CHAPTER – I

INTRODUCES THE THEME OF THE RESEARCH PROJECT AND PRESENTS THE RESEARCH APPROACH
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1.1 AN INTRODUCTION TO THE HOME LOANS

Fantasying of owing a home shows a person’s amount of hard work, compromising with lavishness and in particular collecting funds steadily to pay for his fantasy.

Everybody wants to own a home. Person gets shelter in the home to take rest and feel comfortable. Many commercial banks and financial institutions give loan for home to the people who want to own a home. To attract consumers, banks provide home loans at cheaper rate. Currently banks offer cheapest loan for homes, as a gesture of customer friendly attitude.

Banks were directed by the Reserve Bank of India for encouraging the home loans financing, in view of acute shortage of housing in the country, keeping in mind the current socio-economic role of commercial banks.

As soon as the RBI reduced the bank rate, the market rates of home-loans dropped instantly by 50 basis points. First players in banking sector to announce a 20-years period housing loan were the Union Bank of India and HDFC Bank. Undoubtedly it will certainly boost people's end cost over a
longer duration and to plan their house now; thereby easing fulfillment of a long ago dream of a person to buy a house

For proper maintenance/renovation of home, HDFC also offer Home Improvement Loan. Up to 85% of the renovation cost (100% for existing customers) is financed by HDFC for internal and external repairing and damages and also for redecoration of home like coloring/painting, tiling and flooring, electric and plumbing works, waterproofing, grills and aluminum windows, etc.

HDFC currently dropped 50 basis point on home loan rates to all its existing customers who availed home loans on floating rate.

1.2  BENEFITS OF HOME LOANS

Customers who availed home loans are benefited in the following ways:-

Appealing Interest Rates:-

For increasing their customers’ base and to help the customers, many attractive rates of interest are offered by the banks to their customer. According to customers’ need and to facilitate home loans are provided on either fixed or floating rates by many banks.
Assistance in Owning a Home:-

Customers, for owning a home, are provided by technical and financial assistance by the banks.

No Need of a Guarantor:-

Some banks have relieved their customer to find a guarantor for availing the home loan. Now-a-days commercial banks have liberalized their laws for the customers to avail home loans. The guarantor is no more required by the banks to get a loan sanctioned.

Door to Step Services:-

For the benefit of the customers and considering the present busy life of the customers, many banks provide doors to step services to the customers from preliminary level till the disbursement of the home loan. For example, Union Bank of India and ICICI Bank provide doors to step services to the customers.

Loan period:-

According to the loan amount and the creditability of customers many banks provide a longer period for repayment of loan amount, i.e. up to 15-20
years as maximum loan tenures, to lessen burden on customers to repay their home loan.

**Free Accidental Death Insurance:**

A number of banks also propose free accidental death insurance to the customers together with the housing loans for their benefit.

Such home loans benefits have become so popular among customers that anyone who could not afford to buy a house can now buy it with a home loan, thus making their dream of owning a home become true.

1.3 **HOME LOANS DISADVANTAGES:**

A few disadvantages of home loans are also highlighted hereunder:

**Interruptions in Processing of Home Loan:**

Several times the process of providing home loans gets delayed, because of interruptions in completion of various formulations. As a result, customers are weakened mentally and financially as well.
**Fluctuating interest rates:-**

Due to one or other reasons, at different intervals, floating rates fluctuate. Such fluctuations lead to increased rate of interest and thereby increase the price of home loans.

**Higher Cost of Processing:-**

A high processing fee is charged by the public sector banks for sanctioning home loans. Serious charges at different levels are levied from the customers to carry out the requirements. Consumers are often deprived of availing home loan benefits, if they are not in a position to pay such charges.

**Obstructions in home loan disbursement:-**

For disbursement of home loan amount, a customer has to face a lot of problems. Home loan disbursement to the customers gets delayed customers, owing to the legal formalities involved, hence causing obstructions in the way of the customers to get a home loan.

