State of the Low-Income Housing Market
Encouraging Progress & Opportunity to Realize Dreams of Millions

By Aditya Agarwal, Vikram Jain and Ashish Karamchandani

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About Monitor Deloitte

Monitor Deloitte is one of the global brand of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee which renders management consulting services, advising corporations, Governments and international development agencies worldwide. In 2005, we founded Monitor Inclusive Markets (MIM) in India to "use market-based solutions to create social change". The aim was to create and promote profitable businesses that also create social impact. We did a one year long in-depth field based study of over 300 “market-based solutions” across a diverse range of sectors to identify high potential business models and understand why most such solutions do not scale. This is the first fact based research in this space and the results are available in our book "Emerging Markets, Emerging Models".

Our Housing Work

One such high potential opportunity identified was housing for low-income customers. We identified a target segment of households who now earn INR 10,000 - 25,000 per month and rent rooms in slums and low income neighborhoods. These people – 15 million households – live in poorly constructed, small, cramped houses, with deplorable sanitary conditions and lack access to basic neighborhood amenities. They aspire to live in, and can afford to buy, houses between 250-400 square feet in the suburbs at market prices. These houses, while commercially feasible - an estimated market size of INR 9 lakh crore - were not being built, and these customers were also unable to access mortgages. We used our understanding of the market and the customers’ needs to develop a set of innovative business models that are commercially attractive. We have been able to get developers like Foliage and Mahindra and new players like Jerry Rao (of VBHC) to start organizations to create low income housing. We have helped entrepreneurs like Rajnish Dhall and established players like Muthoot Pappachan Group to start housing finance companies focusing on serving informal sector customers (customers without income proof and earning less than INR 25,000 per month). We estimate that over a hundred and fifty developers have put over 80,000 apartments in the INR 3-10 lakh range on the market in the last 5 years. At the request of Secretary, MoHUPA, we have also provided inputs on recommendations of ‘Affordable Housing Task Force’. We are currently supporting the department of Housing and Urban Development, Govt. of Odisha to create a conducive affordable housing policy for the state. Our housing work has been supported by NHB, World Bank, Michael & Susan Dell Foundation, DFID, IFC, The Rockefeller Foundation and FEM.

About the Authors

Aditya Agarwal has been leading the ‘State of the Market’ study. He has also been actively involved in broad sector work of MIM across customer education, financial inclusion and other market-based solutions.

Vikram Jain heads the Low-Income Housing Practice at MIM. He has led numerous engagements providing inputs to the Government on conducive policy to catalyse the low-income housing sector. He has led projects to understand customers’ home buying experiences, preferences and trade-offs, including evaluating organisations to address some of their challenges.

Ashish Karamchandani is the founder of MIM, and has led the group’s focus on catalysing market-based approaches to improve the lives and livelihoods of the global poor – working both at a broad sector level (developing a more rigorous underpinning of the opportunity, its drivers and barriers and how to address the barriers), and at the level of specific initiatives. One of the specific initiatives Ashish is extensively involved in is low income housing, an area in which MIM has been working to 'make the market' at an ecosystem level for the past six years.

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Executive Summary

Housing for the urban poor in India has failed to keep up with the rapid urbanisation. This has led to low-income families living in cramped, sub-standard and often rented accommodations with limited access to civic amenities. The Government estimates a shortage of more than 18 million homes, of which 95% are in the EWS and LIG segment, an income class with families earning up to INR 16,000 per month. Many of the EWS and LIG families cannot afford privately built housing unless the Government provides some subsidy. There is also a large proportion of urban low-income families, with a monthly household income of INR 10,000 – 25,000, who can afford privately built formal housing costing INR 4 – 10 lakh without any aid from the Government. There is an estimated need of 15 million homes for these low-income customers, which translates into an opportunity of INR ~9 lakh crore for developers and INR ~7 lakh crore for housing finance companies.

There is an increased interest in supplying housing and housing finance to low-income customers but the gap between supply and need is huge. Increased efforts are needed from practitioners (e.g. developers, housing finance companies) and facilitators (e.g. Government, international development agencies, foundations) to bridge this gap. Providing information about the opportunity, current status and best practices would assist new practitioners enter this market and help existing practitioners expand, geographically and numerically, to serve this market better. Providing on-the-ground data to facilitators would help them in their decision making process to catalyse the market. This report was conceived with the above two objectives. The report focuses only on market based, i.e. privately-built and privately-financed, solutions for low-income housing in India.

The core findings of this report are based on an extensive (1,000 man days over six months) study of the current Low-Income Housing (LIH) market. The effort spanned research in 22 cities, interviews of 27 active developers and 9 HFCs serving the low-income customer. These findings were supplemented with insights from two historical market studies and numerous customer research projects. A number of organizations and individuals associated with this sector have also contributed to this effort.

The key finding is that the market is beginning to serve the low-income customer. At least 30,500 units below INR 10 lakh have been launched in 132 projects across 22 cities in the period Jun '11 to Jan '13. Three cities, Ahmedabad, Mumbai and Indore, have developed well with over 20 projects in each city providing housing below INR 10 lakh, thereby offering choice of locations and developers to customers. Around 30% of the supply is priced below INR 6 lakh. Developers are constructing smaller formats (e.g. 1 Room Kitchen) in these cities which are more affordable and it is encouraging to see that they sell ~25% quicker compared to larger formats (e.g. 1 or 2 Bedroom Hall Kitchen). Access to housing finance for formal and informal (no proof of income) low-income customers has also improved. A number of new players have entered this market and today over 10 companies are serving the low-income customer. These new HFCs have a combined loan portfolio of INR ~1,000 crore, are growing at 100-300% per annum and have near zero NPAs. The supply of housing is low compared to the need, but housing finance, which was almost non-existent for informal low-income customers five years ago, is growing well.

For the market to scale and realize the dreams of millions, a deeper understanding of the aspirations, opportunities and challenges of the key market participants is essential.

- LIH Developers are convinced of the opportunity but are operating in a difficult environment. Majority of the 27 surveyed LIH developers expressed satisfaction on the viability of their business and 90% intend to continue to build LIH. Typically these developers were purchasing land at INR 200 – 300 per square foot (on FSI basis), constructing at INR 850 – 1000 per square foot and selling at INR 1400 – 1700 per square foot. Most projects would sell 80% of their units within 12 months. Seventy-eight percent of the developers were doing the construction themselves to control cost and time overruns. Top three challenges cited were increasing land prices, increasing construction costs and long approval timelines. Some developers were refining their products (e.g. smaller projects) to avoid certain approvals and most expressed interest to try new technologies to save costs.
- Housing finance companies are growing rapidly despite high cost of debt. HFCs have started targeting different segments (e.g. developer built housing, incremental housing, new projects, resale properties) within the low-income customer group. The number of players and geographic coverage of each player is growing. In the absence of formal documentation, HFCs typically use a field-based credit assessment process, leading to higher operating costs. HFCs have access to debt at 10-14% and therefore lend to customers at 13-17%. Limited access to debt and high cost of debt are the two key challenges cited by HFCs. Despite these challenges, most HFCs expect a continued healthy growth.
- The Government is becoming increasingly cognizant of the role private sector can play in addressing the housing needs of low-income customers. A number of Government entities at the Central, State and Urban Local Body level have taken steps to incentivize private sector to build housing for the urban poor. They haved used various supply-side interventions, including mandating reservations, providing subsidies (e.g. extra FSI, reduced taxes), providing fast approvals and earmarking land for EWS / LIG housing. The Government has introduced demand-side interventions for beneficiaries, including interest rate subsidy and reduced taxes (e.g. stamp duty, registration). Greater the number of beneficiaries served by the private sector, lower is the burden on the Government, lower is the incidence of new slums and sooner cities become "slum-free".
- Low-income customers are happy with their new homes. Improved living conditions, secure neighbourhoods, larger homes and improved utilities are some of the functional benefits cited by customers. The new housing has also had a positive psychological impact on customers. They felt a sense of upgradation, a feeling of belonging, pride of ownership and a surge in aspirations. Lack of clarity on maintenance responsibilities, longer commutes to workplaces and higher cost of living were some of the challenges cited by customers, but for most of them it was a dream-come-true.

The opportunity to realize the dreams of millions can only be delivered with both the Government and the private sector playing their part. Government could create a conducive environment for low-income developers (not necessarily subsidies), provide targeted subsidies to low-income customers and provide low-cost credit to HFCs and developers serving low-income customers. Developers could build smaller formats and smaller units as they are more affordable, provide 100% loan papers to improve customer affordability and provide transparency on maintenance costs and responsibilities. Housing finance companies could expand to new geographies improving developer perception of real demand and educate customers on the home buying process through standard pamphlets. Other stakeholders could spread the word about the potential opportunity in low-income housing to attract developers in new geographies, support Government initiatives in creating conducive policies and periodically publish market data to support decision making.

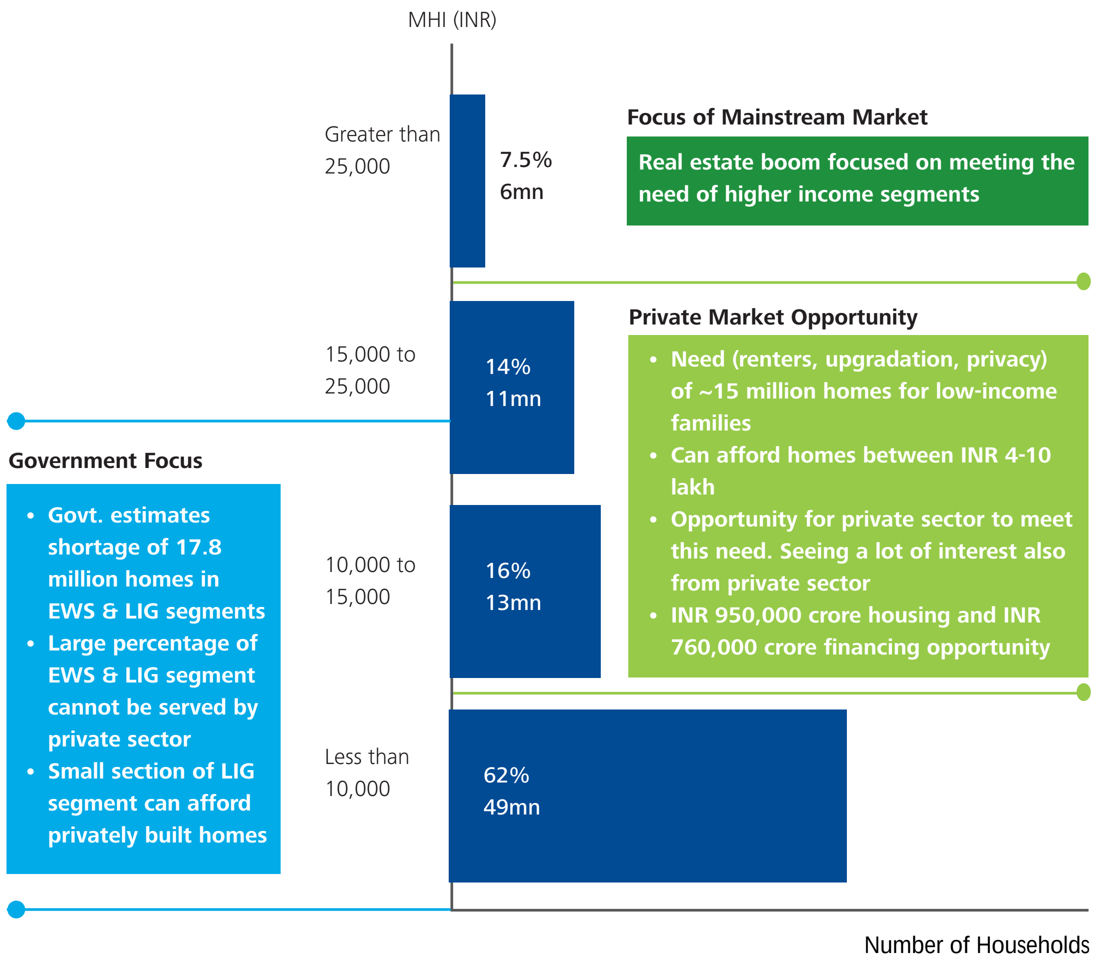
Context

Housing for Urban Poor – A Huge Need and an Untapped Opportunity

Traditionally, the private sector real estate market has focused on serving the needs of higher income segments of urban India. Housing finance has also been primarily geared towards higher income segments, and that too the formal sector. Consequently, participation as home owners in real estate has been primarily of the the population with a monthly household income of at least INR 25,000. However, a majority of the urban population, 92% or 73 million households (see figure 1), earns less than INR 25,000 per month and most of the new housing being constructed has so far been unaffordable for them.

There is a huge need for housing in the lower-income population. As per the Government of India, there is a shortage of 18.78 million homes in urban India, 95% of which is accounted for by the EWS[4] (households with annual income of less than INR 1 lakh) and LIG segments (households with annual income of INR 1-2 lakh). The Government recognizes that much of this population cannot afford private sector led housing and hence is trying different approaches to meet their needs – upgrading slums, rehabilitating slums, mandating private sector projects to have reservations for EWS/LIG housing, providing interest rate subsidies and waiving stamp duties.

