

LESSON – 7A**HOUSING FINANCE****7A.0 Objective:**

After going through this lesson, you will be able to understand

- Emergence of housing finance
- Role being played by institutional players

Structure:

7a.1 Introduction

7a.2 Role of Institutional Players

7a.3 Tenure of a Housing Loan

7a.4 Repayment Schedule of Loans

7a.5 Role of National Housing Bank (NHB)

7a.6 Borrowing and Acceptance of Deposits by NHB

7a.7 Housing finance System

7a.8 Housing and Urban Development Corporation (HUDCO)

7a.9 Insurance Corporations

7a.10 Commercial Banks

7a.11 Co-operative Banks

7a.12 Specialised Housing finance Institutions

7a.13 Securitisation Process

7a.14 Competition in Housing finance

7a. 15 Future Scenerio

7a.16 Summary

7a. 17 Self Assessment Questions

7a. 18 Further Readings

7a.1 Introduction :

From the time immortal shelter is considered to be the basic necessity of a Humans being To the Homoc Sepian no other problem is as worrying and mind boggling as the housing problem. To construct a house is a distant dream in the lives of many people. Conservatively in our country most of the people used to dependent on their Provident Fund and gratuity amounts received after retirement for the purchase or construction of a house. Loan is considered to be the last resort for many a people in yesteryears. Employees who are in transferable Jobs also give

importance to construct a house at the fag end of their career or they will decide where to settle just before the retirement. Hence this is a major burning problem for many people.

In a populated country like India many people are below the poverty line and to construct a house is a big dream for them. People below the poverty line have been living in slum areas. Even after attainment of Independence there is no considerable momentum in this sector.

However with the emergence of housing finance as a major business in the country an increasingly large member of people are going for housing loans. As a result the housing and real estate sector in our country is undergoing unprecedented change. There is another reason for this also. In search of Employment villagers are migrating to towns and cities. Due to this phenomenon there is a need to develop urban infrastructure. Consequent to the introduction of economic reforms internationally reputed industrial houses are feeling that Indian market is very attractive and they are of the opinion that "IF YOU ARE NOT IN INDIA TODAY, YOU MAY AS WELL NOT BE IN BUSINESS".

The sustained demand from the international Technology Sector certainly changed the Urban Land Landscape of our country. Bangalore has positioned it self as the IT Capital of India and there is intensive competition in the area among Bangalore, Hyderabad and Chennai. Several multinational companies are evincing keen interest to start their operations in India to take advantage of low costs. Since human resource being the chief element in the Industry, the hiring and houses of people both at their work place and home assume great-importance and hence the need to create space for people to work and live, which in turn triggers the development of other related Infrastructure. Young I.T employees are being paid good salaries and on an average before attainment of 30 years they are planning to acquire a house property. Just married I.T couples are also preferring to possess the house in order to avail the Income Tax Concessions. Indians are migrating to other countries and their savings at work places are being sent to their parents and the parents are purchasing / constructing beautiful homes, apartments etc.

The predominant trend has been to setup world class business centers often camups style establishments. Some of these locations are being formed as the "TEMPLES OF MODERN INDIA". Just an indication of the extent of Real Estate Development taking place. The Housing Industry today has been transformed into a Buyer's market with service standards having to keep pace with the ever rising customers expectations.

The emergence of Housing finance as a major Business in the country, an increasingly large number of people are going for Housing Loans. Incomes of families are rising and their purchasing capacity as well as loan re-paying capacities are also going up. At present both public sector banks, private sector banks and foreign banks are liberally coming forward to extend loan facilities to prospective buyers. The Government of India has been giving substantial encouragement to the Housing Sector. The social structure of the Indian families is going through a sea change as the joint family is fast giving way to the nuclear family concept. The pressure to have one's Home is high among these families.

7a.2 Role of Institutional Players:

Many Institutions such as State Bank of India, Canara Bank, Indian Overseas Bank, Syndicate Bank, in fact all Public Sector Banks are Providing Housing finance at attractive and affordable rates. A part from these banks, HDFC, LIC, PNBHF, ICICI, are very active in this area. All these institutions offer number of Home Loan Products to its clientele that include plot purchase

loan, house construction loans, home / flat purchase loan, house improvement loan and extension loan. Royal Sundaram Home Loans is very Popular in southern India.

7a.3 Tenure of Loan:

The tenure of loan depends upon age, need of the customer, purpose of loan, repayment capacity, tenure of service etc. On an average house owners are taking the loan for 15 years on Equated Monthly Installments (EMI) Cost of Loan: All the housing finance Institutions charge processing and administration fee which is linked to the amount of loan from customers. The quantum of charges affects the cost of loan to be borne by the customer.

