Scheme, as soon as possible, without waiting for the acquisition of land by the society (see para 7.5 below). To avail of loan under HLA to the full extent, members are advised to contribute approximately one percent of the cost of the house per month to HLA.

7.3 Allotment of the houses/plots should be made strictly on the basis of the month of opening the Home Loan Account. For the members who have joined the society before January 1, 1990, however, the allotment can be made as per the existing practice in accordance with the by-laws of the society. Members, who join the society on or after 1.1.1990, will be allotted the plot/house in accordance with the provisions of HLA and the bye-laws of the society will need to be amended accordingly.

7.4 Preference will be given to the projects of the co-operative societies proposing smaller average size of dwellings/plots, preferably in small and medium towns. Preference will be accorded to projects on lands allotted to co-operative society by the public agencies and/or where trunk/peripheral infrastructure is available.

7.5 Project will normally be financed on land which is in physical possession of the society without any encumbrance and encroachment. Projects will also be considered where the land is being allotted by a public agency or is being procured through negotiations and understanding of sales has been reached. The cost of land, if it has already been paid by the society, can be included in the project cost.

7.6 The project proposal should have the approval of the planning and local authorities, wherever applicable, so as to be in line with the proposed development of the area and also be acceptable to the local authorities to ensure proper maintenance of services later.

7.7 Appropriate planning and design parameters and technology should be adopted to economise on cost of infrastructure.

7.8 Investment in land development and shelter project should be time bound to ensure lower costs to the beneficiaries. The project period will be determined, at the time of approval of the project, on a realistic basis taking into account all relevant factors. Once fixed, however, it is expected to be adhered to through strict monitoring. Projects not executed according to agreed time schedule will attract higher rate of interest on loan.

7.9 During the construction of project, a display board at site should prominently indicate that:

219

The project is financed by
____________________ Bank/HFI
Under National Housing Bank Scheme
for the members of the HLA Scheme of NHB.

Planning Parameters

8.1 In the case of plotted development, where houses are built on individual plots, the average size of the plots in the layout shall not be more than 100 sq.m. and no plot shall normally measure more than 200 sq.m.

8.2 The average size of the dwelling units to be built, should not be more than 60 sq.m. of built-up accommodation and no dwelling unit should have built up accommodation of more than 120 sq.m.

N.B. The permissible average size of 60 sq.m. of built-up accommodation can be relaxed marginally so long as the average cost of builtup accommodation does not exceed Rs.2.25 lakhs. Similarly, the average size of 100 sq.m. of serviced plot can be relaxed marginally so long as the average cost per plot does not exceed Rs.75,000.

8.3 Optimal use of land should be achieved in the layout planning. Provision should be made for community facilities, such as parks and open spaces, community centre etc. in the layout. Parks, open spaces and roads should be properly landscaped to create healthy living environment.

Infrastructure provisions (general)

9.1 Every dwelling unit should have access to water supply and toilet facilities.

9.2 Minimum acceptable standards should be adopted using appropriate technological development in planning, design and use of materials so as to keep the cost within affordable limits.

9.3 The approach of providing services on incremental basis may also be considered, wherever technically feasible and financially sound. The initial cost of services may be kept low by providing basic minimal level of infrastructure which could be upgraded over a period of time.

9.4 Where off-site infrastructure is required to be provided for servicing the area under development, apportioned cost of such off-site infrastructure may also be included in the project cost.

9.5 Infrastructure provisions should be in conformity with the master plan/interim development plan, if any.

Project Implementation

10.1 The land development will be taken up by the co-operative society while the dwelling units can be constructed either by the co-operative society or by the members of the society individually. Wherever the houses are to be built by the members individually, it should form integral part of the project. Group housing construction shall be undertaken by the co-operative society.

10.2 Use of appropriate, innovative and cost effective building materials and construction technology and efficient structural design will be encouraged.

10.3 Use of building materials based on agricultural or industrial wastes and those which replace or substantially reduce the use of timber will be preferred.

10.4 The time schedule for the implementation of the project should be carefully worked out and supported with bar chart showing appropriate linkages of various activities, the physical progress and investment pattern.

Pricing

11. The prices charged from the members should be based on the documented price of land, cost of development and construction as per specifications pre-determined, appropriate escalation during the project period, design, supervision and management charges, and the cost of funds. As far as possible, the project should be completed within the cost approved at the time of sanction of the project.

Financing of the project

12.1 NHB will provide finance for the project upto 100 percent of the project cost. Funds will be made available by the bank/HFI to the co-operative society in the form of loan, for the project period (which will be three years, including the period required for allotment and handing over). All these loans by the bank/HFI will be fully refinanced by NHB. The loans will have to be fully secured .

