



REFORMS IN LAND

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CONTEXT OF THE PAPER

- Shleifer, and Vishny (1997, 1998): importance of equity and creditor rights in financial systems
- Credit markets develop where creditors rights are better protected; (See Stiglitz (2001) and Hart (2000) for a review)
- *“Well-functioning insolvency laws reduce financial distress for corporate sector;Improve resource allocation, efficiencyequity... stability of the financial system”* (Claessens and Klapper, 2002)
- Thrust area of IFC/World Bank, model laws by UNCITRAL/EBRD
- Larr, 1994 defines collateral as "an asset that upon liquidation is adequate to cover most or all of the lender's risk exposure including principal, accrued interest and collection costs”



COLLATERAL – ECONOMIC IMPACT

- Two functions of Collateral
 - Signalling function– higher the amount and quality of collateral, higher the firm signals its unwillingness to default (Tybout, 1983, 1984; Bester, 1987)
 - Enforcement function: Collateral covers for exogenous shocks by reducing the lenders loss given default (Barro, 1976, Benjamin, 1978).
- Binswanger et al (1986) define collateral on 3 characteristics
 - appropriability: ability to dispose the asset quickly and with no loss in value in case of default. The liquidation of the collateral has to be easy, low-risk, and with low impact costs
 - ability to de-risk of collateral specific risks
 - appropriate returns to the borrower during the tenure of the loan
- All this at low marginal costs of collateralisation



LAND AS PREFERRED COLLATERAL

- Land preferred by lenders also
 - No depreciation
 - Fixed asset/immovable
 - Insured against third party exogenous shocks (de-risked)
 - Therefore, 'appropriable'
- Costs of collateralisation of land impacts
 - Credit rationing (to give credit or not to, how much to give)
 - Interest rates
 - Loss-given default



COLLATERALISED LAND

Item of assets	Rural			Urban		
	Cultivator	Non-cultivator	All	Self - employed	others	all
Land	83.14	64.60	72.60	76.77	38.95	46.95
Building	11.57	28.39	21.13	18.11	52.03	44.86



BORROWER'S SIDE OF THE STORY

- India – investment in land :
 - Formal financial system
 - 52-60% of retail loans directly or indirectly against property
 - 45% of firms borrow against land and building
 - NBFC
 - Higher proportion of NBFC credit against property directly or indirectly (including land loans) 70 %
 - Informal
 - Professional Money lenders - substantial loans (70%) against land;
 - Informal source of finance against property as important as formal source of finance.
 - Higher you go to informal finance, greater dependence on land collateralisation



INSOLVENCY, CREDITORS' RIGHTS AND LAND

- Ease of Collateralising Land depends on
 - borrowers' ability to pledge land for collateral,
 - the lenders ability to accept land as collateral,
 - institutional structures that determine the marginal costs of collateralisation of land at two times
 - **Time of loan origination**
 - **Time of repossession**



INSOLVENCY, CREDITORS' RIGHTS AND LAND

- Issues with land as collateral
 - Ex-ante : High costs of collateralisation and low appropriability lead to credit rationing; inefficient credit markets; financial exclusion
 - Ex-post : higher loss-given default, individual bank failures and systemic financial distress, social welfare losses.
- Process for collateralisation of land cumbersome
 - Legal report (title information report)
 - Valuers reports
 - Mortgaged documents
 - Physical verification of site



CHECKLIST FOR COLLATERALISATION 1

○ **Ownership and Title**

- Does the land belong to the borrower? Is there a document trail that establishes the owners' right to alienate the property, which includes registration deeds, deeds of gift or succession?

○ **Parcel Identification**

- Is the land properly identifiable in classified records? Are these borne out in other documentation such as registration/sale deeds, mutation certificates, etc.

○ **Liens**

- Has the land been already pledged with other lenders? Are there other contractual obligations (long term lease, tenancy agreements) that may reduce the ability of the lender to possess and sell the property in case of default? This may include unpaid dues to government, building societies, etc.



