

CHAPTER I

Housing Finance in India

1.1 *Housing Scenario*

The total housing shortage in the country in 1997 was estimated to be 13.66 million units, of which 7.57 million units were in urban areas. More than 90 *per cent* of this shortage was for the poor and low income category. Against this background, the National Housing and Habitat Policy (NHHP) was formulated in 1998 and stressed on:

- removing legal, financial and administrative barriers for facilitating access to loans, finance and technology;
- ensuring that housing, along with supporting services, was treated as a priority and at par with the infrastructure sector;
- the creation of surpluses in housing stock; and
- providing quality and cost-effective shelters especially to the vulnerable groups and the poor.

The draft National Urban Housing and Habitat Policy, 2005, while focussing on urban shelters, emphasised on the promotion of larger flow of funds to meet the revenue requirements of urban housing and infrastructure using innovative tools. It recognised that based on historical growth patterns, the urban population of India was likely to grow to 360 million in the year 2010 and to 533 million by the year 2025. The document noted the Planning Commission's projection of total requirement of urban housing during the 10th Plan period (2002-2007) of 22.44 million dwelling units including the backlog of 8.89 million units at the beginning of this Plan. With rising incomes, favorable demographic profiles, swelling middle class and rapid urbanisation, the demand is projected to rise to 73.96 million units for rural and urban areas during the 11th Plan period (2007-2012).

1.2 *Role of the National Housing Bank*

The National Housing Bank (NHB), a fully-owned subsidiary of the Reserve Bank of India, was set up in 1988 to accelerate housing finance activity in India and to promote the Housing Finance Companies (HFCs) by providing financial support to them. It acts as the apex institution and regulator of the housing finance industry.

The NHB has issued guidelines to the HFCs on prudential norms for income recognition, asset classification, provisioning for bad and doubtful debts, capital adequacy and concentration of credit investment. The NHB also conducts inspection of the HFCs to ensure proper compliance with the prudential norms and prevent the affairs of any of them being conducted in a manner detrimental to the interests of the depositors or their own. Guidelines for asset liability management system for the HFCs have also been issued by the NHB.

1.3 Scope of Audit

As on 31 March 2006, there were seven HFCs under the audit jurisdiction of the Comptroller and Auditor General of India. The performance audit conducted between June 2006 and January 2007 has covered the working of the following five HFCs for the five years from 2001-02 to 2005-06:

- (i) Housing and Urban Development Corporation Limited (HUDCO)
- (ii) BOB Housing Finance Limited (BOBHFL)
- (iii) Cent Bank Home Finance Limited (CBHFL)
- (iv) IDBI Home Finance Limited (IHFL)
- (v) PNB Housing Finance Limited (PNBHFL)

The two HFCs, *viz.*, Indbank Housing Limited and Corpbank Homes Limited, were not covered in this performance audit; the former has stopped its lending operations since 1998 while the latter was re-merged in October 2006 with Corporation Bank, its parent and promoter bank.

1.4 Audit objectives

The audit objectives were to assess:

- the trends in housing finance activity vis-à-vis those of the Central public sector HFCs during the period 2001-02 to 2005-06;
- the overall performance of the Central public sector HFCs against selected benchmarks;
- that controls relating to appraisal of applications, sanction and disbursement of loans were sound and effective, and covered the risk of lending; and
- that adequate monitoring mechanisms existed especially for timely recovery of dues and resorting to timely legal action in case of default.

1.5 Audit Criteria

Audit Criteria identified for the purpose of the performance audit for different critical activities of housing finance were:

- The cost of borrowings, net interest margin, and ratio of employee cost to the disbursements in one of the leading HFCs in the private sector, *viz.*, Housing Development and Finance Corporation Limited (HDFC) has been adopted for measuring the efficiency of the five HFCs covered under performance audit;
- System to verify credentials of borrowers and pre-disbursement conditions as laid down by the HFCs;
- Mechanism to monitor actual utilisation of funds;
- Level of Non Performing Assets; and
- Strategic guidance to deal with continuous defaults.

1.6 Audit methodology

This performance audit covered the assessment of requirement of resources, method of scrutiny of applications/ projects, procedure of scrutiny of applications including feasibility appraisal, disbursement procedures, recovery, follow-up and other legal formalities in accordance with the Issue Analysis and Study Design Matrix prepared for this purpose.

For selection of units, two risk parameters viz., level of NPAs /defaults in the unit and/or level of sanctions to private agencies were identified. Number of units selected is given in Table 1:

Table 1: Selection of Regional Offices/ Branches

HFCs	Total number of Regional Offices or Branches	Number of Regional Offices or Branches selected for audit
HUDCO	20	8
BOBHFL	23	3
CBHFL	12	5
IHFL	16	4
PNBHFL	28	6

Individual cases at unit level were selected on random sample basis with the risk parameter of level of default as the key parameter.

1.7 Acknowledgement

The performance audit started with an entry conference with the Managements of the HFCs in April 2006. The draft Audit Report was issued to the Managements in March/April 2007 and to their Administrative Ministries (Ministry of Finance and Ministry of Housing and Urban Poverty Alleviation) in April 2007. Replies from the Managements of all HFCs except BOBHFL have been received and suitably incorporated in the draft modified Audit Report, which was issued to the Administrative Ministries and Managements in September 2007. A presentation on the audit findings and recommendations was made during the meeting of the Audit Board with the representatives of the Administrative Ministries and Managements of HUDCO, CBHFL, IHFL and PNBHFL in October 2007. The replies from the Managements of all the HFCs, and from the Administrative Ministries have been received and suitably incorporated in the report. The Management of Bank of Baroda (representing erstwhile BOBHFL) replied that in view of merger of BOBHFL with it with effect from 1 April 2006, the submission of reply was not feasible. Audit acknowledges the cooperation and assistance afforded by the Managements and the Administrative Ministries at all levels at various stages of this audit.