12.2 The loan for individual component/units whether serviced plots, constructed dwelling units, will be charged interest rates in accordance with the interest rates structure prescribed by the Reserve Bank of India from time to time. Rates of interest w.e.f. September 22, 1990 are :

Amount of loan *	*Rate of interest (%)*
Upto and inclusive of Rs.7,500	10.0
Over Rs.7,500 and upto Rs.15,000	11.5
Over Rs.15,000 and upto Rs.25,000	12.0
Over Rs.25,000 and upto Rs.50,000	14.0
Over Rs.50,000 and upto Rs.2.00 lakhs	15.0
Over Rs.2.00 lakhs	minimum 16.0

* *The lending rate structure relates to the aggregate loan for each unit which the agency avails from HUDCO, other HFIs and scheduled banks. The rate of interest will be related to the amount of loan and is not on slab basis.*

12.3 On completion of project, it is not obligatory to take loans under HLA. Allottees can avail of loans from any agency they like, even at lower rates of interest. In the case of housing loans under HLA, the interest rates chargeable are as under:

221

Amount of loan	Rate of Interest (%)
Upto Rs.50,000	10.5*
Rs.50,001 to Rs.1,00,000	12.0
Rs.1,00,001 to Rs.2,00,000	13.5
more than Rs.2,00,000	14.5

* *Savings under HLA scheme carry interest rate of 10 per cent. The differential is, thus, only half a percent. Further, a concessional rate of 10 per cent will be charged for housing loans upto Rs.7,500 taken by economically weaker sections.*

12.4 The loan will be released in stages according to the progress of the work. On completion of the project and allotment of houses, individual members of the society will obtain loans from the bank/HFI under HLA scheme. If the amount of loan under the HLA scheme is not sufficient, bank/HFI may provide a supplementary loan at the rate of interest prescribed by RBI for normal housing loan (as given in pare 12.3). All such loans by the banks/HFIs will be fully refinanced by NHB.

Where the member of the society, is not eligible for loan under HLA, due to not having completed the minimum period of subscription to HLA, the bank/HFI with whom the HLA has been opened, will sanction a housing loan at the rate of interest prescribed by RBI for normal housing loans. All such loans will also be fully refinanced by NHB.

The loan so sanctioned to the members of the co-operative society will be adjusted against the loan made available to the society. Thereafter members will be responsible for making regular repayment of their loan and interest thereon to the bank/HFI.

12.5 The co-operative society will provide security to the bank/HFI for the housing loans given to the members. Wherever the ownership of the houses is required to be transferred in the name of the individual members, it will be permitted only when the members have repaid the loan and the interest. Under HLA scheme, houses built cannot be sold for a period of five years after completion.

Operation & Maintenance

13. The project report should bring out an appropriate system or methodology for the purpose of maintaining the services either on co-operative basis or through the local authority.

Institutional and management requirements

14. The co-operative society should have adequate organisational and managerial capacity and capability for implementation of the project. The co-operative societies are advised to engage qualified professionals required to execute the project within the time frame.

Submission of Projects

15.1 As soon as the co-operative Society is allotted land by a public housing agency or acquires land by any other means, including land assembly, on its specific location, a project proposal may be submitted.

15.2 The Project proposal from the co-operative societies for financing by NHB should be sent in two stages:

i. *Planning proposal* indicating location, conceptual layout and building design, approximate cost and time frame and any other relevant information required for preliminary appraisal of the project.

ii. *Detailed project report* may be sent with the detailed layout and building design, design brief, cost estimate, use of low cost technology, Bar Chart, organisational structure, cash flow and other relevant details to enable complete appraisal of the Project.

15.3 All Planning Proposals / DPRs should be submitted in triplicate, to the bank/HFI through which the co-operative society proposes to avail financial assistance. The bank/HFI will retain one copy of the Planning proposal with it and forward two copies to NHB at New Delhi office for approval.

* * *

Guidelines for Land Development & Shelter Projects
Professional Developers

1. National Housing Bank has formulated guidelines for Land Development and Shelter Projects by public agencies in April, 1989. Housing Finance Institutions, to be promoted and regulated by the NHB, will be expected to pay attention to meet the credit needs of public, co-operative and private agencies engaged in land development and housing construction. The guiding principle is to counteract speculation and facilitate the supply of serviced land for housing. Recognising the important role of the developers in housing, NHB has now formulated guidelines for financing land development and shelter projects by the professional developers.

2. The developers may undertake projects of land development either for plotted development or for group housing or a mix of both i.e. individual plots and group housing pockets. Integrated projects for land development, which include land acquisition, on-site infrastructure and apportioned cost of off-site infrastructure(wherever necessary) only will be considered. Proposal for land acquisition alone will not be entertained.