Figure 1 Urban Income Pyramid[1] and the Low-Income[2] Housing Opportunity[3]



1 Income-classification as of July '12 adjusted over 2004-05 data using WPI index
Source: Census 2011; India Human Development Survey, 2004-05; Website of Office of the Economic Advisor, Ministry of Commerce and Industry, Government of India

2 Low-income customer defined as households earning INR 10,000 to INR 25,000 per month

3 Percentage of renters by income segment as per Monthly Per Capita Expenditure (MPCE) based data. Other need factors – congestion factor (lack of private space) of 18-19% in urban India, 15% of low-income customers live in joint families
Source: NSS 65th round, Housing Condition and Amenities in India, 2008-09; Technical Group on Urban Housing Shortage (2012-17) by MoHUPA; 'Unintended Consequences' study of Monitor Inclusive Markets

4 Revised income criteria for EWS & LIG segments as per MoHUPA's revision of definitions in November 2012; Source: Website of Press Information Bureau, Government of India

Nearly 11 million households earn between INR 15,000-25,000 per month and another 13 million earn between INR 10,000-15,000 per month (see figure 1). Almost 40-45% of this population lives in rented accommodation and would like to buy their own house. An additional 15-20% of non-renting households would also like to buy housing (aspiration to upgrade, need for private space, expansion of family etc.). As per well accepted industry metrics, a typical household can afford a house up to forty times of their monthly income. Using this metric, these segments can afford to buy a house between INR 6-10 lakh (USD 11,000-18,000[5]) and INR 4-6 lakh (USD 7,300-11,000) respectively. Given current land and construction costs, it is possible for private players to build houses at these price-points and cater to a housing market of 13-15 million units which is potentially worth INR 8.5 – 9.5 lakh crore (USD 155-170 Bn).

Historically, access to housing finance has also been difficult for low-income customers. A majority of this segment works in the informal sector making it even more difficult for these customers to avail housing finance from traditional financial institutions. At about 80% LTV (Loan To Value ratio), this is an INR 700,000-760,000 crore (USD 125-140 Bn) opportunity for housing finance companies. In addition, with the increased interest rate subsidy provided by the Central Government through Rajiv Rin Yojana (RRY), an EWS family with monthly household income (MHI) of INR 8,500 could afford a home for INR 4 lakh thereby increasing the demand for privately built low-income homes by an additional 2 million units and INR 85,000-95,000 crore[6] (USD 15-17 Bn).

The focus of this report is on private sector efforts to provide housing for the low-income households that are earning between INR 10,000-25,000 per month and can afford privately built housing between INR 4 – 10 lakh.

Need for 'State of the Market' Report

Since 2006, Monitor Inclusive Markets (MIM) has been working at multiple levels to create a low income housing industry in India (see figure 2). The MIM team has helped establish the business potential and viability of the opportunity for private developers and housing finance companies. The team has also assisted the entry of several developers (e.g. Santosh Associates, Foliage, Value Budget Housing Corporation, Mahindra Lifespaces) and housing finance companies (e.g. MHFC, Muthoot) in the low-income housing sector. Multiple studies on understanding customer needs, addressing stakeholder challenges and supporting conducive policy have addressed other needs of the LIH market.

Looking back over the past seven years, the progress of the LIH market has been encouraging and the stories we hear from low-income customers about their new houses (and the impact on their lives) are heart-warming. The business model continues to be viable for both developers and housing finance companies. Supply of housing finance has steadily increased and there are now a number of housing finance companies who are actively lending to formal and informal low-income customers.

5 1 USD = 55 INR

6 6.26 million households in the income segment of INR 8,500-10,000. Percentage of renters at 28%, additional need of 15-20% Source: Census 2011; India Human Development Survey, 2004-05; NSS 65th Round, Housing Condition and Amenities in India, 2008-09

In our role as a market facilitator, we conduct regular scans of the market to track progress and are also in continuous dialogue with different stakeholders – practitioners, Government, funders and other institutions – to keep track of the market pulse. One such dipstick market scan in June 2012, informed us that while supply was growing, the numbers were not enough compared to the demand. We also sensed an increasing interest from Government and other stakeholders (NHB, WB, DFID, KFW, etc.) to know more about the progress of the sector and the role that the private sector could play in meeting this huge need of housing for the urban poor. This led us to write a 'State of the Market' report with the objective to

- Attract new developers to the low-income housing space and get existing developers to build more units by providing them with information on customer insights, market trends, current housing and financing activity and characteristics of supply
- Support Governments, international development agencies and foundations in their decision making process by providing them with a fact base of "on the ground" data

Figure 2 Overview of Monitor Inclusive Markets' Sustained Engagement with the Low Income Housing Market

2006 2007 2008 2009 2010 2011 2012

Housing Supply

Opportunity Blueprint

- Identified LIH as an attractive area
  - USD 245 Bn market serving ~ 21 Million Households
- Conducted research across the value chain to understand needs, constraints and opportunities
- Identified "supply" as the "cut-in" and developed new business model around 'leveraging aggregated formal sector demand"

Model Validation

- "Pounded the pavement": Promoted the model with developers to get pilots going
- Supported implementation: Mortgages, land selection, architectural designs, construction technologies, etc.
- Marketed directly to customers: Aggregated customers for pilot projects from local factories
  - First pilots sold out in record time
- Feedback from pilots and interactions with over 3,000 customers led to refining the business model and other elements of LIH business

Accelerated & Robust Supply

- Raised awareness with over 600 developers, plus investors, planners, etc.
- Worked with corporates like TVS and Mahindra to drive greater and faster scale in supply of LIH units
- Analyzed Unintended Consequences of housing on low-income customers
- Evaluated Demand Aggregator: a new business model
- Studied Micromortgages: Need Based Approach Towards Financial Inclusion

Housing Finance

- Tailored model for informal LI customers through field-based verification
- Incubated first housing finance company (HFC) dedicated to serving informal low income customers
- Built strategy and sourced CEO for new HFC of a corporate group
- Raised awareness of the opportunity and the model

Government

- Worked in association and with support of NHB and World Bank to identify LIH as an attractive market-based opportunity
- Engaged with local, state and central Governments to attract more developers
- Supporting central and state Governments in creating conducive policy

About the Report

Focus of the report has been to present evidence of market-based efforts in the LIH sector

The 'State of the Market' report includes:

- Analysis on new LIH supply in the below INR 10 lakh price range between Jun '11 – Jan '13
- Insights on the low-income housing developers building this supply
- Insights on housing finance companies that are financing these homes
- Feedback of low-income customers buying these homes
- Observations on Government initiatives to promote private sector activities
- Suggestions for different stakeholders to move the space forward

The report draws on evidence from three different sets of studies on LIH market conducted by Monitor Deloitte over the last few years:

- Prior market studies which covered the periods of Dec '07 – May '10 (Study 1) and Jun '10 – May '11 (Study 2) respectively
- Recent market study which covered the time period of Jun '11 – Jan '13 (Study 3)
- Multiple customer insight studies over different time periods

Majority of the evidence in this report is based on key findings from extensive research conducted in the recent study

This study covered data on the LIH market corresponding to a 19 month period from Jun '11 to Jan '13. A substantial effort – over 300 man days of effort by Monitor Deloitte consultants supported by more than 700 man days of effort by an on-ground market research team over a period of six months – has been made on gathering and verifying the data in the study. The information provided here has been synthesized from our research conducted in 22 cities and conversations with 27 LIH developers, 9 HFCs and over 700 customers.

An in-depth survey was executed in eight cities[7] by a market research agency under the direct supervision and active participation of Monitor Deloitte consultants. In each of these eight cities, the research team identified potential areas of LIH activity by leveraging the HFC network, conducting in-depth desk research and using their in-house knowledge. The research team then walked the streets in these areas to collect relevant data through a structured questionnaire. The team contacted over 2,300 potential LIH projects in these eight cities but only 96 projects qualified (see Box 1 for qualification criteria) for inclusion in the study. The information collected from these 96 projects (size, phase information, price appreciation, product sizes, availability of units, additional charges, structural configuration, social infrastructure and investor presence) went through a detailed quality check process at the field level with the information being verified by either in-person visits or phone calls by Monitor Deloitte consultants.

For the other 14 cities[8] the data (project size, unit price, unit volume only) was collected through a quick survey primarily by leveraging local HFC networks and conducting desk research. The qualification criteria remained the same as in the eight cities. Data collected from these 14 cities was also verified over the phone by the Monitor Deloitte team. In addition, quick targeted trips were conducted to Hyderabad, Bhubaneswar and Pune.

Box 1: Qualification Criteria of Projects Included in the Study

- **No. of units: total number of units in the project to be greater than 50**
- **Launch date: project/phase launch must be between Jun '11 & Jan '13**
- **Price: affordable for a customer earning INR 25,000/month as of Jan 2012 – i.e. not more than INR 10 lakh (ex-taxes & duties) indexed to Jan 2012**

Overall, across 22 cities, the team identified and analysed data from 132 LIH projects for this report. While the supply number reported in this report is a combination of data from all 132 projects, the detailed analysis of supply in subsequent sections is based on the 96 projects from the 8 cities where an in-depth survey was conducted.

The team also interviewed 27 active developers spread across 11 cities and 9 housing finance companies serving the low-income customer. Multiple face-to-face conversations were conducted by Monitor Deloitte team with these organizations to understand their motivations, key business processes and associated challenges, business viability and future plans. Besides the key findings that have been incorporated in the study, additional information from the survey is available separately with the MIM team.

Historical perspective on the LIH market is provided by two other studies

Prior to the state of the market study, the MIM team has also conducted two different studies in the past to track the progress of LIH sector.

- Study 1: Building Houses Financing Homes – undertaken in 2010, this study was a pan-India scan of the LIH market and tracked progress corresponding to a 30 month period from Dec '07 to May '10.

7 Study was intended to be both broad and exhaustive in its coverage. Hence, fixed a number (eight) which was both manageable to research and broad enough to correctly represent the overall state of the market. Selected Mumbai, Ahmedabad, Indore, Jaipur, Delhi-NCR, Chennai, Nagpur and Kolkata as these were large urban centers spread well across different regions. This set of cities also covered markets with significant LIH activity

8 Cities known to have LIH supply based on information from HFCs, secondary research and past researches

Figure 3 Geographical Coverage of the Research

This was a first of its kind effort to capture the key constituents of the market and was supported by the National Housing Bank, First Initiative and the World Bank
- Study 2: Assessment of Effective Demand and Supply Potential for LIG/EWS Households – undertaken in mid 2011, the study had the dual objective of assessing the effective demand from EWS/LIG segments and the supply in the target price range. The study was conducted for the NHB and the World Bank to identify funding opportunities in the sector for NHB.

Customer and Government perspectives in the report have been formed with information from past projects

For the customer perspective shared in this report, we have used data from our 700 qualitative and quantitative interviews across two different studies:

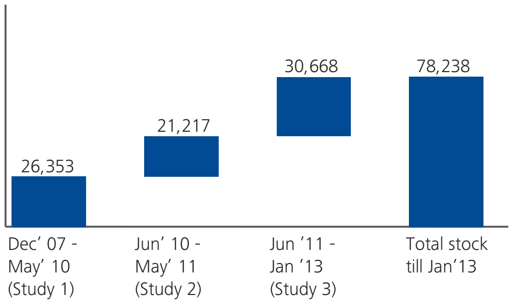
- 'Unintended Consequences of Low-Income Housing' sponsored by The Rockefeller Foundation and Michael & Susan Dell Foundation
- 'Micromortgages: Needs Based Approach Towards Financial Inclusion' sponsored by the Foreign & Commonwealth Office

The Government perspective has been formed from our recent work and interactions with
- Ministry of Housing and Urban Poverty Alleviation, Government of India
- Housing and Urban Development Department, Government of Odisha
- Ghaziabad Development Authority
- International development agencies, including Department for International Development (DFID) and the World Bank

Progress of the Low-income Housing Market

In essence, the LIH industry has made substantial progress within the last few years. The LIH market has gained both depth (more projects in a geography) and breadth (expansion into new geographies) and is being supported well by a thriving set of HFCs. The supply is being absorbed well and a sizeable amount of it is also being purchased by the target customer segment. The Government is becoming increasingly cognizant of the role that private sector can play in meeting the housing need for low-income customers. The following sections examine each of the above facets of progress in more detail.

