ART Housing Finance – Coverage

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The Times of India (Kanchan Gogate)

Publication	**The Times of India**
Headline	ARE YOU A LOAN A RANGER?
Page Number	1
Edition	Bangalore
Date	21st December 2018

Thanks to the RBI's latest mandate (wherein banks would now have to link loans across categories to floating interest rates), new and existing home-owners will get more transparent home loan deals

ARE YOU A *LOAN* RANGER?

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Home loan borrowers now need not worry whether they should choose fixed or floating interest rates. The Reserve Bank of India (RBI) has introduced a new policy measure with regards to loan pricing. From April 2019, it will be mandatory for banks to link all floating rate loans using external benchmarks. This benchmark can be the RBI's repo rate, yield on the 91-day or 182-day Treasury Bill, or any other yardstick produced by the Financial Benchmarks of India. This means for home loan pricing, rates will now be decided by the markets and not the banks.

Experts feel that this move is in favour of home loan borrowers, as they can now get more transparent deals with the process bringing more standardisation and ease of understanding. There will be a uniform benchmark for the loan category. Existing borrowers will also switch their loans to the new benchmark.

The RBI's move to benchmark loans to external market-linked factors is a welcome one. However, the chosen benchmark needs to be stable and not subject to too much volatility. It will be better if banks can also link their lending to HFCs/NBFCs with this benchmark so as to ensure elimination of basis risk and ease of transmission.

R Sridhar, executive vice-chairman and CEO, IndoStar Capital Finance

It has been observed that home loan borrowers have not benefitted on instances of reduction in key policy rates. There has been a delay in transmission of policy rate reduction on many occasions. With the adoption of these external benchmarks that are reflective of the market interest rates, consumers are likely to benefit on their home loans as well.

Arvind Nandan, executive director - research, Knight Frank

WHAT IS THE NEW POLICY?

- ➜ Mandatory for banks to link all floating rate loans to external benchmarks from April 2019;
- ➜ As of now, all loans are linked to Marginal Cost of Lending Rate (MCLR);
- ➜ MCLR is an internal benchmark;
- ➜ Due to the MCLR system, borrowers couldn't benefit from RBI rate cut;
- ➜ MCLR benchmark gave more power to banks to decide on pricing (based on their business);
- ➜ Under the new policy, MCLR basis for pricing will be eliminated;
- ➜ Amid external benchmark, banks can choose any of the following:
  - **RBI repo rate;**
  - **91 or 182-day Treasury Bill yield;**
  - **Any other market interest benchmark produced by Financial Benchmarks India.**
- ➜ Interest rates may change every month under new policy.

The move will benefit home loan borrowers, as markets will decide loan rates. Even existing borrowers will switch to the new external benchmark. Chances of benefits of RBI rate cuts getting passed on to the borrowers are higher here. Overall, there is a fair play in loan pricing.

Nagesh Sharma, founder, Mera Loan Doctor

HOW DO BORROWERS BENEFIT?

- ✔ Markets to decide home loan rates and not banks;
- ✔ Uniform system for home loan pricing;
- ✔ RBI rate cut benefits can be directly passed on to borrowers;
- ✔ New system overcomes the problems of MCLR loans;
- ✔ More transparency in home loan deals;
- ✔ Standardisation of home loan pricing;
- ✔ An improved ease of understanding;
- ✔ Existing borrowers can also switch loans to floating rates. A better way to compare loans from different banks;
- ✔ At present, only two banks in the country use external benchmark for home loan;
- ✔ RBI kept its repo rate unchanged in the latest bi-monthly policy;
- ✔ There are no chances of interest rate rising in the nearest future.

GOOD TIMES AHEAD:

- Affordability in most cities has improved with property cost coming down six-eight times the annual household income in 2018-19 compared to 11-13 times five years ago, says CRISIL report;
- Affordability factor is expected to come closer to the ideal band, given a moderate growth in income estimated for mid-income households;
- Amid HFCs facing liquidity threat, the housing finance sector has been steadily growing;
- Housing credit growth is expected to be 17-19 per cent, says ICRA report.

From a customer point of view, this will certainly improve transparency in terms of pricing, as a uniform benchmark will be adopted, thus ensuring standardisation. This will also make it easy for the customer to understand the pricing mechanism and its effect on their borrowing. Since different lending entities will have different cost funds basis their source of liability profiles, impact on their earnings will be only assessed post implementation of new benchmark pricing method.

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