General

3.1 Land development and shelter project will be financed only on such land as is in physical possession of the developer without any encumbrance and encroachment. Projects can also be considered where the land is being procured through negotiations and understanding of sales has been reached. The cost of land, if it has already been paid by the developer, can be included in the project cost.

3.2 As a pre-condition for approval of land development and shelter projects, the developer will be required to give preferential allotment of plots developed or houses built, to the members of the Home Loan Account(HLA) Scheme of the National Housing Bank, at predetermined prices. Among the members of HLA, allotment will be made strictly on the basis of the month of opening the HLA, that is, those who opened accounts in July, 1989 anywhere in India, will have precedence over those who opened accounts in August, 1989 and so on. A certificate from the concerned bank will be required to be submitted for this purpose.

3.3 The developers will be free to sell the developed plots/houses/flats to the extent of not more than 20 per cent of the saleable land as approved in the project or not more than 20 per cent of the total built-up space, whichever is less, subject to the condition that the developers will simultaneously develop the whole area or construct all the dwelling units. The plot/houses/flats on the balance 80 per cent of the saleable land or 80 per cent of the built-up space shall be sold at pre-determined prices to be approved by NHB at the time of appraisal of the project.

3.4 Preference will be given to projects for land development and housing with smaller size of plots/dwelling units, preferably in small and medium towns.

3.5 The project proposal should have the approval of the planning and local authority, wherever applicable, and be in line with the proposed development of the area.

3.6 Projects of only those developers, who engage qualified professionals required to execute the project will be considered. Appropriate parameters and technology should be adopted to economise the cost of infrastructure.

224

3.7 Investment in land development and housing projects should be time bound to ensure lower costs to the beneficiaries. Normally, a period not exceeding three years is envisaged. Construction of houses, where taken up, is expected to commence as soon as possible after the land becomes suitable for the purpose. The project period will be determined at the time of approval of the project on a realistic basis taking into account all relevant facts. Once fixed, however, it is expected to be adhered to through strict monitoring. Projects not executed according to agreed time schedule will attract higher rate of interest on loan.

3.8 An open advertisement will be inserted by the developers in the local newspapers inviting members of HLA and others to apply for allotment. Members of HLA will have first preference for allotment. Where sufficient number of members of the HLA do not apply for allotment, the developer will be free to sell the remaining plots/houses/flats to the general public, who apply for the same, by draw of lots, but at the predetermined prices, in consultation with the financing institution.

3.9 During the construction of project, a display board at site should prominently indicate that:

The project is financed by
________________ Bank/HFI
Under National Housing Bank Scheme
for the members of the HLA Scheme of NHB.

Layout pattern

4.1 Normally projects with a construction of 20 dwelling units or more will be considered for financing. Preference will be given to a project on land allotted to a developer by the public agencies and where trunk/peripheral infrastructure is available.

4.2 In the land to be developed, at least 75 per cent of the plots should be of size less than or upto 60 sq.m. per dwelling unit and remaining 25 per cent of the plots may be more than 60 sq.m. and no plot shall normally be more than 200 sq.m.The size of 60 sq.m. of plot can be relaxed marginally so long as the overall cost of the plot does not exceed Rs. 50,000. At the same time, minimum 50 per cent of the net residential area should be allocated to small plots. Further, keeping in view the living habits, availability and cost of land, for the projects to be taken up in rural, hilly and tribal areas and in small and medium towns, the proportion of the lower size plots may be relaxed so long as the average size of the plots is not more than 100 sq.m. (relaxable marginally, if the average cost of plot does not exceed Rs. 75,000).

4.3 The mix of plots/houses proposed in the project, should have a wide range of different sizes so as to cater to households of all income levels.

4.4 The layout should generally conform to the following land use:

	land under each use
saleable	
residential, work places, schools, institutions, shops, community places etc.	65 – 70% minimum
non-saleable	
roads, pedestrian paths, drains, public and semi-public open spaces.	30 – 35% maximum

Note: *The layout pattern will be considered flexibly.*

225

Infrastructure provisions

5.1 Minimum acceptable standards should be adopted using appropriate technological development in planning, design and use of materials so as to keep the cost within affordable limits.

5.2 The approach of providing services on incremental basis may also be considered, wherever technically feasible and financially sound. The initial cost of services may be kept low by providing basic minimal level of infrastructure which could be upgraded over a period of time.

5.3 Infrastructure provisions should be in conformity with the master plan/interim development plan, if any.

5.4 Wherever the infrastructure is linked with external source/network such as water supply, sewage disposal, electricity etc., a certificate from the appropriate authorities regarding their availability within the time frame and cost will be required, which can be included in the project cost.

