Development of Indian Home Loan Industry

B.C.M.Patnaik [a], Ipseeta Satpathy[b], Nihar Ranjan Samal[c]

[a]Associate Professor School Of Management, Kiit University Bhubaneswar, Odisha, India

[b]Professor School Of Management, Kiit University Bhubaneswar, Odisha, India

[c]Research Scholar School Of Management, Kiit University Bhubaneswar, Odisha, India

Abstract

The present paper is an attempt to understand the growth and development of Indian home loan Industry. In this regard secondary source is taken as base. The various issues addressed includes structure of home loan, growth and development ,current scenario, RBI directives, Challenges faced by home loan Industry and future of home loan industry. The objective of the present paper is to understand the various development phases and to undertake the empirical study on housing loan industry.

KEYWORDS- Home loan Industry, growth, development and financing.

An Overview

Buying a house is the single largest investment of an individual. The housing finance is growing at a rapid speed. The major sources of finance for housing for both buyer as well as builders have been largely from the unorganized sector (Dangwal. R C 1998). In India most of the people depend on their provident fund and gratuity amounts received after retirement for buying a house. The people started relying upon the housing finance institutions (both banks and housing finance companies). India has changed socially and there is no stigma attached today to go for borrowed funds. The emergence of housing finance is a major business in the country. The housing finance institutions fulfill the shortage of housing in India. The demand for housing loans is rapidly increasing in recent years. The reasons for this are easy affordability of housing, declined property prices, reduced interest rates and attractive tax incentives.

Objectives

- ✓ To understand the various phases of growth and development
- ✓ To take empirical study on Indian home loan Industry

Methodology

The secondary data have been considered for the present study

Structure of the Home Loan industry in India

Structure of Housing Finance in India

Indian Housing Market can effectively be divided in to three types:

a) A legal private sector which caters for the higher and middle income groups.

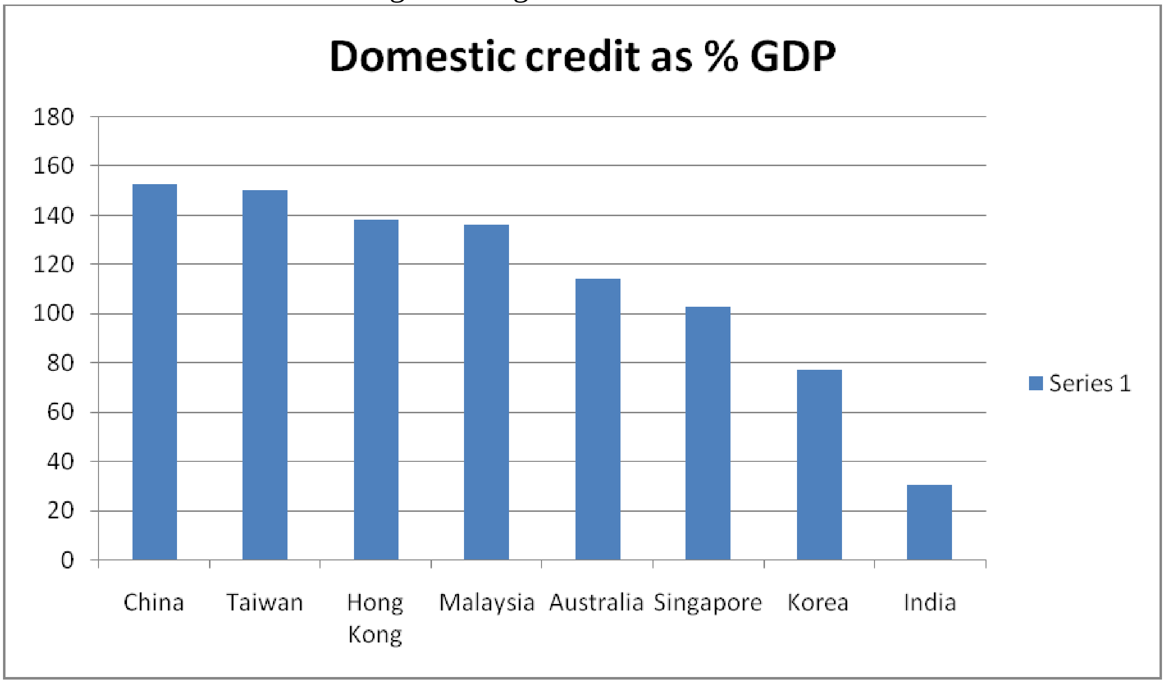
b) Public Sector Housing for State employees and a limited amount of social housing for the poor.

