

## A STUDY ON INDIAN MORTGAGE INDUSTRY

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### ABSTRACT

The goal of this paper is to study the Indian mortgage Industry from 2001 to 2009 in order to understand the change in industry performance and taste of customers with change in economic condition. The second objective of the study was to find the factor which influences customer decision on availing a loan. The change in industry performance was studied through the survey conducted with banks officers and an attempt was made to crystallize the lenders' viewpoint. To find the factor influencing the customers decision a survey was conducted with NRIs. For the data analysis statistical tool SPSS has been used. The focus has been on frequency and percentage analysis to interpret the responses. Through secondary data initiatives taken by the Government of India to boost industry has been studied.. The study brought out that change in demography has influenced industry performance. The change is customer taste and perception and priority of service quality affect business of any organization.

The research results bring out the avenues where the banks need to focus in order to generate more business and also identifies the future prospects of the industry.

**Key Words:** Mortgage industry, Non- Resident Indians, Government Initiatives, Indian housing sector.

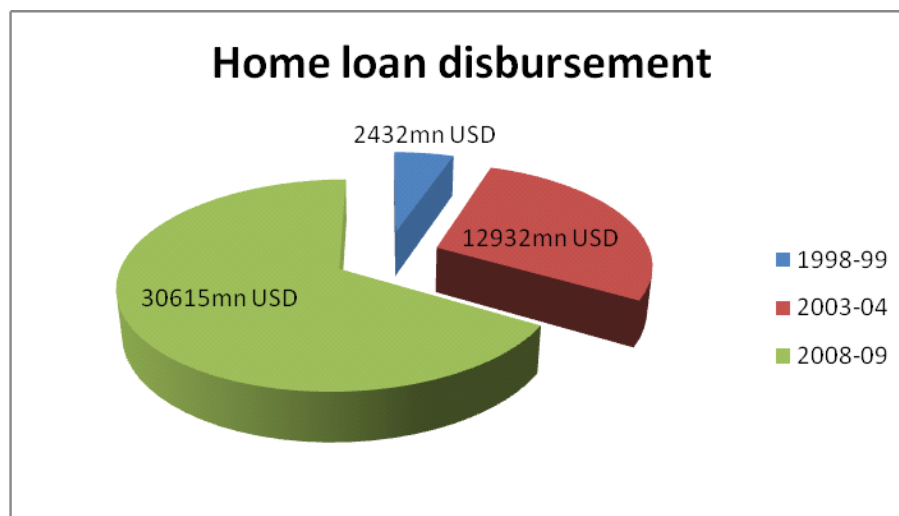
JEL Classification: G 21 & G 28.

## INTRODUCTION

With the shift in the Indian economy from the manufacturing sector to a service sector, the growth is expected to be strong especially in the banking services. Banking as a whole is undergoing a change, and the same is likely to be seen more in retail banking, mortgages and investments.

The Indian mortgage industry is the horizon for great opportunities, tremendous growth and wonderful returns over a period of time. This sector has seen various changes over the period of time. The swing has been seen in residential properties, malls, commercial centers and IT hubs. The Indian real estate market as well as the industry is a lucrative field for foreign investors. This sector has also brought in the development of special economic zones. The growth in this industry ranges wide; it includes in itself development of Tier II and Tier III cities.

The industry has seen various changes with changes in economic scenario and is growing at a very fast rate. The paper focuses on the parameters that have affected the performance of industry.



The study is centered on the period 2001 to 2009 which would help understand how the industry has performed at various phases of the business cycle. The period has its significance as it covers boom to current slowdown. Thus in this paper an analysis of the factors leading to the growth of this sector, the changes that have come over with time, the role that NRIs play and the initiatives taken by the government at various stages have been considered.

## LITERATURE REVIEW

The paper covers the literature review under the sub-heads of Mortgage industry, non-resident Indian and the Indian mortgage industry and government initiatives. This helps in focusing in each aspect in detail.

## MORTGAGE INDUSTRY

1. The article Indian Housing Sector Analysis, by Shushmul Maheswari<sup>1</sup>; discusses about the report by RNCOS on “Indian Housing Sector Analysis”. RNCOS report “Indian Housing Sector Analysis” provides exhaustive information and objective analysis on the growing housing industry in India, its components and supporting financing structure. The report also discusses the market structure, current and past market

<sup>1</sup> <http://www.istockanalyst.com/article/viewarticle/articleid/3169983>

performance and factors critical to the success of housing industry in India. Detailed data and rational analysis helps investors, financial service providers and global banking players to navigate through the latest trends in the Indian housing industry. A forecast has been given based on the correlation between past market growth and also the growth in base drivers, such as household size, disposable personal income, GDP growth, long-term interest rates, competitive structure, government support, contribution by housing financing industry and growing industrialization. The paper stresses that the industry will see tremendous growth in the coming years and is expected to cross the other industrial sectors in terms of GDP.