Construction of houses

6.1 Along with area development, shelter component may also be included in the project with the following criteria :

i. Every dwelling unit should have access to water supply and toilet facilities.

ii. Use of appropriate, innovative and cost effective building materials and construction technology and efficient structural design will be encouraged.

iii. Use of building materials based on agricultural or industrial wastes and those which replace or substantially reduce the use of timber will be preferred.

6.2 75 per cent of the dwelling units should have a built up accommodation ranging upto 40 sq.m. (or within an overall cost of Rs.1.5 lakhs) and no house/flat, will have built-up accommodation of more than 120 sq.m. At the same time, 50 per cent of the net built-up area should be allocated to the small dwelling units.

6.3 Minimum density of 100 dwelling units per hectare (125 dwelling units per hectare, in metropolitan cities with population of more than 10 lakhs) will have to be achieved. Low-rise high-density development will be preferred.

6.4 The above guidelines will be applicable to all land development and shelter projects with land area measuring two hectares and above. For smaller plots, measuring less than two hectares in area, flexible norms, within reasonable limits, can be adopted to respond to the special needs or the potential of the neighbourhood.

Pricing

7.1 The pre-determined prices will ensure a fair return on investment by the developer. The prices charged from the beneficiaries shall not include any speculative element, i.e. they would be based on the documented price of land or current registration price or price fixed by the Registration Department for purposes of payment of stamp duty (supported by relevant certificate), cost of construction as per specifications pre-

226

determined, appropriate escalation during the project period, cost of funds and a reasonable profit margin. No increase on the pre-determined prices will be allowed.

7.2 At the time of approving the predetermined prices for various categories of houses/flats, NHB may insist on an element of cross subsidisation in favour of smaller units without affecting the overall financial viability of the project.

Financing of Project

8.1 National Housing Bank will finance the developer through a bank/HFI. NHB will finance the project upto 80 percent of the project cost(para 3.2). The loan will be released in stages according to the progress of the work after the developer has invested his own share of investment i.e. 20 percent of the project cost. Funds will be made available by the bank/HFI to the developer in the form of loan, for the project period (which will be three years, including the period required for allotment and handing over). All such loans by the bank/HFI will be fully refinanced by NHB. The loans will have to be fully secured.

8.2 The loan for individual component/units whether serviced plots, constructed dwelling units, will be charged interest rates in accordance with the interest rates structure prescribed by the Reserve Bank of India from time to time. Rates of interest w.e.f. September 22, 1990 are :

Amount of loan *	*Rate of interest (%)*
Upto and inclusive of Rs.7,500	10.0
Over Rs.7,500 and upto Rs.15,000	11.5
Over Rs.15,000 and upto Rs.25,000	12.0
Over Rs.25,000 and upto Rs.50,000	14.0
Over Rs.50,000 and upto Rs.2.00 lakhs	15.0
Over Rs.2.00 lakhs	minimum 16.0

* *The lending rate structure relates to the aggregate loan for each unit which the agency avails from HUDCO, other HFI's and scheduled banks. The rate of interest will be related to the amount of loan and is not on slab basis.*

8.3 On completion of project, The plots/houses will be sold to the allottees on outright sale basis. The allottees can avail of loans from any agency they like, even at lower rates of interest. For example, in the case of housing loans under HLA, the interest rates chargeable are as under :

Amount of loan	*Rate of Interest (%)*
Upto Rs.50,000	10.5*
Rs.50,001 to Rs.1,00,000	12.0
Rs.1,00,001 to Rs.2,00,000	13.5
more than Rs.2,00,000	14.5

* *Savings under HLA scheme carry interest rate of 10 per cent. The differential is, thus, only half a percent. Further, a concessional rate of 10 per cent will be charged for housing loans upto Rs.7,500 taken by economically weaker sections.*

8.4 If the amount of loan under the HLA scheme is not sufficient, banks/HFIs may provide a supplementary loan at the rate of interest prescribed by RBI for normal housing loan as given in para 8.2 above. All such loans by the banks/HFIs will be fully refinanced by the

227

National Housing Bank. Where the allottee is not a member of HLA or is not eligible for loan under HLA due to not having completed the minimum period of subscription to HLA, the bank/HFI with whom the HLA has been opened, will sanction a housing loan at the rate of interest prescribed by RBI for normal housing loans. All such loans will also be fully refinanced by NHB. The loan so sanctioned to the allottees will be adjusted against the loan made to the developer. Thereafter members will be responsible for making regular repayment of their loan and interest thereon to the bank/HFI.

