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Is the Indian Housing Finance Industry Keeping Pace with Changing Demographics?

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Introduction

India features amongst the world's most promising economies, with a slew of factors fuelling its growth story. The average age of an Indian hovering around 30 and the global outlook of this young population are definite drivers behind the past decade's upbeat consumer trends, global corporations across sectors flocking to the country to leverage the potent Indian talent base, and international brands trying to reach out to customers even in the Tier-II and III towns of India.

Interestingly, this global outlook has not been at the cost of local and regional attributes this young populace identifies itself with. Take, for instance, celebrating Durga Puja attired in international lifestyle brands in the midst of a pandal that serves both *puchkas* and doughnuts, or Ferrero Rocher chocolates being accepted in the fare of *mithais*.

This unique attribute of the Indian customer is also well reflected in his investing patterns. While the larger investing base straddles traditional and modern instruments alike in building a robust portfolio, real estate and gold feature high on his list of assets. In fact, besides a life insurance policy, a piece of land or a house is the first large investment that every Indian makes—sometimes, nowadays, as early as at 25 years of age.

Against this backdrop of the consumer's psyche, given below is an analysis of the Indian demographics and how, correspondingly, the housing finance sector has evolved.

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India: Demographic Overview

India has recorded a 17.64 per cent growth in its population which rose from 1,02,87,37,436 in 2001 to 1,21,05,69,573 in 2011. While housing stock increased by 31.02 per cent from 18.7 crores in 2001 to 24.5 crores in 2011, the number of households increased by 28.65 per cent from 19.2 crores in 2001 to 24.7 crores in 2011. Despite a significant network of formal financial institutions providing home loans, the Indian demand for housing (and consequently housing finance) has not yet been completely addressed.

As per the latest government estimates, the urban housing shortage is 18.78 million units while the rural housing shortage has been approximated at 43.67 million units. These figures suggest that in spite of numerous efforts by the Indian government and lending institutions, financial inclusion still remains a concept on paper for a major portion of the population.

Evolution of the Indian Housing Finance Sector

Housing finance has been a proposition offered by money lenders and nationalised banks almost through the whole of the past century. To accelerate the pace of growth of the housing finance market of India, the National Housing Bank (NHB), a fully owned subsidiary of the Reserve Bank of India (RBI), was set up as the industry's regulator in 1988. The primary objective of NHB was to promote a network of dedicated housing finance institutions to serve diverse regions and different income groups. Over the years, NHB has supported the growth story of housing finance companies (HFCs) and continues to support their sustainable development with a concerted focus on the bottom end of the customer segment pyramid. HFCs are regulated by the NHB the way banks are regulated by RBI. Any policy amendments or new announcements are gradually implemented by both regulatory bodies, thereby avoiding disparity in the regulatory framework of home loan products.

The last two decades have seen the emergence of three of India's largest HFCs, which today share among themselves the largest market share. The past years have also witnessed the entry of many focused housing finance players, and as of 30 June 2013, the total number of HFCs registered with NHB stands at 57, of which 39 have been granted certificates of registration to accept public deposits. Of all the HFCs, a select few have been responsible for taking housing finance to the unbanked in the urban and rural parts of the country, serving the requirements of the otherwise ignored segments. Dewan Housing Finance Corporation Limited (DHFL), for instance, pioneered enabling financial access to the lower-and middle-income (LMI) segment in semi-urban and rural parts of India three decades ago, and continues serving the segment profitably.

The share of housing finance companies in the home loan market grew to 36 per cent as in March 2013 from 26 per cent in 2005. The total outstanding of housing loan portfolio as of 31 March 2013 stood at Rs. 2,90,427 crore, with an annual growth of 30.69 per cent. Industry analysts claim that the top five HFCs account for close to 85-90 per cent share of the retail home loans offered.

As the core business of a HFC is providing 'housing finance', they have honed expertise in offering better services, faster loan processing and disbursement at competitive interest rates. This has also resulted in numerous tie-ups and home loan syndication agreements between HFCs and public as well as private-sector banks. Despite the competitive environment, the housing finance industry has witnessed healthy growth in home loans in the last fiscal, owing to deeper penetration and focused approach of HFCs across Tier II and III locations. HFCs are often preferred by borrowers given that loan processing is relatively faster and simpler compared to public sector banks.