2. In the article Housing Sector in India – Issues, Opportunities and Challenges<sup>2</sup> emphasis has been given on the factors that led to growth in this sector. The main factors mentioned are population growth, shift of population from rural to urban areas, emergence of nuclear families and like. It also speaks of the first housing finance company and entry of banks in this field. Based on studies it specifies that there is need to develop low cost houses using easily available building materials and innovative technology to build houses affordable by all.

3. In NHB's article Housing Policy;<sup>3</sup> the policy formed by the NHB has been presented. It talks about the 'The National Urban Housing and Habitat Policy 2007' has been discussed. The policy had been brought out keeping in mind the changing socio-economic scenario of urban areas. The policy envisages specific roles by central government, state government, local bodies, banks and financial institutes. The role of NHB has been discussed under development of secondary mortgage market and for financing slum up gradation.

4. India has slowly but steadily been improving on the housing sector, the standard is now comparable on an international platform. In the article, India's Housing Market Prospect (International) by O'Connor Robert<sup>4</sup>; it has been stated that economic restructuring over the last decade has begun to open up the country to outside capital and ideas. It state that legal impediments, tax barriers to securitization and cultural attitudes toward debt all portend that India's mortgage market has a long way to go, but the progress is occurring slowly with time.

5. With the global economic crisis, the Indian mortgage industry has also been hit. A study by CRISIL had anticipated the slowdown in housing loan disbursals. The article Home Loan Disbursal to slow down in 2007-08 – CRISIL<sup>5</sup> brings out the view. It states that though the asset quality remains comfortable, but profitability will be muted. According to the study housing sector disbursal would grow in the period by 20 per cent which is lower than 30 per cent of the trend that has been witnessed over the past few years.

## **NRI and INDIAN MORTGAGE INDUSTRY**

1. The article by Elina Mohanty and Radhika Menon, NRI home Loan Surging <sup>6</sup>talks about the concept of home among the NRIs. It deals with the relaxation of credit policy that led to the growth of the NRI home

<sup>2</sup> <http://www.flipkart.com/housing-sector-india-issues-opportunities/8131414019-tu23f9lc14>

<sup>3</sup> [http://nhb.co.in/urban\\_housing/housing\\_policies.php](http://nhb.co.in/urban_housing/housing_policies.php)

<sup>4</sup> Publication: Mortgage Banking, 1<sup>st</sup> November 2001.

<sup>5</sup> <http://www.banknetindia.com/banking/70423.htm>

<sup>6</sup> <http://www.thehindubusinessline.com/2006/12/24/stories/2006122404570100.htm>

loans and also about the big ticket size of the loans availed by them. The average ticket size of home loans availed by the NRIs is generally two to three times higher than those availed by domestic customers. The major contributors are the Middle East, US and UK. According to Anup Bagchi, “NRIs generally look for large properties in India, because of the lifestyle enjoyed overseas. A surging Indian economy has prompted many NRIs settled overseas to relocate to India”

2. NRIs and their love for the country, a matter of inexpressible joy for realty developers – is the caption to the article ‘Soaring Real Estate Industry, Courtesy NRIs’<sup>7</sup> tells about the expectations of the real estate developers from the NRIs. Two years back real estate showed a beginning of growth, boom and huge profits. This trend followed for quite long but then came the time for this rosy picture to fade and correction came into the scene. With the beginning of this correction phase, real estate turned to be not so attractive, not so profitable and a difficulty for a common man who desired to own home or one who found himself stuck in the home loan trap. High profile NRIs are now choosing to come back home, to their own land. Almost all the major cities, both metros and tier II cities fall on the radar of NRIs who plan to come back and settle here in India, Bangalore alone has witnessed a comeback of 35000 NRIs. India being an economy that’s growing at a high pace and seeing innumerable changes in almost every aspect portrays herself to be a challenge. With these diasporas real estate is undoubtedly to grow despite of the severe dip in the domestic demand. NRIs now constitute 20-25% of the total real estate market and this migration is expected to grow the industry @ 20% annually.

