CHAPTER-II

Research Design and Methodology
2.1. INTRODUCTION

Finance plays a crucial role in housing construction. But investments in housing are normally locked up in the form of fixed assets. In contrast to industrial and agricultural sectors, investments in housing do not generate any substantial return to the investors. Further, the lending institution has to patiently wait for longer duration to recover the amount lent to the borrowers of housing loans as against agricultural and industrial financing, wherein the recovery of loans will be completed much earlier. In case of housing finance, repayment of loan is not related to the income generated from the investment of the loan amount. It is the salary or other income of the borrowers in repayment of housing loans. It is thus evident that the nature of housing finance differs vastly from agricultural and industrial finance.

Housing finance has now been attracting a lot of attention in the country and the role of housing finance institutions in alleviating the housing problem in India has gained crucial importance. In fact, during the past two to three years the growth in housing finance is very high and exorbitant and the competition in the home loan industry is heating up with players constantly innovating and coming up with new ways to promote their products. This competitive growth is good for the consumer, for the lending institution, it could spell higher Non Performing Assets (NPAs). The unhealthy competition influences the reduction in interest rates and margins there by it will effect the asset liability mismatch of loans and also return on investment.

With growing number of Housing Finance Institutions (HfIs) and increased competition, the housing sector has become increasingly market driven. The sector has offered good business opportunities for the lending agencies and attractive terms for the borrowers. There are instances of fraud in the housing loan market, which is not checked, can impact the lending sentiments in the sector. There is a definite need for standardization and uniformity in practices in order to improve transparency in the market and bring greater efficiency. No sincere efforts were made to study about the housing finance by different institutional agencies and the problems of borrowers and the lending agencies are confronted with. The above considerations have given rise to the present study.
The flow of credit to the housing sector has shown phenomenal growth mainly an account of contributions of HDFC, LIC, HFC’s and Commercial Banks which have emerged as significant players in the housing finance system. Hence, the present study is an attempt to review and analyze the housing finance providing by the HDFC Bank, LICHFL, ICICI Bank and SBI to individual borrowers in Chittoor District of Andhra Pradesh.

2.2. SIGNIFICANCE OF THE STUDY

The growing rate of population needs more investment in the housing sector. Since independence low priority was given to housing due to factors like large capital resources required, high capital output ratio and top priority was given to sectors like the agriculture, industries, power, communications etc. Housing problem in India came to the fore in the pre-independence days and the intensity of the problem had gradually increased thereafter. The shortage of housing stock which stood at 7 million in 1901 reached to 22.9 million in 1991 and 24.7 million by 2001. The Eleventh Five Year Plan has estimated that the housing shortage is likely to go up to 26.53 million during this plan period (2007-2012). The housing sector has now been recognized as a potent engine of economic growth and the authorities at the higher levels identified “Housing for All” as a priority area in the agenda for governance.

Paucity of housing finance has been identified as one of the basic factors for housing problem in the country. The Housing Policy (1998) has stated that a specialized housing finance system has to be developed to increase the flow of funds for the creation of new housing stock and to improve the quality of existing housing stock in all parts of the country. The last three to four decades have seen significant institutional development in the area of housing finance in our country.

Investment in housing is an important lever of economic development. The growth in housing and housing finance activities in recent years reflects the buoyant state of housing finance market in the country. The growth in the housing sector not withstanding, there is enormous scope of improvement as the present level of investment in housing in our country is measure as compared to the figures of more than 50 per cent in some of the developed countries like USA, UK and Netherlands.
In this context, an analysis of the role, cost and significance of different sources of housing finance is warranted. It is also significant to probe whether the pattern of mobilizing funds for housing differs in relation to the varied social and economic backgrounds of people. Another important aspect which needs special investigation is recovery of housing loans. It is also imperative to know about the performance and problems of specialist housing finance institutions in the country. All these issues call for empirical study.

2.3. REVIEW OF LITERATURE

There are various studies made in the field of housing finance in India. But, most of the studies concentrated on weaker sections housing, rural housing and co-operative housing. This study is an attempt on housing finance by different financial institutions basing on empirical data. Some of the relevant studies are reviewed under.

Varghese in his work on “Housing Problem in India” examined about the housing finance in India and presented the sector wise (public & private) analysis of housing finance in India².