CHECKLIST FOR COLLATERALISATION 2

○ **Legality of Usage**

- Do the constructions/settlements that are on the land adhere to local laws? Have laws regarding conversion of land and permitted land use been followed? If the land has a situated building that is put to a certain use, is the use allowed as per master plan documents, and are planning permissions valid? Have development control regulations been followed in these cases?

○ **Valuation**

- Is the risk-adjusted value of land sufficient enough to cover the loan in case of distress?? What is the value of different assets within the parcel (land and buildings and interiors)? How is risk adjustment provided for?

○ **Recovery**

- If there is default, can the land be sold to recover dues owed easily? (Recovery after default)



ISSUES WITH LAND

- NO SINGLE VIEW
 - Land rights scattered; no title guarantee by state
 - Titles are presumptive, not conclusive; no Torrens' titles
 - Land registers and cadastre information unavailable.
 - Boundaries and ownership details conflict across different departments: fragmented jurisdictions, coverage, and operational domains (revenue dept, rural land dept, survey and settlement departments) maintaining different levels /details of data
 - Land registries with incomplete records, manual record-keeping
 - Lack of administrative and judicial enforcement capacity
 - 70% or more lands in certain administrative jurisdictions are legally impaired.



ISSUES WITH LAND

- Many suggested reforms (FSLRC)
 - Full computerization and integration of land records
 - Full cadastral mapping of land
 - Settlement of land disputes.
 - Compulsory registration of all transactions.
 - Elimination of restrictions on land markets
 - Remote and easy access to registration procedures and to land records.
 - Standardization of forms and computerization of land offices.
 - Reduction of stamp duty.



RECOVERY

- SARFAESI has proved quite effective
 - Anecdotal evidence
 - Black money in land, high value transactions are difficult to complete
 - Agricultural land not under SARFAESI
- Recovery timelines are not followed – borrowers in some cases play off SARFAESI vs. DRT.
 - Frivolous applications
- Role of the DM – responsibility /authority mismatch



IMPACT ON LENDER

- Collateral does not work as good signalling mechanism
 - Dependence on other information to reduce asymmetry
- The Loan-to-value ratio that may be provided against collateral reduces, leading to under-leveraging of assets.
- Marginal costs of collateralisation increase.
 - Marginal costs of collateralisation involve not only the financial costs of evaluating collateral, but also the processing time spent on providing credit and on recovery
- Systemic dead weight losses are increased due to loss of credit-supply.



SUGGESTIONS

- Lenders need a transparent, efficient means of obtaining security that would reduce their transaction costs and guarantee them recovery of their debts in case of default.
- Strategic, requiring a complete systemic overhaul – out of reach of lenders, government's domain
- Opportunistic and process oriented reforms
 - This is our focus



SUGGESTIONS - STRATEGIC

- Better land titling systems
 - Implement modernised cadastre system and use it to bring all new urban and existing urban areas, rural zones, and informal settlements into the ambit of the law.
- Strengthening the court system and developing alternative dispute resolution techniques
- Efficient registration system with unrestricted access (registration process on average takes 62 days, and costs on average 7.7 per cent of the property value – highest amongst all BRICS)
- Credit information registry sharing made public;



SUGGESTIONS - OPPORTUNISTIC

- Use Valuers data smartly
 - Create a system whereby all transactions through all lenders are geo-plotted and aggregate valuation information is shared.
 - All locations geo-referenced. All documentary evidence available in digitised formats for parcel under question
 - Potential price changes captured; GIS map hot areas, perform analytics on credit exposures by administrative jurisdiction/location
 - Similar to Uniform Mortgage Data Program in the US



SUGGESTIONS - OPPORTUNISTIC



- Document dictionary
 - Different states have different documentary requirements
 - Common minimum documentary library used across all lenders
 - Assists in providing better valuation reports
- Link CERSAI to documentary evidence available (similar to KYC for lands);
 - rate cleanliness of land within the banking system and use this information to make credit rationing decisions