3. In another article the steps and initiatives taken by the developers and real estate dealers have been highlighted. In this article Realtors woo NRIs, HNIs with luxury apartments<sup>8</sup> the various projects and villas that are coming up across various cities have been dealt with. It talks of the price of these projects which range between 3 crore to 50 crore and how the real estate agents are marketing themselves on a global platform.

4. In the article NRIs stay away from Investment in Real Estate<sup>9</sup> gives the picture of current transition in economy. The NRIs who over the years have increased their investments in Indian properties with relaxation in policy norms are staying away from immediate investments in this sector. The article presents the period of the financial year where most NRIs visit India, search for properties and purchase those. But the meltdown that hit the entire world brought in a different scenario.

## GOVERNMENT INITIATIVES

1. In the study Housing – Engine of Economic Growth, by Peter D. F. Cardozo, Managing Director, CAN FIN Home Ltd<sup>10</sup>; the initiatives taken by government of India has been highlighted. It throws light on a study instituted by HUDCO to evaluate the impact of investment in the housing sector on GDP and employment has found that housing sector ranks third among the fourteen major sectors in terms of total

<sup>7</sup> Press Release, March 20, 2007

<sup>8</sup> [http://economictimes.indiatimes.com/Markets/Real\\_Estate/Realty\\_Trends/Realtors\\_woo\\_NRIs\\_HNIs\\_with\\_luxury\\_apartments/articleshow/2875908.cms](http://economictimes.indiatimes.com/Markets/Real_Estate/Realty_Trends/Realtors_woo_NRIs_HNIs_with_luxury_apartments/articleshow/2875908.cms)

<sup>9</sup> <http://www.indianrealtynews.com/nri/nris-stay-away-from-investment-in-real-estate.html>

<sup>10</sup> [http://www.naredco.org/article\\_article\\_12.doc](http://www.naredco.org/article_article_12.doc)

linkage effect with other sectors of the national economy. In terms of income multiplier, it ranks fourth and is ahead of other sectors like transport and agriculture. It is estimated that a unit increase in the final expenditure would generate additional income as high as five times. It also puts forward the view of the McKinsey report which was presented to the Honorable Prime Minister has emphasized that housing must be accorded highest priority to accelerate GDP growth. World Bank has recognized that policies to promote free markets lead to healthy sectors which in turn help drive economic growth, a phenomenon which we are now witnessing in India.

2. The government of India has taken various steps in the inflow of FDI. FDI Flow in India 200711 has touched 15.7 billion USD. FDI inflows to India have been growing at a high rate for the last few years. In UNCAD's World Investment report, it has been stated that India has been ranked fourth in terms of receiving FDI during the year 2006-07, which amounted to 22 billion USD with a growth rate of 126 per cent. The role of government of India in this regards is noteworthy. The Government of India has granted permission to foreign investors to set up joint venture companies with various private sector units in India. The article states the reason behind such step is to promote country specific investment. The countries involved in this are US, Japan, Taiwan, UK, Germany, Singapore, France, South Korea, Switzerland and Italy.

3. Government must speed up its expenditure on infrastructure and support to the poor to stimulate the economy is what S. L. Rao feels and states in the article 'Reviving the Economy: Need bold Initiatives' 12. The lending pattern has been hit by the US sub-prime crisis with major impact on housing. In the given scenario banks and lending institutions must get the government's guarantee against defaults to encourage them to resume lending. The article provides few initiatives that need to be taken on priority to boost the market. The author gives few unprecedented steps and suggests them to be implemented without delay to revive economy.

4. In the article, Will the stimulus package accelerate growth? 13; starts on the note 'With these packages the ball now lies on the developers' court, if they are willing to pass the benefits, real estate demand is sure to pick up' Thus we can understand the flow of the article which goes further to say that customer are optimistic about real estate prices going further down. Thus they are holding back from investing in this sector with the anticipation that prices would fall further in the near future. Thus even though State Bank of India is giving a special scheme for home loan buyers the demand is yet to pick up. Judging by the market sentiments and viewpoints of few real estate leaders the article goes further to say that the property prices which is now seeing a downward trend would by April 2011 start to rise again.

## LIMITATIONS OF STUDY

The limitations of the study are as under Customer Access: There is no direct access to the customer of the bank. The cases studied are already approved, thus no further credit processing of the cases. Also the NRI customers are not well versed about the industry.

Survey: Though regular follow-up was done on NRI customers and the out stationed bank officials the response received was both low and time consuming.