Sundram suggested that the Insurance Corporation may be set up to extend insurance coverage to the home loan borrowers as housing loans are long term investments in nature and involve considerable risk to the lenders³.

Sharma in his book ‘Housing Finance in India’ reiterates that housing finance is one of the areas of public finance which has not received enough attention in the country. He has stated that its full potential is yet to be explored and exploited. It is also pointed out that the steep imbalance in the demand and supply situations has already pushed housing prices quite beyond the reach of those very millions who require adequate shelter⁴.

Chiranjoy Sen in his study reported that the structured sources in the Indian housing finance sector are not backed by other sources which are prevalent abroad like mutual funds, venture capital funds, development trusts, real estate investment trust and debt securitisation. He has also observed that the sector till now has been marked by lack of institutionalisation⁵.
Shelley Singh and Udayan Ray in their study identified that the increase in demand for housing loans has been spreading beyond the Metros into smaller towns and there has been a significant increase in loan disbursements in the small towns of the country in recent years. They have also pointed out that a combination of favorable conditions ranging from low and stable real estate prices and low interest rates is helping the prospective house owners realise their dreams.

Kavita Dutta and Gareth Jones in their study “Housing and Finance in developing countries” dealt with the formal and informal housing finance markets in two Indian cities, Vizag and Hyderabad of Andhra Pradesh. They examine to what extent each finance market is comprisable with the survival strategies of the low income house holds.

Alpana Sivam and Sadasivam observed in their study that the housing demands, development of housing finance and formal housing agencies in both public and private sectors. According to them, they are neither fast enough to meet demand nor cheaply enough to reach the poor. As a consequence, an informal sector has emerged in almost all cities in India.

Singh and Sharma focused on the fact that the main objective of NHB, is to promote and establish housing finance institutions in the country as well as to provide refinance facilities to housing finance corporations and scheduled commercial banks. Their study also analyses the region wise disbursements of individual house loans, their portfolio amounts and defaults.

Samantak Das stated that the National Housing Policy aims at mobilizing resources and facilitating expansion of investment in housing. The author also highlighted the steps taken up by the government to concentrate on upgrading and improving the facilities and creating a proper environment for housing finance activities by eliminating constraints.

Khan stated that for millions of ordinary Indians, owning a home has remained a cherished dream over the decade. Today, a favorable mixture of various factors is helping them to realize that dream faster than ever before.
Kohli in his book "Housing Finance Agencies in India" elaborately discussed about various housing finance agencies which are actively involved in providing finance to the housing sector. He mentioned that the housing finance sector is growing rapidly much because of the tax incentives. Even then, the housing problem in India is the ever widening gap between supply and demand of housing because of multiplication of families. The percentage of owner occupied houses to total houses is quite unsatisfactory in India. The large chunk of Indians live in rented houses by paying exorbitant rates of rent. He explained the role of National Housing Bank in facilitating housing finance and the functions of Housing Finance Companies (HFCs) in a nutshell. He analyzed the loan appraisal practices of different financial agencies in India. The maximum admissible loan amount, disbursed period, interest rates, repayment procedures are discussed and compared among various institutions. He concluded that the proportion of investment in public sector housing has declined which the same in private sector has increased. Only 10 per cent of the total market share is with the organized housing finance such remaining in un-organized sector. There is dominance of three/four big HFIs in the overall housing industry.12

Giriappa in his book analyzed the demand and supply of houses and housing finance in India. The rural and urban housing needs, constructions and cost aspects are described in his study. Various programmes have been introduced to provide shelter for rural poor such as Indira Awas Yojana, Jawahar Rozgar Yojana and Rural Housing Scheme. The National Housing Policy recognizes the housing norms will have to be evolved at the local level with regard to diverse climatic conditions and life styles of the people.

