



**Mainstreaming Affordable Housing
in India**

Moving towards Housing for All by 2022

August 2016





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Background and Introduction

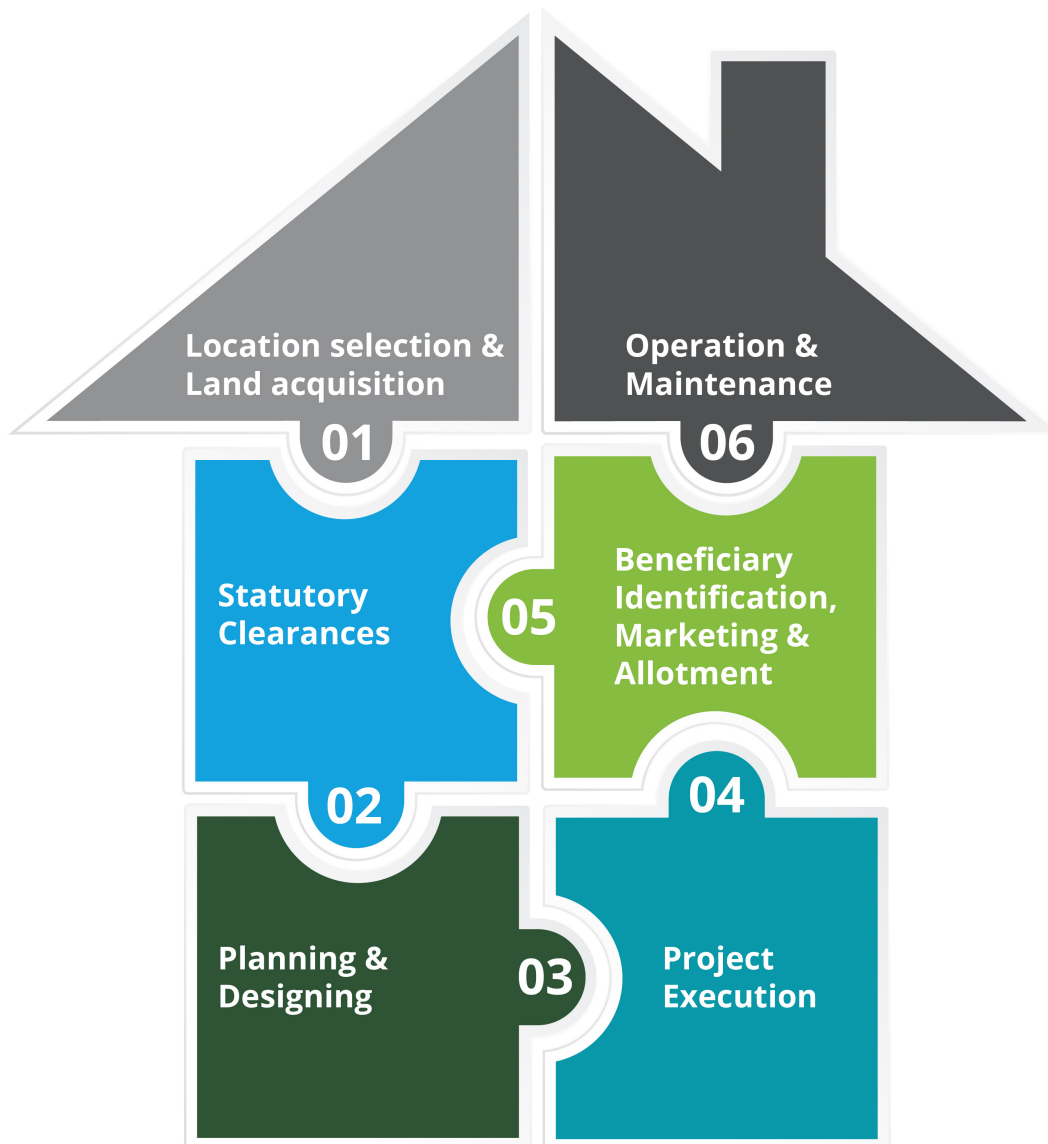
India is a rapidly urbanising country facing development challenges associated with rapid growth. One of the key challenges for a developing country like India is urban migration, which is further exacerbated by limited resources to meet increasing housing demands. The high percentage of labour migration from rural areas to cities has contributed to urban congestion, pressure on basic amenities such as water and sanitation, etc., and most of all, housing shortages in cities across India. At the national level, the government estimated a shortage of more than 18.78 million homes at the beginning of 2012, of which 95% were in the EWS (Economically Weaker Sections) and LIG (Low Income Group) segments. Further, the country's total urban housing shortage is projected to be about 30 million by 2022. This ever increasing gap between demand and supply in the affordable housing segment is forcing people to live in slums and informal settlements. It is evident that the issue, if not dealt with effectively, can have tremendous negative impact on the country's economic growth and poverty reduction efforts. Even though the urban housing shortage is primarily driven by EWS and LIG segments in India, the majority of the capacity addition has been going on in the segments beyond the reach of EWS and LIG customers. Real Estate developers and private players are focusing primarily on MIG and HIG segments owing to the higher returns from these projects. On the other hand high land costs, delay in project approvals, increasing raw material costs and low profit margins have made low-cost housing projects less attractive to the private developers. Also, housing (including Affordable Housing) being a state subject creates complexities in implementation because of precarious financial condition of development authorities, state/city-level agencies and their limited capacities in handling in these projects.