8.5 The plots developed/houses built under the scheme cannot be sold for a period of five years after taking possession. This provision may be relaxed in case of dire distress subject to such conditions as may be deemed fit to be imposed.

Operation & maintenance

9. The project report should bring out an appropriate system or methodology for the purpose of maintaining the services either on co-operative basis or through the local authority.

Project implementation

10. The time schedule for the implementation of the project should be carefully worked out and supported with CPM/PERT chart or Bar chart with appropriate linkages; showing the physical progress and investment pattern.

Organisational and management requirements

11. Details of the existing organisation and of managerial capacity and capability should be incorporated in the project report.

12. Land development and shelter projects will be considered flexibily, subject to three basic parameters :

i. It should be an integrated project for land development (including land assembly) and on-site infrastructure to develop buildable sites and construction of houses..

ii. 80 per cent of developed land/built-up space will be sold with preferential allotment to members of HLA scheme of NHB at pre-determined prices.

iii. 75 per cent of the houses built shall have built-up accommodation ranging upto 40 sq.m.(or within an overall cost of Rs. 1.5 lakhs) and no dwelling unit shall have a built-up accommodation of more than 120 sq.m.

Submission of projects

13. The proposals for land development and shelter projects may be sent in two stages:

i. *Planning proposal* indicating location, access to infrastructure services, conceptual layout and land use pattern, use of low cost technology, approximate cost and time frame and any other relevant information required for preliminary appraisal of the project.

ii. *Detailed project report* may be sent with detailed layout and designs, duly approved by planning and local authority wherever applicable, design brief, cost estimates, pricing, PERT/CPM/Bar chart, organisational structure, cash flow, and other relevant details to enable complete appraisal of the project.

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228

Guidelines for Rental Housing Projects (annexure 7)

1. National Housing Bank recognises the need for employers in the organised sector undertaking housing schemes for their employees and workers, keeping in view the considerable shortage of staff housing in the public and private sectors, and to generally increase the housing stock in the country. The National Housing Bank, therefore, proposes to finance rental housing projects by public and private sector institutions.

General

2.1 National Housing Bank will consider proposals from public and private institutions for rental housing schemes with the following criteria:

i. The proposal is to provide rental housing *exclusively* to the employees of the borrowing institution.

N.B: This condition may be relaxed in the case of rental housing for specific disadvantaged groups (i.e. working women) subject to:

a. additional safeguards being provided for the servicing of loan ; and

b. all the dwelling units being of built-up accommodation not exceeding 40 sq.mtrs.(or within an overall cost of Rs. 1.5 lakhs per unit).

ii. The institution is financially viable and has the capacity to repay the loan and interest within the stipulated period.

2.2 Investment in the housing project shall be time bound. The project period will be determined at the time of approval of the project on realistic basis, taking into account all relevant factors. The projects shall be implemented strictly within the time schedule agreed at the time of approval of the project. Projects not executed according to agreed time schedule will attract higher rate of interest on loan.

2.3 Rental housing project will be financed on such land as is in the physical possession of the institution without any encumbrance and encroachment and also have assured availability of off-site infrastructure within the project time frame. The cost of land can however be included in the project cost.

2.4 The project proposal should be in line with the proposed development of the area and should have the approval of the planning and local authorities.

2.5 Appropriate planning and design parameters and technology should be adopted to economise in the cost of on-site infrastructure and construction of dwelling units. The dwelling unit should preferably be designed with emphasis on efficient spatial design of the dwelling unit. Use of appropriate and cost effective material and construction technology and efficient structural design will be encouraged. Use of building material based on agriculture or industrial wastes and those which replace or substantially reduce the use of timber will be preferred.

2.6 Projects of only those institutions, which engage qualified professionals to execute the project will be considered.

2.7 During the construction of the project, a display board at site should prominently indicate that:

The project is financed by
__________________ Bank/HFI
Under National Housing Bank Scheme

Nature of development

3.1 Normally, group housing projects will be considered for financing under rental housing scheme. Minimum density of 100 dwelling units per hectare (125 dwelling units per hectare in metropolitan cities with population of more than 10 lakhs)will have to be achieved. Low rise high density development will be preferred.

3.2 To meet the needs of low income employees, the *average* size of dwelling unit should have a built-up accommodation of not more than 60 sq.m. and no dwelling unit shall have a built-up accommodation of more than 120 sq.m. Preference will be given to projects for land development and housing with smaller size of plots/dwelling units. The *average* size of 60 sq.m. of builtup accomodation can be relaxed marginally so long as the overall *average* cost of the dwelling unit does not exceed Rs. 2.25 lakhs).