Housing finance through different Five Year Plans is discussed in detailed. He focused on various subsidized housing programmes implemented in Dakshina Kannada under central and state government assistance. He suggested that not as the procedures have to be simplified and harassment of the fresh borrowers should be reduced, it has to be made flexible and customer friendly. The interest rates have to be rationalized in keeping with the market rates and the borrowers capacity of repayment13.
Ravi Kumar stated that financial sector reforms in India have brought out rapid changes in the structure of financial markets, more particularly in commercial banks. Commercial banks are taking up new service lines, designing innovative products and expanding business into areas higher to unknown to traditional bankers. In the process, commercial banks are now exposed to more risks. New products and financial instruments have made in roads into the banking business vocabulary and made it imperative for banks to acquire new skills and improve their knowledge base, particularly in new areas such as derivations, futures, options, risk management, asset liability management, etc. He analyzed the financial statements of banks and critically evaluated the risk management in banks. The investment rate risk, liquidity risk, credit risk, contingency risk are some of the risks he analyzed. Risk management basically involves identification, quantification, policy formulation, strategy to transform the exposures to the desired form and monitoring risk levels and restoring them to the standards. Asset Liability Management (ALM) is concerned with strategic balance sheet management involving risks caused by changes in the interest rates, exchange rates and the liquidity position of the bank. He designed various methods to tackle the above said risks involved in ALM and showed how to implement them.

Keka Lahiri described that the intense competition has led to competitive interest rates and narrowing down of margins in order to expand and capture better market shares, the banks have actually over looked the credit worthiness of the customers. He mentioned that, not only in India, but also the world economy has faced the same problem and as a result the housing finance markets have been flooded with debt.

Singh and Singh in their work mentioned that the economic liberalization led to the emergence of the variety of new players in the financial sector like Non Banking Finance Companies (NBFCs), high-tech private banks, subsidiaries of Public Sector Banks (PSBs) and more branches of existing and new foreign banks. The triple rated corporates and blue chip companies have started sourcing capital market directly for their financial needs both domestic and international. Hence, demand for bank credit of these high rated companies has become feeble and their demands on banks for low interest rates, quick and personalized service tailored to their individual requirements have increased man fold. This pin points the need for upgrading the credit appraisal skills of bankers to enable them to segregate between low and high credit risk and take
product credit decisions. They concentrated on financial statement analysis of banks and financial institutions and various risks involved in bank lending. They discussed in detailed about how to tackle the NPAs and to appraisal of new projects.

Padhiri and Misra in their study on rural housing finance laid an attention on Orissa state. They stated that the housing condition of Orissa is deplorable due to gap between demand and supply in housing has been widening year after year. They focused on the role of Housing and Urban Development Corporation (HUDCO) in promoting rural finance in the state. It is an accepted fact that the state of Orissa is a land of villages. Since more then 87 per cent of it’s population lives in villages and a village is considered to be the basic unit of development. The problem of housing in Orissa is of a very high magnitude in comparison to other states. The Orissa Rural Housing and Development Corporation (ORHDC) was incorporated on 19th August, 1994 to provide housing finance both in rural and urban areas with a prime focus on the Economically Weaker Sections (EWS) and Lower Income Groups (LIG). The ORHDC has also introduced a new scheme, known as “Credit Linked Housing Scheme” to help the poor people in Orissa. HUDCO has given special thrust to rural housing. It is observed that nearly 90 per cent of the total number of dwelling units sanctioned by HUDCO is for EWS and LIG and more than 56 per cent of residential dwelling units are for rural areas.

Singh and Singh in their study on “Risk Management in Banks” analyzed the financial sector reforms in India and the Asset Liability Management in banks. They discussed various risks involved in lending and the challenges in Credit Risk Management (CRM). Management of risk should be a major concern of top management of banks. The Board of Directors should clearly articulate risk management policies, procedures, prudential risk limits, review mechanisms and reporting and auditing systems.

Venkateswarlu in his book “Urbanization in India – Problems and Prospects” covers a wide range of aspects of present urban scenario viz., urban and regional planning, provision of urban infrastructure, key issues in water supply and transport, environment housing property alleviation etc., An attempt has also been made to analyze such problems and has endeavored to depict a new perspective with sanctioned approaches and innovative interventions for better urban governance.
through urban agenda for 21st century in the light of the 74th Constitutional Amendment.

Rapid urbanization in India is becoming the key issue for all policy makers in the country. The problems of urban areas are now becoming obvious and dominant. Poverty and social alienation of millions living in urban areas are being reflected through inadequate shelter, in accessibility to safe drinking water, insufficient public transport, ill planned townships, unsecured owing to growing urban violence, etc., Sustainable development of both natural and human resources has become very necessary to mitigate such problems. He concluded that the urban agenda for the 21st century should, therefore, not be confined to better city planning only but should also works for development of a new urban society with better physical, social as well as ethical quality of life.