To successfully build India's Affordable Housing, collaboration between the central government ministries, state governments, urban local bodies, civil society, private sector, and financial institutions is essential. The collective agenda must advance the efficiency of affordable housing sector at an optimally low cost, while maintaining safety standards and basic amenities. To mainstream affordable housing,

the government needs to predominantly act as an enabler for development and be involved in facilitating investments, both public and private, and streamlining processes across the value chain. Stakeholders will benefit from the availability of suitable land parcels with the requisite trunk infrastructure, expedited clearances, and an adequate organisation of financing. Moreover, for the planning and design process to transition smoothly into project execution, it is important that the development authorities have requisite capacity to handle projects of this type and scale which seems to be lacking. Lack of availability of suitable financing options for beneficiaries who predominantly work in informal segments is another bottleneck for mainstreaming of affordable housing in India. Furthermore, it is equally important that awareness amongst the intended beneficiaries increases to bring them into the fold of formal banking sector.

Another key aspect that is widely neglected while planning an Affordable Housing Project is the maintenance post hand over of units to the customers/beneficiaries. This eventually creates 'New Urban Slums' and defeats the purpose of creating these assets in the first place. It is of utmost importance to address this aspect to create sustainable benefits of creation of these assets. The Government of India in its schemes has taken many steps to boost the sector, but challenges still remain. For instance, while Rajiv Awas Yojana (RAY) envisaged an O&M fund for maintenance of assets created under the scheme with a onetime contribution from the central government, it could not be implemented at a wider level. Further, this feature is absent in the PMAY (Pradhan Mantri Awas Yojana) We need to keep in perspective that Affordable Housing Projects will cater to a much needed highly productive economic workforce in the country. It is imperative that both public and private sector join forces and drive innovations for developing sustainable habitats and vibrant communities. This document highlights some of the key issues and challenges of the sector and measures that can be thought to address these shortcomings and create an enabling environment to achieve Gol's goal to achieve housing for all by 2022.

The Affordable Housing sector ecosystem



From need identification of the project, location selection to sustainability and maintenance, the value chain identifies all the stages of an Affordable Housing Project. However, to understand the bottlenecks to a wider implementation of Affordable Housing Projects, it is essential to understand stake holders perspective. Going beyond the value chain, one needs to look at the macro and micro policy environment, market actors for goods and services in the sector, and most importantly the people and the communities being created. It is of utmost significance to look at the issue holistically and design interventions to address the concerns/ shortcomings of various stakeholders ranging from development authorities, governments, developers, contractors, material and technology providers, Financial institutions, NGOs, beneficiaries to asset management firms (for O&M).