Figure 4 LIH Units Launched (Dec '07 – Jan '13)



Steady Increase in Supply

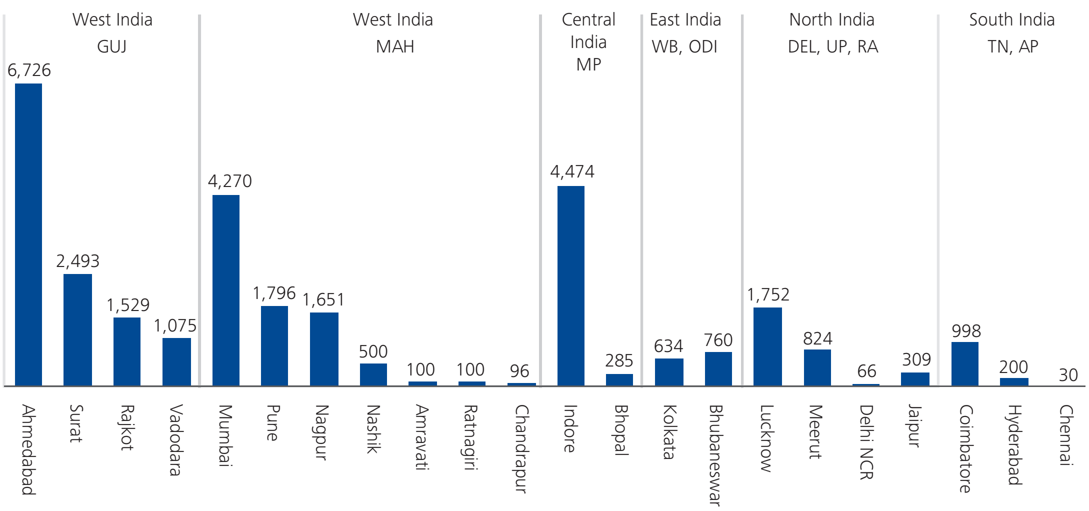
At least 78,000 LIH units between INR 3-10 lakh launched in the last 5 years

Housing supply has steadily increased over the last few years. Since 2007, as per three different studies of MIM, at least 78,000 LIH units (see figure 4[9]) have been launched across India. Almost twice as many units have been launched in the last 30-month period as compared to the previous one.

30,500 LIH units launched in 132 projects in 22 cities between Jun '11 – Jan '13

Amongst the 22 cities (see figure 5), Ahmedabad, Mumbai and Indore are seeing good volumes of supply. The western and central states of Gujarat, Maharashtra and Madhya Pradesh are doing better than the rest of the country. In the northern region, there is limited LIH supply. The industrial belt of Rewari/Dharuhera etc. in the Delhi-NCR region could potentially see some LIH supply emerge in future as a few developers have expressed interest in building below INR 10 lakh housing in these geographies. In the eastern region, some LIH developers have emerged in Kolkata and Bhubaneswar. In Bhubaneswar, there is potential for more supply in future as there has been a concerted effort by the state Government to promote low-income housing. In the southern region, the progress has been least promising – longer approval timelines, cultural resistance to move to multi-storey flat format are some of the reasons cited by developers for not entering this space.

Figure 5 City-wise Breakdown of LIH Supply (June '11 – Jan '13)



9 The studies were intended to be exhaustive for select cities and total supply number for pan-India is likely to be much more; Source: NHB/WB Project on MBS for LIH in India, NHB/WB study on Assessing LIH supply, Eight City LIH Study and State of the Market Study by Monitor Inclusive Markets

Breadth and depth of the LIH market has increased

Comparing the present (Jun '11 – Jan '13) supply and its spread (see figures 6 & 7) with the findings from the 2010 study (Dec. '07 – May '10), there are some interesting observations:

- Wider geographic spread – LIH supply seen in 22 cities which is more than twice the number in 2010. Robust activity in cities like Ahmedabad and Mumbai has resulted in emergence of activity in nearby cities (e.g. Surat, Rajkot, Vadodara, Pune, Nashik) forming clusters of activity
- Fewer large projects – compared to 2010, while the supply has increased from 26,000 to 30,500 units, the project count has gone up almost four-fold from 29 projects in 2010 to 132 in the latest study. The present study showed less of the 3,000 unit (Poddar, Bhivpuri) or 5,000 unit (TMC, Karjat) projects that were a part of the 2010 study. Nearly 60% of supply mapped in this study has come from projects with less than 500 units. Perhaps this shift is an indication of the difficulty in executing large projects. At the same time it suggests that local (nearly 75% of surveyed developers operate in only one city) traditional mid-sized real estate players have entered the LIH space and are now building below INR 10 lakh homes to tap the LIH opportunity
- More choice for customers – in Ahmedabad, Indore and Mumbai more than 20 LIH projects were launched during the 19 month period of this study thereby offering customers greater choice of project locations and developers

The market's robustness is also reflected in the fact that nearly 90% of surveyed developers cited 'sizeable demand' as a motivation for entering the low-income housing market. At the same time, the social impact of quality housing for low-income customers is not lost on a number of developers, and nearly half of them said that they look at their LIH ventures as a good social cause as well.

Figure 6 Spread of LIH Activity As per Study 1

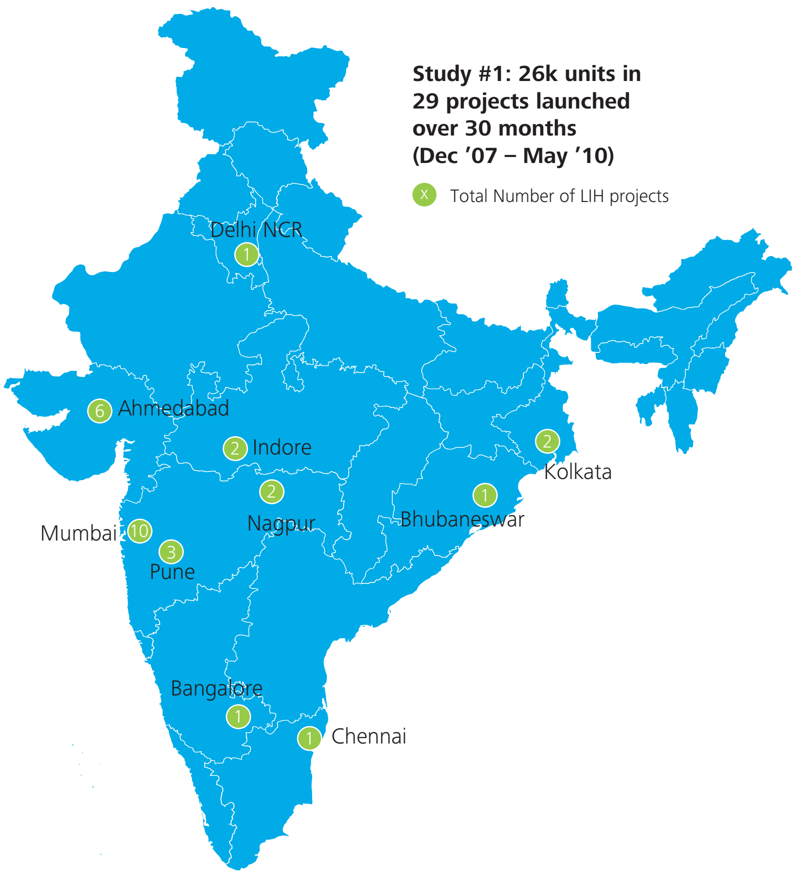
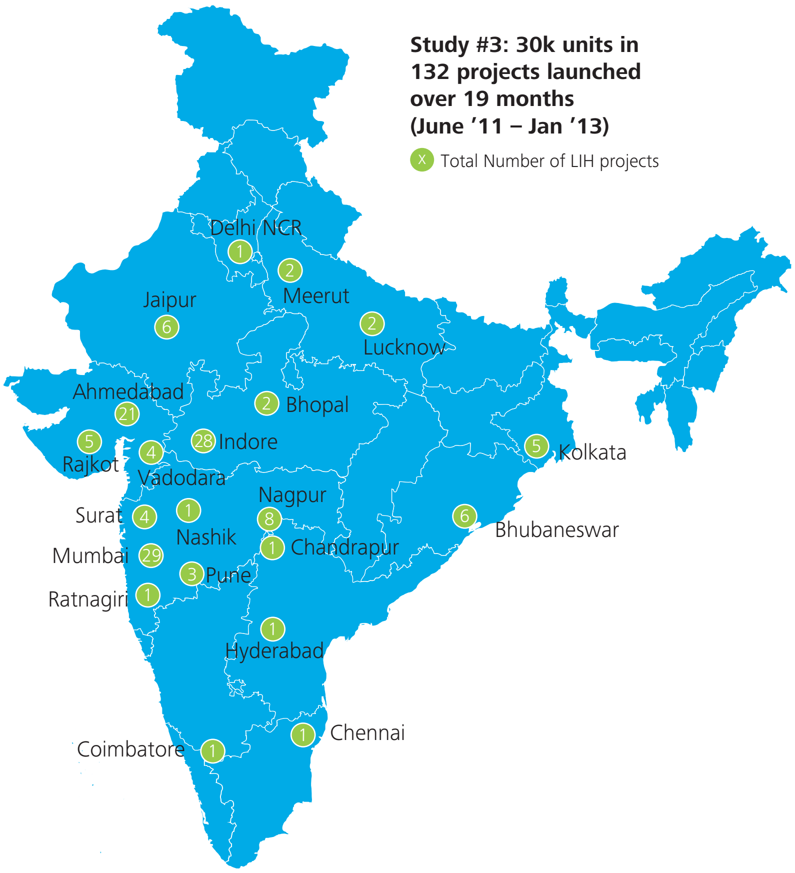


Figure 7 Spread of LIH Activity As per Study 3



Small developers could help faster geographic expansion

Small developers (building 10-50 units) could also play a role in increasing below INR 10 lakh supply. A quick scan, in Indore, revealed almost 30 small developers actively building LIH, supplying around 500 units of below INR 10 lakh housing. These small developers were also building much faster as compared to mid-large developers. However, overall volume by these developers are currently small and activity is not evenly spread across cities. A similar scan, in Ahmedabad, didn't reveal any small developers building units below INR 10 lakh and similarly, in Jaipur, a majority of small developers were building larger formats and their product was not targeted or appropriate for the low-income cutsomer segment. It might be worthwhile to monitor the small developer activity as they could add significant supply to the below INR 10 lakh housing market.

Thriving Housing Finance Industry

New HFCs have built a combined loan book of INR 1,000 crore

A number of housing finance companies are now actively lending in the below INR 10 lakh market. From 1990s to early 2000s only two players were actively lending to low-income or informal[10] segment customers. But over the past few years, a number of new players have entered the market and now more than 10 housing finance companies are actively lending to low-income customers. A number of these HFCs are targeting informal[10] customers who form 70% of the customer base in this segment. While the two established players-DHFL and Gruh have built very large loan books over the years, even new players have built a combined book of close to INR ~1,000 crore (see figure 8) in a short period of time. Last year alone, these new players disbursed close to INR 500 crore (see figure 9).

10 Informal customers are those with no proof of Income

Figure 8 Loan Book Size (INR crore) of Active HFCs[11]

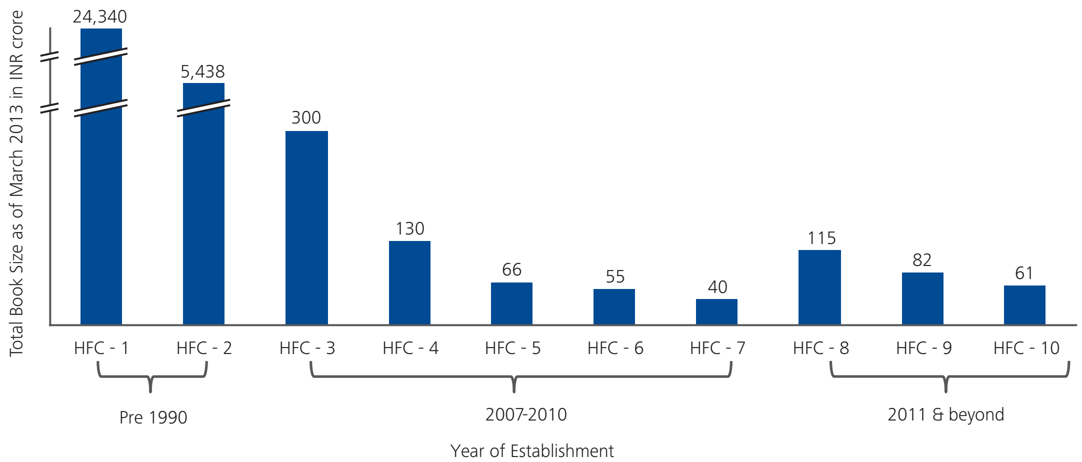
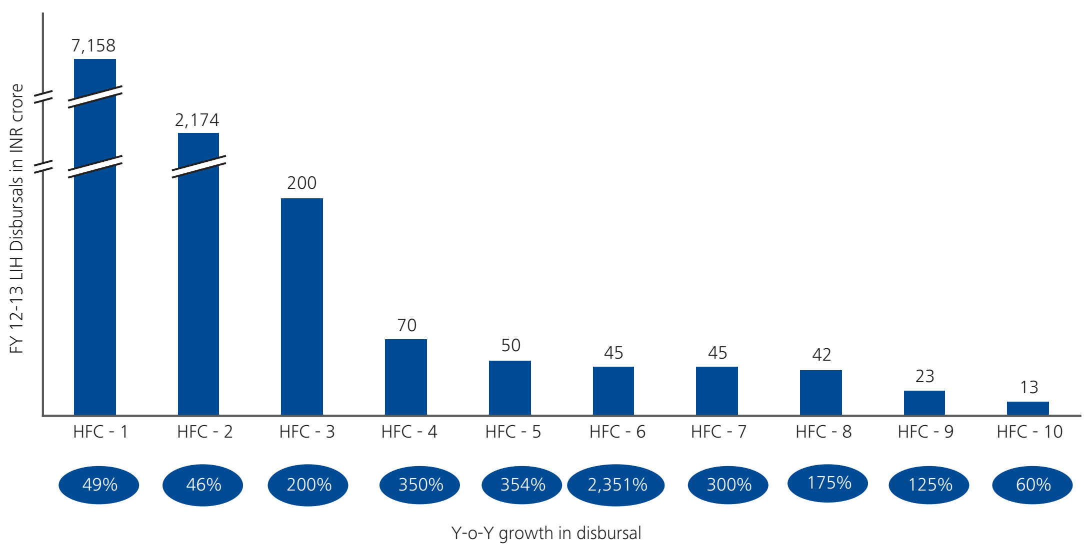