Miglani in his study on “Urban Housing in Developing Economy” deeply focused on various aspects of housing finance. He examines structure of rent, role of rent regulations, housing investment, investment of surplus of funds, utilization of external finance for housing factors that determine demand for housing, etc., relating to urban house holders and considers the structure of housing both in the rural and urban areas. Besides, housing shortages, investment requirement, elasticity of demand, income generation and capital formation in housing are some of the main areas of interest which have been systematically studied. In addition, a focus on the demand for and supply of housing in order to come out from the serious crisis of housing shortage and silent crisis in housing plan, policy and programme.

Venkatesh in his book described that predatory lending refers financial practices by mortgage companies, creditors or brokers which involve engaging in deception, manipulating borrowers using aggressive sales tactics or taking undue advantage of borrower’s ignorance about loan terms. These practices often targeted at low-income individuals are often combined with abusive loan terms such as loan flipping, charging of excessive fees and very high interest rates, extending loans ignoring the borrower’s repayment ability and outright fraud. Predatory lending has played a key role in the United States sub-prime crisis which had global implications. Although questions regarding the magnitude remain, there are fears, that it could be worse than anticipated. The sub-prime crisis cannot be resolved completely without eradicating
the existence of predatory lending practices. He stated that un-ethical practices followed by predatory lenders like imposing huge pre-payment penalties, granting loans above the value of the house, delaying in formation on payments, providing incorrect information on pay offs etc., end up blocking the borrower’s access to other market rate financing. He concluded that predatory lenders use combinations of numerous tactics to convince borrowers to take high risk loans, which eventually strip the equity from their houses. In most of the cases, the borrowers are unaware of the chances detrimental to their interest in loan documents or are led to believe that those chances are not important.

Sugan C Jain in his book pointed out that an asset becomes non-performing if it fails to contribute any income to the owners. He discussed elaborately about the causes for Non Performing Assets (NPAs), RBI guidelines relating to NPAs and other issues pertaining to NPAs. He suggested various measures to curb the NPAs. Early alert system, preventing slippage, effective recovery management and settlements through compromise are some of them. He concluded that a strategic planning is must to manage NPAs effectively and to control them to a maximum level.

Subba Rao in his article mentioned that traditionally, the housing finance segment has been associated with very low risks. But empirical evidence suggests that NPAs in the Indian housing finance sector are much higher than those experienced in a developed market such as the United States. The competition in the home loan industry is heating up with players constantly innovating and coming up with new ways promote their products. These un-healthy competition influence the reduction in interest rates and margins and there by it will effect the asset liability mismatch of bank loans and also return on investment. He identified the drawbacks in housing finance and suggested some remedial measures to overcome them.

Rajasekhar and Saravanga in their article analyze the trend in the growth and structure of Life Insurance Corporation Housing Finance Limited (LICHFL) in Chennai city and find out the relation performance of LICHFL in providing housing loans. They stated that majority of the respondents opted housing loans for the purpose of purchase a house or flat instead of construct a house in Chennai city and they preferred flexible rate of interest option rather fixed rate of interest. They further added that the borrowers of home loan faced problems like delay in sanction and
disbursement, irrelevant securitization, cumbersome procedure, etc. They concluded that the borrowers of LICHFL, Chennai city, though they come across several problems, they expressed their satisfaction against the lending institutions because they are enjoying with own houses or flats and forget the initial pains in getting loans.

Hari Chandra in his article reveals that though the government attention has been increasing in this sphere of activity, due to budgetary constraints and other pressing problems the housing shortage and substandard houses has increased over the years. Therefore, the role of institutional finance assumes vital importance. He attempted briefly to bring out the involvement of HUDCO and HDFC in promoting housing finance. HUDCO is mainly focus on economically weaker sections to provide housing finance. Whereas HDFC with its branch network meet the individual requirements with retail lending by providing an impetus for the development of more ownership housing.

Raminidharan in his article pointed out that there is a tremendous growth in bank finance to housing during the past 3-4 years because of fiscal benefits like tax concessions to individuals, stable real estate prices and availability of housing loans at affordable interest rates in the market, investment options have dried up with lower interest rates, slashing of interest rate on housing loans, etc. The other supporting reasons for growth in housing loans are growing population, nuclear family system, easy availability of housing loans, shortage of dwelling units, ownership Vs rental decision, etc. He mentioned that banks are facing the challenges in the area of housing finance as declining spreads, asset liability mismatch, concentration on salaried persons only, fixed rate lending risk, etc.