3.3 Wherever individual housing is proposed to be constructed, following parameters shall apply :

i. The land under residential use shall not be less than 50% of the total area.

ii. Average size of the plot per dwelling should not be more than 100 sq.m. and no plot should normally be more than 200 sq.m. in size.

3.4 Parks/public open space and roads should be properly landscaped. Community amenities such as schools, community centre etc. wherever necessary, can be incorporated in the project cost, including the cost of landscaping and plantation of adequate number of trees to create healthy living environment.

Infrastructure provisions

4.1 Minimum acceptable standards should be adopted using appropriate technology in planning, design and use of material so as to keep the cost as low as possible.

4.2 Wherever the infrastructure is linked with external source/network such as water supply, sewage disposal, electricity etc. a certificate from the appropriate authority regarding their availability within the time frame and cost will be required.

Financing

5.1 National Housing Bank will finance the institutions through their bank/HFI approved by NHB for this purpose. The extent of finance provided by NHB will be upto 100% of the cost of construction (excluding the cost of land) or not exceeding 75% of the project cost, including the cost of land, whichever is less. The institution should have adequate resources to invest its own share of the project cost. The expenditure already incurred on the project will, however, not be reimbursed. The loan will be released in stages according to the progress of the work. NHB will also consider financing purchase of ready built dwelling units by the employer for use as rental housing for its own employees, provided it conforms to the parameters as stated in para 3 above.

5.2 Funds will be made available by the bank/HFI to the institution in the form of a loan, at interest rate of 16%. All such loans by the bank/HFI will be fully refinanced by NHB. The loans will have to be fully secured. The entire loan along with accrued interest will be payable within a period of ten years from the date of last drawl in equated half yearly instalments.

5.3 It is expected that the borrowing agency will recover reasonable lease charges from their employees, and review the same periodically.

Project Implementation

6. Time schedule for the implementation of the project should be carefully worked out and supported with PERT/CPM Chart or Bar Chart showing appropriate linkages with various activities including cash flow. The project report should also bring out a proper system or methodology for the purpose of maintaining these services. Details of the existing organisation and of managerial capacity should be incorporated in the project report, to ensure timely implementation of the project.

Submission of Projects

7.1 The proposal for rental housing scheme should be sent, in two stages:

i. *Planning proposal* indicating location, conceptual layout and building design, approximate cost and time frame and any other relevant information required for preliminary appraisal of the project.

ii. *Detailed project report* may be sent with the detailed layout and building design, design brief, cost estimate, use of low cost technology, PERT/CPM/Bar Chart, organisation structure, cash flow and other relevant details to enable complete appraisal of the Project.

7.2 All Planning Proposals / DPRs should be submitted in triplicate, to the bank/HFI through which the co-operative society proposes to avail financial assistance. The bank/HFI will retain one copy of the Planning proposal with it and forward two copies to NHB at New Delhi office for approval.

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231

Guidelines for Building Material Projects

1. Increased availability of finance and land for building houses will put pressure on the supply of building materials and construction components. On an average, materials account for about 70 per cent of the cost of construction. Inadequate supply and increase in prices of basic building materials like bricks, timber etc. adversely affects the construction of houses and slows down housing activity. While the development and expansion of production of building materials such as cement and steel may not pose much of a problem, the production of other building materials, scattered over different parts of the country, needs to be augmented, quality improved and cost reduction achieved.

2. To build houses, especially for low income group category, building materials have to be made available at reasonable prices. On a very rough estimate, for construction of one million houses within the affordability of low income group will require building materials of the value of Rs.2,000 crores. The existing supply of the conventional building materials is far too inadequate to meet this additional requirement.

3. NHB proposes to extend support to the industries which will increase supply of building materials at affordable prices and result in construction at lower costs. In particular, NHB will support production and use of:

i. locally produced, low cost building materials and construction components,

ii. standardised building materials and components,

iii. building materials and components produced by using agricultural, industrial and other wastes,

iv. building materials and components which replace or substantially reduce the use of scarce resources like wood, and

v. low energy consumption building materials and components.

4. NHB will also support research and development which will improve construction technology. Studies on innovative building methods, technology, design and standardisation of material and components will be encouraged.

5. Improving the availability of building materials of acceptable quality at affordable prices is a difficult and complex process. An appropriate institutional set up is required to promote application and commercial exploitation of alternative building materials and construction components developed by various research and development institutions and also to encourage production and marketing of building materials in a coordinated manner.

6. To achieve the above objectives, NHB will support setting up of building material industries/companies for manufacture of various building materials and construction components (full or partial system) to be used in housing programme and coordinate marketing effort for distribution and sale of these housing kits including technical services required for use of such materials and components.