Figure 9 Annual Loan Disbursals (INR crore) of Active HFCs[11]



Disbursals of new HFCs are growing at 100-300% on an annual basis

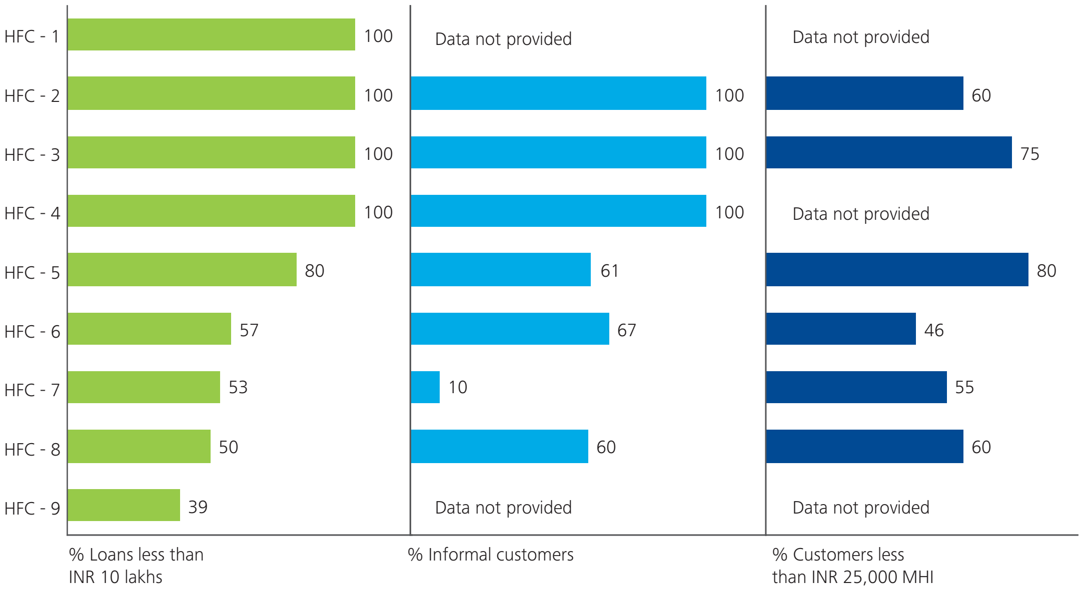
Importantly, all the players are seeing good growth – established players are growing at over 40% year-on-year and new players are doubling or tripling their disbursals every year.

HFCs are serving both formal and informal low-income customers

HFCs are serving a number of formal and informal low-income customers. A majority of these customers take loan for less than INR 10 lakh, work in the informal sector and have a monthly household income of less than INR 25,000 (see figure 10). Thus these HFCs have built a business with the core offering targeting the low-income family, with formal or informal income.

11 This is not an exhaustive representation of active HFCs as some other companies who are also actively lending in this market were not a part of the detailed HFC survey

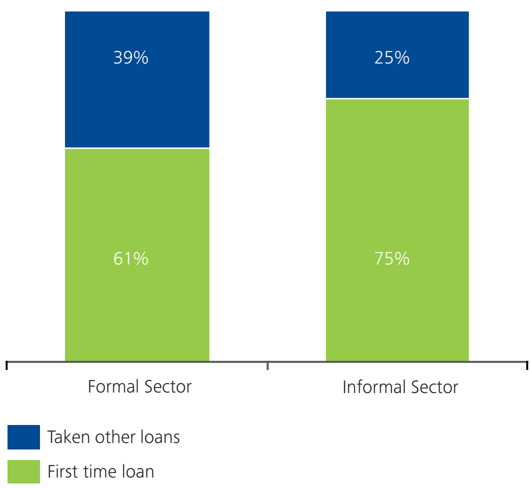
Figure 10 Composition of HFC Loan Portfolio[12]



HFC lending to informal customers has contributed to greater financial inclusion

These HFCs have also helped in financial inclusion (see figure 11[13]), as nearly 60% of formal sector customers and 75% of informal sector customers previously had never taken loan from a formal financial institution. A housing loan for the purchase of their new home was the first exposure to a formal loan product for many customers. Repayment of the loan is also creating a documented repayment track record which helps increase the credit worthiness of these customers.

Figure 11 Prior Experience of Loan[13]



12 For HFCs 5, 6 and 8 these figures correspond to percentage portfolio less than INR 8 lakh

13 Based on conversations with 50 low-income housing finance customers; Source: 'Micromortgages: Needs Based Approach Towards Financial Inclusion' by Monitor Inclusive Markets

Absorption of LIH Supply

LIH projects have sold well across the surveyed cities

Encouragingly, the LIH supply which was launched during the period of this study is being absorbed well across all the cities. Analysing the absorption of LIH supply:

- Nearly 70% of the total supply launched in the two six month periods of June '11 – Nov '11 and Dec '11 – May '12 was reported to be sold. And nearly 45% of the supply launched in the last six months of the study, i.e. post May '12 was reported to be sold
- Across the three large supply centres, the city of Mumbai had absorbed about 77% of total units launched while Ahmedabad and Indore absorbed 53% and 55% of LIH units launched during the period of this study
- It is also important to note that not all projects sell equally well. The study revealed more than one example where the project had been launched for over 15 months but wasn't selling as expected because of either poor location or the developer having a bad reputation

Overall, developers were satisfied with the sales momentum of their LIH projects. Most of the surveyed developers reported that they have been able to sell 80% of their inventory within 12 months of project launch. Over the sales cycle, price escalation of 5-15% is a routine practice and most developers seemed satisfied with the current sales cycle of their LIH projects.

Most of the potential customers were eager to move into a new house

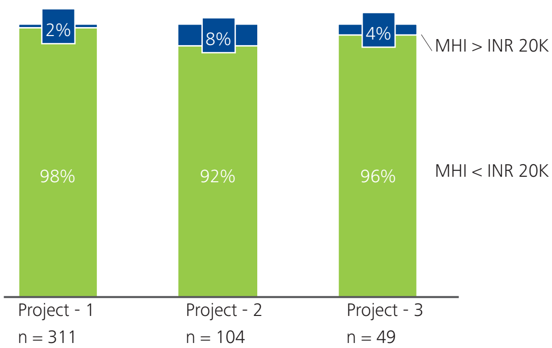
A detailed customer research exercise to understand pre-purchase (booking) behaviour of LIH customers was conducted, where a broad range of respondents were interviewed to understand their perspectives. Most of the respondents indicated an eagerness to shift to better, self-owned houses. Overall, about 75% of the total customers buying into LIH projects had intentions to move into these homes and a majority of them were also from the target income group (less than INR 25,000 MHI).

Occupants, both owners and tenants, are from the target income segment

As a follow up exercise to understand shifts in customer preferences post moving in, a detailed analysis of the profile of actual occupants was conducted in three different LIH projects in Ahmedabad and Pune. Nearly 40% of the units were occupied and more than 90% of families (see figure 12[14]) living in these projects had a monthly household income of less than INR 20,000.

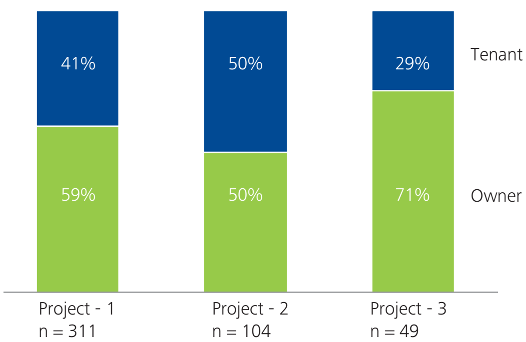
Analysis of occupants also revealed that nearly 30-40% of total occupants (see figure 13) in these projects were tenants. One of the positive outcomes of these projects has been creation of quality rental stock for the low-income customer.

Figure 12 Income-profile of Occupants



n = number of customers interviewed

Figure 13 Owners vs Tenants



n = number of customers interviewed

14 Occupancy was established by knocking on doors and speaking to respondents and/or neighbors to establish residency. The number of customers (n) indicates customers who were interviewed

Government's Cognizance of the Role of Private Sector Supply

Governments at States and ULBs have built and continue to build housing for the urban poor. Numerous Government efforts are underway to make cities "slum-free". But the rapid urbanization has left a huge gap between the need in EWS and LIG segments and supply. Increasingly, Governments are realizing that a) the private sector could play a big role in bridging this gap and b) since there is insufficient supply for the segment of customers just above LIG, the housing produced for EWS and LIG could be captured by this segment.

Governments are leveraging private sector players to bridge the housing gap by:

- Mandating developers to make housing for EWS / LIG. The Central Government in its JNNURM scheme has recommended reservations for EWS / LIG and some State Governments are implementing it
- Providing subsidy and creating an enabling environment so developers produce more housing for LMIG / MIG segment. The Central Government is promoting private sector participation through various schemes (e.g. RAY, AHIP). State Governments have announced policies (e.g. Rajasthan's and Odisha's affordable housing policy) and measures (e.g. zoning in Ahmedabad) to cause developers to build low-income houses
- Improving beneficiary affordability to reduce the burden of buying a home and increase the number of low-income customers that can afford to buy a home. NHB and Central Government have offered lower cost refinancing and ISHUP subsidies to improve affordability of low-income customers, and they are exploring increasing the extent of the ISHUP subsidies. Some state Governments (e.g. Rajasthan) have reduced stamp duty and registration charges for customers to improve their ability to afford a home
- Setting standards to facilitate the market. The Central Government is taking a lead in developing a set of standards – clear definition of beneficiary segments, minimum size of habitable units, criteria for projects to qualify for subsidies, etc. – that can be used by state and local Governments for policy guidelines

Deep Dive into the State of LIH Market

This chapter describes the characteristics of the LIH supply in the market. The business structures, processes, motivations and challenges of both developers and HFCs serving this segment have been described. The Government has a key role to play in moving the space forward and recent Government efforts towards catalysing this market have been examined. Finally, insights from the impact of low-income housing on customers and their interactions in the new environment have been documented.

Characteristics of the LIH Supply

Mixed-income projects contribute most of the supply

60% of the total supply analysed in the survey is being contributed by mixed-income projects (see figure 14). These are projects with units above and below INR 10 lakh, though a majority of them are restricted to an upper range of INR 20 lakh. In these projects, below INR 10 lakh units are primarily the small format houses. Such a high proportion of mixed-income projects, perhaps suggests that developers see a sizable opportunity in the income segment of less than INR 25,000 per month and also the higher income segment which earns up to INR 50,000 per month.

INR 4 lakh is the minimum price-point of a privately built unit

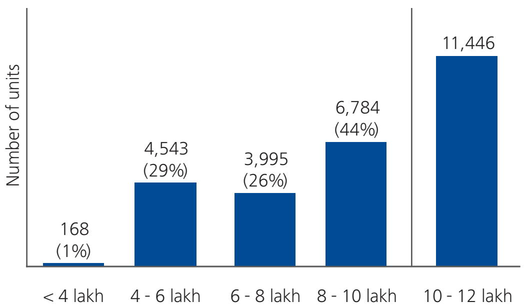
Analysing the launch price of surveyed LIH projects (see figure 15), about 29% of the total supply was launched between the price of INR 4-6 lakh and the balance 71% was launched in the price range of INR 6-10 lakh. Of nearly 90 projects for which in-depth data was available, only 10 projects contributed to supply in the lower price range of INR 4-6 lakh. The study estimates that nearly 40% of the total market potential is between INR 4-6 lakh and considering that only 10% of surveyed projects were offering houses in the INR 4-6 lakh price point there is a need for more projects to sell houses at these prices.

It is also worth noting the supply in the INR 10-12 lakh price range. In 8 cities where the in-depth study was administered, there were almost 11,500 units in this price range, equivalent to about 75% of total units below INR 10 lakh (see figure 15). This survey was designed to be exhaustive only for the below INR 10 lakh supply and the actual number of INR 10-12 lakh units is likely to be much more in these 8 cities. Healthy activity in this price range is a good opportunity for HFCs as they look to scale their operations.

Figure 14 Split of LIH Supply by Project Type[15]

15 Projects where all the units were below INR 10 lakh (when indexed to Jan 2012) are referred to as 'Only LIH' projects

Figure 15 Available Supply by Price Range for Eight Cities[16]



Studying Mumbai as an example, a combination of supply trends suggest that it is becoming increasingly difficult for developers to offer houses at below INR 10 lakh price point in the city. There has been a gradual decline in the new below INR 10 lakh supply in the city. In the eighteen month period of the study, nearly 75% of the total below INR 10 lakh supply in Mumbai was launched in the first six month period.