c) The unregulated sector, largely comprising squatter settlements and slums, generally in which about 30 million people live.

Apart from this broad classification, Housing Market can be further subdivided into Rural and Urban, Formal and Informal. It clearly distinguishes between urban and rural markets. In both the category of the people, availability of illegal inputs such as material for construction, land etc., play a major role. Access to land and finance is the major problem in the Urban Housing Market, while in the rural area it is of resource availability, income distribution, priorities within housing services, etc. In fact the rural and urban markets function in different manner as far as inputs are concerned. Equilibrium in the Housing Market cannot be achieved even by an advanced country, due to innumerable sub-markets such as inputs market, wherein there are different markets for land, labour, materials, infrastructure, etc. Often the interaction of these market forces decides the unit price of a housing stock.

Indian Home loans industry is growing at a fast pace of 30% per annum, which is shown in the statistics with average ticket size (loan size) and amount disbursed is rising every year, the opportunities have become more dominant for different organization in India. The demand drivers are fast growing middle class population, rise in working women workforce, bigger aspirations of youth, Tax saving, Transparency in the real estate market. Indian credit report in comparison to the other Asian countries is shown in the statistics below, which is among the lowest.

However in India credit/loan is termed as bad, many Indians of traditional thought do not take credit as it is reflecting in the figures below:-



Source: CII and compiled data

Growth and development of home loan Industry in India

In I980's there was a series of development that had a positive effect on the housing finance sector. They are as follows :

The planning commission set up several task forced during 1979-84 and reviewed strategies for housing development in 1985, the Reserve Bank of India (RBI) made many recommendations for liberalization in the housing financial system based on the Chakraborthy Committee Report in 1987, the Insurance Act of India was amended to allow the Life Insurance Corporation (LIC) and the General Insurance Corporation (GIC) to enter the housing finance business in 1988, the National Housing Bank was set up as a subsidiary of the RBI to act as an apex regulatory and promotional agency in 1989, the RBI allowed Commercial banks to make large loans for housing without an interest rate or loan quantity ceiling.

The National Housing Bank (NHB) was set with the equity support from the RBI and is intended to act as the apex institution for coordinating and developing the housing finance schemes. In 1989, UTI has set up a housing and construction investment fund for direct investment in construction projects and real estate development. The entry of LIC and GIC, and many banks like SBI and Canara Bank through their subsidiaries has been stated to be another landmark in the promotion of housing industry. The system has also been characterized by the emergence of several specialized financial institutions. These have considerably strengthened the organization of the housing finance system in the country. The Housing Finance Companies (HFCs) were set up under the directions of the NHB. The process of liberalization covered the retail housing finance sector substantially. The most significant change was the enhancement of the amount set aside by the commercial banks. This amount is made used for lending to the housing sector from 1.5% to 3% in the Union budget 1999-2000. The Government of India had recently made the development of the housing sector. It is considered as a priority both from the demand and the supply side. This is done by fiscal concessions to the providers of the house and to the borrowers.

The revolution of home loan industry in India can be divided into five distinct phases:

Table-2.1
Phases home loan industry

Phase-I	Before 1970	Government Domination
Phase-II	1970-1980	HUDCO and HDFC establishes
Phase-III	1980-1990	Establishment of NHB
Phase-IV	1990-2000	Liberalization of Interest Rate
Phase-V	2000 to Present	High Growth

Source: Chandrasekar, V. (2010)

The first phase began before 1970 when the sole provider of any house building support was the Government of India(GoI) through its various social schemes for public housing. The government implemented these schemes through state housing boards which were responsible for allocating serviced land and houses to individuals based on the principles of social equity.