These are a few disadvantages or limitations of availing home loans. A few banks charge high installments for repayment of the home loan amount, thereby causing problems to customers. A good and prompt service to the customers can remove these limitations.
1.4 HOME LOANS DISBURSEMENT:

The every bank has its own procedure to disburse the loan amount among customers. After choosing your right home, the next step is disbursement of home loans. The loan amount is disbursed after identifying and selecting the purchased property or home and thereafter submitting the necessary legal documents. In the disbursement of home loans a clear title and full verification to ensure that a person has full rights on his house. The 230A clearance of seller and/or 371 clearances from the appropriate authority of income tax are also needed.

Eligibility criteria:

In India, any individual whether a resident or a non-residence, can call for a home loan, if he intends owning a house. Even, if a person has decided to purchase a home in the coming period, he/she can also apply for a home loan before even finalizing the home. After the utmost amount needed for purchase of the property is decided, the Housing Finance Institutions or Banks will let the customer plan out the budget as to how much he/she is eligible for.

1.4.1 Conditions regarding co-applicants:

All Housing Finance Institutions set down criteria as to who can be the co-applicants. Co-applicants to the loan will be co-owners of the property.
Minors are not permitted to be as either co-owner or as co-applicants by these institutions as per law, as they cannot enter into a legal contract. Even friends or relatives who are not in blood relations are also not permitted to take a property jointly. However, to get a higher loan income of co-applicants can be clubbed together for eligibility. A Table clarifying co-applicant’s acceptability of relationship for income clubbing is given below:

**Clubbing Income of Co-applicants:**- It is as follows:-

Combination Income Clubbing: -

- **Husband-Wife:** - Income of husband-wife can be clubbed.

- **Parent - son:** - It can be clubbed if only son is there but not if any male sibling exists.

- **Brother-Brother:** - If they plan to stay together in the new property and are currently staying together, only then their income-can be clubbed for availing home loans.

- **Brother-Sister:** - No clubbing-is possible.

- **Sister-Sister:** - No clubbing is possible.

- **Parent-Minor- Child:** - No clubbing is possible in this case also.
1.4.2 General Terms and Conditions:

The following terms and conditions are pertinent for availing basic home loan. However, these terms and conditions are likely to change on the basis of the variations of the home loan product. In general home loans, normally the following conditions are applicable:

1) The loan to value ratio (LTV) cannot go in excess of a particular percentage. LTV differs product-wise and from every individual Housing Finance Institutional Bank (HFI/B) to another. For covering cost of property various component of the value of the property are calculated.

2) On different terms and conditions HFI/Bs provide different tenures. Although, the maximum tenure for repayment of home loans is nominally fixed by HFI/Bs.

3) 50 percent of the monthly gross income of the customer is the amount that is normally restricted as installment to be paid by the customer.

4) The current loan, which is limited to 50% of the gross monthly income, is included in the total monthly outflow towards all the availed loans.

5) One’s eligibility for a loan amount is calculated according to the LTV, the HR and the FOIR norms, which is the lowest as per one's eligibility.
6) Most HFIs/Bs consider the profile before they judge the repayment capacity. The judgment is based on age, qualifications, number of dependents, occupation, nature of candidate’s business, employment details, work experience, employer credentials, history of any previous loans repayment that have been availed of and the the last 3-4 years turnover etc., if he/she is self-employed.

7) Before the disbursement of the loan, the customers have to arrange for the personal guarantee from other individuals for the repayment of loans, as some HFIs/Bs insist on such guarantees.

8) The property should be technically clear before the HFIs/Bs disburses the loans amount. Most of institutions and banks have a team of technical experts who, before the disbursement of loan, the site is visited to obtain a technical report. This is also beneficial to the customer as they check for the technical quality and compliance with local laws.

9) Before one avails disbursement of the home loan amount, he/she should be well aware that the property for which he availing loan is legally clear. Before the disbursement of loan amount, Housing-Finance Institutions /Banks (HFIs/Bs) take legal clearance from their own lawyers. This proves to be beneficial to the customers as a legal expert checks his/her documentation to ensure that he/she get a proper title to the property.
10) The disbursement of the loan will be by one single cheque if it is a ready property otherwise it will made as per construction of the property progresses. In case of a part disbursement, the customer is levied a simple interest or PEMI on the disbursement of loan amount.