7a.4 Repayment Schedule of Loan:

The Loan is repaid in the form of installments. Mostly the installments are to be paid monthly. The repayment of loan in the case of most of the Housing finance Institution are in the form of Equated Monthly (EMI). Some Institutions permit the customers to repay the amount at any time but normally it is paid in Equated Monthly Installments and has a provision of Bi-annual system of repayment in case of agriculturists. Some other loan options available are Front Loaded, Ballon Type or Back Loaded. In case of Front Loaded system the Installments will be very high. In case of Ballon type the total loan period will be divided into Three parts and in the initial years the installment will be low and in the middle period the installment will be high and again at the fag end period the installment amount will bellow. Some Private Housing finance Companies are charging at 'FLAT RATE'. The interest will be spread for the entire loan period. For prompt payment there will be some concession of 1 or 2 percent keeping in mind the competition level among Housing finance Institutions. Almost all the Institutions are offering fixed or floating rate of Interest to their customers.

7a.5 Role of National Housing Bank (NHB):

This Institution was established as a fully owned subsidiary of the Reserve Bank of India (RBI) in the year 1988 under the NHB Act 1987 to operate as a Principal Agency to promote Housing finance Institution (HFIs) at both local and Regional Levels and to Provide financial and other support to the. The NHB is a body corporate. It can establish offices / agencies at any place with the prior approval of the Reserve Bank of India. It was incepted with an authorised paid up capital of Rs. 350 crores and it is fully subscribed by the RBI. The authorised capital can be increased up to Rs. 2000 crores by the Union Government in consultation with the Reserve Bank of India. The Board of Directors of the National Housing Bank may issue the increased authorised capital on terms and conditions determined from time to time. At the minimum 51% of its issued capital would be held by the RBI / Government / Public Sector Banks and other Institutions owned / controlled by the Government.

The supervision, direction and management of the affairs and business of the NHB is vested in its Board of Directors which exercises all powers and executes all acts and things on its behalf. Subject to the provisions of the NHB Act, the Board while discharging its functions has to act on Business Principles with due regard to Public Interest. The NHB is allowed to the following kinds of Business.

- a) Promoting, establishing, supporting / Aiding in the promotion establishment / support of Housing Financing Institutions.
- b) Making of loans and Advances or rendering any other form of financial assistance, what so ever for housing activities to HFI's, Banks, State Co-operative, Agricultural and Rural Development Banks or any other Institutions / class of Institutions notified by the Government.

- c) Subscribing to / purchasing stocks, shares, bonds, debentures and securities of every other description.
- d) Guaranteeing the Financial Obligations of HFI's and Under writing the issue of stocks / shares / Bonds / Debentures / Other Securities of HFI's.
- e) Drawing, accepting, discounting / rediscounting, buying / selling and dealing in Bills of Exchange / Promissory Notes, bonds / debentures, hundies, coupons / other instruments.
- ea) Buying / selling or otherwise dealing in any loans / advances secured by mortgage / charge of immovable property relating to banks / HFI's.
- eb) Creating Trust (s) and Transferring loans / advances together with / without securities to HFIs for a consideration.
- ec) Setting aside loans / advances held by NHB and issuing / selling securities based upon them in the form of debt obligations / trust certificates of beneficial interest / other instruments and to act as trustee for the holders of such securities.
- ed) setting up of Mutual Funds for undertaking housing finance activities.
- ee) Undertaking / participating in housing mortgage insurance.
- f) Promoting / forming / conduction or associating in promotion / formation conduct of companion / mortgage banks / subsidiaries societies / Trusts / other associations of persons it may deem fit for carrying out all / any of its functions under NHB Act.
- g) Undertaking research and surveys on construction techniques and other studies relating to shelter / Housing and Human settlement.
- h) Formulating schemes for purposes of mobilization of resources and extension of credit for Housing.
- i) Formulating scheme (s) for purposes of mobilization of resources and extension of credit for Housing for the economically weaker sections of society, which may be subsidised by the Government or any other source.
- j) Organising Training Programmes / Seminars / Symposia on matters relating to Housing.
- k) Providing guidelines to HFIs to ensure their growth on sound lines.
- l) Providing Technical / Administrative assistance to HFIs.
- m) Co-ordinating with Life Insurance Corporation of India the unit trusts of India. The General Insurance Corporation of India and other Financial Institutions in the discharge of its overall functions.
- n) Exercising all powers and functions in the performance of duties entrusted to it under the NHB Act or under any other law in force for the time being.
- o) Acting as a Agent of the Central / State Government / RBI or of any authority as may be authorised by the RBI.
- p) Any other kind of Business which the Government may on the recommendations of the RBI authorize.
- q) Generally, doing of all such matters and things as may be incidental to or consequential upon the exercise of its powers or the discharge of its duties under the NHB Act.

