REAL ESTATE AND CONSTRUCTION

Bridging the Urban Housing Shortage in India

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Foreword from KPMG in India

By 2050, 900 million people will be added to Indian cities\(^1\). The rapid pace of urbanisation owing to the rural–urban migration is putting a strain on the urban infrastructure in these cities. As urban development takes place, a growing concern for India’s urban planners is the massive urban housing shortage plaguing the country. The shortage, prominent within the EWS (economically weaker sections) and LIG (lower income groups), is estimated at 18.78 million households in 2012\(^2\).

A thrust on encouraging private sector participation in affordable housing, traditionally the domain of the Government, could provide the answer to India’s urban housing predicament. But as things stand, affordable housing remains a challenging proposition for developers. Issues continue to persist in land availability and pricing, project approval processes and other areas which make low cost housing projects uneconomical for private developers.

Making affordable housing work in India necessitates the active involvement of all the stakeholders concerned. Radical thinking on the part of the Government can provide the much needed fillip to affordable housing development in the country. Steps such as establishment of a single window clearance system, formulation of innovative micro mortgage lending models and tax subsidies would encourage private sector involvement. The developers, on their part, need to adopt innovative and low-cost technologies which could enable them to deliver affordable houses quickly and cost-effectively.

Given this backdrop, the study: ‘Bridging the Urban Housing Shortage in India’, a joint effort of NAREDCO and KPMG in India, discusses at length on the rising trend of urbanisation in India and the looming urban housing shortage. It further deliberates on the constraints faced by real estate developers in their bid to bridge the gap through affordable housing. Finally, the study dwells on the measures that can be taken by various stakeholders which can make housing affordable for the urban masses in India.

Richard Rekhy  
CEO, KPMG in India

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1. Urban Infrastructure in India, FICCI, October 2011  
2. Report of the Technical Urban Group (TG-12) on Urban Housing Shortage 2012-17, Ministry of Housing and Urban Poverty Alleviation, September 2012
Foreword from NAREDCO

India’s urban population registered a decadal growth of 32 percent rising from 285 million to 377 million between 2001 and 2011\(^3\). It is opined that this trend is likely to persist on the back of robust economic development across the country. Given this scenario, it becomes critical to fill the existing gaps in the country’s strained urban infrastructure and in particular, housing. Primarily, it would be important to address the need in the EWS (economically weaker sections) and LIG (lower income groups), which currently account for 95 percent\(^4\) of urban housing shortage in the country.

Furthermore, 10 Indian States contribute to three-fourths of the urban housing shortage.\(^5\) By providing affordable housing, the real estate sector can play a pivotal role in urban development of these states as well as the country. However, as things stand, the real estate sector faces considerable headwinds. Rising cost pressures and a difficult regulatory scenario are among the primary concerns.

State and Central Government support in the form of liberal regulations and inclusive growth policies could provide the means to harnessing the full potential of affordable housing in the country.

The study prepared by National Real Estate Development Council, the apex body of real estate industry, in conjunction with KPMG in India details the constraints for affordable housing and suggests viable and practical solutions which could help the country in mending the gap.

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\(^3\) Census of India 2011; KPMG in India analysis
\(^4\) Report of the Technical Urban Group (TG-12) on Urban Housing Shortage 2012-17, Ministry of Housing and Urban Poverty Alleviation, September 2012
\(^5\) Report of the Technical Urban Group (TG-12) on Urban Housing Shortage 2012-17, Ministry of Housing and Urban Poverty Alleviation, September 2012, KPMG in India analysis
Urban Housing Shortage in India
Urban population set to outgrow overall population growth

India’s urban population has grown at a CAGR of 2.8 percent over 2001-2011, resulting in an increase in the urbanization rate from 27.8 percent to 31.2 percent.\(^6\) Out of India’s 1.21 billion population, 377 million people are urban dwellers.\(^6\) The Federation of Indian Chambers of Commerce (FICCI) estimates that by 2050, the country’s cities would witness a net increase of 900 million people.\(^7\) Furthermore, over 2012-2050, the pace of urbanization is likely to increase at a CAGR of 2.1 percent – double than that of China.\(^8\)

With the country’s agriculture sector having a limited absorption capacity, majority of the growth in urbanisation is expected to be a consequence of rural-to-urban migration. Post economic liberalization, India’s manufacturing and services sector has seen an influx in employment from the rural youth. With the country expected to witness rapid industrialization, the trend of migration from rural to urban areas is likely to continue.