<sup>11</sup> <http://business.mapsofindia.com/fdi-india/flow-2007.html>

<sup>12</sup> Deccan Herald, Dec 9, 2008

<sup>13</sup> Realty World, April – June 2009, Complimentary with Financial Express

Lack Of Latest Data: The lack of latest data especially in the NRI segment made it difficult to interpret accurate trend in their role

## OBJECTIVES OF THE STUDY

The objectives of this study are as under:

- ☐ To study the Progress of Indian Mortgage Industry from 2001 to 2009
- ☐ To understand the Business Cycle from boom to the current slowdown, to analyze methods to boost the housing sector
- ☐ To study and analyze the role of non-resident Indians in the Indian mortgage industry in the past and present.

## METHOD OF INVESTIGATION

The research is both descriptive and exploratory in nature and is based on both primary and secondary data. For the primary data collection the study divided into two parts. In the first part a survey was conducted with bank officials. It was over various banks and about 105 respondents were contacted of which 89 reverted. Part of survey was by direct visit to banks while part of it was through mailers.

The questionnaire had 24 questions which were divided into three parts. The first had few general questions to serve as warm up questions as well take the response of the interviewee of the market in general. The second part was most significant for the study as it brought out the changing trend of the housing sector. The final questions were focused on ways to revive the market from its current downturn scenario. The variety ranged from checklist to Likert scale questions. The structured questionnaire was finalized after conducting a pilot survey with 10 officials to test validity and reliability. The second part was a survey with non-resident Indians. The questions here were mainly checklist type, with few based on ranking. The survey was conducted through mailers and the number of respondents contacted was 80.

The data was analyzed using frequency and percentage analysis. For some questions trend analysis was conducted. The statistical tool used for the analysis is SPSS. For secondary data research papers, news articles and data available in journals and internet was used

## HYPOTHESES

The hypotheses may be stated as:

(1) demography which includes the average age group, income level of people and their tastes have affected the industry positively and lead to its growth.

(2) with growth risk and delinquency levels also increase.

In today's fast growing service industry the quality of service is what differentiates a firm from others.

(3) The additional offers made by companies say documentation, duration and rates offered are of lesser significance.

## RESULTS & DISCUSSION

The paper covered two surveys. The first survey is with the lenders – which help in analyzing the performance of the Indian mortgage industry over the period 2001 to 2009 through a survey with the

lenders and the role of NRIs over the period and about home loan processing in general. In the survey, an analysis of the changing pattern has been done. The second survey is with NRIs to judge their preference while availing a home loan from India. The study covers the Indian mortgage industry from 2001 to 2009. The year 2008- 09 saw a change in the housing sector mainly due to the ripple effect of the US sub-prime crisis. The government thus took initiatives to boost the demand in the housing sector through the above mentioned strategies. The lenders ranked these options based on the experience and knowledge of market and customer needs. This helped understand how a bank reacts to economic situations and how it should prepare itself from such economic shocks. The figure on the right shows the lenders choice in boosting the housing demand. It is clear that majority of them feel that lending rates is the key driving factor and the lowest influencer is tax benefits. The same is highlighted with the trend lines.

(1) The average age of customers has come down from 42 to 31. In the period the average age of customers availing home loans were 40 plus. This has over the period come down to an average of 30. This shows that the younger group is now inclined towards availing home loan. Thus for any financial institute who is out in the market for lending business the target audience should be the people in this age group. The strategies that the banks come out with should be based on the said target, their needs and preference.

(2) With reference to delinquency rate over the period of 2001 to 2009, The rate was highest in the phase 2004 to 2008. The underlying reason being aggressive marketing and lending in the days of boom. The best example of such lending is the US sub-prime crisis. India is in a much better situation compared to some other countries because of the stringent banking norms. Though the economic situation has faced a slow down but the policies have helped it survive. Learning from this the banks should take utmost care when going for funding. The risk strategies have come in as a saviour but other norms related to credit and marketing should follow suit.

(3). The year 2008- 09 saw a change in the housing sector mainly due to the ripple effect of the US sub-prime crisis. The government thus took initiatives to boost the demand in the housing sector through the above mentioned strategies. The lenders ranked these options based on the experience and knowledge of market and customer needs. This helped understand how a bank reacts to economic situations and how it should prepare itself from such economic shocks. The figure on the right shows the lenders choice in boosting the housing demand. It is clear that majority of them feel that lending rates is the key driving factor and the lowest influencer is tax benefits. The same is highlighted with the trend lines. This would also help the central bank in its policy making, as the lenders reaction comes out clearly in the given chart.