Increasing prevalence of small formats which sell quicker

Small formats (like 1 RKs) and small homes (compact 1 BHKs/2BHKs) increase the affordability for low-income customers. In the city of Mumbai, because of high real estate prices, the customers have long been used to small formats. But in other cities, developers are nervous about small formats as they are unsure of the demand for such small units. Overall, 1 BHK is the dominant product format but there is increasing interest towards small format 1RKs (see figure 16). In Mumbai, given higher per square foot prices and the price cap of INR 10 lakh, 72% of total supply is comprised of 1RKs. Even in Ahmedabad, where per square foot prices are lower, nearly half of the total supply coming up is small format 1RKs. In Indore too there has been entry of 1RKs and nearly 15% of the total supply is accounted for by this product type.

Even more encouragingly, small formats have sold better than large formats (see figure17). This is good news for developers who are already building small format units and a planning tip for others who have not yet considered small formats for their projects.

Figure 16 Product-mix Across Cities[17]

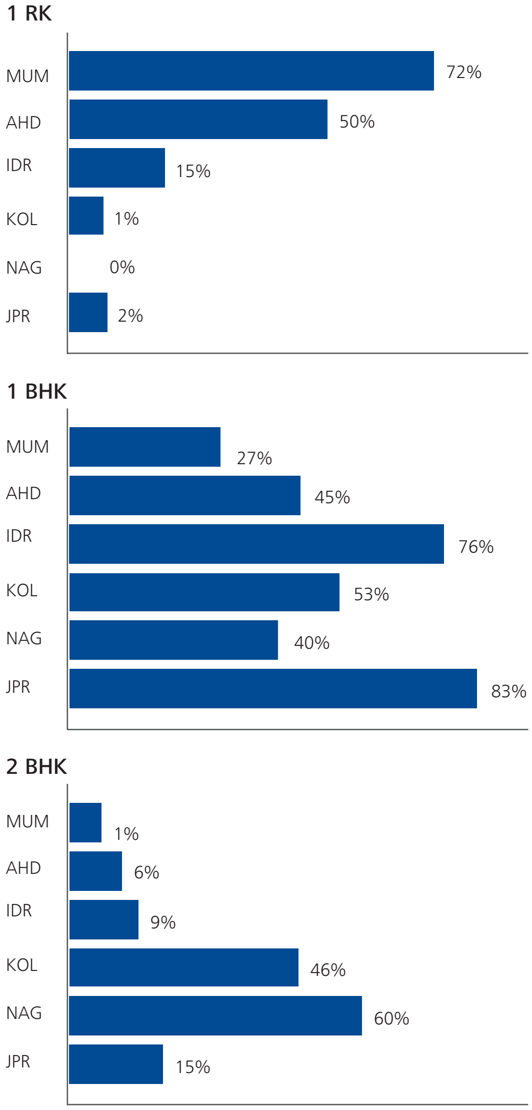
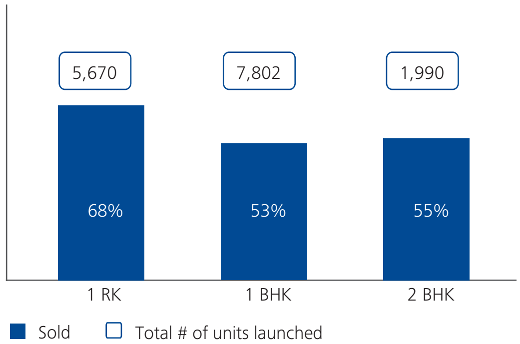


Figure 17 Percentage of Units Sold by Product-type



16 Launch price ex-taxes & duty indexed to January 2012

17 Insufficient number of data points in Delhi and Chennai

Customers prefer more rooms to larger rooms

This study also suggests that customers prefer a smaller house with more rooms than a larger house with fewer rooms. In South India, 90% of customers who were shown both a 1 BHK (409 sq. ft. saleable) and a compact 2 BHK (382 sq. ft. saleable) preferred the latter. This implies that smaller room sizes are acceptable to most low-income customers.

LIH developments in developed markets (Ahmedabad, Indore, Mumbai) are spread across the city

In the surveyed cities, combination of three different factors – land price, connectivity and proximity to industrial activity – determined the development and spread of low-income housing projects. In developed markets – Ahmedabad, Indore and Mumbai – LIH activity was spread across a number of geographical areas (see figure 18). In each of these development pockets, the three factors (or two) have been conducive enough to allow for development of LIH.

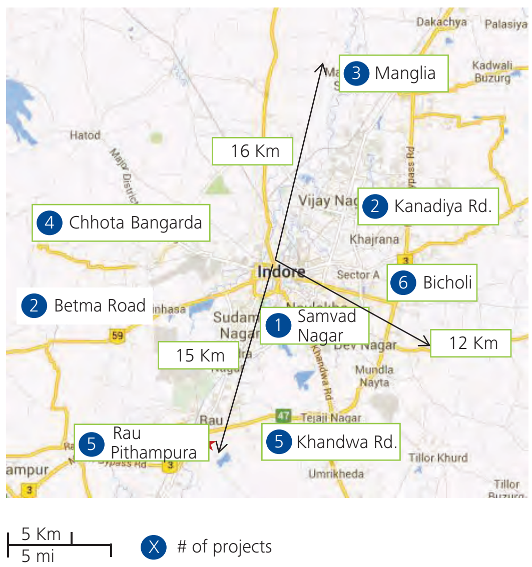
In Ahmedabad, the LIH supply is emerging on new ring roads and main arteries leading to the city center. Towards the south-west, supply is coming up near the industrial areas of Moraiya Gam and Bavla. There is virtually no activity in the northern part of the city as traditionally it has been one of the more expensive areas of the city.

Development in Indore is quite well spread and the LIH projects are coming up all around the periphery on arterial roads leading to the city centre. Proximity to industrial areas is playing an important role in development of Rau-Pithampura and Khandwa Road as LIH hotspots. As expected, the development in Mumbai is taking place along the railway lines – Boisar, Palghar towards north and Panvel, Badlapur, Neral, Asangaon towards east are the areas with good activity. Industrial activity in Boisar and extension of Mumbai suburban railway network has helped make Boisar and surrounding areas a favourable location for LIH development. In Panvel, the projects are coming up in villages like Morbhe and Khopoli of the New Panvel region. Suburbs of Vasind and Shahpur near Asangaon are emerging as LIH centers. Extension of suburban rail links to these suburbs has made these locations conducive for LIH development.

Figure 18 Geographic Spread of LIH Projects

Ahmedabad

Indore



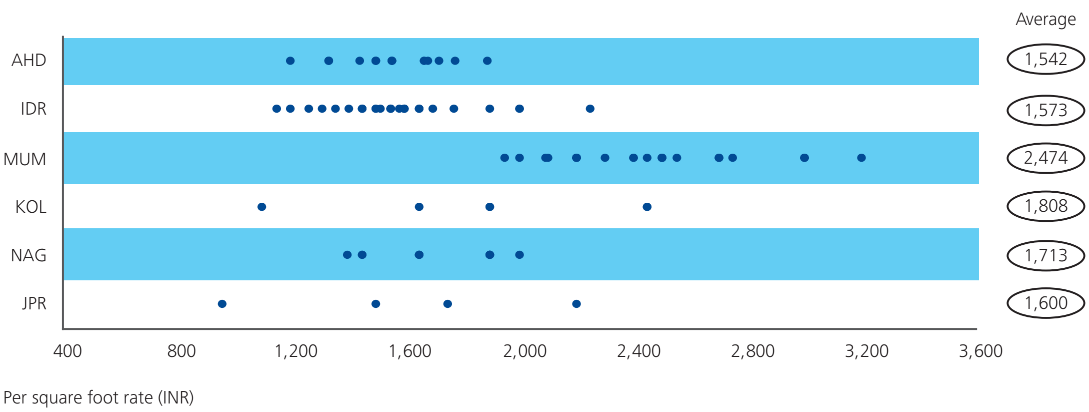
Developed markets show some similarities in pricing spread, product mix and investor presence

While the development pattern (locations, size of projects, etc.) of each city is different and determined by local factors, there are three similarities that were observed in the more developed markets of Ahmedabad, Indore and Mumbai.

- Concentration of product price – more than 70% of the supply in these cities is concentrated within 10-15% of the average per square foot price for the city. On a per square foot basis, Mumbai is the most expensive city of the three with an average current basic of INR 2,474. Ahmedabad and Indore have lower (and similar) average prices of INR 1,542 and INR 1,573 respectively on a per square foot basis (see figure 19)
- Presence of small formats – developers in Mumbai, Ahmedabad and Indore are building 1 RK units which also sell quicker. In Ahmedabad, 60% of 1 RKs were between 400-500 sq. ft. saleable area. The size of these units could be reduced further to make them even more affordable for low-income customers
- Limited investor presence – in both Mumbai and Ahmedabad, more than 75% of projects reported that investors account for less than 25% of their total customer base. Indore reported a slightly higher percentage of investors but the situation in these three cities is completely different from Nagpur where 80% of projects reported that investors account for more than half of their total customers

Mumbai

Figure 19 Variation of Per Square Foot Rates across Cities (current basic at saleable)[18]



18 In the chart, each dot represents a project and its current basic price on saleable area. Important to note that these are current prices and not the price at which the project was launched. Insufficient number of data points in Delhi and Chennai for analysis

Insights on Low Income Housing Developers

Developers prefer outright purchase of land for their LIH projects vs. Joint Ventures (JVs)

Land acquisition is the most important aspect of the business for any real estate developer and it is no different for LIH developers. More than 80% of surveyed LIH developers said that they purchase the land outright for their LIH projects (see figure 20). Many felt that in a JV, land owner's and developer's objectives are not aligned as the land owner would want to charge the maximum (and design specifications accordingly) and sell flats in phases, whereas an LIH developer's intention is to build and sell quickly.

Developers typically look for land which is priced between INR 200–400 per square foot on FSI basis. Roads and transport links are an important requirement when choosing land. Proximity to industrial centres and presence of social infrastructure (grocery stores, medical facility, schools, etc.) are some other criteria to identify a good land parcel. Some developers also said that they look for land in gram panchayat areas or within 200-500 meters of a village so that approvals are easier.

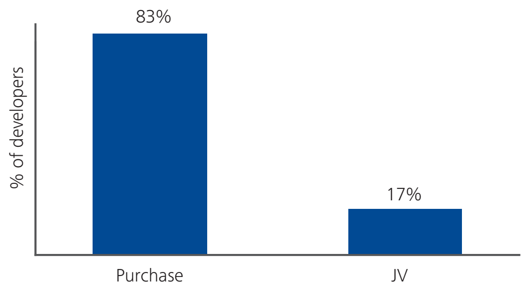
LIH developers prefer to do their own construction

Nearly 80% of the surveyed developers (see figure 21) preferred to do the construction on their own or in other words were themselves the prime contractors of their project. Being prime allowed them to have lower costs, manage escalations, deliver on time and also control the quality of the product. A developer from Indore stated that "since becoming prime, their construction costs have come down by at least INR 150-200 on a per square foot basis". Another developer who recently became prime said that "third party construction agencies are very unprofessional and it is very difficult to get them to stick to deadlines".

Less than INR 1,000 per square foot is the construction cost benchmark for LIH developers

Nearly 70% of surveyed developers said that their total construction costs, inclusive of infrastructure development, were less than INR 1,000 per square foot (see figure 22). Spread of costs across developments in Ahmedabad and Indore was low (similar to the concentration in selling prices in these markets) as there is more uniformity in the available products in the market. On the other hand, there was a wide spread in the construction cost of two developments from Nagpur.

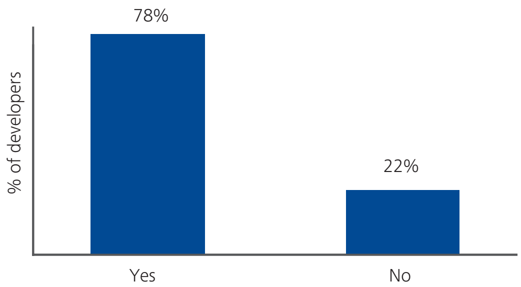
Figure 20 Mode of Land Acquisition



Box 2: Comments from Developers on Land Selection

- **"Look for land serviced with basic infrastructure, well connected by transport services, at a comfortable unpolluted distance from industries which can get fast approvals"**
- **"Only buy residential land, 500 m around villages are classified as residential"**
- **"Look for land near an existing village as all the social infrastructure is already present"**

Figure 21 Prime Contractor



The value propositions of these developments were different and the market is not yet sure of the right product for the LIH segment.

Labour comprises anywhere between 30-40% of the cost while material accounts for the rest. Developers across the country are struggling with the inflationary environment and are citing a 15-20% year-on-year increase in both labour and material costs. 63% of developers rated rising construction costs as one of the top two challenges to their LIH business.

There is interest to try new technologies but adoption is low at the moment

Across developers, there was a strong interest to explore new construction techniques but examples of actual usage are very few. Aluminium formwork has been put in practice by players like Naik Navare and VBHC for their LIH projects and by Pandhe Group in their Government sponsored mass-housing projects. Besides these examples there was very little innovation in the use of construction technology. There was hesitation amongst developers due to

- their organization's ability to execute using these technologies
- acceptance of these technologies by customers

Developers are managing the risk of cancellation by pre-approvals and or flexible payment system

Some of the earlier entrants in the LIH business suffered from a very high rate of cancellation in their LIH projects. Loan ineligibility was the primary reason for the cancellations. In addition, many customers couldn't make the lump-sum down payment on time. As a response to these challenges, almost 70% of the surveyed developers reported that they show flexibility in collecting down payment allowing customers to pay over an extended time period or in instalments. Most of the developers are now also pre-screening the customers to gauge their loan eligibility. This is typically done during the launch event where the invited HFCs give a quick eligibility estimate to the customer before he/she proceeds to make the booking. As a result, cancellation percentage for most of the developers is in the range of 5-10%. However, some developers (mostly new to LIH) also cited cancellation in the range of 25-30%.