Looming housing shortage in urban India

Growing concentration of people in urban areas has resulted in an increase in the number of people living in slums and squatter settlements. Skyrocketing prices of land and real estate in urban areas have induced the poor and the economically weaker sections of the society to occupy the marginal lands typified by poor housing stock, congestion and obsolescence. It is apparent that substantial housing shortage looms in Urban India and a wide gap exists between the demand and supply of housing, both in terms of quantity and quality.

According to a report submitted by a technical committee to the Ministry of Housing and Urban Poverty Alleviation (MHUPA), India’s urban housing shortage is estimated at nearly 18.78 million households in 2012.\(^9\) Besides those living in obsolescent houses, 80 percent\(^9\) of these households are living in congested houses and are in requirement of new houses. The report also highlights that nearly one million households are living in non-serviceable katcha houses, while over half a million households are in homeless conditions.\(^9\)

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\(^6\) Census of India 2011  
\(^7\) Urban Infrastructure in India, FICCI, October 2011  
\(^8\) Opportunities in an Urbanizing World, Credit Suisse, April 2012  
\(^9\) Report of the Technical Urban Group (TG-12) on Urban Housing Shortage 2012-17, Ministry of Housing and Urban Poverty Alleviation, September 2012
Of the total urban housing shortage, nearly 62 percent houses are self-owned, while 38 percent families live in rented homes. The below table illustrates the break-up of housing shortage in both these categories in urban India:

<table>
<thead>
<tr>
<th>Tenure</th>
<th>Number of families living in old houses</th>
<th>Families living in katcha houses</th>
<th>Number of families living in congestion</th>
<th>Families without homes</th>
<th>Total Urban housing shortage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Self-owned</td>
<td>1,395,735</td>
<td>770,817</td>
<td>9,188,746</td>
<td>326,430</td>
<td>11,681,728</td>
</tr>
<tr>
<td>Rented</td>
<td>870,417</td>
<td>219,183</td>
<td>5,700,019</td>
<td>203,570</td>
<td>6,993,189</td>
</tr>
</tbody>
</table>

Source: Report of the Technical Urban Group (TG-12) on Urban Housing Shortage 2012-17, Ministry of Housing and Urban Poverty Alleviation, September 2012

10 States contribute to three-fourths of the urban housing shortage

The State-wise data shows a mixed picture where both developed as well as less developed states have families living in poor housing conditions. Uttar Pradesh has a housing shortage of over three million homes followed by Maharashtra (1.97 mn), West Bengal (1.33 mn), Andhra Pradesh (1.27 mn) and Tamil Nadu (1.25 mn). The top 10 states, in terms of urban housing shortage, contribute to 14.3 million or 76 percent of housing shortage. 10
Affordable housing – The order of the day

India’s urban housing shortage is being primarily driven by the EWS and LIG categories. However, majority of the housing supply that has been built across urban India is beyond the affordability of the EWS and LIG segment. Real estate developers, private players in particular, have primarily targeted luxury, high-end and upper-mid housing segment owing to the higher returns that can be gained from such projects. Further, high land costs, archaic building bye laws, stringent licensing norms, delay in project approval and unfavorable banking policies made low cost housing projects uneconomical for private developers.

Hence, traditionally, low cost housing has been the domain of the government. In the past three decades, government has adopted several policies assisting the delivery of affordable housing for the EWS, LIG and lower MIG. These policy initiatives focused on transition of public sector role as ‘facilitator’, increased role of the private sector, decentralization, development of fiscal incentives and concessions, accelerated flow of housing finance and promotion of environment-friendly, cost-effective and pro-poor technology. Taking into account the emerging challenges of required shelter and growth of slums in urban areas, government further launched Jawaharlal Nehru National Urban Renewal Mission (JNNURM) in 2005 and formulated the National Urban Housing and Habitat Policy in December 2007.

The real estate sector in India underwent considerable changes post the global liquidity crisis. Downturn and liquidity crunch forced developers to adopt a two pronged strategy - smaller units at lesser prices. This oriented developers to focus on the Affordable Housing segment, which has become the buzz word in the real estate market for the last few years. During 2009–2012, the real estate developers in the country have launched projects in the affordable segment across Indian cities, with units priced between INR 5-10 Lakhs (USD 10,000–20,000).