7a.6. Borrowing and Acceptance of Deposits:

For purposes of carrying out its functions the NHB may

- a) Issue and sell Bonds and Debentures with or without the guarantee of the Central Government in such manner and on such terms on may be prescribed.
- b) Borrow money from the Central Government, Banks, Financial Institutions, Mutual Funds and from any other authority or organization or Institution approved by the Government on such terms and conditions as may be agreed upon.
- c) Accepting Deposits repayable after such period and on such forms as may generally or specially be approved by the RBI.

- d) Borrow money from the RBI (i) By way of loans and advances and generally obtain financial assistance in a manner specified by the RBI (ii) out of the National Housing Credit (Long Term operation) Fund established under sec. 46 – D of the RBI Act.
- e) Receive for services rendered, remuneration, commission, commitment charges, consultancy charges, service charges royalties, premium, license fee and other considerations of any description.
- f) Receive gifts, grants, donations or benefactions from the Government or any other source.

7a.7. Housing finance System:

The implementation of Housing finance Policies presupposes efficient institutional arrangements. Although there were a large number of agencies providing direct finance to individuals for house construction, there was no well established finance system till the mid eighties in as much as it had not been integrated with the main financial system of the country. The establishment of the National Housing Bank (NHB), a fully owned subsidiary of the Reserve Bank of India as an apex Institution was the end of the fulfillment of a long overdue need of the Housing finance Industry in India. The system has also been characterised by the emergence of several specialised financial institutions that have considerably strengthened the organization of the Housing finance system in the country. At present, there are about 320 Housing finance companies of which 26 are registered with the NHB and which account 98 percent of the Total Housing Loan disbursed. Following are the main agencies operating in our country.

- a) **Central and State Governments:** Till the mid eighties the responsibility to provide Housing finance rested by and large with the Government. The Central and State Governments indirectly support the housing building effort. The Union Government has introduced from time to time various social housing schemes. The role of the Central Government against these schemes is confined to laying down broad principles providing necessary advice and rendering financial assistance in the shape of loans and subsidies to the State Governments and Union Territories. The Central Government has set up the Housing and Urban Development Corporation (HUDCO) to finance and undertake housing and Urban development Programmes Development of land for satellite towns besides setting up of a building materials industry.

The Central Government provides necessary fulcrum to the HUDCO and guarantees the Bonds issued by it. Apart from this the Central Government and respective State Governments provide house building advances to their employees. The responsibility of the Central Government is to evolve the policies and the respective State Governments are the real implementers.

7a.8. Housing and Urban Development Corporation (HUDCO):

HUDCO was established on 25th April 1970 as a fully owned Government of India enterprise with the following objectives.

- a) To provide long-term finance for construction of houses for the residential purposes or finance or undertake housing and urban development programmes in the country.
- b) To finance or undertake the establishment of New Satellite Towns.
- c) To finance or undertake the establishment of the building materials industries.
- d) Administer the monies received from the government of India and other such grants for purposes of financing or undertaking housing and urban development programmes.
- e) To subscribe to the debentures and bonds to be issued by the State Housing Boards, Improvement Trusts, Development Authorities and so on specially for the purpose of financing housing and urban development programmes.

7a.9. Insurance Organizations / Corporations:

The Life Insurance Corporation of India and General Insurance Corporation support housing activity both directly and indirectly. Besides subscribing to bonds of the HUDCO and State Housing Boards, LIC grants loans to the states for their Rural Housing Programmes and to Public Sector Companies for construction of Staff Quarters. Though LIC has been granting loans directly to individuals the impetus to housing finance was provided. In June 1989, the LIC promoted a subsidiary for the purpose namely LIC Home Finance Ltd.

7a.10. Commercial Banks:

The trend of commercial banks lending to individuals for housing emerged in the wake of the report of the working group on the role of banking system in providing finance to housing schemes. (R.C SHAH Working Group the RBI 1978). They have been lending to the Housing sector based on Annual Credit allocations made by the RBI. In terms of the RBI guidelines, scheduled commercial banks are required to allocate 1.5 percent of their incremental deposits for disbursing on housing finance every year. Of this allocation 20 per cent has to be by way of direct housing loans which again at least half, that is 10 per cent of the allocation, has to be rural and semi – urban areas. Another 30 per cent could be for indirect lending by way of term loans to housing institutions, housing finance companies and public housing agencies for the acquisition and development of land and to private builders for construction. The balance 50 per cent is for subscription to the HUDCO and the NHB Bonds.

7a.11. Co-operative Banks:

The Co-operative Banking Sector consists of state co-operative banks (SCBS). District control co-operative banks (DCBs) and primary urban co-operative Banks (PUCBs). The First set of comprehensive guidelines for these co-operative banks were issued in 1984 by the RBI. Co-operative Banks, Finance Individuals, Co-operative group Housing Societies, Housing Boards and others who under take housing projects for the Economically weaker sections, Low Income groups and Middle Income groups.