11) In most cases, the disbursement of the loan amount is made in favour of either the seller or the builder or the development authority or the society, according to the case. Under special circumstances only the disbursement will come in the customer’s favour.

12) The repayment of loan can be made in many methods by the customers. Through deduction in the salary of the customer, standing instructions or Auto debit instructions to bank, post-dated cheques.

13) As the case may be, the customer has to repay the principle amount two ways, i.e. i) on annually reducing basis; or ii) monthly reducing basis.

Above terms and conditions, with respect to the home loans, are generally followed by most of the Housing finance Institutions/Banks. However, a few special Housing Finance Institutions or Banks vary on specific terms and conditions.
1.4.3 Charges applicable to avail home loans:

Discussed below are the special kinds of charges applicable to avail home loans:

a) Processing fees:

First of all is the processing fee. This is a charge that is levied by most HFIs/Bs. It is a percentage of the sanctioned loan amount and is normally paid when the application form is submitted. Instead of a percentage, some HFIs also charge a particular fee according to the loan amount. The fees paid in excess is adjusted at the time of submission of application with the charges, when a lower amount is sanctioned, which one makes to the HFI/B. The processing fee is refunded by most HFIs/Bs, in case of rejection of the loan application.

b) Administrative fees:

Administrative fee is a percentage of the approved loan amount. HFI/B collects this amount for issuing interest certificates, maintaining customer’s records, technical and legal charges, etc throughout loan’s tenure. This charge is paid by the customer on receipt of offer letter from HFI/B. This payment is made before availing the disbursement amount.
c) Rate of interest:-

Rate of interest is applicable throughout the loan amount’s tenure and is charged on the principal monthly reducing manner. Customers are given an option to choose the rate of interest from either a fixed or a variable rate by most HFIs/Bs.

d) Legal Charges:-

Legal charges are levied by some HFIs/Bs mainly Public Sector Banks which they incur on their panel of lawyers on getting the property documents vetted.

e) Technical Charges:-

To meet their cost on visit to the customer’s property for ensuring quality of construction and according to the norms of the respective approval authority, certain Housing Finance Institutions/Banks (HFIs/Bs) levy technical charges.

f) Stamp Duty and Registration Charges:-

The Stamp Duty and Registration Charge are levied on to customer by HFIs, in case of registered mortgage, which varies from state to state depending on the state laws where one buys a property.
g) Charges on Personal Guarantee:-

HFIs demand for personal guarantees from the customers. Charges on stamping of personal guarantee given by the customer are also recovered from the customer.

h) Cheque Bounce Charges:-

HFIs levy a nominal charges on the customer whenever a cheque, through payments is made to HFIs, get dishonored.

i) Delayed payment charges:-

If the customer delays the payment of installments beyond the due date, HFIs/Bs charge for the delayed payment from the customer.

j) Additional charges:-

Most HFI charge a particular percentage on the delayed payment. When a customer fails to clear the dues within a stipulated time frame these charges are levied.
k) Incidental charge:-

When a representative from HFI/B is sent for collection of outstanding dues, incidental charges are payable from the customer which normally charged at an even rate per visit. Most HFIs/Bs levy these charges.

l) Prepayment Charges:-

When a customer makes a part prepayment or a full repayment of the loan, penalty of prepayment charges is charged by HFIs/Bs. This is levied only on round sum payments and not on the EMIs that is paid by the customer. This charge is not levied on the entire outstanding principal, but only on the amount prepaid by one. These charges are gradually being discount. These charges are levied by most Housing Finance Institutions and Banks while granting home loan to the customers. The decision on the repayment capacity shall be talked about as follows.