Shortage amplified for the EWS

Urban housing shortage is prominent across the economically weaker sections (EWS) and low income groups (LIG) which together constitute over 95 percent of the total housing shortage. The shortage amongst the middle income groups (MIG) and above is estimated at 4.38 percent.
The affordable housing projects launched by private developers have significantly contributed to the 25 percent\textsuperscript{14} decline in urban housing shortage in the last five years. Although, the urban housing shortage remains substantial, it is clear that active participation from private developers could help in tackling the urban housing shortage in India.

However, affordable housing development continues to be a challenging proposition for developers and further policies need to be formulated by the Government to encourage greater participation from the private sector in the form of technological solutions, project financing and project delivery.

\textsuperscript{14} ‘Urban housing shortage declines 25% in five years to 18.7 mn in 2012’, Business Standard, 23 September 2012
Urban Housing Shortage

Constraints for Real Estate Developers
Unavailability of urban land

High population density in urban areas has triggered a huge demand for urban land. There is a growing need to revisit previously conceived government regulations which have created an artificial land shortage and pushed up land prices in India. Without Government support, the limited availability of land in urban areas makes it unviable for developers to take up affordable housing projects. Further, the substantial non-marketable urban lands used by Government-owned entities such as railways can be used more efficiently. A number of these land parcels are present in centrally located areas. Through better monitoring authorities can make more optimum use of these land parcels and prevent the on-going proliferation of slums and squatter settlements in these areas.
Delay in approvals from multiple local authorities

Estimates reveal that real estate developers are required to pass the approvals through 150 tables in about 40 departments of central and state governments and municipal corporations. Delays in project approvals could add 25-30 percent to the project cost. Better co-ordination among the multiple authorities in dealing with various permissions/approvals can encourage real estate developers to invest in the affordable housing segment. Currently, it takes nearly two to three years for a developer to commence construction after having entered into an agreement for land purchase.

Source: ‘Corruption and Transparency in Realty - The Reality’, infrawindow.com
THREE
Rising construction costs

Unlike premium residential projects, where pricing is largely guided by land costs, prices of affordable homes are primarily driven by the cost of construction. Construction costs form nearly 50 percent to 60 percent of the total selling price in affordable housing projects while for luxury projects this figure is 18 percent to 20 percent.\(^{17}\) Contrary to land prices, which decline exponentially as projects move away from centrally located to peripheral areas of a city, construction costs fall at a gradual rate from luxury projects to low-income housing projects. Hence, construction cost minimization is a vital aspect of making affordable housing projects viable. Raw materials, including steel, cement, sand, bricks, etc, have witnessed price escalation of 20-50 percent\(^{18}\) in the recent past. Owing to the success of the National Rural Employment Guarantee Act (NREGA) scheme, the labor shortage in construction has risen and this has further impacted the construction costs as it has lead to a considerable rise in wage levels.

<table>
<thead>
<tr>
<th>Cost heads</th>
<th>2010 (INR)</th>
<th>2011 (INR)</th>
<th>Change (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cement (cost per bag)</td>
<td>200</td>
<td>270</td>
<td>35%</td>
</tr>
<tr>
<td>Labor (cost per day)</td>
<td>250</td>
<td>325</td>
<td>30%</td>
</tr>
</tbody>
</table>

Source: Achieving Sustainable Growth in Reality, KPMG–CREDAI, December, 2011

FOUR
Lack of skilled manpower

India’s real estate sector continues to grapple with the issue of manpower shortage. This shortage can have an adverse impact on the delivery and cost of affordable housing projects. There is need to enhance the education and training capacity offered through various schemes to meet the demand of the large percentage of unskilled workers in the Indian labor market.