7. The following Guidelines have been formulated for assisting industrial units/companies manufacturing building material falling within the above broad category :

i. Eligibility

a. NHB prefers to support building material projects based on new or innovative technologies using locally available raw/waste materials in the region so as to increase and broadbase the supply of building materials of acceptable quality at affordable prices. Preference will also be given for projects in the areas where there is scarcity of

232

standardised building material for house construction. NHB will also support projects on imported technology from other countries provided the technology can be quickly absorbed in India to obviate recurring outflow of foreign exchange and help in lowering construction costs.

b. Companies seeking NHB assistance may be required to satisfy the following criteria:

i. It should be a public/private limited company and be professionally managed normally with a paid-up capital of not less than Rs.1.00 crore.

ii. NHB may at its discretion nominate one or two directors on the Board of the Company.

iii. The company should undertake to obtain prior approval of NHB before appointing/ reappointing or removing auditor/auditors.

ii. Evaluation of the project

a. NHB will provide financial assistance for projects meeting the parameters laid down in these guidelines, after satisfying itself with the technical feasibility and financial viability of projects. Preference will be given to projects which have been appraised and approved by HUDCO for its equity participation.

b. Projects which are appraised and approved by banks/state financial institutions for providing equity participation and/or term loan will also be considered.

iii. Financing

The promoters are expected to contribute at least 20% of the project cost by way of equity. NHB will provide equity support which may extend to 30% of paid-up capital on merits of each case.

iv. Procedure for inviting equity participation by NHB

The proposal for equity assistance should be submitted in triplicate to the National Housing Bank along with the following documents:

a. Project Report.

b. Memorandum and Articles of Association of the company.

c. Approval of the financial institution/banks/HUDCO for the project for providing equity/term loan.

* * *

ANNEX: 3.1:
CREDIT RISK ON INDIVIDUAL LOANS

Annex 3.1
Credit Risk on Individual Loans

The lack of an effective foreclosure procedure in India conditions the underwriting and credit process for housing loans. Foreclosure takes a minimum of five to seven years and is an impractical option in virtually all circumstances. Consequently, it is more accurate to speak of housing credit than mortgage loans--the fundamental security for housing loans is the credit of the borrower rather than the collateral. The difficulties with foreclosure have encouraged conservative underwriting and thorough collection procedures.

Four factors affect credit risk: the collateral represented by the property, the individual's capacity to repay, the term of the loan, and the loan approval process. These factors are examined below for individual loans, which currently represent the bulk of HFC assets,

(a) Collateral, Equity, and Title. The maximum loan-to-value ratio used by the HFCs visited ranged from 70 to 85 percent. These HFCs estimated the average loan-to-value ration at 50 to 65 percent of appraised value. Appraisal were done by technical personnel from the HFC based on the construction cost of the house plus the land value in cases of construction or market price in the cases of sale.

However, the low loan-to-value ratio increases the problem of verifying the borrower's other sources of equity. Sums already spent on construction are often one of these sources of equity. A large portion of individual loans made by HFCs--ranging from 20 to 40 percent--involve construction of a house, extension, or home improvement. HFCs customarily verify the value added in construction by either a site visit of HFC technical staff or an inspection by a local engineer. Another source of equity is the borrower's savings, which HFCs verify by examining postal account savings books and other records of borrower assets.

Achieving secure title is often a problem, particularly for loans on apartment units, which customarily represent about 50 percent of individual loans in urban areas, and for low-income borrowers, who often live on property with a clouded legal history. Finally, communal ownership of land in some regions, such as northeastern India, requires special methods. HFCs routinely take multiple proofs of title, including property tax receipts, the deed, a declaration by the local government that the borrower is the owner of the property and pays taxes, and title searches by local government.

(b) Repayment Capacity and Guarantor. The maximum debt service to gross income ratio is customarily 30 to 40 percent; for USAID HG loans, the maximum is 30 percent. If the ratio exceeds this figure, special dispensation is required, often from the managing director. This figure compares with maximum debt-service-to-income ratios of 30-50 percent in the United States.

Some HFCs require that all borrowers have a guarantor for the loan. Others require guarantors for all but the most easily qualified borrowers and lowest loan-to-value ratio properties. Particularly given the lack of a foreclosure law and procedure, the requirement of a guarantor is a key to exercising "moral pressure" on mortgagors who fall behind on their payments.