1.4.4 Judgment of repayment capacity based on income:-

To understand the repayment capacity, first of all a customer’s source of income is considered. At the outset, classification of customers into salaried and self-employed individuals becomes a necessity.
a) Salaried individual’s income is considered as follows:

Gross monthly income as figured on the salary slip

**Minus:** Any non-regular flexible income figured in the salary slip (e.g. overtime, etc.)

**Plus:** 50 per cent of the last six months average flexible income

**Plus:** Average variable payment’s 50 per cent with proof like traveling refund etc.

**Plus:** Any other voucher/cash payments, with proof.

**Plus:** House Rent Allowance if not revealed in the salary slip.

The above income is evaluated by using FOIR and IIR norms for calculating eligibility. For FOIR calculation the payment of all current installment that one has availed, is also considered. The smaller of the two is considered as the maximum capacity of repayment.

b) Self-employed individuals’ are classified Professionals and non-professionals for consideration of their income.
• **Professionals:-** Comprised of lawyers, chartered accountants, doctors, architects, etc. For calculating their eligibility, most HFIs compute their income by using the gross professional receipts and not just net profit only.

• **Non-Professionals:-** For calculating income of non-professionals, the following ways have been adopted by HFIs:-

The profit and loss account exhibiting last 2 years net profits average (Income Tax Returns should have been filed regularly that too by the due date).

**Minus:-** Any abnormal and non-recurring natured income affecting the profits to a large extent, like sale of property, etc..

**Plus: -** Any abnormal and non-recurring natured expenses i.e. maintenance and repairs that were not benefited from and badly affecting the profits.

**Plus:-** 50 per cent of the last two years average depreciation.

Calculation of eligibility is done by calculating the above income using FOIR and IIR norms. For FOIR calculation and eligibility, the payment of all current installment that one has availed, is also considered. The smaller of the two is considered as the maximum capacity of repayment.
1.4.5 Credit documentation:-

Based on one’s employer, qualifications, experience, etc. the documents differ between one and another HFI/B. For a general home loan an exhaustive list of credit documents is needed and the documents that are required are as follows: -

(a) Income Documents:-

Income documents for salaried are appointment letter, salary-slip of the last three months, salary certificate, retainer-ship agreement, in case of consultant employer’s issued Form 16 in name of customer. Income document for self employed are: i) profit and loss account statement of last three years, duly attested by Chartered Accountant; ii) Balance Sheet of last three years, duly attested by Chartered Accountant; and iii) duly certified by the Income Tax authorities, Income Tax Returns with computation chart for the last three years.

b) Proof of employment:-

As a proof of employment the customer needs to provide employer’s issued Identity Card and business card.
(c) **Employer’s Details (In case of private limited company):**

Employers’ profile on their letterhead issued by a competent person containing:

- Name of the promoter/directors
- Promoters/directors background
- Nature of business of the employer
- Annual turnover of the employer
- Last 2-3 years annual reports of the employer
- Number of employees
- Factories / Branches
- Suppliers’ List
- Clients/customers list
(d) **Age Proof (Any one of the following):**

UID Card, Voter's ID card, Passport, PAN card, Employer's ID card, Ration card, Birth certificate and School leaving certificate.

(e) **Residence Proof (Anyone of the following) :**

Passport, UID Card, Voter's Card, Rent agreement (if the customer is staying on rent), Ration card, Bank Pass book, PAN card, Allotment letter from the company (if he/she is residing in company quarters).

(f) **Proof of name change (If applicable) :**

Marriage certificate. A copy of the official gazette reflecting the change of name, copy of a newspaper advertisement showing the change of name,

(g) **Investment Proof (If necessary):**

If required by the HFC, last six months bank statements, last six months bank statement of all salary and operating accounts, current accounts, in case of self-employed, photocopies of other investments.
1.4.6 Legal documentation:-

For mortgaging the property the following legal documents of the property are needed to be surrendered to the HFC. Depending upon the type of financed property, the list of documents varies state-wise. Documents that are required are given below.

a) Offer letter’s acceptance copy, issued by the HFC/B.

b) Property’s Title documents including–

- Duly registered Sale Agreement
- Receipts of own contributions
- Receipt of Registration and Allotment letter
- Property documents representing ownership, if applicable
- Possession letter or lease agreement, in case the property is purchased from a development authority
- Mortgage deed, in case a registered mortgage is opted by the HFC.
c) Developer’s, society or development authority’s No Objection Certificate as applicable.

d) Post dated cheques for the EMIs.

e) Additional security and their documents, in case of security details’ alternator.

f) Personal Guarantees, wherever required.