<table>
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<tr>
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<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Real Estate</td>
<td>10,790</td>
<td>14,515</td>
<td>20,692</td>
<td>24,981</td>
<td>14,191</td>
</tr>
</tbody>
</table>

Source: Human Resource and Skill Requirements in Building, Construction Industry and Real Estate Services, NSDC

\(^{17}\) “Urban housing shortage rising in India”, The Times of India, 5July 2012
\(^{18}\) Achieving Sustainable Growth in Reality, KPMG–CREDAI, December, 2011
FIVE

Financing constraints for low-income groups

The current financing mechanism in the country is tilted towards servicing the MIG & above segments. As a result, the households falling under LIG and EWS category find it difficult to secure formal housing finance. Commercial banks and other traditional means of housing finance typically do not serve low-income groups, whose income may vary with crop seasons, or is below the ‘viable’ threshold to ensure repayment, or who cannot provide collateral for loans. Further, housing finance companies (HFCs) are unable to serve the LIG and EWS categories owing to their inability to provide the required documentation for hassle free disbursal of loans. The loan market of INR 3-10 lakhs is estimated at INR 1,100,000 crore. Despite this, less than 20 percent of the INR 55, 200 crore worth of housing loans disbursed by HFCs in FY2011 were in the loan bracket of INR 3-10 lakhs.

Size-wise loan disbursement by HFC’s in India

<table>
<thead>
<tr>
<th>Total Amount</th>
<th>33,804 Cr</th>
<th>45,569 Cr</th>
<th>55,200 Cr</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009</td>
<td>100.00%</td>
<td>80.00%</td>
<td>60.00%</td>
</tr>
<tr>
<td>2010</td>
<td></td>
<td>80.00%</td>
<td>76.66%</td>
</tr>
<tr>
<td>2011</td>
<td></td>
<td>75.99%</td>
<td></td>
</tr>
</tbody>
</table>

Source: Report on Trend and Progress of Housing in India, National Housing Bank, 2011; KPMG in India analysis

19 Micromortgages: A Macro Opportunity in Low-Income Housing Finance, Monitor Inclusive Markets, October 2010
20 Report on Trend and Progress of Housing in India, National Housing Bank, 2011; KPMG in India analysis
Along with the buyers, real estate developers are also grappling with funding challenges. Banks have curtailed their exposure to real estate citing cautious measures leaving high cost finance options such as Non-banking Financial Companies (NBFCs) and Private Equity (PE) funding as the only source of finance. Moreover, high cost of finance coupled with the waning demand has disrupted the cash flow situation of developers. Hence, developers are now deferring their project launches, thereby altering the slated supply. Also, high cost of finance is restraining them from lowering housing prices.

There is a growing need to revisit regulations such as the Rent Control Act, which are proving to be a deterrent in the development of rental houses and redevelopment of areas with old properties. By formulating more clear and defined guidelines within building bylaws and rules for Floor Space Index (FSI), zoning and development plans the local urban authorities in India can reduce the difficulties faced in planning for construction projects in India.

Taxability of real estate transactions in India has been a matter of dispute and litigation as the Union Government, individual State Governments and local authorities are empowered to impose various indirect taxes on developers21. Once a more clear definition on whether ‘the real estate property’ is a product or service is provided by the Government, developers would gain a breather from the current double taxation regime. The Government also needs to revisit the non uniformity in stamp duties across the country. The stamp duty to be paid at the time of execution of the underlying instrument varies from 5 percent to 15 percent22 of the value of property in different States.

21 KPMG in India analysis
22 Achieving Sustainable Growth in Reality, KPMG-CREDAI, December, 2011
Urban Housing Shortage

The Way Forward
**Improve land planning and utilization**

The Government needs to ensure adequate availability of land for housing and infrastructure by computerization of land records, use of Geographical Information Systems, efficient dispute redressal mechanisms and implementation of master plans. Urban Local Bodies (ULBs) and Urban Development Departments (UDDs) should identify dedicated zones for development of affordable housing in the city’s master plans and should develop them within a planned schedule.

**Viable business model to encourage further involvement of the private sector**

Making affordable housing a viable business model can motivate private real estate developers to participate actively and aggressively in this segment. The Government can direct ULBs and UDDs to incentivise private developers in the affordable housing segment by allowing them access to cheaper land, awarding higher FSI, reduction in the number and the time taken for approvals, assisting with infrastructure development, easier home loans and interest rate and tax subsidies.

**Provide incentives on construction and other allied costs**

Providing incentives which can reduce the construction cost for developers would not only make the project viable for developers but also make it affordable for the buyers. This is because construction costs drive the pricing in case of affordable housing units.

