

HOUSING MICROFINANCE: EVOLVING NEW APPROACHES FOR INCLUSIVE RURAL HOUSING

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ABSTRACT

Housing is one of the basic needs of man and is also considered a fundamental human right. It is used as a key indicator in defining the living quality among the poorer sections of the society. Hygienic and dignified living is a challenge for poor across the world and is further aggravated in case the housing is not appropriate. Not just from the fundamental rights point of view but also from the point of view of hygienic and dignified living condition it is important to improve housing conditions for the poor. Kutchra and semi-pucca houses often lack the ability to provide clean running water, sanitation, sewage removal and other amenities that are closely associated with elementary health. The study does an empirical study in the Backward districts of Maharashtra to vindicate the need for new initiatives and to provide housing to rural poor through Housing Microfinance. Though the study is regarding the HMF initiatives all over India, the scope of the empirical investigation (field study) is limited to two districts each of the backward regions of Maharashtra viz. 'Marathwada' and Vidarbha.

Keywords: Rural Housing, Housing Microfinance, New Approaches to Rural Housing, Incremental Housing, Rural Development

INTRODUCTION

Housing is one of the basic needs of man and is also considered a fundamental human right. In recent times, it is used as a key indicator in defining the living quality among the poor sections of the society. Hygienic and dignified living is a challenge for poor across the world and is further aggravated in case the housing is not appropriate. Not just from the fundamental rights point of view but also from the point of view of hygienic and dignified living condition it is important to improve housing conditions for the poor. The criticality of proper housing is most acutely felt in the rural areas, urban slums and poorer sections of the developing countries. Kutchra and semi-pucca houses often lack the ability to provide clean running water, sanitation, sewage removal and other amenities that are closely associated with elementary health. In India, specifically in

rural India, there are considerable constrains in creating decent shelter for the poor. This is further compounded by the lack of successful initiatives in creating access to housing finance.

The issue of “Affordable Housing for All” is a challenge in respect to the flow of credit as well as the pricing. The flow of credit is dependent chiefly on Government subsidies, banks and financial institutions. To meet the demand, it is important that non-grant based and non-government sustainable channels are established. But these mainstream financial institutions are restricted by issues not limited to but including credit, land title, legislations, risk mitigations. These issues are critical if the rural affordable housing finance market is to be developed and scaled.

OBJECTIVE OF THE STUDY

The study was conducted to vindicate the following hypothesis with respect to rural housing

1. There is huge unmet demand for housing credit at lower segment
2. Progressive housing or incremental housing over time is common among low income groups due to lack of access to adequate housing credit.
3. There is lack of innovative product design in housing microfinance programme. Existing products are only a scaled down version of the prevalent housing products which are not fit for the rural poor.
4. One of the major deterrents to the growth of Rural Housing is inadequacy of the prime security, viz. clear title to the land where house is to be built, which repels the bankers and other financial institutions from extending housing finance.

The analysis in this paper is expected to offer some useful understanding about low segment housing finance in the study areas.

RESEARCH METHODOLOGY

This research paper is conceptual and analytical in nature based on field survey and subsequent analysis of the survey data. The data used for this research paper is both primary and secondary in nature.

A. Primary Data

Though the study is regarding the condition of land records all over India, the scope of the empirical investigation (field study) is limited to two districts each of the backward regions of Maharashtra viz. ‘Marathwada’ and Vidarbha based on interviews with members of SHGs in villages. The two backward regions of Marathwada and Vidarbha from Maharashtra were

chosen. Beed and Osmanabad from former and Yavatmal and Wardha from the latter were selected for the survey. These districts are among the 100 most backward districts of India.

$$\text{Survey Sample} = \frac{Z^2 * (p) * (1-p)}{C^2}$$

Total Population – 2,97,18,200
Confidence Interval – 4%
Confidence Level – 95%

Where:

Z = Z value (e.g. 1.96 for 95% confidence level)

p = percentage picking a choice, expressed as decimal

(.5 used for sample size needed)

c = confidence interval, expressed as decimal

(e.g., .04 = ±4)

Total sample size thus derived was 600. Of this 150 samples were collected from each district. Total 8 villages from Beed, 20 from Osmanabad, 28 from Wardha and 24 from Yavatmal districts were surveyed for the study with an average sample of 8 households per Village.

B. Secondary Data

Secondary data was collected from various books, internet and the publications of RBI, IBA, NHB, MoRD, Census and other publications, studies and articles on rural housing and housing microfinance.