The second phase starts with the establishment of the public housing company, Housing and Urban Development Corporation (HUDCO). HUDCO was created to assist and promote housing and urban development programs with government agency. HUDCO still plays an important role in implementing government initiatives such as the Valmiki Ambedkar Awas Yojna which was launched by Government of

India(GoI) in 2001-02 to provide shelter or upgrade the existing shelter for the people living below poverty line in the urban slums. Another important private player, Housing Development Finance Company (HDFC) was established in 1977. HDFC pioneered in individual lending, based on market principles. HDFC today is one of the largest home loan providers of the country and its success displayed that financing homes can be a very profitable business.

The third phase covers the decade of 1980s, which is marked by the establishment of the country's housing finance regulator - National Housing Bank in 1987. The era also involved the government in directing various agencies like insurance companies, commercial banks (Under priority lending requirements which allowed banks to allocate 1.5% of their incremental deposits to housing under RBI guidelines.), provident funds and mutual funds to invest part of their increment sources on housing. Two Insurance companies, LIC and GIC, started supporting the sector both directly through their newly established housing finance companies and indirectly by investing a proportion of their net accretions in socially oriented schemes.

The fourth phase is the era after liberalization and is characterized by dramatic changes in pricing of loans. Before 1994, the pricing of home loans were regulated by the NHB based on a differential rates charged according to the size of the loan. This policy was amended in 1994 and providers were free to charge market rates for the loans above 25,000. The fourth phase saw a dominance of fixed interest rates, but variable rate offers started emerging at the end of the decade.

The fifth Phase of rapid growth in the sector started after the millennium. Home loan disbursements rapidly grew during the first few years of this phase. The lower interest rate regime, rising disposable incomes, stable property prices and fiscal incentives made housing finance an attractive business. Home loan disbursements grew to 7,68,191.90 million in 2005 from 1,47,012 million in 2001. The year 2003 witnessed an annual growth rate of 76% in loan disbursements.

Current scenario of home loans in India:-

In order to understand the recent trends we need to know or understand various factors. These factors play vital role in Indian home loan market. These include interest rate on which banks provide home loan, tax rebate on home loan and its impact. Apart from this to understand the recent trend we need to compare the trends of home loan of different years. Here we have compared the interest and other market trends of year 2010 with 2009-10. This kind of comparison gives the result which helps us to understand the trends of market of any industry. Apart from the impact of present and past economic ups and down also affect the trends. Today the US slowdown is the major issue which has affected almost all the industry. So we have also discussed this issue in terms to define trend of home loan market in India.

In 2017, housing supply and pricing will be the key drivers, while demand for single-family housing will remain strong—mirroring 2016. Positive job gains and attractive interest rates continue to bring buyers to the market. Consumer confidence will improve as employment growth remains positive, interest rates stay attractive, and consumers continue to improve their balance sheets.

On the other hand, supply is struggling to keep up with demand as builders struggle to come back to the market. Moreover, the foreclosure inventory has evaporated and the excess of available existing homes is gone. Coupling these realities with low interest rates is resulting in pricing growth that outpaces inflation. In particular submarkets, with very strong demand characteristics and constrained supply, it is likely that unsustainable pricing exists. In summary, the 2017 housing market will be strong, but buyers should beware of potential pricing “bubbles” resulting from an imbalance between supply and demand.

