
Rating Rationale for **Housing & Urban Development Corporation Limited's** Unsecured Non Convertible Debenture Issue of INR 10 billion

Issue Rating: BWR AAA

Outlook: Stable

Brickwork Ratings has assigned BWR AAA (Pronounced BWR Triple A) with stable outlook for Housing & Urban Development Corporation Ltd.'s (HUDCO) Unsecured Non Convertible Debenture Issue of INR 10 billion or Rs. 1000 Crore. Brickwork Ratings' 'BWR AAA' rating stands for an instrument that is considered to offer EXCELLENT credit quality / safety in terms of timely servicing of principal and interest obligations. The rating factored in 100% GoI ownership and the support provided by it to HUDCO, important role played by HUDCO and the appreciable performance achieved by it vis-à-vis the various parameters stipulated in the MoU with the GoI in promoting housing and infrastructural development in the country, which is a national priority. It has also kept in view the strong recommendations made by the high powered committee appointed by the Govt. to continue to provide full support by the Govt. to HUDCO, for a period of seven years to enable it to rejuvenate and continue to play its vital role in the national economy.

HUDCO performs a public policy role in financing the government's policies in urban infrastructure and low-cost housing. Given the Government's renewed focus on these areas and expectations that HUDCO can play a more active role, the government is considering providing more tangible forms of support to HUDCO in future. The government has in the past provided HUDCO with explicit letters of support to help it raise domestic funds more efficiently, and this practice may be revived.

HUDCO's ability to sustain growth in its operations, given the increasing competition, and at the same time maintain its asset quality and collections will have an important bearing on the company's credit risk profile.

BWR has essentially relied upon audited financial statements of FY March 2009 and the past four years, projected financial figures, information and clarification provided by HUDCO.

HUDCO has posted strong growth in total business, increase in net worth, interest income, spread, EPS, and PAT. HUDCO's expenditure is on declining trend as well. HUDCO has also shown good performance according to the performance criteria as per MoU between HUDCO and Ministry of Housing and & Urban Poverty Alleviation (GoI).

Considering the fact that HUDCO caters to the Economically Weaker Sections (EWS) and Lower Income Group (LIG), HUDCO has still managed to improve its asset quality continuously. From year 2005 HUDCO had exhibited a decline in NNPA almost by 5%. HUDCO has also extended its business in Social Urban Infrastructure sector, which will help in increase its bottom line.

HUDCO's net profit has almost increased by 7% from INR 373 crores in 2008 to INR 401 crores in 2009. HUDCO has also reported a net decrease in NNPA from 5.72% in 2008 to 4.87% in 2009.

HUDCO's financial information:

Table 1					
(Amount in INR. Crores)	2005	2006	2007	2008	2009
Loan Approvals	13862	10099	12163	13501	14754
Loan Disbursement	5921	3767	3452	3754	4019
Cumulative Disbursement	12057	15824	19276	23030	27049
Total Loan	20861	21349	21065	21073	21427

Loan disbursement has not seen proportionate increase as Loan approvals. Low loan disbursement is attributed to the declining ability of the State Governments to extend guarantees and securities. At the same time, availability of grant from the GoI, and multilateral funding form World Bank, ADB, etc. at lower interest rates has contributed towards lesser releases by HUDCO.

Table 2 gives the details of sanction and release of loans for FY-09.

Table 2		
POSITION AS ON 31.03.2009	INR crore	INR crore
	SANCTIONS	RELEASES
SBU'S		
Social Housing, Action Plan, NGO	480	73.46
Value added real estate- Non Priority housing	1109.88	703.72
Value added real estate (Commercial, Social Infrastructure, IT Sector etc.)	940.6	704.16
Retail Finance (Individual Housing loans)	42.85	40.39
Energy/Emerging Sector	8127.32	1797.71
Water, Sanitation, Sewerage, Drainage, Solid waste management	2331.63	318.08
Roads Transport	1721.84	381.7
Total	14754.12	4019.22

In terms of Earnings, total income is almost stagnant at INR 2713 crores in FY-09 compared to INR 2729 crores in FY-08. This stagnant income is due to low disbursements in loans as mentioned above. However there has been constant decrease in Both GNPA and NNPA. GNPA for HUDCO was 8.60% for FY-09 compared to 9.70% for FY-08.