RURAL HOUSING IN INDIA

Housing always requires a larger fund in comparison to what is required to fulfil other basic necessities like food and clothing. Due to the fund requirement, housing is last on the priority list for poor and low income groups because lack of affordability. In spite of it being aspirational and having direct impact on safety, health, dignified living, socio-economic status, it has to be ignored due to lack of adequate provisions to attain it. Most of the rural people are stuck with the long, slow and laborious process of building and repairing their house to serve the bare basic need for the immediate future. Even the barest minimum is a luxury for the majority.

Apart from the huge shortage in rural housing in India, there is also a huge disparity between the demand and supply of housing units and housing finance across different social groups.

Economically Weaker Sections (EWS) and Low Income Groups (LIG) constitute about 99% of the shortage in housing (10th Plan).

Large number of EWS and LIG households are deprived of formal access to housing finance as they are unable to fulfil the eligibility criterion. Government run programs have a lot of inherent weakness in terms of implementation and people must wait for many years to get their turn in the queue. Desired results are still evasive, despite multiple efforts by the Government in introducing different methodologies in product design and implementation to make the program effective and transparent. Most of these programs are uniform in nature and lack specific customization that fits the local needs.

Major factors affecting inclusive rural housing and acting as constraints to lending institutions are given below.

- Inconsistent cash flows of the rural population, particularly for those associated with agriculture or agriculture allied activities due to vagaries of nature.
- Difficult to apply a uniform model to assess income for rural borrowers in the absence of documentary proof of income
- No special tax benefits or incentives to lending institutions
- Poor rural network of Banks as well as HFCs
- Absence of dedicated rural product and targets
- High stamp duty required for doing simple mortgage
- Difficulties in obtaining clear title deeds which can be effectively marketed as securities
- Difficulties in enforcing securities in rural areas
- Absence of title deeds jeopardize efforts to legally establish the title to the property
- High operational cost incurred by lending institutions along with the overall perception of rural business being riskier and dependent on vagaries of nature, make rural housing finance less attractive business for lenders.

HOUSING MICROFINANCE

A prominent reality which is often scarcely appreciated is that a very small share of the rural population qualifies for traditional mortgage loans, affecting the majority of rural population's ability to purchase or build their own homes through non-grant based finance. Typically, not more than 10-20% of the rural population will have the ability to fulfil the requirements laid out by traditional mortgage financiers for extending housing loans. What is even more amazing and catastrophic from a developmental perspective is that some of the most important and dynamic middle-income population virtually lacks a market-based mortgage finance sector.

In sharp contrast to traditional mortgage financiers in rural market, Housing Microfinance is not overly dependent on existence of clear title deeds, documented income proofs or income tax returns for extending credit. The current limit for unsecured financing by MFIs has been raised to one lakh by RBI. This amount is even more than the IAY subsidy. MFI in India retain title deeds more from the perspective of psychological pressure on the borrower without the intention of using the security for attaching the property or taking legal action. The primary reasons for these include

- a) Legal action is a very costly and time consuming process
- b) It not easy to execute the security in rural areas
- c) Morally difficult to take a poor person's only home or land.

“Housing microfinance has come into its own. Filling a void created by the limitations of traditional housing finance and building on the lessons of the recent microfinance revolution, housing microfinance has come of age as a discrete area of practice that intersects housing finance and microfinance.” (Daphnis and Ferguson, 2004)

Microfinance has developed mechanisms to enhance credit to low-income families in the absence of clear land title through flexible underwriting and alternative collateral. Microfinance institutions bridge the gap between conventional lending, and micro housing finance has emerged as powerful because of its ability to evaluate credit worthiness and to enforce repayments on uncollateralized loans in cost-effective way (Ferguson 1999, Baumann 2000, McLeod 2000, Erb 2000). From the borrower or household standpoint, investment will take place if there is reasonable assurance of security.

RESULTS AND SUGGESTIONS

A. Demand for Housing

More than 60% of the house-holds across the surveyed districts reported to be in semi-pucca or kutcha condition. Also, module wise there is heavy demand for upgradation of existing units.