Critical Issues & their significance



There are various factors affecting the pace of affordable housing development in the country and restricting private sector participation in the sector. Examining the value chain of an Affordable Housing Project helps identify these critical issues and the corresponding bottlenecks. While doing so, it is important to critically examine the stakeholders involved in various activities and get a holistic understanding of the issues from stakeholders' perspective. The key factors emerging from a close examination include the following:

1. Improper selection of land parcels for AH projects

- Lack of availability of suitable land parcel within city limits
- High prices of land discouraging developer driven projects
- Lack of employment opportunities in the vicinity discouraging people from staying in these units
- Lack of External trunk infrastructure, Social infrastructure and Connectivity through public transport options, increasing the cost of living thereby resulting in lower occupation

2. Lengthy statutory clearance & approval processes

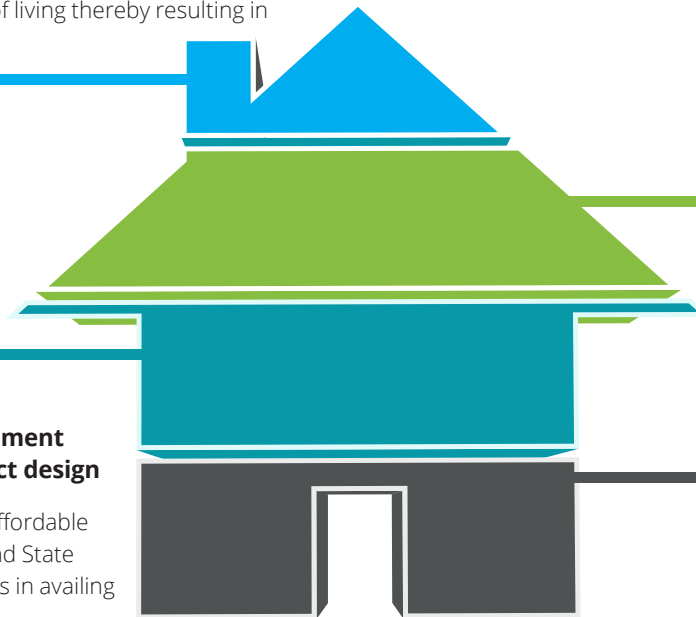
- Over 20-30 clearances needed for each housing project, that too from multiple authorities
- Takes over 2 years for obtaining all the approvals, increasing the gestation period and project cost

3. Shortcomings in development norms, planning & project design

- Incongruence between the affordable housing policies of Central and State governments creating hurdles in availing the benefits of GoI schemes
- Restrictive FAR norms, density norms which make the affordable housing segment unattractive
- Insufficient action in providing social and external connectivity infrastructure by the concerned authority

4. Lack of participation of large organised real estate players

- Low profit margins
- High sensitivities to changes in input costs, project delays, etc.
- Lack of availability of skilled manpower



Other critical challenges

5. High cost of construction finance

- High cost of funds for construction finance (Developers in this segment are typically city/region specific having limited bandwidth) making these projects unviable
- Lack of suitable credit enhancing financial products for developers

6. Lack of a suitable mechanism for maintenance

- Negligence in maintenance of Affordable Housing units creating 'New Urban Slums'
- Lack of sufficient funds/Institutional mechanism to facilitate the required maintenance

7. Lack of access to credit (beneficiaries)

- Irregular, informal income sources with variations due to seasonality
- Risk management practices, cost structures of Banks, HFCs not aligned to these kind of customers
- Higher lending rates (small loan size, higher perceived risk)
- Lack of awareness among customers about financing options and Govt schemes such as Credit Linked Subsidy Scheme (CLSS)



8. Challenges in Beneficiary selection

- Beneficiaries do not relocate to the units allotted to them (location not suited to their occupation)
- Challenges in beneficiary selection process
- Lack of a beneficiary database to facilitate AH developers/ FIs to identify their target customers

9. Capacity constraints

- Inadequate capacity of implementing agencies
- lack of private participation, beyond land arbitrate models and guidance documents for PPP in the sector such as Model Concession Agreements/ guidelines
- Lack of mainstreaming of low cost technologies to achieve economies of scale



Government of India Initiatives & Interventions



Affordable Housing has been one of focus areas for the government over the past few years. The following are some of the policies, programmes, and initiatives undertaken by the GoI in Affordable Housing sector:

01. Pradhan Mantri Awas Yojana (PMAY- 2015): To address the shortcomings of the erstwhile programs and to evolve an all-encompassing scheme, The Pradhan Mantri Awas Yojana (PMAY) was launched in June 2015 to build 20 million houses for individuals who fall under EWS and LIG categories. In order to address the shortfall, the scheme envisages to tackle the issues through four models: In situ Slum Redevelopment, Affordable Housing in Partnership and Subsidy for beneficiary-led individual house construction and Credit linked subsidy. In addition, it has suggested policy reforms to implementing agencies.
02. External Commercial Borrowing (ECB) has been allowed for affordable housing projects from 2012 to enable lower interest cost for developers and ensured better capital availability for developers of low-cost housing. In 2013, the parameters for extending ECB to Slum Rehabilitation Projects, were outlined.
03. Opening up of Foreign Direct Investment (FDI) for development of townships, housing, built-up infrastructure and construction-development. However, not much traction has been seen in the Affordable Housing segment till date.
04. The Central Board of Direct Taxes (CBDT) has extended the benefits of section 35AD (permitting 150% of capital expenditure as tax deduction) of the Income Tax Act, 1961 with effect from assessment year 2012-13 to affordable housing. . However, practically, there were no takers of this scheme as developers / builders have minimal costs capitalized in their books as capital costs. Major chunk of costs is represented by housing units as inventory / stock in trade not as capital asset in order to be eligible to claim the benefit of investment linked incentive.

05. In addition to the service tax exemptions already available, Construction of the following has been exempted from service tax from 1 March 2016:

- Low cost houses up to a carpet area of 60 square meters in a housing project under 'Affordable Housing in Partnership' component of Housing for All (Urban) Mission / Pradhan Mantri Awas Yojana
- Low cost houses up to a carpet area of 60 square meters in a housing project under any housing scheme of the State Government

06. The Credit Risk Guarantee Fund with a corpus of Rs 1200 Cr in collaboration with NHB was set up (2012) to facilitate credit availability to low income customers without any collateral. The purpose is to guarantee the lending agencies for loan to LIG/EWS borrowers for loan amount up to INR 8 lakhs and unit size not exceeding 430 sq.ft, thereby reducing the perceived risks for the lending institutions and catalyze the flow of credit to low income housing sector.

07. Urban Housing Fund Refinancing Scheme with a corpus of Rs 2000 crores in the year 2013-14 has been created. The purpose of this scheme is to provide refinance assistance in respect of loans extended by HFCs to public agencies, private agencies, developers, builders for their AH projects. The arrangement is applicable for slum improvement/ rehabilitation as well as for AH projects where unit costs do not exceed INR 30 lakhs. The tenure of the refinance under the Scheme will be co-terminus with the PLI's loan to the agency subject to maximum tenure of 5 years.

08. Tax free bonds are issued by HUDCO and NHB to ensure lower cost of borrowing by them and in turn reduce their onward lending costs.

09. Efforts in increasing the ease of doing business especially in obtaining construction permits in urban areas has been stepped up and several initiatives undertaken. For example, Single Window clearance has been initiated through an integrated online portal in select cities.

10. Recent amendments to the Finance Act (2016) have introduced a 100% tax holiday to affordable housing subject to the following conditions:

- Project approved by competent authority after 1 June 2016 but on or before 31 March 2019
- Project is completed within 3 years from date of approval and certificate of completion of project as a whole to be obtained from competent authority
- Build up area of commercial establishments not to exceed 3% of the aggregate built-up area
- Plot of land measuring not less than 1,000 sq. mts. in case of metro cities / within 25 kms from metro cities and not less than 2,000 sq. mts. in case of other cities
- Size of the residential unit is not more than 30 sq. mts. in case of metro cities / within 25kms from metro cities and 60 sq. mts for other cities

11. The Government (in the Budget for FY 16-17) has also considered the needs of the buyer and allowed an additional deduction up to INR 50,000 in respect to interest for first time home buyers. Also the time period for acquisition/construction is enhanced to 5 years. In addition to the above, the central government and select state governments have initiated a number of positive and reinforcing measures to give a fillip to the affordable housing sector.





Unfinished Agenda

To advance the Affordable Housing sector and help gain a much needed momentum, interventions should not be planned in isolation but rather a multi-pronged approach should be adopted to address the shortcomings at various stages of the value chain and build a supportive ecosystem. Although the Government of India has taken many steps in the right direction, there are areas of improvement to transform the sector canvas to a vibrant and delivery-oriented landscape, as listed below. It is imperative that both public and private sector come together and drive innovations for developing livable habitats and vibrant communities.