GoI has taken the following Initiatives to support the housing Sector in the recent years :

The Central Government has taken a few steps towards making ‘Housing for all’ a reality by 2022. The Pradhan Mantri Awas Yojana (PMAY) was launched in June 2015. The Government envisages building affordable pucca houses with water facility, sanitation and electricity supply round-the-clock. The scheme originally was meant to cover people in the EWS (annual income not exceeding Rs.3 lakh) and LIG (annual income not exceeding Rs. 6 lakh) sections, but has recently expanded its scope to cater to the housing needs of the mid-income group, besides the economically weaker sections (EWS) and low-income group (LIG). PMAY scheme comprises of four key aspects. One, it aims to transform slum areas by building homes for slum dwellers in collaboration with private developers. Two, it plans to give a credit-linked subsidy to weaker and mid income sections on loans taken for new construction or renovation of existing homes. Three, the Government will chip in with financial assistance for affordable housing projects done in partnership with States/ Union Territories for the EWS. Four, it will extend direct financial assistance of Rs.1.5 lakh to EWS.

GST impact on Housing Sector

The real estate sector is estimated to account for about five per cent of India’s gross domestic product (GDP) and is considered the second-largest employer in the country, according to an E&Y report from 2015.

However, the sector faces issues in terms of macroeconomic conditions and fiscal policy decisions. One such challenge is the management of the multiple indirect tax levies, such as VAT, service tax, excise, stamp duty and registration fees. Since the GST is to subsume multiple indirect taxes, it will simplify tax compliance and minimise the scope for double taxation. So, there is clear reason for home buyers to cheer, even if they have to pay slightly more in case the standard GST rate is high.

RBI Directive for Home Loans

The Reserve Bank of India (RBI) has in the latest directive asked the Indian banks to be more "fair and transparent" while signing their agreements with the consumers. This has come following complaints from various consumer sections regarding home loans. It has emphasized on the fact that while giving a home loan, the banks should not charge usurious interest rate to the borrower in such a fashion which often results in pro-bank and against consumer interest.

- Households should get credit counseling before signing any loan agreement. In such case, banks should give credit counseling to customer before giving a loan. Any non-governmental organization can also give independent credit counseling to small borrowers.

- Consumers often complain of not receiving benefits of falling interest rates as banks tie their floating rate loans with its PLR and even when rates fall, the banks kept the PLR unchanged. But when interest rates are hiked, the banks increase the benchmark rate, thus making customers pay a higher rate and consequently increase the number of EMIs too. The RBI has asked the banks to mend rules for the same. However, RBI in its latest development has brought a concept of MCLR(Marginal Cost of Fund Based Lending Rate), which refers to a minimum interest rate a Bank can charge the borrower below which Bank can not lend and this is a resultant of the RBI's Policy Rates, thereby brought a scope to pass on the benefit of the RBI's Interest Rate Change on the borrowers.
- Individual borrowers should ask for the exact tenure and EMI while taking a fixed rate loan. The RBI has also resolved to look into all consumer complaints if it is bought to the regulator's notice.
- The IRDA (insurance regulator) has powers to take action against banks if a customer feels cheated while buying an insurance product along with the Home Loan. On its regulatory role, the RBI is trying to maintain a balance between the extent of freedom granted to the banks and the objectives of governance.

Challenges for home loan industry

The housing finance sector has emerged as one of the outstanding successes over the last decade. In the earlier scenario, there were select few dominant players in the housing finance industry, whereas in the current scenario, there is an increase in the number of players in the housing finance industry over last three years. This has increased a hefty competition in the housing finance industry.

Declining interest Rates

The interesting trend that has emerges in the housing finance market over the last few years is the decreasing importance of interest rates (Anil K Khandelwal 2002). This acts as a competitive tool. The interest rate charged by a small HFC was at least two-and-a-half to three percentage point higher than the rate charged by HDFC. The banks would of course charge the lowest rate. The nationalized commercial banks, still offer the lowest rates on some occasion. There is not much difference in the interest rates amongst the various players in the housing loan segment.