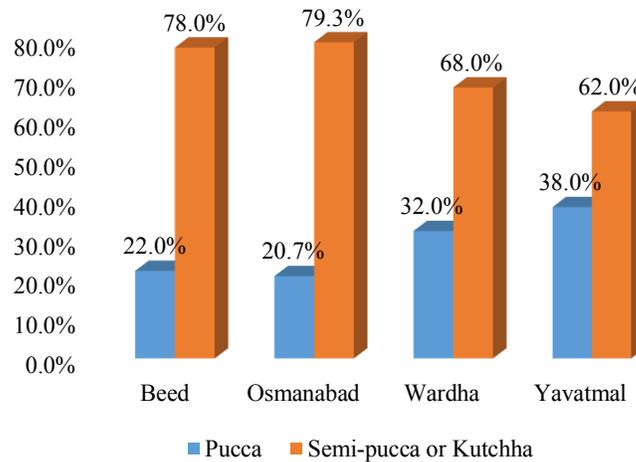


Figure 1: Condition of current housing in the sample district wise

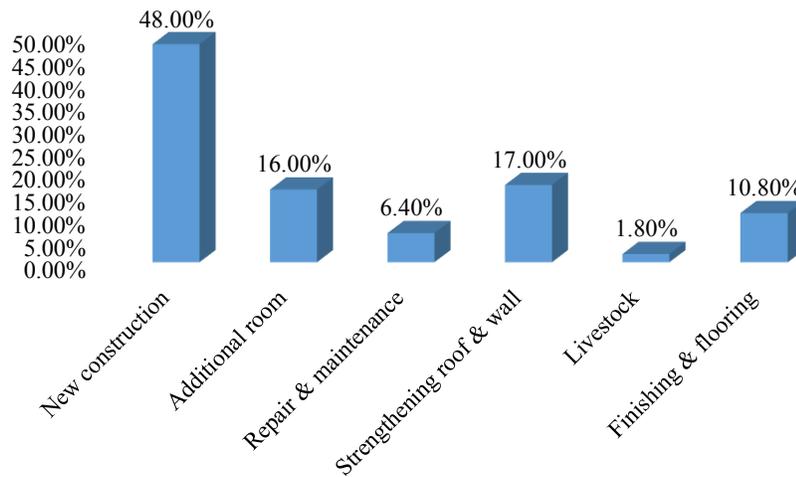


Figure 2: Demand for housing modules in sample

Building over longer period from their own savings, people are able to build the house to serve as the basic necessity, but is prone to the vagaries of nature, requiring continuous repair and maintenance. There is a huge unmet demand for housing lower segment in rural areas both for upgradation of households from semi-pucca or kuchha to Pucca or additional construction or repair and renovation. This volume of demand cannot be serviced by Government grant and subsidies alone. There is a need for formal finance market availability to service the credit requirement for the fulfilment of the demand.

B. Progressive/Incremental Housing

Quantum and tenure of a housing loan is critical for low-income groups and households with irregular income. These households due to the constraints of credit develop a tendency to build house over time referred as 'progressive incremental housing' or 'progressive/incremental build'. It implies that poor households build gradually and incrementally, a few rooms at a time (Ferguson, 2003). Housing Microfinance of small loans of a shorter tenor will suit to the housing credit need of the target groups.

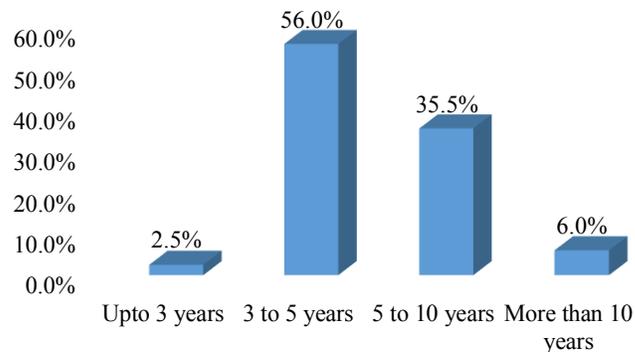


Figure 3: Tenure requirement for Housing Loans in the sample

The desired tenure by more than 90% of the respondents was between 3 to 10 years with an average of 5-6 years. This requirement of tenure can be attributed to inconsistent cash flows through rural income which cannot be predicted for long term. Thus, to align the construction to the loan amount, a modular or incremental construction is ideally suited.

Incremental housing enables the borrower to build the house progressively thereby

- Decreasing the EMI amount
- Decreasing the tenure, for which he should have assured income
- Reduced loan burden at any given time

C. Product for rural housing finance

One of the major concerns for EWS and LIG groups in rural India is access to housing finance. Though the overall disbursements of housing loans by Housing Finance Companies and Public Sector Banks has seen a CAGR of almost 30%, rural housing constituted only 8-12% of the total disbursements. Also, the proportion of rural housing loans has been stagnant at about 10% of the

total housing finance portfolio in Banks. This figure will be further lower if we exclude the rural areas closer to urban centres. Primary reason associated with lack of adequate dedicated housing finance products and focus by the lending institutions towards rural areas.

High transactions cost to lend low income group, lack of clear land titles, low profit margins, uncertainty of repossession etc. are major factors prohibiting many housing financing institutions to step into low segment housing finance business. On the other hand, there is hardly any incentive for them doing this. However, low margin and low repaying capacity in case of low segment housing credit market may not be true in all contexts. In the words of the Prof Muhammad Yunus *“Its not people that are not credit-worthy, it is banks that are not people-worthy”*.