Encouragingly, 90% of surveyed developers plan to continue building LIH

58% of the developers reported that their profits met expectations. However, 86% of the developers also said that they were happy (see figure 23) with the eventual profit margins of their LIH projects. Developers are also borrowing strategies from traditional real estate business to improve their realization:

- 61% developers release their supply in a staggered manner to hedge against rising costs
- 71% developers plan their project in a phase-wise manner
- 59% developers levy a preferential location charge to improve their average price realization

Figure 22 Construction Cost by City

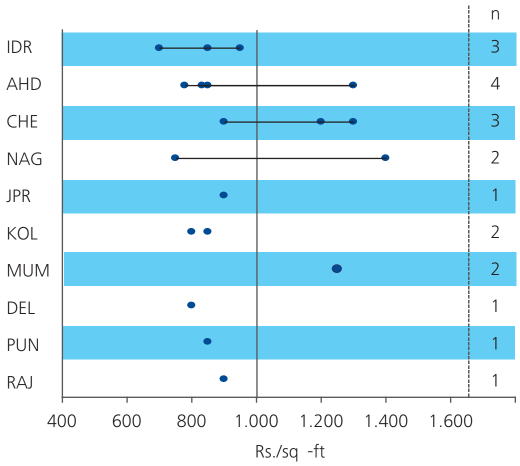
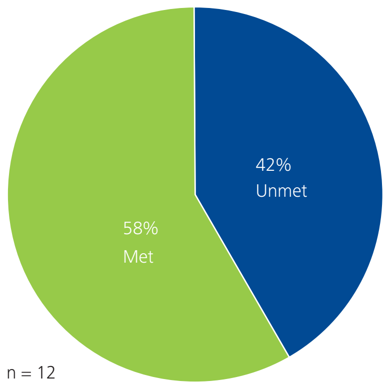
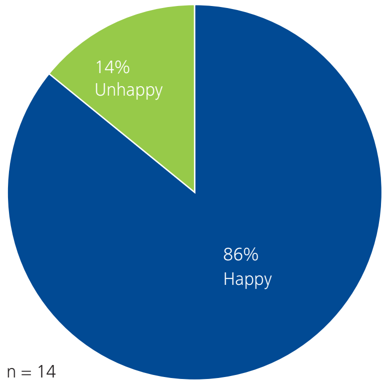


Figure 23 Viability of LIH Business as Reported by Developers

Were your profitability expectations met?



Are you happy with project profitability?



Importantly, 90% of surveyed developers said they intend to continue building in the LIH space. This confidence from developers, especially from a set where 2/3rd of them are already on their second or more projects, bodes well for the industry.

Insights on Low Income Housing Finance Companies

The HFC ecosystem is evolving and there are four different kinds of players in the market

The study looked at business models of each of the HFCs in detail and mapped the businesses of the HFCs on two dimensions:

- The first dimension was the type of housing purchased or constructed – new, resale or incremental
- The second dimension was the source of supply – whether the housing was being built by an individual, a small developer (building 2-20 units), or by a mid-large developer (building mass-housing of 100-1,000 units)

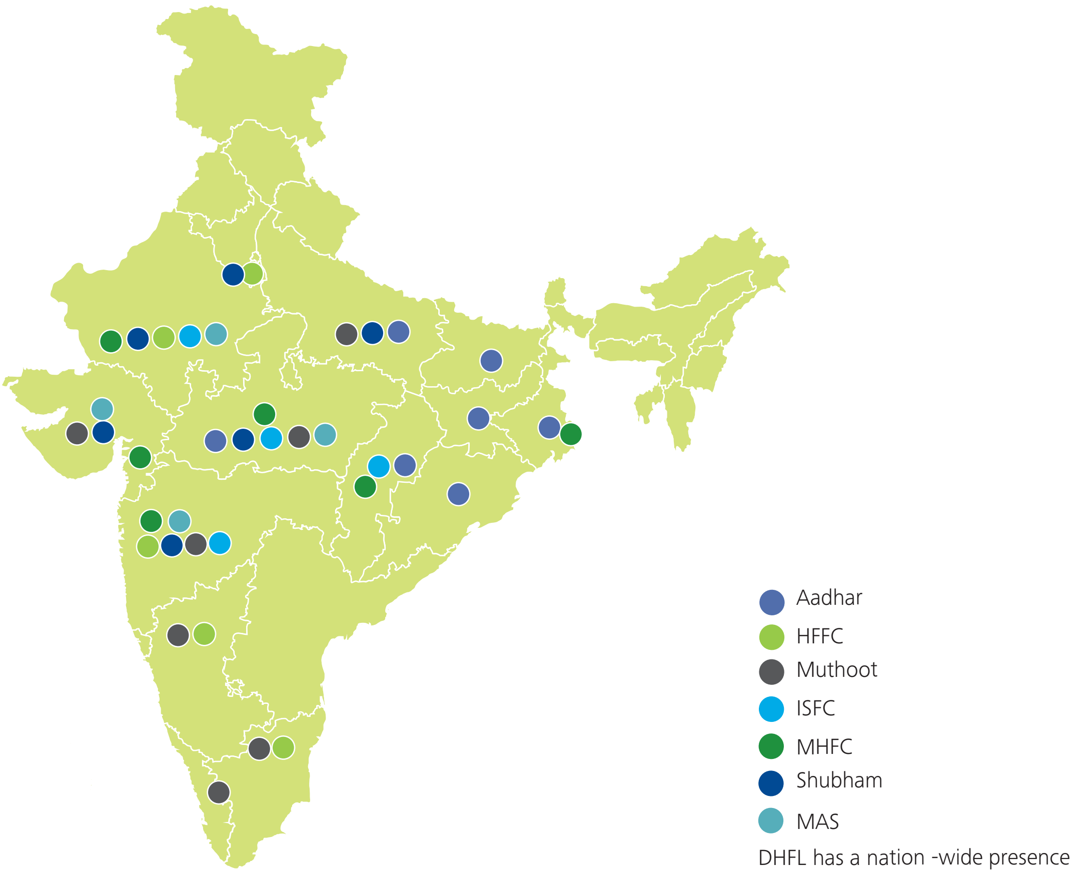
Mapping each of the analysed HFCs on these two dimensions, four different kinds of players emerge (see figure 24):

- ISFC is focused on supply sourced from individuals in the form of incremental housing
- Shubham is focused on financing resale units of individual owners
- Players like DHFL, Aadhar, MAS are focused on meeting the needs of the LIH customer segment, without aligning themselves to a particular kind of supply
- Players like MHFC, HFFC and Muthoot are doing project tie-ups and financing customers of LIH projects of mid to large sized developers

The choice that each of these players makes on where to play in the market has an implication on their business models and cost structures. For instance, a player like MHFC or Muthoot conducts due diligence on a large project and gets access to 100-200 units for financing, whereas a player like Shubham has to conduct a title search on each individual property it finances. Not only are cost structures different for different kinds of players but the way each organization is set up for scale is also very different. Some HFCs have also started to finance Government led housing for low-income customers. For instance MHFC is giving loans to low-income customers of mass-housing projects by Rajasthan Housing Board and Shubham is giving loans on housing units where plots are made available by Madhya Pradesh Housing Board or Indore Development Authority. These HFCs are also spreading well throughout the country (see figure 25).

Figure 24 Representative Low-income Housing Finance Market Map – India, 2013

Figure 25 Geographic Presence of Housing Finance Companies



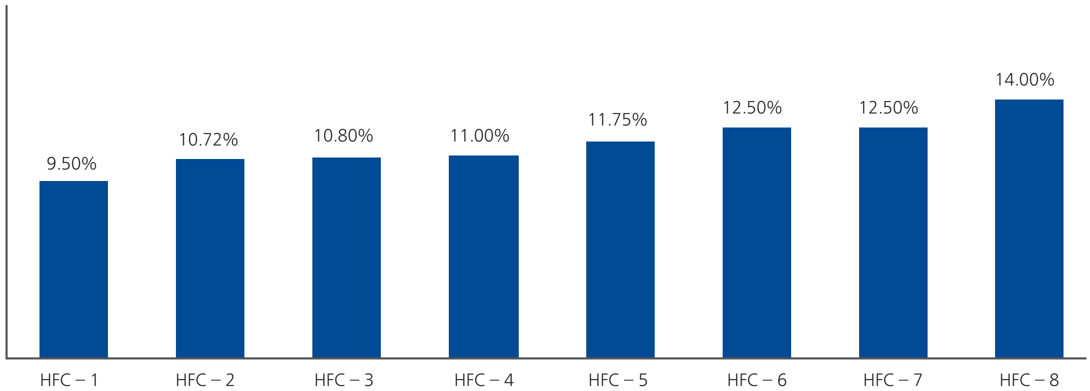
Most new HFCs serving low-income customers have near zero NPAs

Robustness of portfolio of these HFCs is reflected in the near-zero NPA numbers (see figure 26) reported by all of the new HFCs (HFC with the NPA of 0.73% is an established player, operating since the 1990s). Even delayed payments for most of these HFCs are under control at about 2-5% of the total EMIs due in a month. Average ticket size for most of these HFCs is in the range of INR 5-6 lakh and LTVs are 60-70%. Average loan tenors are in the range of 12-15 years which is in-line with mainstream housing finance tenors. Most of the housing finance companies also follow a conservative income assessment practice in their lending operations. A particular HFC from the survey reported some customers making a monthly prepayment of 0.5% on loans with an average tenor of 15 years. A 0.5% prepayment translates into a 30-40% increase in EMI for the customer. Ability of customers to afford prepayment also reflects the quality of the portfolio being built by these HFCs.

Figure 26 Characteristics of HFCs Loan Portfolio

HFC	NPAs	Average Ticket Size (INR lakh)	LTVs	Loan Tenor (years)
HFC – 1	0.73%	10.4	66%	9
HFC – 2	0%	6	70%	16
HFC – 3	0%	6.2	67%	14
HFC – 4	0%	5.6	60%	15
HFC – 5	0%	4.5	65%	N.A.
HFC – 6	<0.01%	3.5	<25%	12
HFC – 7	0%	9	60%	16
HFC – 8	0%	4.5	55%	11

Figure 27 Cost of Debt for HFCs



High cost of borrowing and operations

The surveyed HFCs cited 9.5% to 14% as their cost of debt (see figure 27), which is significantly higher than that of mainstream financial institutions on average[19].

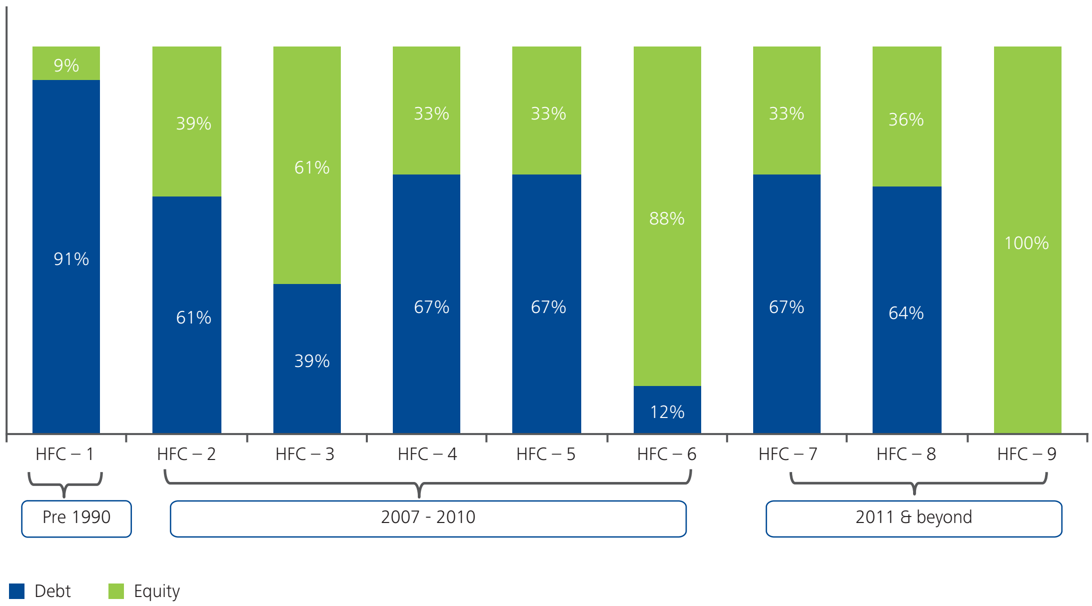
Adding their own cost of operations which is in the range of 1-1.5% (higher than mainstream financial institutions[20]) and profit, the HFCs lend from 11% on the lower end to a maximum of 17%. In fact, 50% of the surveyed HFCs identified cost of debt as one of their top two business challenges.