The International Finance Corporation (IFC), a member of the World Bank group, has also taken such focused initiatives to enable home ownership in the lower income segment. IFC, in association with DHFL, established India's first low-income segment focused housing finance company in 2011, Aadhar Housing Finance Ltd. Over the last three years of its operations, Aadhar has strengthened its operations in the seven identified low-income states of the country and offers home loans to the low-income groups (incomes ranging from Rs. 5,000 to Rs. 25,000 per month). Aadhar offers loans up to only Rs. 12 lakh. Recently, Aadhar forayed into the Gujarat market with a multi-location presence.

Consumer Trends

In what way does a present-day home buyer differ from those in the past?

Today's home buyer is much younger than earlier; secondly, there are a greater number of joint applications, primarily to enhance eligibility; and thirdly, pre-payment of the first loan is increasing, so that the buyer may acquire a second home—usually considered as an asset investment by the buyer—with a fresh loan. These are the three major changes that have been witnessed in the Indian home loan segment in the recent past.

Buying a home for yesterday's generation comprised creation of a place of one's own where retirement would be comfortable. Usually, the person would have been living in a joint family and the new home would also mark the separation from a large, joint family to a nuclear family—which would soon morph into a joint family again as the children would already be of the age where they would be all set for marriage. For today's generation, the focus is on being economically self-sufficient in an India where incomes have risen at entry levels; a young adult just a few years into the job market starts to work at acquiring his own home—with obvious help from a home loan.

The key difference between today's home buyer and those in the past is a changed attitude. The scenario earlier was that an individual worked all his life and continued saving, and near the age of retirement, bought his own home. Taking a loan was not considered appropriate behaviour from a social perspective; buying a home was something done with one's own money. At the most, the home buyer would borrow within the family. The average age of the first home buyer a decade ago was 38 years. This again, was a change from the scenario a decade earlier to it, when the average home buyer's age was estimated to be around 43 years.

Today's young home buyer reflects the changed Indian economic scenario, and seeking a home loan is seen as part of the process of asset creation rather than borrowing money. The down payment, i.e., initial money required for the home, is usually saved over the first few working years, also supported by, in some cases, the returns of forays as a small investor in the equity market. 'Credit' is no longer a dirty word, and personal loans are at times availed of to bridge the gap between the loan amount sanctioned and the fiscal resources available with the young loan applicant.

Leveraging resources is something that comes easily to today's young home loan applicant, and a joint home loan is usually the norm. Young Indians who have just started earning may not be individually eligible for the sort of loan they would need to buy an 'entry level' home; they very quickly realise that a joint application increases eligibility for better loans. At times, couples have tied the knot earlier than they would have ideally in order to enhance their eligibility. Given the way residential real estate prices have risen in recent years, their thinking seems to be valid.

It is not only young buyers who are buying homes. The market is also witnessing middle-aged home buyers, but the difference in the types of homes being bought by both has nothing to do with age or generation-based preferences. At the lower half of the pyramid are buyers who know they do not have sufficient finances to buy a home of their choice in terms of location or size. So, they opt for homes that are 'entry level', bought with the understanding that some years down the line, they will 'upgrade' to the next level—a larger-sized flat in a nearby area or an entirely new location, one which is closer to their place of work or is considered 'posh'.

The middle-aged buyer is not necessarily someone who could not afford a home thus far; usually, it is someone who opted to stay in a leave-license accommodation while saving money to buy a home in a location of choice. This is also another emerging trend. However, what stands out as unique in the Indian market is that home as an investment is still in vogue.

Funding options are usually the same—savings, and in some instances, investments made over the past few years which are brought in as 'their contribution', while the balance is taken by means of a mortgage. They shop for the best home loans, usually making the rounds of different Home Finance options before zeroing in on what is the best for them. Home buyers are also increasingly using online resources to collect information. Realty exhibitions are another source for collating data and comparing the best available deals, and today's home loan applicant fully explores all such options. Some home loan providers also provide property search options.