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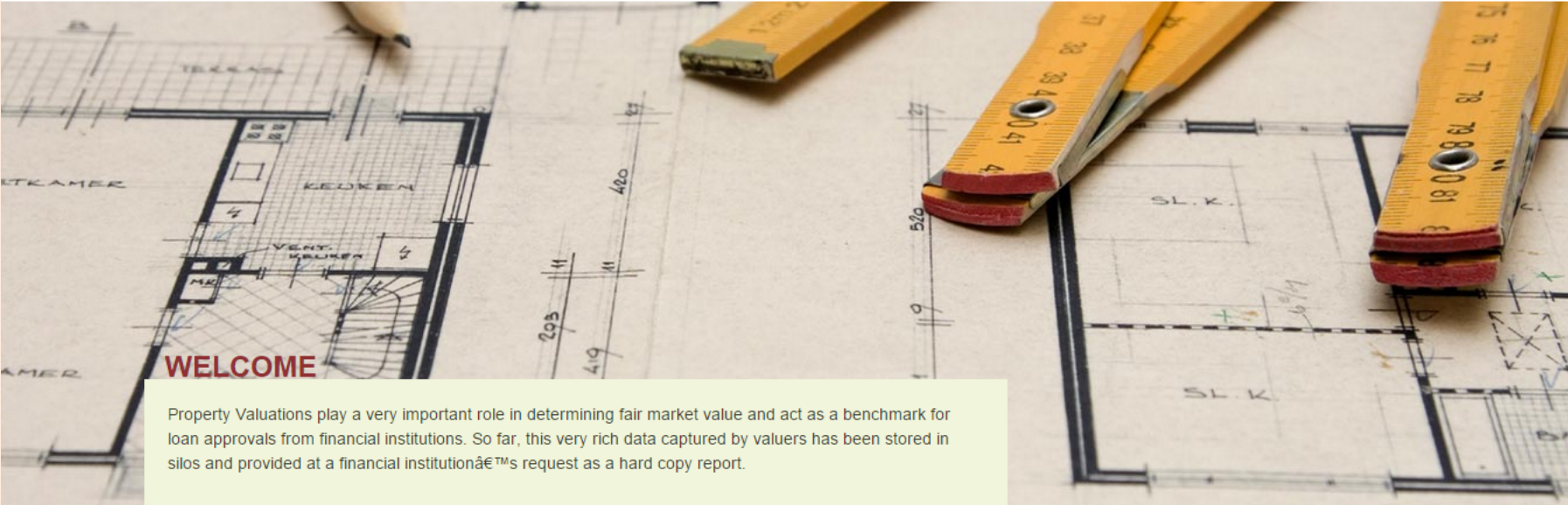
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WELCOME

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IIMB Real Estate Research Initiative (RERI) is integrating this data in an attempt to move towards a standardized format and provide meaningful analytics with this information. A centrally collected dataset of all valuations is one of the goals of our larger transparency initiative. Log into our secure portal to firsthand experience the convenience of generating standardized valuation reports.

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VALUER'S SURVEY

Please enter the following information for evaluating the property. The fields with the asterix * are mandatory fields and need to be filled.

1. General Details

2. Surrounding Locality Details

3. Property Details

4. Structural Details

5. Quality of Construction

6. Plan Approvals

7. Valuation of property

Logout

1.1 Valuation reference no *












1.2 Valuation initiated by *

1.3 Name of the Valuer *

1.4 Date of valuation *

1.5 Purpose of valuation *

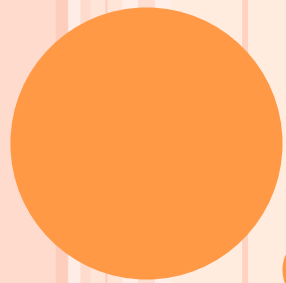
1.6 Person/s accompanying/available at the site at the time of survey



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THANK YOU
Questions

