ASSESSING RISK

Home loan firms target self-employed segment

Lenders look for new ways to assess credit risk for self-employed customers as they aim to grow their portfolios

BY VISHWANATH NAIR
vishwanath.n@livemint.com

MUMBAI

Small and medium-size housing finance companies are looking for newer ways to assess the creditworthiness of the self-employed, as they try and expand their lending to this segment as a way to grow their home loan portfolio.

The self-employed are often considered to be higher-risk customers due to the lack of a certified income proof. As a result, rates offered to these customers are 100-200 basis points higher than the average interest rate charged by home loan companies. One basis point is one-hundredth of a percentage point.

Higher-rate loans mean additional margins for these firms if they can find a way to manage the risk.

To do this, these finance firms are now increasingly monitoring income surrogates to assess creditworthiness. These surrogates could be anything from sales invoices from their business to their average bank balances to the outlook for the business they are in.

These indirect ways of assessing income give an idea about the person's monthly repayment ability, which, in turn, is used to work backwards and arrive at a loan amount.

"The idea is to look at self-employed customers in smaller towns which are not covered well by banks and housing finance players. The value of the houses are low and chances of default are less," said Anil Kothuri, president and head of retail finance, Edelweiss Capital.

Kothuri says that presently, two out of every three new customers who come to Edelweiss for home loans are self-employed.

While the average home loan interest rate charged in the company is at around 12%, for self-employed customers, this can go up to 14%, he added.

Typically, banks and larger housing finance companies function in the salaried individuals market, which is considered to be a safer customer segment. In case of self-employed customers, these institutions only consider those with a proven track record and a minimum of three years of income tax returns.

In the case of Dewan Housing Finance Ltd, the share of loans to self-employed customers stands at about 20% of its ₹53,795 crore home loan book. The company takes into account any transactions by the borrower which may reflect in banking channels in order to assess the customer's cash flows.

Still, Harshil Mehta, chief executive officer of Dewan Housing Finance, says that lenders need to be very prudent while growing their home loans in the self-employed space due to the higher risk involved.

The company has not seen stress arising from this segment owing to its cautious approach, said Mehta.

Sachin Chaudhary, national business head at Indiabulls Housing Finance, has a different view. Chaudhary believes that independent assessment of income surrogates actually paints a clearer picture about the client's financial position compared to traditional income proofs, which can be inflated.

"Assessment of actual cash flows in income surrogates reflects the financial health of the applicant, making it a better profile for the lender," Chaudhary said.

Presently, self-employed customers contribute about 35% of the ₹54,022 crore outstanding home loan book at Indiabulls Housing. While assessing these customers, the company looks at financial documents such as income tax returns, balance sheets and profit and loss accounts of their businesses.

"However, a small portion of approximately 20-25% of such profiles is also assessed on their cash flows reflecting in bank statements and industry-specific profit margins," Chaudhary said.

The home loan segment is considered relatively safe as it is backed by property and this may be one reason why lenders are willing to take on additional risk.

According to estimates by rating agency Icra Ratings, the average gross non-performing assets ratio of housing finance companies stood at about 0.7%, as on 31 March.

The home loan industry had exceeded ₹10.6 trillion in total, as on 31 March, according to ICRA Ratings. Of this, about ₹4 trillion came from housing finance companies.

"Among the banking and financial institutions segment, housing loans have traditionally been one of the safer asset classes in India. This is partly due to the fact that housing loans are extended largely to salaried first-time home-owners mostly for residential purposes and not really for speculative ones. Having said this, any significant broad-based correction in real estate prices over the near-mid term (though this is not the base case assumption) can materially impact asset quality of housing finance companies," said Cyrus Dadabhoy, senior analyst, financial institutions group, India Ratings.

Presently, the housing finance industry is dominated by banks such as State Bank of India, Bank of Baroda and Bank of India, which have a big retail portfolio largely propped by home loans. Among housing finance firms, the market is dominated by Housing Development Finance Corp. Ltd and LIC Housing Finance.

However, since this segment remains one of the faster-growing home loan segments, smaller firms and new entrants are trying to make a dent in the market. Between July 2014 and July 2015, housing loans grew by 17.8%, according to data from the Reserve Bank of India.