Low debt-equity ratio of the new HFCs

Not only is debt expensive, its access is also a concern for the HFCs. While established HFCs have been able to scale using debt, the new players are still struggling to achieve good debt-equity ratio. Most of the recent entrants have a debt-equity ratio of less than 2:1 which is much lower as compared to the 10:1 ratio of established HFCs (see figure 28).

Of the surveyed HFCs, 63% identified access to debt as one of their top two business challenges. Refinance from NHB is also on the top of the wish-list for several HFCs as currently only three of the nine surveyed have received funding from NHB.

Figure 28 Capital Structure of HFCs



19 HDFC's average cost of debt for FY '13 was 9.68%; Source: Investor Presentation by HDFC Ltd for quarter ended March, 2013

20 HDFC's average admin cost/ asset ratio was 0.3% for FY '13; Source: Investor Presentation by HDFC Ltd for quarter ended March, 2013

In spite of these challenges, HFCs expect to continue growing rapidly

Besides debt, 29% of HFCs also cited lack of organized housing supply as one of the top two challenges they faced in the business. Focus on different sources of supply by HFCs is also perhaps a strategic response to this challenge. Lack of organized housing supply is also forcing players to look at nearby small towns (and not just the city limits) from their existing big-city branches to source customers. Another challenge for HFCs, albeit cited as low currently, is the cherry-picking of good customers by mainstream financial institutions. Some HFCs reported instances of loans getting prepaid because of poaching of customers by banks.

Encouragingly, in spite of these challenges, most of the HFCs expect to continue to grow healthily. The HFCs are seeing strong traction in the market and both young and established HFCs expect strong performance going forward (see box 3).

Box 3: Growth Expectation of Housing Finance Companies

- **"4x growth over the next 3 years"**
- **"Grow book to Rs. 1,000 Cr (13x) over the next 3 years"**
- **"Loan book growth of 22% to 25% over the next 3 years"**

Government Efforts to Promote Private Sector Built LIH

Actions are being taken in several ways and at different levels (central, state, local) to catalyse the privately built low-income housing market in India. Some policies have been announced recently and some have been implemented with the impact being seen on the ground.

Mandating developers to make housing for EWS / LIG

Central Government policy (JNNURM) recommends states to reserve 20-25% of developed land for EWS / LIG housing in every new Government or privately built residential project. Four states, Madhya Pradesh, Chhattisgarh, Maharashtra and Jammu & Kashmir have a law for this purpose. And five other states, Odisha, Uttarakhand, Uttar Pradesh, Meghalaya and Bihar have a policy for the same. However, only a few states (e.g. Andhra Pradesh, Karnataka, Tamil Nadu and Rajasthan) have executive instructions to this effect.[21]

Providing subsidy and creating an enabling environment

Governments at various levels – central, state and local – have undertaken several measures to create an enabling environment for low-income housing

- Central Government through 'Affordable Housing in Partnership' and 'Rajiv Awas Yojna (RAY)' is providing private developers with INR 50,000 or 25% of infrastructure costs for affordable housing projects. Till date only 11 projects[22] (8 in Rajasthan and 3 in Karnataka) have been approved under the scheme
- Rajasthan state Government has announced five different schemes for private sector built low-income housing which provide additional FSI and reduced taxes for the developer and the customer. As per Rajasthan Government figures[23], an estimated 34,000 units have been launched under these schemes. Odisha state Government has also announced a similar policy
- Zoning certain areas in a city exclusively for LIH could boost LIH supply (e.g. Gujarat Government has recently designated about 76 sq. kms encircling SP Ring Road as an Affordable Housing Zone[24])
- Central Government through "Committee on Streamlining approval procedures for Real Estate Projects" is looking at ways to reduce the approval timeline of 12-18 months
- The Real Estate (Regulation and Development) Bill, passed by the Union Cabinet, would establish an oversight mechanism to enforce accountability in the Real Estate sector and provide adjudication mechanisms for speedy dispute redressal
- Credit Mortgage Risk Guarantee Fund has been established with a corpus of INR 1,000 crore to minimize credit risk for banks or HFCs providing loans up to INR 5 lakh[25]
- Government of Madhya Pradesh has introduced an online Automated Building Plan Approval System to speed up submission and approval of building plans
- Ghaziabad Development Authority has also introduced an automated building plan approval system to quicken the approval process

21 Source: Report on the Demands for Grants (2013-2014) of MoHUPA dated 23rd April 2013 (http://164.100.47.134/lsscommittee/Urban%20Development/pr_files/Press%20Release%20DFG%20HUPA.pdf)

22 DMU Report RAY (http://mhupa.gov.in/W_new/DMU_REPORT_RAY.pdf)

23 Presentation by RK Vijayvargia, Senior Town Planner, Govt. of Rajasthan, at Affordable Housing Workshop in Bhubaneswar on 9th April 2013

24 Revised Development Plan 2021 (http://auda.org.in/Note%20on%20Revised%20Development%20Plan%202021.pdf)

25 Presentation by Additional Secretary, MoHUPA, GoI dated 6th June 2013 given to State and Housing urban development officials

Improving beneficiary affordability

The Central Government and the housing finance regulatory body have instituted measures to improve beneficiary affordability.

- Central Government's ISHUP (Interest Subsidy scheme for Housing the Urban Poor) scheme provides 5% interest subsidy to beneficiaries (loans less than INR 1.6 lakh are eligible) on a loan amount of up to INR 1 lakh. ISHUP was budgeted to support 3.10 lakh borrowers, but only 12,182 beneficiaries availed the facility[26]. This scheme is now being replaced by Rajiv Rin Yojana (RRY) in the 12th Five Year plan. RRY intends to provide housing loans up to INR 5 lakh for EWS and INR 8 lakh for LIG with an interest subsidy of 5% restricted up to INR 5 lakh[27]
- Central Government provides 1% interest subvention on loans up to INR 15 lakh provided cost of the housing unit does not exceed INR 25 lakh with NHB designated as the nodal agency. A total of INR 300 crore[28] was disbursed in 2011-12 under this scheme
- NHB through various schemes provides lower cost refinance to HFCs. Of the nine HFCs interviewed that were lending to low-income informal customers, only three had received refinance from NHB and total amount received was on average ~25% of the total loan portfolio[29]

Setting standards to direct subsidy

The Central Government (through the Affordable Housing Task Force recommendations) has taken a lead in defining the beneficiary (e.g. Economically Weaker Section family earning < INR 1 lakh per annum, low-income group family earning < INR 2 lakh per annum etc.), the minimum size of the habitable unit, and criteria for a project to qualify for subsidies. States have also defined beneficiaries, house sizes and eligibility criteria for their schemes.

Impact on Customers

Customers are satisfied with low-income housing

Home owners interviewed[30] after moving in to their new low-income homes expressed a high level of satisfaction across four key dimensions:

- Improved living conditions – open spaces in and around the site, natural light and good ventilation and attached toilets and bathrooms
- Good neighbourhood – 'gated complex' gave a sense of security to most owners and also meant a secure environment for their children to play. Quality of neignbours (and hence good environment for their children to grow up in) was also apprecaited by the customers
- Larger unit sizes – for most customers, the new home was larger or had lesser number of occupants and hence a larger per capita living space for them
- Improved utilities – 24/7 water supply in the new house was a big improvement over the previous housing of these customers

Customers expressed that remoteness of the location from the centre of the city was the only negative aspect of their new housing. Remote location meant more time and higher cost of travel to work or school. For some customers, access to public transport from their new house was also poor and it took extra planning for any travel to the city.

26 Source: Report on the Demands for Grants, MoHUPA, 2013-14
27 Source: Presentation by Additional Secretary, MoHUPA, 6th June 2013
28 Source: NHB website
29 Source: Monitor Deloitte analysis based on interviews of 9 HFCs (DHFL, HFFC, Muthoot, ISFC, Aadhar, MAS, MHFC, Shriram, Shubham)
30 Source: Qualitative and primary interviews with customers (over 200) in Ahmedabad and Pune across three different projects

Housing finance has improved knowledge and attitude of low-income customers towards formal financial institutions

The business model of the new HFCs which is based on a 'flexible customer assessment model' has helped address accessibility issues and moved customers (especially those working in the informal segment) closer to full financial inclusion. For a majority of the customers, housing finance for their new home was their first exposure to a loan product from a formal institution. The loan application experience has improved customer knowledge of the loan terms and increased their confidence in dealing with bank processes. A reduction in savings (primarily due to higher EMI payments vs. rent) has promoted greater financial discipline and savings management to meet monthly EMI commitments. There is also an increased willingness from customers to consider formal loans as an alternative source of funding for other major expenses. Finally, low-income housing finance has enabled these customers to build an important asset that will reduce their expenses in the longer term and can shield them from financial shocks or emergencies in future.

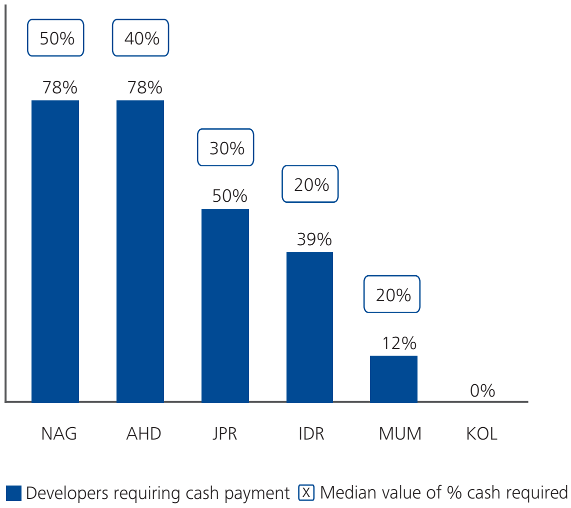
Prevalence of cash component is affecting affordability in some markets

In some markets, especially Nagpur and Ahmedabad, there was a high prevalence of the cash component in LIH projects. In Nagpur, sales officers at 78% of projects said that they require a portion of the unit price to be paid in cash and 50% of the total flat cost was reported as the median value of cash component required in these projects (see figure 29). The high cash component reduces the affordability of the home for end users as the cash amount is usually excluded from the price of the house used to calculate the loan. LIH developers should consider providing "100% loan papers" to make housing more accessible to genuine low-income buyers.

Delay in project completion has a big impact on lives of low-income customers

Each of the surveyed customers had experienced delays in the range of 12-24 months. The delay in delivery (and hence possession) impacted customers on numerous fronts – finances, planning for children's education and other unforeseen circumstances (see box 4).

Figure 29 Requirement of 'Cash' towards Payment for Flat Purchase



Box 4: Impact of Project Delays – Some Customer Responses

- **"I was in a loss, the bank was at benefit, builder was at benefit. I had to pay 30k-40k more as interest, instead I would have utilized that money for renovating the house."**
- **"Instead of 18 months, they took 28 months to give possession. I had taken admission for my son much earlier in a school here, thinking that they will give possession in ten months. So, I had to spend more and start sending him here."**

Post moving-in, maintenance of the project is an issue

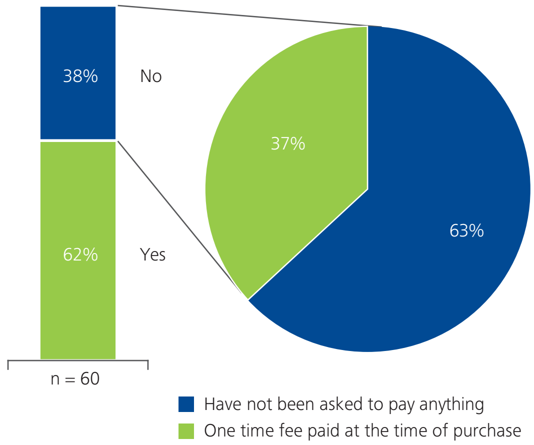
Post moving into their new house, lack of clarity on maintenance services and charges has been an issue for customers. Most residents had only a perfunctory awareness of responsibility and charges for the maintenance services. In Ahmedabad, it was surprising to find that even customers from the same project had significantly different understanding of the maintenance fee and what it covered (see figure 30). 38% of customers were not paying maintenance fees as they felt either a) they had paid it at the time of purchase or b) they had not been asked to pay.

Lack of clear communication from developers could be the reason behind the confusion. For a lot of surveyed projects in the 'state of the market' survey, the sales officer at the site was not clear whether maintenance charges were being levied or not. For instance, sales officers from 53% of surveyed projects in Ahmedabad and 93% in Indore had no clarity whether maintenance was being charged or not. But wherever maintainance was charged, it was affordable at INR 1-1.50 per square foot on a monthly basis.

The Psychological impact of housing has been positive

Moving into the new housing has given the low-income customers a sense of upgradation, a feeling of belonging, pride of ownership and importantly a surge in aspirations. (see box 5)

Figure 30 Maintenance Paid (Ahmedabad Project)



Box 5: Impact of New Housing on Low-income Customers

- **"We feel better here. Our life style has changed, now we are experiencing city life. And after all this is our own house."**
- **"First, I was a 'Pardesi' (an outsider) but now that I have my own house, I feel a sense of belonging in Indore."**
- **"Here, we don't feel any tension or fear. And, if somebody visits us, they would like the house… we also don't feel ashamed of our house."**
- **"I will look for a plot. Today I am in a flat, tomorrow I'll build a house and put a shop there."**

The Gap to Realize the Dreams of Millions

The LIH market – housing and housing finance – has made several strides forward and is now serving many low-income families. Yet the gap between current supply and potential need is staggering. Against a potential need of 13-15 million units for households that earn between INR 10,000-25,000 per month, the market has so far launched 78,000 LIH units, which is less than 1% of the total need. To increase the supply of housing and finance, there is a need to address challenges in the business environment for existing players. However, the gap cannot be addressed by current players alone and there is a need to attract new players. The affordability of low-income customers has to be improved so that more families can participate in this market. Finally, the industry needs to grow robustly and address the issues being faced by low-income customers during and after the purchase of their new housing.