Service and Product Innovation

The service and product innovation are the only way to differentiate one company's product from another. This is due to the absence of a significant difference in interest rates. The difference of a half-a-percentage point in interest on housing loans can be easily offset by quick and reliable service. The product innovation as used to capture the market in this industry. The competition has made the housing finance institutions look for the needs not met in a seemingly straight forward product. Now the HFCs are offering insurance packages that come attached to a housing loan product. The severe competition will bring few more innovations in the future. The product innovation is unlikely to remain unique for long because companies quickly mimic a successful introduction. The only benefit from product innovation is to build an image and the advantage of being the first to capture the market.

Smaller HFCs

The image building is likely to be very crucial to all HFCs. The traditional strengths of HDFC, ICICI and LIC housing finance made the life of smaller HFCs very tough. The smaller HFCs are likely to be more active in smaller towns. The smaller towns are less likely to witness head-on competition from bigger players. So in this segment the smaller HFCs try to capture the market

HFCs vs Banks

The banks aid HFCs are competing each other in the housing finance market. The severe competition between these two housing finance providers had made them to adopt various strategies to increase their market share. The HFCs are facing lot of constraints as against the banks. The banks have access to lower cost of funds compared to HFCs because banks have easy access to low cost retail funds and low minimum capital adequacy ratio. The HFCs are not given refinance by NHB at competitive rates. The banks despite a late entrant have overtaken the HFCs in the home loan markets. The share of banks in total home loan disbursements has risen from 43.6% in the year 2000-01 to 65.5% in 2002-03.

Consumer Services

The current housing finance market is skewed in the favor of the buyers. The home buyers are rushing to take a housing loan without fully exploring the options available. The housing finance sector has certainly become more competitive in recent times. The banks and housing finance companies market their housing finance products much more aggressively. The customers are seeking more convenience in the entire process of acquiring a home as well as the finance for it (Rajiv Sabharwal 2002). Therefore the marketing has assumed significance in the rapid increase in activity of housing finance sector. The housing finance institutions are resorting to various marketing strategies to effectively market the specialized finance products. The housing finance providers are trying to satisfy the customer. As far as the industry is concerned the customer appears to gain from the competition in the way of better products better prices and better services (Gunit Chadha 2002). The real discriminating point, as far as the customer is concerned, will become his perception of the quality of service of one company over the other.

Future of home loan industry in India

The housing finance is likely to remain a low risk low margin business that records fast growth in the foreseeable future. The market is likely to get a little broader based approach(Mistry K K 2002). The HDFC’s market share may be eaten by ICICI. The industry will continue to be dominated by a handful of big players and it is difficult to see beyond HDFC, LIC Housing Finance and ICICI as dominant players at this point. The HFCs will continue to operate in a highly competitive market with higher demand for home finance. The housing shortage and the government initiatives and above all the customer-centric interest rates will be the drivers of HFCs. The improvement in products, services, access and reduction in interest rates will retain and create customers. The buyers are the ultimate beneficiaries at large. There are several bottlenecks exist in this industry. They have to be taken care of, before any of the above can bring about an improvement in the prospects of the industry. The overall demand for housing is ever rising and the same would be reflected on the demand for funds. Hence the profitability of the industry should commence on the positive track in the future.

The HFCs and banks may adopt some marketing strategies in future to increase their market share in the home loan sector. They may tap newer segments such as packages for professionals, single clearance loans up to Rs. 15 lakhs, providing personalized services to customers, cross selling by capitalizing on the networks of other companies, competitive pricing in terms of lower interest rates and front end charges etc. They also have started entering into tie-ups with reputed builders and development authorities and private developers. The housing finance institutions will increase their reach by penetrating into rural and semi urban areas. The greater publicity through newspapers, websites and other media will fetch greater importance in this industry.

Concluding note

It is well understood that housing is not a problem of all, but it is a problem of economically poor and middle class families. So the home loan providers should target to serve for these sectors for better economic development. The chapter clearly explained the home loan scene in India. Though the major players are concentrating on various services they have to concentrate on satisfying the customers. The future of housing finance is witnessing stiff competition. This force the public sector banks to come out with strong strategies.

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