The aforementioned documents do not cover the entire list they are just to point out. It is notable to mention that the previous chain of agreement is also need to be taken in a resale case,

1.4.7 Benefits of tax to the individuals applying for home loans:-

Tax Benefits to individuals are currently available only for the Home Loans and Home Extension Loans products.

Property Insurance:-

A few HFIs persist on a mortgage redemption life insurance policy. In such case the customer is benefited by an interest rate reduction. Even if HFIs do not persist, to safeguard the asset against any kind of damage or loss, it is better to go in for property insurance. The tenure for the property
insurance can be the choice of the customer. The insurance premium is changed up front. A huge discount is offered by most insurance companies on the rate of premium for larger tenures. Presently, the premium is charged at seventy-seven for every lakh of property for a year. So a customer has to fulfill various conditions to be eligible for availing home loan from a Housing Finance Institution/Bank After fulfilling these conditions, a customer can avail loan at low interest rate i.e. fixed rate floating rate. A decision on a fixed-rate loan or a floating-rate loan is a function of two factors where a customer has to decide where to go i.e. One’s awareness of where interest rates in the economy are heading towards and his capacity to bear the change in interest rate. One can take advantage of floating-rate loan as when there is fall in interest rates but can loose if interest rate again and again. However this decision is based on the perception of the consumer.

1.5 INDIA REPORT ON FINANCIAL PERFORMANCE OF INDIAN BANKS IN HOUSING LOAN:

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 though do not take credit as it is reflecting in the figures below:-
1.5.1 Indian home loans Industry:-

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.
1.5.2 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.

1.6 SLOWDOWN IMPACT OF MARKET ON HOME LOAN IN INDIA:-

The United States was under threat of recession. This is clear why the Indian markets slowed down taking an indication from the possibility of recession threat in the US and economic slowdown globally. U.S slowdown has affected almost all sectors not only in US but to all over the world. Indian economy has also been affected by this slowdown because India is a growing country and almost in all sectors various multinational companies have major contribution. So the role of this slowdown is a major issue to be discussed while talking about Home Loan Market in India.

It appeared that banks like UTI Bank, SBI, HDFC, ICICI and IDBI are now making a premeditated endeavor to control their positions in the market of home loans. Situation is such that if a customer who just advanced a private sector bank for about Rs.10 lakh home loan for a 15-years tenure period was shocked to found that he was disbursed to be just Rs 5 lakh. On records, most bankers point out a little decline in home loan disbursement due to the recent increase in the rate of interest, but in their portfolio they aren’t accepting it.
A private sector banker, however, said “The slowdown in the home loan market for select players like ICICI Bank was evident from January. ICICI Bank's average home loan disbursement in a month is around Rs 2,500 crore in a month, which has come down to almost Rs 2,000 crore in March.” Officials of ICICI Bank denied any slowness in their home loan collection. They said they on loan disbursement they had been impacted due to recent reduction in interest rates. In absolute terms, however, it is still low. The deposit growth is around 17% for the sector whilst the credit is growing at almost 28%, even after this slowdown, forcing banks to be cautious. A floating rate of 8 to 8.25 per cent is charged by HFIIs on home loans beyond Rs.20 lakh. Initial estimates by bankers suggested that there will a 25-50 basis points (0.25% to 0.5%) increase in rate for home loans and other segments. In the first year, there will be lesser increase in rates of interest although there is a 60 basis points growth in the provisioning requirement, depending upon capital ability of the banks as the increase in provisioning and risk weightage would affect the return on equity for banks. Fragile banks and banks with a variety of home loans may hike interest rates first as they are more likely to be affected.

