

Aadhar Housing Finance Ltd.

COMPANY BACKGROUND

Aadhar Housing Finance Ltd. (AHFL) enables home ownership for low- and lower middle-income households in India. Established in 2011 as a registered Housing Finance Company (HFC), AHFL is regulated by India's National Housing Bank. This new company is a joint venture by IFC and IFC client Dewan Housing Finance Corporation Ltd. (DHFL). DHFL has over 26 years of experience in home loans to 160,000+ low- and middle-income households. DHFL and its subsidiary, DHFL Vysya Housing Finance Ltd., are majority stakeholders in AHFL while IFC holds a 20% equity stake.

Country: India

Sector: Housing Finance

IFC's Investment: \$4.5 million in equity

In its first five years of operation, AHFL will target India's underserved low-income states of Bihar, Madhya Pradesh, Uttar Pradesh, Orissa, Chhattisgarh, and Jharkhand.

DRIVERS FOR AHFL'S INCLUSIVE BUSINESS MODEL

- Growing demand for and supply of affordable housing, including through self-construction
- Increasing demand but limited availability of housing finance for low-income customers
- Government incentives—including interest rate subsidies and refinancing—for affordable housing lenders
- Home ownership tax incentives for individuals

Urbanization, the growth of nuclear families, and rising incomes are boosting demand for housing in India, but there is an estimated housing shortage of 72 million units. One-third of the shortage in urban areas is in low-income states, while 99% is experienced by low-income households. In 2007, to reduce this housing deficit, the Government of India released the National Urban Housing and Habitat Policy to achieve the national goal of affordable housing for all. Resulting government incentives are helping to increase the stock of affordable housing. But as demand currently outstrips supply, many low-income households will need to construct their own homes.

The growth in affordable housing—whether ready-made or self-constructed—is, in turn, fueling demand for housing finance. But housing finance for low-income customers and in low-income states remains underpenetrated for several

reasons. First, HFCs and banks favor middle- and high-income customers in states with dense urban populations. Second, private banks focus on higher interest personal loans than on home loans. Third, public sector banks in low-income states prefer customers who need larger housing loans than AHFL's target segment, and are also slow and selective. The government is, therefore, seeking to increase housing finance penetration through favorable refinancing and interest rate subsidies for lenders. The Reserve Bank of India has, for example, categorized housing loans up to Rs.2 million (\$40,000) as a priority sector. The demand for housing finance is also being fuelled by changes in tax deduction limits. Principal repayments of up to Rs.0.1 million (\$2,000) and interest payments of up to Rs.0.15 million (\$2,940) are now allowed as deductions from individuals' gross taxable income.

AHFL'S INCLUSIVE BUSINESS MODEL

Providing housing finance to low- and lower middle-income customers in India poses several challenges for lenders. These customers may not have identity cards or income statements. They often construct their own homes, requiring special technical appraisal. Their loan repayments can be affected by irregular cash flows. And unclear land titles can cause legal issues.

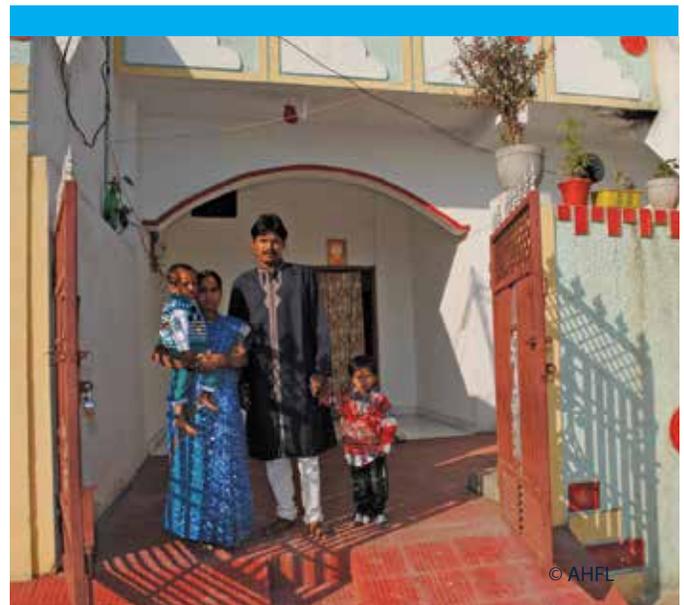
AHFL has found ways to address these challenges to provide housing finance to this target segment.

More than half of AHFL's customers have an average monthly household income between Rs.5,000 (\$100) and Rs.20,000 (\$400); 75% are salaried and 25% are self-employed; and 30-50% of customers live in urban areas, 10% in rural areas, and the remainder in semi-urban areas. Salaried borrowers are typically low pay grade employees such as drivers, police constables, and government school teachers. Self-employed borrowers, whose average monthly income is Rs.10,000 (\$195), are generally small merchants, commodity traders, garage owners, mechanics, general store owners, and agriculture workers.