(c) Loan Term. The term of loans varies from 7 to 20 years and is generally set at the difference between the borrower's age and age of retirement, usually taken as 58. Thus, a 50 year old would get an 8 year term, while a 30 year old would get a 20 year term. Although understandable, this procedure effectively eliminates most people over age 51 from receiving housing loans as the minimum loan term is 7 years. In comparison, loan terms of first mortgages in the United States are virtually always 30 years if the borrower demonstrates sufficient repayment capacity for the first 2-3 years of the loan, regardless of the borrower's age. Hence, the setting of loan term in India is quite conservative.

(d) Loan Approval. The loan approval process differs depending on the size of the loan. The procedure of Can Fin Homes is typical. Loans up to 1 lakh are sanctioned by the branch manager. Above this amount, loans go to the headquarters office: loans from 1 lakh to 3 lakhs are sanctioned by the general manager; loans 3 lakhs to 15 lakhs are sanctioned by the managing director; loans 15 lakhs to 1 crore are sanctioned by a committee of directors; loans above 1 crore must be approved by the board of directors.

ANNEX 4.1:
SAMPLING LOAN DISBURSEMENT RECORDS TO VERIFY HOUSEHOLD ELIGIBILITY FOR HG FINANCING

Annex 4.1
Sampling Loan Disbursement Records to Verify Household Eligibility for HG Financing

In the HG-003 program current practice is to attribute all loans for Rs. 50,000 or less refinanced by NHB to the HG program. I.e., the assumption is that such loans are taken by borrowers with incomes at or below the median of household incomes in urban areas. While use of the Rs. 50,000 rule of thumb is convenient and on its face appears reasonable in terms of the size of loan for which a low-income household could make payments, it has not been subjected to systematic empirical verification. This annex outlines a procedure for testing the validity of the rule of thumb, using loan file records from HFCs whose loans have been refinanced by NHB.

Questions to be Answered

The primary question to be addressed is what share of loans below Rs. 50,000 qualify for HG financing. However, several additional questions can also be addressed with data gathered at the same time. These include:

1. What share of loans qualifying for HG financing are going to female borrowers, and what share going to borrowers age 50 or older?

2. What share of qualifying loans are for house purchase/ construction and what share for home improvements?

3. How does the share of qualifying loans vary by city size and region of the country? I.e., should alternative rules of thumb be used in the future for different locations?

Data to be Gathered

To address the questions just listed, the following data items should be extracted from loan disbursement files at the participating HFCs:

1. HFC id number
2. branch id number (so the city size and region of the property can be captured)
3. borrower income
4. borrower age
5. borrower sex
6. borrower family status (single, married, etc.)
7. dwelling size (40 square meters or larger)
8. property value
9. loan amount
10. type of loan (improvement/expansion versus purchase/ construction)

Sampling Plan

Data will be gathered from the loan files of each of the HFCs whose loans have been financing by the HG program (through the NHB). Most HFCs now have branches, and, depending upon where the HFC keeps its loan files, it may be necessary for the data collection to be done at the branches. It is possible, but not very likely, that all of the information listed above will be available from the HFCs' computerized files.

1. Sample Size. The size of the sample needed depends upon the expected share of HG-financed loans actually taken by a household with income below the urban median, the desired precision of the estimate of the actual share of loans that qualify, and the degree of statistical reliability desired. For these factors, note the following:

(a) At this time there is no reliable estimate of the share of HG-financed loans that actually qualify for this financing. Conservatively, one can assume the value to be in the .5 to .6 range.

(b) The precision of the estimate is reflected in the confidence interval around the estimate, for example, one might want the estimate to be reliable within plus or minus 5 percentage points. So if the estimate were .8, then one would know that at a stated level of statistical significance the actual value lies in the range .75 to .85. For this purpose, a confidence interval of plus or minus 5 percentage points seems reasonable.

(c) Statistical reliability addresses the likelihood that the estimate could have arisen from chance rather than be fact. A standard reliability standard is .95, i.e., the chance that the true value of the share of qualifying loans lies outside of the confidence interval is five percent.

Based on these parameters a total sample size of [to be filled in Washington] is required.

2. Drawing the sample. A sample of the size just indicated should be drawn using records at NHB. Specifically, a simple listing should be made of the account numbers of all loans against which HG-funds were disbursed. The total number of loans included should be divided by the sample size to obtain the sampling interval. A random start should then be taken within the first interval, and this loan and every loan at the same point in each subsequent interval included in the sample.

Each of the sample loans just identified should then be allocated to the HFC originating it, i.e., a list of all the loans sampled for each HFC should be compiled. Then a listing of all of the sample loans for each HFC should be sent to the HFC with a cover letter asking the HFC to identify the location of the file containing the necessary data for each loan.

Based on the information received in response to these letters, the field work can be organized for going to the loan files to code the data listed above for computer entry. Analyses can then be performed to address the questions stated at the beginning of this annex.