Table 3					
(Amount in INR. Crores)	2005	2006	2007	2008	2009
Total Income	2777	2298	2610	2729	2713
Total Expenditure	3197	1918	2143	2170	1942
Net Profit	396	260	308	373	401
Net Worth	3410	3628	3913	4191	4668
Borrowings	21217	21461	20383	18903	19249
GNPA	14.37%	11.73%	11.08%	9.70%	8.60%
Net NPA	11.11%	8.60%	7.78%	5.72%	4.87%
EPS (INR.) FV INR. 1000	200.31	130	154.04	186.69	200.3

However, HUDCO has posted net profit increase of 7.21% from INR 374 crores for FY 2008 to INR 401 crores for FY 09. HUDCO's net interest income recorded a growth of 0.65% during the same period. HUDCO's net worth has increased progressively from INR 4191 crores in 2008 to INR 4668 crores in 2009.

Background

HUDCO was established on April 25, 1970 as a fully owned enterprise of the Government of India. It is the only Housing Finance Company in India, which has full government support. In its almost 40 years of operations, HUDCO has constantly ameliorated the housing conditions of all groups with a thrust to the needs of the Low Income Group (LIG) and Economically Weaker Sections (EWS). Every 9 out of 10 dwelling units supported by HUDCO is to EWS/LIG. HUDCO today has emerged as the leading national techno-financing institution with the major objective of financing/encouraging the housing activity in the country and alleviating housing shortage of all groups in rural and urban areas and also the development of urban infrastructure of various shades in human settlements.

HUDCO's makes more than 80% of the socially oriented housing loans to EWS/LIG. Because of lending made to economically weaker section of society HUDCO has relatively high level of NPA when compared to the industry average. However, loans made by HUDCO are secured by the Government. In the case of default, Security of the State Govt. guarantee may be invoked. Also after signing the MoU with Ministry of Housing & Urban Poverty Alleviation (MHUPA), MHUPA has ensured to help HUDCO with recoveries. NPA principal outstanding for Govt. agencies is INR 1891 crores, which is almost 80% of the total NPA principal outstanding, which most likely will be recovered. Close monitoring and stricter recovery policies of HUDCO are resulting in lower level of NPA each year. From year 2008 HUDCO had exhibited a decline in NNPA almost by 1% from 5.72% to 4.87%.

MoU between HUDCO and Ministry of Housing & Urban Poverty Alleviation (GoI)

HUDCO and Ministry of Housing & Urban Poverty Alleviation (GoI) have signed a MoU. The mission of the committee is to continue to promote sustainable habitat development to enhance the quality of life.

Following are the major objectives of the MoU:

- To continue to provide technical and financial assistance for housing and related activities with special focus on the Economically Weaker Section (EWS) and Low Income Group (LIG) both in rural and urban areas.
- To continue and undertake urban and rural infrastructure projects relating to water supply, sanitation, solid waste mgmt., drainage, transport and other social and commercial infrastructure.
- To continue finance and support innovative, disaster resistance, energy saving, environment friendly and cost effective and affordable housing.
- To continue to assist in the implementation of Action Plan Schemes of the Central Govt. including assisting the Govt. of India in appraisal, monitoring and funding JNNURM projects and also assist Govt. as ISHUP, Affordable Housing in Partnership Programme.
- To augment resource mobilization in a prudent manner and to put such resources to optimum use.
- To continue to explore the reduction of lending rates for the EWS.
- To attach priority to turn-key mgmt. consultancy projects, PMC of housing projects and to prepare DPR for projects and also to prepare City Development Plan and Master Plan.
- To continue to strengthen the project appraisal/evaluation and monitoring system within HUDCO with induction of professional and experts as well as outsourcing such functions in which expertise is better available outside HUDCO.
- To diversify the activities of HUDCO. To enter into consortiums and other arrangements with other similarly placed financial institutions in order to expand the lending base of HUDCO.
- To continue to maintain the quality of loan assets by monitoring loan recovery and strive to eliminate NPAs.