(4) As can be seen that of the customers surveyed 62.8 % feel that rate of interest is a very important factor in their decision making. Only 9% felt that it was not that important a factor in their decision making. For them other criteria were more important.

(5) The frequency analysis shows that 62.8% agree that it is a decision making factor, while 19.2 % are indifferent towards loan tenure while availing a home loan.

(6) 37.2 % agree that documentation is an important factor while availing home loans, while one group of 26.9 % strongly agree and the other 26.9% are indifferent towards documentation involved.

(7) Insurance offered does not appear to occupy the mind of the customer to a great extent. Only 44.9% have responded that it is an important factor while a cumulative of 46.2 % are either indifferent or disagree to it.

(8) Whether a customer has existing relationship with the bank or not does not seem to affect majority of the customers. 44.9% of them are indifferent towards this factor. Only 26.9 % strongly agree with it.

(9) To understand the effect of current global slowdown on the decision making, the question on it was forwarded to the customers. 55.1% agreed to its effect on the decision in availing home loan on current date.

(10) We can see from the sample surveyed 72.72% have not yet availed any home loan from India, even though a majority of them is staying abroad for over 10 years. This can serve as a potential customer base for the Indian mortgage industry. The survey has covered only 78 respondents from the Middle East and US, but it has been covered earlier about NRI concentration in other parts of the world, which would provide a good customer base. Once a few of them is tracked, with good service (which for the NRIs is a major deciding factor more because of physical absence of both parties) the banks are generate more business through customer reference.

(11) 45.45% of the sampled respondents wish to avail home loan in India. The home finance companies and banks should focus on these customers on priority and address their needs. The banks should strategize to convert the wishes to needs and wants. These customers too would serve as further reference and hence business for the housing sector of India.

(12) A majority of them voted for reduce property prices. Only 18.18% wanted reduction in interest rates and 9.09% felt both options are equally feasible. This would come as a good learning for the developers who are eyeing on the NRIs for business transaction to increase.

## RECOMMENDATIONS

The observations of the responses obtained in the survey and the study in mortgage industry in general helped come up with following strategies which could be adopted by HFCs, banks and other financial institutes.

- Target Audience: The research showed that the average age group of customer has come down and is round 31. It also showed that more business men are now taking loans. The banking organizations should strategize to market the product to them. Another prospective customer base is professional segment, which needs to be addressed.
- Property type: The number of builder purchases has increased over the years and self construction cases have reduced. As a marketing strategy the institute can establish tie-ups with developers in order to access a wider customer base and in turn facilitate faster processing.
- Business Source: The research shows that a major volume of the business comes from the direct sales team of the bank. Also the survey with NRI customers shows that service of the bank is a primary deciding factor – when they avail loan. The organizations should have regular training for its sales team updating them on the product and policy, so that to improve business, service and image of company.
- Property price: In order to revive market both lenders and borrowers feel that this is the best feasible option. Though reduction has come across some areas the same has to be more wide spread.
- Risk Strategies: The impact of the fallacies in funding is can be well judged with the global impact of the US subprime crisis. The banks should review the risk strategies and the change that is having. This would help sustain growth as well as maintain healthy market.



- Expansion: The demand for housing is increasing, as is the spread in Tier I and Tier II cities. In this aspect the banks should strategize to increase its presence in those areas, thereby making funding more feasible

## ENDING REMARKS

If the banks adopt the recommendations above, the industry shall see improvement in service quality and business volume. The future studies could be based on banks that adopt these strategies and verify difference in their performance.

The research helped in identifying future prospects of the industry which are mentioned below:

- Huge demand in housing: As per statistics the population would reach 1350 million by the year 2020, for which there will be additional demand of 70 million new households.
- Rise in income level: The increase in income level will lead to change in consumption pattern and banking habits of the Indians.
- FDI: There is the lot of scope in FDI and NRI remittance which need to be tracked and addressed accordingly
- Tier II and Tier III cities: The growth is visible in every direction. The spread is reaching to Tier II, Tier III cities and other urban areas.

The overall importance can be understood from the fact that India is soon going to have a Housing Index.

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## **GLOSSARY**

CRR – Cash Reserve Ratio

SLR – Statutory Liquidity Ratio

SEP – Self-employed professional

SENP – Self-employed non professional

NRI – Non-resident Indian

GDP – Gross domestic product

HFC – Housing Finance Company

NPA – Non-performing assets

LTV – Loan to value

ROI – Rate of interest

EMI – Equated monthly installment

FDI – Foreign direct investment

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