Home loan providers are also offering value additions like insurance on the property or the property buyer's life, or premium banking facilities at no extra cost. The future is likely to see a potential home loan taker being wooed by loan providers through such means—in the manner witnessed a few years ago—but market forces are always a factor of demand and supply determining price. Therefore, while a builder or developer may want to be pro-active and get his buyer an attractive home loan, it might not always be possible unless there is a product structured in a way so as to be attractive to the loan seeker.

Buying a home is as much a necessity today as it was in the past, and a home loan will be as relevant tomorrow as it was yesterday. There may be some minor changes, but a home mortgage will largely remain what it has been—helping a potential buyer bridge the gap between personal funds and the cost of the 'dream home' they want to make a reality.

Economic Momentum

Housing market is one of the major contributors to the Indian economy. The growing purchasing power of the lower-and middle-income population, changing demographics and government and regulatory support, have all been driving the demand for housing finance. For banks and HFCs, this is an opportune time to understand these trends, identify unexplored markets and devise housing finance solutions.

Although banks occupy a major portion of the housing finance industry, HFCs address the major demand that comes from households at the middle and bottom of the pyramid. HFCs are required for increasing access and affordability to housing finance among the LIG segments. Moreover, HFCs, being dedicated home loan providers, are better equipped to provide improved product packaging, customer relevance and service. When looking at the growth rate and balance sheets of some of the leading housing finance players, most of them have outperformed their peers. Mortgage penetration is at 9 per cent of GDP compared to 5-6 per cent earlier. This trend of increasing customer penetration of HFCs will mean more customers have access to financing their home purchase needs.

The NHB has in the recent past initiated various refinance schemes to promote affordable housing for the urban low-income segment, rural housing and energy-efficient homes. NHB has set up the Central Registry of Securitization Asset Reconstruction and Security Interest of India (CERSAI), Credit Risk Guarantee Fund Trust for Low Income Housing (CRGF TLIH), India Mortgage Guarantee Company Pvt. Ltd. (IMGIC) and has drafted a Real Estate Regulation and Development Bill. NHB's RESIDEX covers 26 cities as of this date.

The Finance Ministry has also supported affordable housing by allowing External Commercial Borrowings (ECBs) for low-cost affordable housing projects by HFCs as well as for builders for construction. However, the ECB limit will need to be substantially increased in order for it to make a positive dent in addressing the housing demand-supply gap.

Last but not least, the acceleration in GDP growth has raised the demand for housing. As a percentage of GDP, outstanding housing credit from banks rose from 1.2 per cent in 2001 to a peak of 5.3 per cent in 2006 before moderating to 4.2 per cent by March 2012. The weighted average lending rate (WALR) on housing loan first declined from 12.8 per cent in March 2001 to a low of 8.6 per cent in 2006 before again marginally rising recently. Though the interest rate on housing finance has gone up since 2006, it has remained below the overall weighted average lending rate of banks (Mohanty, 2013).

Challenges

Although there are various Government of India initiatives as well as schemes of institutions like World Bank and its members like the International Finance Corporation (IFC), there still exists a challenge at the ground level: the simple availability or production of affordable housing projects.

While HFCs organise builder-consumer events and also provide project cost management, technology transfer and marketing support to builders even in Tier III and IV locations, the demand and supply gap is huge. With enhanced focus towards this developer-builder community, the challenge in question can certainly be overcome. Ensuring production of affordable housing projects will also control migration of the rural populace to urban locations in the hope of better lifestyle. Government intervention at the infrastructure level with respect to roads, sanitation, potable water, sewage management, electricity, education and job opportunities will indeed sustain the development of rural India. However, Corporate India has to innovate ways to support this transformation, i.e., not only philanthropically, but also by in-building a sustainable, socially-inclusive business model.

Outlook

More than 50 per cent of India's population is below the age of 25 years and more than 65 per cent is below the age of 35 years as per the 2011 census. The average age of an Indian will be 29 years by 2030. With the housing gap expected to considerably further increase by 2030, the Indian housing finance sector is expected to grow significantly. The economic boost, emerging global markets exposure, changing lifestyles and international cultural influx will continue defining the new-age Indian home loan customer and the industry at large.

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