Banks insist on clear land title, irregular income of the borrowers and their servicing capacity, quality of construction, repayment conditions and beneficiary identification processes that hardly fulfill by poor and low income groups. This has resulted in very low penetration of traditional mortgage finance market, particularly in low income housing. In India, the mortgage to GDP ratio is estimated at 2% against 51% in USA and between 15-20% in South East Asian countries. So, supply of formal housing finance to poor and low income groups is limited and selective that helped in accentuating access to housing finance in lower segment. Below is the list of constrains that deter financial institutions in extending rural housing credit along with new approaches that can be introduced to address them.



Figure 4: Reasons for lack of lender interest in rural housing along with possible solutions

D. Absence of Land Records

While many rural villagers own their homes, which they likely built themselves, they rarely own the property on which they live. Typically, in rural India, villagers are granted land from the government or live on land passed down to them from their ancestors. These land rights exist through means other than a title deed. Bruce Ferguson calls these land rights ‘para-legal title’ which he believes should be recognized by housing MFIs when disbursing a loan. This legitimizes the rights of villagers whose lack of legal title would otherwise prohibit them from obtaining a loan from formal financial institutions.

Although para-legal title serves as a reasonable proxy, it cannot be recognized on a mass scale. Lack of title prevents lenders from addressing the housing shortage issue in rural areas. A National Housing Bank (NHB) report in 2000 noted the complexity of the issue:

“The primary lending institutions have expressed that they are unable to lend more in the rural areas mainly because of absence of clear title to the land on which the house is to be constructed and non-acceptability of agricultural land as collateral security for housing. The respective State Governments will have to play a facilitating role so that the lending institutions can lend with comfort to the people in these areas.”

In the sample of our survey, almost 87% of the households did not hold any title deed.

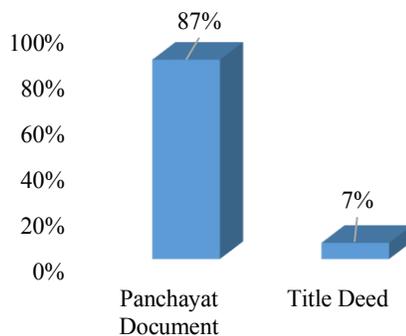


Figure 5: Availability of clear title deeds in sample area

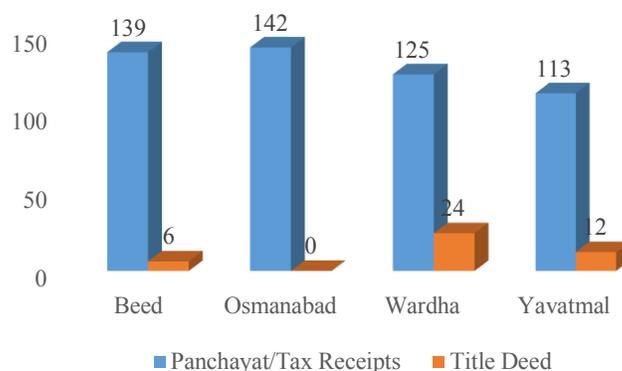


Figure 6: Availability of clear title deeds in sample area district wise

Access to land and property rights is a complex issue worldwide. The problem for those without land will remain a major challenge. The legal and administrative barriers for those with land who lack title are also daunting. In some states progress, has been made in tackling the property formalization issue. Lessons are being learned, and the technological advances in property and registry reform are dramatically lowering costs, which should accelerate the titling processes. This should in turn enhance efforts to increase the flow of housing finance to low- and moderate-income groups.

CONCLUSION

A striking but still unappreciated reality underlies most housing programs, policies, and discussions in emerging countries: only a small share of the population can qualify for a traditional mortgage. Even more amazing and catastrophic from a developmental perspective, some of the most important and dynamic middle-income population virtually lacks a market-based mortgage finance sector.

As housing microfinance is concerned, in spite of these obstacles posed by credit history and the lack of title, the existence of formal credit history a full title has not always been necessary for housing microfinance, as some MFIs have already proven. Most MFIs in India retain legal title from their clients only as a psychological deterrent, without any intention of repossessing the house in the event of default.

This study suggests that HMF (Housing Microfinance) is not a fad or the novelty du jour in international housing. To the contrary, the evidence demonstrates that HMF is one of the few recent innovations in development work that is a "natural." HMF can have great positive impact in the lives of the low and moderate income household majority, and can operate without

subsidies and is - hence - financially sustainable. It will be one of the major contributors toward inclusive rural housing.

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