Arora in his paper stated that with the increase in the focus of the banks on the housing loans activity, lending to quantum jump of lending to this sector, increase in the number of frauds in housing loans. The frauds from the borrowers side are impersonation, submission of fake title deeds, preparation of multiple set of a single title deed and creation of the duplicate mortgage, selling of the property without clearing the existing loan, submission of highly inflated valuation report and cost estimates for purchase, construction of the house etc. He further mentioned that safeguards to prevent the occurrence of the frauds in housing loans are required to be
taken at all these stages of lending i.e. (i) Pre-sanction appraisal; (ii) Documentation and creation of security; and (iii) Post-sanction follow and verification of the end-use. As a part of pre-sanction appraisal Know Your Customer (KYC) norms, site verification, valuation, cost estimation, approval of map, photo of the IP are necessary. As a post sanction follow-up the bankers should monitor the progress in construction through personal site visits. It is ensured that there is no diversification of funds.

2.4. OBJECTIVES OF THE STUDY

- to review the growth of housing finance in India;
- to study the institutional setup for housing in India;
- to examine the loan appraisal practices of select Housing Financial Institutions (HFIs);
- to analyze the problems of borrowers and select HFIs in Chittoor district;
- to make relevant suggestions and recommendations for effective and viable housing finance.

2.5. RESEARCH METHODOLOGY

The area of the study is confined to Chittoor district of Andhra Pradesh. To cover the wide range of population spread over the district, a two stage sampling plan is considered to be more convenient and effective. Selection of branches formed the first stage and borrowers the second stage. The branch network of the sample HFIs in the district is LICHLFL – 1; HDFC – 1; ICICI -3; SBI – 38. These four HFIs are dominant group in providing housing finance and they cover more than 60 per cent of the home loan business in the district. In keeping view, in the first stage, one branch of each Housing Financial Institution (HFI) i.e., LICHLFL (Tirupati), HDFC Bank (Tirupati), ICICI Bank (Madanapalli) and SBI (Chittoor main branch) are selected by purposive sampling.

In the second stage, out of 1502 total home loan borrowers a sample of around 20 per cent i.e. 300 borrowers from 4 HFIs (75 from each HFI) are purposely selected through stratified random sampling technique, keeping in view corporates, small businessmen, employees and self-employed. While doing so, proportionate
representation is followed. Two sets of detailed structured schedules are prepared to collect the opinions from the borrowers as well as the officials concerned.

2.6. DATA COLLECTION

The study has made use of both the primary and secondary data. Primary Data is collected from the sample respondents who have taken housing loans from the sample HFIs. Pre-tested schedules are developed and personally administered for the purpose. The perceptions of managers and staff members of select Housing Financial Institutions are elicited.

Secondary data is obtained from Journals, magazines, periodicals, books, dailies, reports of the Government of India, National Building Organization (NBO), Reserve Bank of India (RBI), National Housing Bank (NHB), commercial banks, Five Year Plans of both the Government of India and Government of Andhra Pradesh, Annual Reports of Housing Development Finance Corporation (HDFC), Housing Urban Development Corporation (HUDCO), National Co-operative Housing Federation, LIC, GIC and downloads from various websites. Besides, published and unpublished proceedings of various Seminars and Conferences are consulted.

2.7. TOOLS OF ANALYSIS

The data is processed, tabulated, analysed and interpreted with the help of tools such as averages, percentages, ANOVA, t-test, chi square test, etc. Further, graphs and diagrams are also made use of to illustrate the facts and figures wherever necessary.

2.8. SCOPE AND LIMITATIONS OF THE STUDY

The study confines to the performance of housing finance by selected HFIs in Chittoor district of Andhra Pradesh. The study, therefore, excludes other financial institutions, and also other categories of borrowers of housing loan like builders, professionals and beneficiaries under Government Schemes. The sample borrowers are the individual borrowers who have constructed residential houses only. HDFC Bank and LICHFL have only one branch in the district. Hence only one branch of each HFI is selected as sample. The sample is very limited. Hence, the opinions
expressed by the limited sample are not to be generalized. The interest rates, processing fee, eligibility conditions and other terms & conditions relating to home loans by select HFIs elicited that are on the particular date and they depend to the changes accordingly.

2.9. CHAPTER SCHEME

The study is presented in Seven Chapters

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