Some of the measures which could help in reduction of construction costs are as follows:

- **Single window approval for projects:** Delays in the project approvals result in substantial cost overruns. Hence a single window approach will help the developers reduce delays and costs.

- **Subsidize construction costs:** In order to reduce construction cost, the Government should provide exemption on taxes and duties on construction materials; provide subsidy to developers for R&D in new low cost materials and technologies; can lower the cost of borrowing for development of affordable housing projects by granting guarantee on the loans etc.

- **The Government can provide exemption from sales tax and reduction in stamp duty.**

**Encourage micro mortgage financing mechanisms**

Fundamental innovations are required in the traditional mortgage-lending model which could enable the informal salaried and self-employed population, who belong to the LIG and EWS segments, in availing housing loans. The Government could encourage effective financing through micro mortgages by utilizing the reach of Self-Help Groups (SHGs) and other innovative financing mechanisms. This would ensure that housing finance is available to large sections of LIG and EWS populations. Flexible payment mechanisms should be put into place considering the fact that households in LIG typically have variable income flows.

**Alternate sources of funding for developers**

REITs and REMFs can be excellent funding opportunities for real estate development provided the ambiguities in taxation and additional transaction cost such as stamp duty are removed. The Government could also look at alternate sources for meeting long-term financing needs by granting infrastructure status to the housing sector. Such move would attract funds from insurance companies, which are mandated to invest 15 percent of their funds in social and infrastructure sector (as per IRDA regulations).
**Improve penetration of rental housing in urban areas**

Rental housing in India has very low penetration unlike many developed economies which have emphasized on affordable or social rental housing that constitutes up to 20-30 percent of their housing stock. In these countries, governments have a large role to play in promoting social housing as most of the rental houses are provided by government or by limited or non-profit housing associations that utilize government incentives. In India, authorities like the MMRDA have launched affordable rental housing scheme. However, the scheme met with limited success as it lacked the necessary enforcement and the required rental management.

<table>
<thead>
<tr>
<th>Country</th>
<th>Percentage of total housing stock*</th>
<th>Percentage of social housing stock by**</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Social rental</td>
<td>Private rental</td>
</tr>
<tr>
<td>UK</td>
<td>20</td>
<td>10</td>
</tr>
<tr>
<td>Ireland</td>
<td>7</td>
<td>11</td>
</tr>
<tr>
<td>USA</td>
<td>3</td>
<td>29</td>
</tr>
<tr>
<td>Australia</td>
<td>5</td>
<td>22</td>
</tr>
<tr>
<td>Canada</td>
<td>6</td>
<td>28</td>
</tr>
<tr>
<td>Austria</td>
<td>23</td>
<td>17</td>
</tr>
<tr>
<td>France</td>
<td>16</td>
<td>24</td>
</tr>
<tr>
<td>The Netherlands</td>
<td>35</td>
<td>12</td>
</tr>
<tr>
<td>Denmark</td>
<td>19</td>
<td>18</td>
</tr>
</tbody>
</table>

Source: International experience in providing affordable housing, IDFC 2011
Note: Housing associations are for-profit, non-profit or limited profit organizations that build and/or manage low-cost or social housing
*Remainder of total housing stock is predominantly ownership
**The social housing stock includes both social rental and ownership units
^Include some for-profit associations, co-operatives, moderate rent agencies and regulated private landlords. Some associations have tenant shareholders

**Initiatives to build talent capacity**

The Government can take initiatives to fill the manpower demand supply gap by collaborating with educational institutions which can impart vocational education and training programs for the real estate professionals at all levels. The developers, on their part, could developing in-house academies and structure training programs to enhance the resource quality of skilled/semi-skilled labor.

**Leverage innovative and low-cost technologies**

Developers should leverage on innovative and low-cost technologies such as pre-fabrication, which can be used to construct affordable houses quickly and cost-effectively. Although, pre-fab materials are 15-20 percent costlier, developers would gain from the dual benefits of higher efficiency and lower labor costs. In Europe and the Middle East, the use of precast concrete and engineering homes technology has enabled certain developers in saving up to 64 percent of the total man hours needed using conventional methods.

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23 International experience in providing affordable housing, IDFC 2011
25 Developers adopting precast concrete and engineering homes technology, The Economic Times, 9 June 2012