Home loan growth of disbursals was at 20 per cent in 2009-10 according to a study by the credit rating agency CRISIL, a Standard & Poor’s company. This rate is lower than the 30 per cent annual increase seen in the past three years, but in absolute terms represents a substantial expansion. The slower growth reflects the impact of rising property prices and interest.
1.7 INTEREST ON HOME LOANS AND MARKET TRENDS IN THE YEAR 2010:-

On announcement of RBI’s sharp cuts in cash reserve ratio (CRR) and the repo rate, interest rate on home loans started become soft from the beginning of the year, particularly on account of new home loans. Since October last year, RBI started slicing the rates of key policy, taking into consideration the deteriorating liquidity circumstances of banks. In the last six months, the Central Bank reduced its key policy interest rates (repo and reverse repo) and reserve ratio (CRR) four times. With the cut in the repo rate funds to commercials were available at a lower cost. On the other hand, the cut in the CRR meant banks do not to maintain more funds with the RBI, and therefore, they will be able to offer more money. As per analysts, within next few months, there will be more cuts in the borrowing rates as the interest rates still have not reached the lowest.

While the expectation of a cut in the interest rate is over and done, the question arises, will it be able to achieve the same levels of 7-8 percent that were there in the past contributing to a sudden growth in the property? In proportion to global trends, as consensus is already building up, in a couple of years we will be heading towards a regime of lower interest rate. As far as domestic economy is concerned, within the last few weeks, there is already a reduction of 1-2 percent on the rate of interest by the banks, triggering for lower rates of interest on the deposit front. Now, cheaper funds will be available with the banks, with regard to the reduction in the deposit rate for
long term deposits (i.e. on 3-5 years) to single digit, cheaper funds will be available with the banks. Since there is a swift drop in inflation, a reduced rate regime can be continued.

Many banks are also offering schemes for home loan at 8% on fixed rate, going after the footsteps of State Bank of India (SBI’s). After three weeks, Indian Banks’ Association (IBA) would review borrowers’ response towards the SBI scheme and if a good response is found, other banks will also follow the same.

Last week, an offer of a flat 8% home loan scheme was announced by SBI to all borrowers. The Chairman of one of the major banks (not to be named) said SBI is having a huge current and savings account (CASA) deposit ratio and, therefore, it can offer home loan at cheaper rate. CASA deposit ratio being the cheapest source of funds for any bank can bring down the average cost of funds. Therefore, the bank can offer cheaper credits while maintaining their net interest margin (NIM).

SBI fixed its new home loan rates at 8% for one year recently. Following SBI, state-owned banks also slashed their home loans rates.
1.8 FINANCIAL YEAR 2011

Banks bettered their FY10 performance in FY11, on the growth of the RBI’s 20% estimate for credit. During the year 2010-11, non-food bank credit also grew to 20.6% compared to 16.8% per cent during the year 2009-10. Industry credit growth remained soaring in the first half of FY11, due to service sector’s increased demand. As compared to 4.1% in the past, personal loans also raised significantly to 17% during 2010-11. Except for credit card receivables, high growth was shown by almost all the components.

In the beginning of 2011, the growth slowed down on account of RBI’s aggressive interest rate policy. The key policy rates of central bank hiked eleven times since March 2010, in order to curtail persistent inflation, which was higher than comfort levels. The present repo rate stands at 8%, with the reverse repo rate at 7%.

Growth on the deposits however, remained at around 17% YoY, relatively on lower side. Liquidity, however, remained firm throughout the year, but towards the end of the year, witnessed some improvement.
Vehicle loans and home loans increased by 24% YoY, and 15% respectively, in the retail sector. Due to reluctance of banks towards unsecured credits, personal loans witnessed a much smaller growth of 17% YoY. Outstanding of credit card also dropped by 10% YoY.

However, as a percentage of GDP in FY11, banks had higher levels of credit, deposits and money supply as compared to FY 10. There was an improved development in the financial sector.
In FY11, a good progress was observed by most private sector banks. As there was increase in pricing power, net interest margins of Indian banks also expanded. In view of overall buoyancy and increase in credit demand during the year, assets and franchises grew significantly.