7a.12. Specialised Housing finance Institutions (HFIS):

There are some Institutions termed as “Specialised HFIs that cater only to the needs of the housing sector. They can be further classified as housing finance companies (HFIs) promoted in the Public / Joint / Private Sectors and Co-operative Housing finance Societies. A major and leading company is Housing Development Finance Corporation (HDFC). It lends mainly for new residential housing to individuals, group of individuals and individual members of co-operative societies. Apart from the HDFC a number of Housing finance Corporations have been sponsored by banks such as the SBI Home Finance Ltd., Canfin Homes Ltd., Ind Bank Housing finance Ltd. And Citi Bank Ltd.,

SECURITISATION: This is a process of Pooling and repackaging of homogeneous illiquid financial assets into marketable securities that can be sold to investors. The process leads to the creation of financial instruments that represent ownership interest in or one secured by segregated income producing asset or pool of Assets. The pool of assets collateralises securities. These assets are generally secured by personal or real property such as automobiles, real estate or equipment loans but in some cases are unsecured credit card debt and consumer loans.

7a.13. Securitisation Process:

1. Assets are originated through receivables, leases, housing loans or any other form of debt by a company and funded on its balance sheet. The company is normally referred to as the 'Originator'.
2. Once a large portfolio of assets has been originated, the assets are analysed as a portfolio and then sold or assigned to a third party, which is normally a special purpose vehicle company (SPV) formed for the specific purpose of funding the assets. It issues debt and purchases receivables from the originator. The SPV is owned by a trust the originator.
3. The administration of the asset is then subcontracted back to the originator by the SPV. It is responsible for collecting interest and principal payments on the loans in the underlying pool of assets and transfer to the SPV.
4. The SPV issues tradable securities to fund the purchase of assets. The performance of these securities is directly linked to the performance of the assets and there is no recourse back to the originator.
5. The investors purchase securities because they are satisfied that securities would be paid in full and on time from the cash flows available in the asset pool. The proceeds from the sale of securities are used to pay the originator.
6. The special purpose vehicle (SPV) agrees to pay any surplus which may arise during its funding of the assets back to the originator. Thus the originator for all practical purposes retains its existing relationships with the borrowers and all of the economies of funding the assets.
7. As cash flow arise on the assets, these are used by the SPV to repay funds to the investors in the securities.

7a.14. Competition in Housing finance:

Towards the end of 1990s against the back drop of lower interest rates, Industrial slow down, sluggish credit off-take and ample liquidity, commercial banks reorganised that if they had to maintain profit margin they need to shift their focus from the wholesale segment and build up their retail portfolios. Some commercial banks devised aggressive marketing campaign to increase the size of their housing segment. This includes intensive advertising campaigns. Waivers of processing and administrative fee, gift offers and other incentives on the spot loan approvals without margin money i.e. cent per cent. Due to these reasons Housing finance Industry to-day has been transformed into 'Buyers Market'. Service standards keep pace with ever rising customers satisfaction.

7a.15. Future Scenario:

As such there is great demand for housing finance in India. In order to give impetus to this sector there is a need to completely change the legal system governing various aspects of real estate. There are several procedures to be followed in different states due to the reason that land is a state subject. Every year Government is increasing Stamp Duty which is a State Subject. This aspect is to be rationalised. Similarly more avenues have to be opened up facilitating long-term finance for the Housing sector. The noteworthy feature is that Securities Exchange Board of India has permitted the mutual fund asset management companies to enter into real estate Arena. At the same time, the introduction of mortgage guarantee or insurance will help a large segment of the society to access Housing finance.

7a.16. Summary:

Housing finance has grown into a major business. Several private and public institutions have entered this field of business. National Housing Bank established as a subsidiary of Reserve

Bank of India is operating as a principal agency to promote Housing finance Institutions. HUDCO established as a fully owned Government of India enterprise provide long term finance for construction of houses for residential purpose.

7a.17. Self Assessment Questions:

1. Discuss the role of National Housing Bank.
2. Explain the role of HUDCO
3. Explain the system of housing finance prevailing in India.

7a.18. Further Readings:

1. VK Bhalla, *Management of Financial Services* Armed Publications Pvt. Ltd, New Delhi.
2. S. Gurusamy, *Financial Services and Systems* Vijay Nirole imprints Pvt. Ltd, Chennai.
3. M Y Khan, *Financial Services*, Tata McGraw Hill, Publishing Co. Ltd., New Delhi.
4. V A Avadhani, *Financial Services*, Himalaya Publishing House, New Delhi.

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