Addressing Challenges in Business Environment

The building approval process is slow and tedious

Fifty-nine percent of the surveyed developers considered the lengthy and tedious approval process to be one of the top two challenges to their business. Some developers reported an approval time-frame of 18-36 months for their projects. As a response, some developers are now designing their business model to minimize approvals (e.g. constructing on gram panchayat land, building G+4 structures, building on small parcels). Absence of many large scale projects in this study is also perhaps an indication of the challenges in approvals faced by such projects. Approval delays especially hurt the LIH developers, as the business model relies on quick execution unlike traditional real estate business where delays are compensated for by price escalation.

Rising construction costs are a major concern for LIH developers

Sixty-percent of developers cited rising (15-20% year-on-year) rising costs of labour and materials as one of the top two challenges to constructing low-income homes.

Availability of affordable land is a challenge for existing players

Availability of affordable land which is also serviced adequately by infrastructure was reported to be one of the top two business challenges by 52% of the surveyed developers. Across the cities, developers reported a 20-30% year-on-year increase in land prices, making it tedious for them to find well connected (with local transport) land parcels for development at an affordable price.

HFCs can scale faster if debt is made more accessible and affordable

Limited access to debt and its high cost is a key business concern for 70% of the surveyed housing finance companies. The housing finance industry is seeing strong traction but the opportunity to provide lower cost mortgages to the end customer could be missed if these HFCs are unable to access adequate debt at a reasonable price.

Attracting More Players to Build LIH

Attracting LIH developers in new geographies

The survey data revealed that the bulk of LIH activity is still concentrated in a few cities and there is a need to attract more players to build LIH outside these geographies. As witnessed in Ahmedabad, Indore and Mumbai, the success of a few early players in a market could have a catalytic effect on the LIH supply in that market.

Attracting more developers in markets with existing activity

Even in markets with good activity there is a need for more players to build LIH supply – for instance, there are approximately 1.2 million households in Ahmedabad and a potential need of 180,000-200,000 low-income houses[31], but the current rate of supply is less than 5,000 units in 18 months.

31 At a population of 6.3 million and assuming an average of 5 members per household there are 1.2 million households. Assuming the same income classification as the national average, 30% i.e. 360,000 fall in target income segment of INR 10,000-25,000. At 40-45% renters and 15-20% demand from non-renters, there is a potential need for 180,000-200,000 houses in the price range of INR 4-10 lakh

Improving Affordability for Low-income Customers

High cash component greatly reduces affordability

Affordability of genuine low-income customers is impacted by requirement of cash towards housing purchase in certain markets. High cash component is a big deterrent for low-income customers as loans can be availed only on the non-cash component. Therefore, the customer needs to have saved up the cash component and down payment thereby greatly reducing their ability to make a purchase.

Developers need to be convinced about the marketability of small formats (1RKs) and smaller houses

Small formats and small houses help improve the affordability of a housing unit for low-income customers. Research indicated that in several cities there was a resistance from developers to build small format units like 1 RKs or smaller 1 BHKs. The pricing on per square foot basis is still affordable in these cities and more small formats by developers could open up the LIH supply. Even in markets with existing activity, adding more small format units and/or reducing the size of traditional 1 BHKs / 2BHKs in current projects could greatly increase the availability and affordability of LIH supply.

Creating a Robust Industry

Insufficient transparency on maintenance charges adversely impacts the customer

Post moving into their new houses, customers are not clear on the maintenance services and its cost. This lack of knowledge could potentially result in poor upkeep of the project thus adversely affecting both the residents and the developer's reputation.

Project delays severely impact customers' financials

Project delays have a big impact on the plans of low income households. Even if the project is delayed, customers have expressed a desire for clear communication from developer to better plan for contingencies.

Way Forward

Opportunity to Realize the Dreams of Millions

Today, in most cities, a privately built apartment of carpet area 25 sq.mt. or 269 sq.ft. (minimum stipulated size) would cost about INR 5.6 lakh. A family at the top end of the EWS segment with access to INR 60,000 for a down payment can only afford a home worth INR 2.95 lakh. Therefore an EWS family requires a subsidy of INR 2.6 lakh to buy the smallest stipulated privately built home. Similarly a family at the top end of LIG segment can afford a house of 24 sq.mt. or 258 sq.ft. without any subsidy (see figure 31).

To realize the dreams of millions, the Government, the private sector and other stakeholders have to play their part to improve affordability of homes for the low-income customer, to increase supply of low-income housing and housing finance and to build a robust industry.

To improve the affordability of housing for the urban poor of India, both supply and demand side measures are required. On the supply side, cheaper land, innovative construction technologies, 100% loan papers, small formats and smaller houses could help. On the demand side, targeted subsidies for the segments who cannot afford privately built housing and making affordable housing finance available for all low-income customers are key.

To increase the supply of housing available for these customers, there is a need to attract more developers and for existing developers to build more units. Existing developers could build more and faster if the approval process was made quicker and supportive for LIH developments. To help the housing finance industry scale, besides more supply of housing, affordable debt has to be made available.

Finally to develop a robust industry, there should be more customer education about the home buying process, more transparency and better communication on issues like maintenance and delivery timelines.

Three Key Suggestions for Government

Create an enabling environment for LIH developers (not subsidies)

One third of the project cost for LIH developers is land that is mostly financed by the developers' own capital. A typical developer would take ~18 months to get approvals and ~18 months to construct. If the approvals were much quicker the same developer with the same capital could produce up to twice as many LIH units.

Figure 31 Affordability of the Top-end of the EWS and LIG Segments

Family Category	EWS	LIG
Monthly household income (INR)	8,333	16,667
Affordable EMI @ 35% MHI (INR)	2,917	5,833
Loan tenure (years)	20	20
Loan eligible @ 14% (INR '000)	235	470
Down payment ready (INR '000)	60	120
Affordable home (INR '000)	295	590
Saleable area of the house @ 1600 psf (sq.ft.)	184	369
Carpet area @ 30% loading (sq.ft.)	129	258

Government could reduce approvals (e.g. zones in a city not requiring Airports Authority approval) needed and provide time-bound approvals. Digitizing land records would also reduce transaction timelines. All housing projects require land with good infrastructure (e.g. roads, sewers, electricity). Laying out infrastructure on the outskirts of city increases the supply of serviced land, opens up more areas for construction and potentially dampens price escalation of serviced land. Earmarking areas in cities for EWS / LIG development while ensuring mixed housing development could also increase supply of EWS / LIG houses.

LIH projects have to utilize land effectively in order to provide the customer a cost effective and habitable house. For LIH projects, FSI of up to 2 could be allowed and some by-laws (e.g. mandatory car parking requirements) could be reviewed. Small houses are affordable and help customers with tight budgets to buy a property which would otherwise be unaffordable for them. Therefore, the Government could consider reducing the minimum size of a dwelling unit to 21 sq. mt.

Provide targeted subsidies to low-income customers

Government could intervene in the market and provide subsidy to bridge the gap between price of house and beneficiary affordability. There are two scenarios in which low-income housing is developed – 1)"Market" scenario where the developer is determining the price and the beneficiary and 2) "Controlled" scenario where the Government is determining the price and the beneficiary.

- "Market" scenario: Any subsidies given to the developer in this scenario may not be passed on to the beneficiary. It would be most effective to provide

subsidies directly to the low-income customer (e.g. waive stamp duty and registration taxes and provide interest rate subsidies to low-income customers)
- "Controlled" scenario: In this scenario, the Government would have to bridge the gap between the market price and the Government target price. Projects could be awarded to the bidder asking for the least viability gap funding. If the Government is auctioning land, an effective mechanism to get EWS housing could be to invite bids for the land in terms of the number of EWS houses the developer would build for the Government in lieu of construction rights on the remaining piece of land

Enable low cost credit to low-income developers and HFCs

HFCs get debt at 10-14% and lend to formal and informal, sometimes unbanked, low-income customers at 11-17%. Reducing the cost of debt for the HFCs could improve affordability for customers. Through NHB, the Government could provide more low cost credit to HFCs serving low-income customers while ensuring this benefit accrues to the customer.

In order to stimulate supply, the Government could consider lowering norms (i.e. allow smaller projects) for foreign direct investment (via equity or debt) in low-income housing projects.

Suggestions for Developers to Improve their Low-income House Offering

Arranging money for a large one-time down payment is a challenge for low-income customers and developers could support customers by (i) providing 100% loan papers, so the customer needs to accumulate only 20% of the price of the house towards down payment and (ii) taking the down payment in instalments. LIH developers can increase the affordability of their product by building smaller sized houses and smaller format (e.g. 1 RK instead of 1BHK) houses.

To be successful, an LIH developer has to manage project costs and timelines well. Cost overruns would make the project unviable for the developer and construction delays would affect the low-income customer as they would have to pay rent and EMI together. Most developers could build reputation, gain trust and enable future sales through word-of-mouth by over delivering slightly on the promises of timelines and product quality (e.g. house delivered to the quality of mock apartment shown).

LIH developers should expect more queries and train their sales team to provide information to customers about the home buying process (e.g. additional charges, down payment required, financing options, society formation, etc.). Developers should provide more transparency on maintenance costs and responsibilities to avoid disagreements and loss of trust later.

Suggestions for Housing Finance companies

Developers, in geographies with no or limited HFC presence, are often not aware that formal and informal low-income customers can get loans and therefore can be served. HFCs could expand to new geographies, as improved visibility of housing finance for low-income customers could convince developers to enter this sector.

HFCs with their national reach could develop and disseminate standard pamphlets to customers to educate them about the home buying process (e.g. loan eligibility, registration of property, society formation and maintenance) in a transparent manner.

Suggestions for Other Stakeholders (e.g. International Development Agencies, Foundations, Industry Associations, Related Industries, Financiers) Interested in Promoting Low-income Housing

One successful low-income project in a city demonstrates the opportunity to other developers and hopefully increases LIH supply in the city. All interested stakeholders should spread the word about the potential opportunity in low-income housing to developers and support Government initiatives in creating conducive policy to catalyse low-income housing in India.

International donor agencies or foundations could support pilot projects in new geographies and invest in innovative construction technologies to boost supply and reduce construction costs respectively.

Stakeholders and practitioners should collaborate to periodically monitor the market, disseminate findings to support decision making and provide feedback to the industry. They could also develop simple content for developers and HFCs to distribute to customers on issues like housing finance, responsibility for maintenance and society formation.

Glossary of Terms

- **Low-income Housing**: the term has been used to describe the privately built below INR 10 lakh housing in urban India
- **HFCs:** Housing Finance Companies
- **MoHUPA:** Ministry of Housing & Urban Poverty Alleviation, Government of India
- **NHB:** National Housing Bank
- **ULBs:** Urban Local Bodies
- **EWS:** Economically Weaker Section, defined by the MoHUPA as urban households which earn less than INR 1 lakh annually
- **LIG:** Low Income Group, defined by the MoHUPA as urban households which earn less than INR 2 lakh annually
- **MHI:** Monthly Household Income
- **MIM:** Monitor Inclusive Markets
- **1RK:** A housing unit with a room and a kitchen
- **1BHK/2BHK:** A housing unit with 1 or 2 bedrooms, a hall and a kitchen
- **FSI:** Floor Space Index - the ratio of a building's total floor area to the size of the piece of land upon which it is built
- **NPA:** Non-Performing Asset
- **JV:** Joint Venture
- **LTV:** Loan To Value
- **AHD:** Ahmedabad
- **AP:** Andhra Pradesh
- **CHE:** Chennai
- **DEL:** Delhi
- **GUJ:** Gujarat
- **IDR:** Indore
- **JPR:** Jaipur
- **KOL:** Kolkata
- **MAH:** Maharashtra
- **MP:** Madhya Pradesh
- **MUM**: Mumbai
- **NAG:** Nagpur
- **ODI:** Odisha
- **PUN:** Pune
- **RA:** Rajasthan
- **RAJ:** Rajkot
- **TN:** Tamil Nadu
- **UP:** Uttar Pradesh
- **WB:** West Bengal

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As of 2013, the Dell family foundation has, through a combination of grants and private equity investments, committed $120 million (INR 660 crore) towards measurable social progress for India's children. In the past three years the foundation has played a catalytic role in the housing market by supporting innovative business models and demonstrating their viability. The foundation also seeks to partner with entrepreneurs and others to catalyze new markets that promote financial inclusion through vocational training, microfinance and other services.

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DHFL was the second housing finance company to be set up in the private sector in India, and its stated business objective was to enable access to affordable housing finance to the lower and middle income groups in India. Today, DHFL strives continually to reach out to its customers through its extensive network of 170 Branches,73 Service Centers, 31 Camps and 9 Regional Processing Offices spread across the length and breadth of the country.