Policy and Institutional interventions to strengthen Project planning and kick-start at a solid ground:

- **Synchronization of State policies with Central policies for Affordable Housing**
 - Alignment of State Affordable Housing policies with Gols Affordable Housing policies to eliminate bottlenecks in availing central incentives as well as ensuring compliance with the State policies, required for approval purposes at state/ city level.
- **Strengthening Beneficiary Database**
 - Strengthening/ creation of a city-wise database for EWS/LIG beneficiaries identifying their income levels, occupation, family size, and prospective work locations. The database to be made available to FIs and developers to help them understand, reach out to their prospective customers and also ensure transparency in allocation of housing units
 - Facility for potential EWS/LIG customers to register themselves with a state level/city level agency and to express their interest to procure an Affordable Housing unit
- **Enhancing the capacities of Implementing Agencies**
 - Preparation of guidelines and framework to assist implementing agencies at state/ city level in effectively managing/ executing Affordable Housing projects.
 - Capacity building of implementing agencies to enable them get a thorough understanding of the complete life cycle of projects developed through new modes of project development e.g. Public Private Partnerships (PPPs), which is one of the key focus of PMAY (i.e. Affordable Housing in Partnership).
 - Preparation of a set of guidance documents such as model bidding documents and concession agreements which could serve as base documents for implementation agencies, thereby saving efforts, time, cost and avoiding implementation issues.

Enhancing the Project execution ecosystem

- **Capacity building of developers**
 - Promotion of knowledge sharing platforms/ forums to help developers understand the best practices/models adopted in other states, adoption of low cost construction technologies and workable solutions to reduce construction costs, among others.
 - Awareness generation about low cost technologies already piloted and demonstrated. Provision of guidance on rates and costs through authorized agencies (such as PWD Schedule of Rates)
- **Capacity building of construction manpower**
 - Eliminate the bottleneck in mainstreaming new technologies by providing appropriate training and skilling the construction manpower in emerging and low cost technologies and developing a pool of skilled manpower.
 - Developing and implementing new certification programs to ascertain the skill of supervisory and managerial workforce in low cost and emerging construction technologies.
- **Access to low cost Construction Finance**
 - Mechanism to evolve a developer rating system (even for small, regional developers) based on completion of similar projects in the past to reduce the perceived risk by FIs and lower the cost of construction finance
 - Development of financial products for credit guarantee/enhancement of small developers/Affordable Housing projects or setting up/ wider implementation of credit guarantee initiatives.
 - Evolve a mechanism to consider this Guarantee fee (for credit enhancement) as a part of mandatory CSR contributions (as per companies act 2013) of companies



Improving access to credit to beneficiaries

- Housing finance
 - Mainstreaming of customer oriented/ customized credit appraisal mechanism and operational processes for informal segment.
 - Removal of 5% cap for finance to HFCs (under Priority Sector Lending norms)
 - Expanding Savings and Subsidy Linked Housing Finance (SSHF) & similar financial products so as to use savings as a proxy for estimating the credit worthiness
 - Guarantee fee payments for Credit Risk Guarantee Fund Trust may be included in the list covering mandatory CSR contributions. This would reduce the burden of this fee on the AH beneficiary
 - Development of a secondary mortgage market such as securitization to ease financial pressure on lending institutions and increase their lending capacity
 - Mandating a portion of project funds to be utilized in establishing a help desk to improve financial literacy of the beneficiaries and create awareness about GoI schemes and financing availability from formal finance sector.

Establish long-term sustainability mechanisms- Operation & Maintenance

- Mechanism for O&M
 - Further to the directions of PMAY, setting up of a Resident Welfare Association (RWA) for external maintenance of AH units should be made mandatory for the project developer.
 - Transferring maintenance responsibility to a specialized 'Asset Management Firm' with annuity payments from the Authority could be considered.
 - Evolving private participation models where developers are mandated to undertake maintenance activities for a longer period (e.g. 7-10 years) with corresponding annuity payments from the authority (Annuity payments only to cover maintenance costs).
 - Creation of a revolving maintenance fund with an initial corpus fund (could be included in the project cost) to cover maintenance costs for a long period.
 - Periodic audits of the quality of assets created along with maintenance audits



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