AHFL offers home loans for three purposes: purchase of a house or apartment for residential use, purchase of a plot of land and construction of a home on it, and improvement or expansion of an existing home. As a benefit, AHFL offers borrowers free insurance to cover property, risk of accidental death, permanent injury that impairs earning capacity, or job loss for a limited period. Loans are between Rs.0.1 to 0.6 million (\$2,000 to \$12,000), but may not exceed 80% of the property cost or 75% of the land cost. The average home loan size is Rs.0.49 million (\$9,800). Approximately 55% of AHFL's customers seek loans to purchase ready-made homes, while 25% seek loans for self-construction. Loan amounts are based on applicants' repayment capacity, age, educational qualifications, stability and continuity of income, number of dependents, co-applicant's income, assets, liabilities, and saving habits among other factors. The maximum loan tenure is 20 years; however, it is limited to the retirement age of 60 years for salaried borrowers and

65 years for self-employed borrowers who do not have a retirement age limit. Interest rates range from 11% to 14.5%. AHFL charges 1.5% of the loan amount as a processing fee.

Home loan applications are processed according to housing finance industry standards in a four-step process that includes an initial assessment, pre-approval, security assessment, and final disbursement. Initially, AHFL has a personal discussion with the applicant/co-applicant and verifies mandatory information such as identity, income, bank account, and credit record. Property details and the validity and enforceability of the title being mortgaged are also checked. AHFL finally conducts a field-level verification of the applicant/co-applicant's residence and place of work. Many low-income customers, however, lack formal borrowing histories and face challenges in providing standard documentation. AHFL may thus waive



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some requirements or accept alternative documentation. For example, women applicants, as well as co-applicants who are illiterate or semi-literate may provide a notarized photo affidavit to confirm identity. When customers cannot provide standard income documents, AHFL verifies income through field visits. AHFL assess the reputation, business, and finances of a salaried applicant's employer or the sales and purchase records of a self-employed applicant.

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Once an applicant clears the assessment, AHFL issues a pre-approval letter to proceed to the security assessment. AHFL's lawyers evaluate property documents to determine if there is a clear and marketable title to the property being financed. Thereafter, AHFL staff conduct a technical appraisal of the property. For self-construction, details such as government approval of land for residential use, adherence to construction guidelines, and reasonable construction cost are checked. AHFL disburses self-construction loans in stages linked to actual progress to ensure proper use of the loan.

AHFL's loan collection system makes repayment easier for low-income customers and efficient for the company. Customers may opt to repay loans through post-dated checks (PDCs) or electronic deduction by their employers



from their salaries, if available. In the case of PDCs, customers give AHFL checks in 36-month equal installments with future dates, and the company deposits one check each month.

Customer interaction and education are AHFL's preferred means to engage low-income customers. The company holds periodic awareness-raising events at workplaces, events with lawyers and architects to discuss technical and legal issues, as well as events at weekly village markets. In addition, AHFL joins forces with banks, home construction material companies, government housing agencies, and affordable housing developers to promote home loans.

RESULTS OF AHFL'S INCLUSIVE BUSINESS MODEL

- 1,613 applications worth \$18.7 million approved, of which 861 loans worth \$8.8 million disbursed in AHFL's first 10 months of operation
- In 2011, 50% of loans to customers with monthly incomes of less than \$400
- 15 branches in 6 states servicing 35 locations

In 2011, its first year of operation, AHFL received more than 3,200 applications from low-income households in four low-income states. AHFL disbursed 861 new loans worth \$8.8 million in that year, and processed loan applications on average within 15 days. Approximately 50% of loans were to customers with monthly incomes between Rs.5,000 (\$100) and Rs.20,000 (\$400). The company estimates that 60% of loans were to customers in semi-urban areas, 30% to customers in urban areas, and 10% in rural areas. AHFL also established 15 branch offices in six states with a staff size of 96.

The company is building strategic partnerships with public sector banks, state-level housing agencies, and affordable

housing builders to expand its reach in underserved geographies. AHFL also provides loans to customers purchasing properties built through the Rajiv Awas Yojna, a government program to build affordable housing in urban areas, under the government's flagship Jawaharlal Nehru National Urban Renewal Mission.

In 2012, AHFL expects to disburse 2,400 loans worth \$24 million, with 50% to customers with incomes less than Rs. 20,000. The company plans to expand to 15 branches servicing 35 locations in low-income states by March 2012, and to grow its staff size to 150 by the end of 2012.

IFC'S ROLE AND VALUE-ADD

IFC's Investment: \$4.5 million in equity
Investment Year: 2010

- Catalyze development of AHFL by bringing on board IFC client DHFL as a strategic partner and investor to launch a joint venture in housing finance
- Enable AHFL to gain access to wider sources of competitive debt financing
- Mobilize equity from other private sector investors and support AHFL in seeking refinancing from the National Housing Bank in India
- Advise AHFL on responsible financing practices and corporate governance, as well as develop education modules for first-time borrowers

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For more information, visit ifc.org/inclusivebusiness and aadharhousing.com