Commitments/Assistance from the Government:

The Government (MHUPA) on its part would take all measures in order to enable HUDCO to function effectively and facilitate attainment not only of the national objectives but also realization of its corporate goals and maintain its operational autonomy.

Assistance to be provided by the Government:

- To help HUDCO in mobilizing resources at lower costs.
- To help HUDCO deal with such externalities which impinge upon its effective functioning, such as, assisting HUDCO for strengthening its net-worth and taking up issues relating to NHB regulations.
- To help HUDCO in resolving default of State Governments and State Agencies.

Report of High Powered Committee to rejuvenate HUDCO

The GoI, Ministry of Housing and Urban Poverty Alleviation, dated 29th May, 2008 set up a High Powered Committee to rejuvenate HUDCO with a view to strengthen its financial position and expansion of activities for better services to poor and weaker sections of the society. Shri Ashok Jha, IAS (Retd.), Former Finance Secretary was the chairman of the committee.

Major terms of reference of this Committee are to suggest measures for:

- Rejuvenating HUDCO and to strengthen its financial position;
- Addressing the agenda of Affordable Housing for All with special reference to Economically Weaker Sections (EWS), Lower Income Group (LIG) and Middle Income Group (MIG);
- Expanding the field of activities of HUDCO and possible areas of expansion.
- Better services to the poor and weaker sections of the society by HUDCO.
- Increase in equity base of HUDCO to enable it to operate on a comfortable Debt-Equity ratio
- Issue of bonds under section 54 EC of the Income Tax Act
- Exemption from payment of Income Tax
- Allowing HUDCO to issue tax free Housing Bonds on American Pattern
- Allowing plan funds allocation towards repayment of over-dues of HUDCO against the Loans availed by State Government and their agencies.
- Relaxation from Credit Concentration (Exposure) norms taking into consideration the response of NHB

Major recommendations from the committee were the following:

- Permit HUDCO to raise funds under the purview of Municipal Tax Free for capital investment in urban infrastructure
- Facilitating HUDCO with a `Letter of Comfort' from the Government, for a period of 3 years, to enable it to get the highest credit rating (AAA), so that that its borrowing cost is more competitive.
- Allowing plan funds pre-emption towards repayment of overdue of HUDCO against the loans availed by State Governments and their para-statal backed by State Govt. If this happens, then this will reduce HUDCO's NPA to less than 2%, which will be in line with the norms of the industry.
- Permission to issue 54(EC) Bonds: At present 54 EC bonds are being marketed at an all inclusive cost of 7.5% as compared to HUDCO's current borrowing cost of 12%. Permission to issue 54(EC) Bonds is likely to result in a saving of INR. 608 crores in three years. This will also address the issue of the asset and liability mismatch.
- Allowing HUDCO to follow RBI norms in respect of credit concentration, which make due allowances for infrastructure projects.
- Plough back of dividend: HUDCO may be permitted to plough back the payment of dividend including dividend tax for a period of 7 years beginning with 2008-09. This would result in a saving of INR. 385 crore over a period of seven years.
- Restoration of equity support to HUDCO: The Committee recommends equity support of INR 100 crore per year for the next seven years is given to HUDCO.

The committee felt that a seven year period of time would suffice for HUDCO to rejuvenate its financial position and there after become a self sustaining entity. In the view of the committee the suggested measures would enable HUDCO to emerge as a stronger and powerful arm effectively meeting the expectations of the GoI.

Rating Outlook

Since its inception HUDCO has been serving the economically weaker sections and people from low income group as well as building urban infrastructure, both vital to economic growths. The asset quality of HUDCO is likely to improve as a consequence of the MoU entered into with MUHPA which has assured necessary help to HUDCO as regards recoveries. Implementation of Jha Committee's strong recommendation are vital to HUDCO's sustainability as they not only

give substantial relief to HUDCO but would also enable its access to low cost fund which is very essential for improving its performance and financials, and continuing to play its vital role in the national economy. While HUDCO's capabilities in continuing with its mission to promote sustainable habitat development to enhance the quality of life of the Indian public is beyond doubt, the key factors which will influence HUDCO's future growth will be its access to low cost funds as well as improving its asset quality and efficiency.

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