Housing Finance Cos: AUMs Poised to Grow in Double-digits in FY24 & FY25

March 22, 2024 I Ratings

CareEdge RATINGS

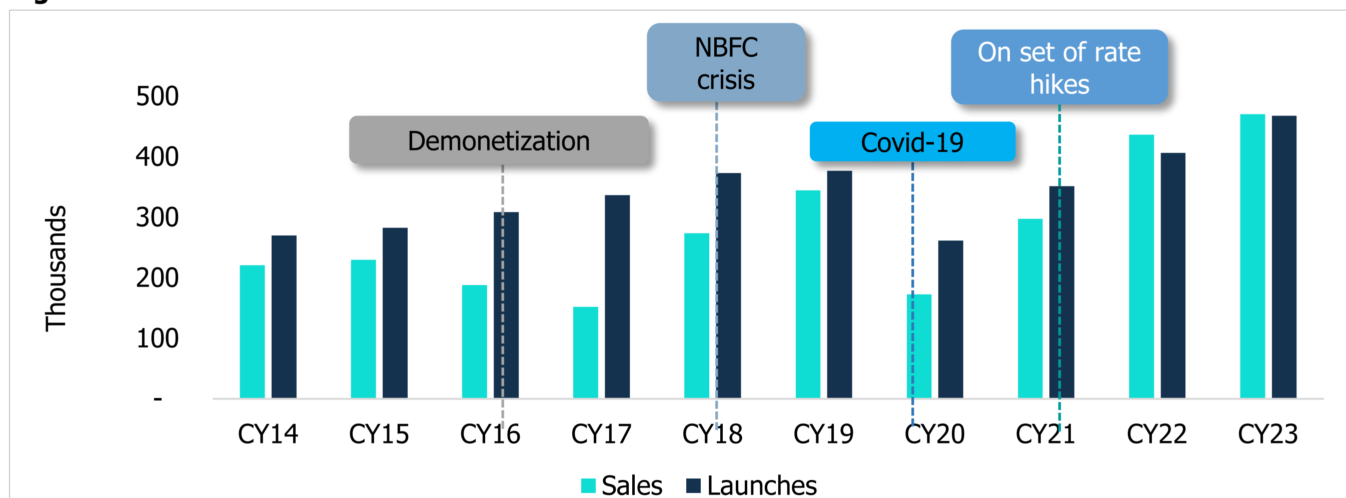
Overview

- The housing finance sector continues to be aided by strong macro drivers supporting demand; despite elevated interest rates, residential sales and launches are on a strong footing.
- Driven by underlying demand and supported by strong balance sheets; housing finance companies (HFCs) are witnessing the continuation of healthy AUM growth.
- Retail portfolio seen growing at a healthy clip; stress in wholesale portfolio gradually ebbing.
- With the declining pace of fresh slippages and recoveries in the wholesale portfolio, asset quality issues are receding for HFCs.
- While net Interest Margins (NIM) are expected to remain under pressure, overall profitability is expected to improve on the back of waning asset quality stress.

Strong drivers accelerating demand for housing

The Indian residential real estate sector is experiencing robust demand, backed by strong macroeconomic fundamentals. While drivers such as improving affordability, rising urbanization, low mortgage to GDP ratio, favourable demographics & government policies have been traditional underlying growth drivers; shift in post pandemic consumer behaviour towards preference for open living spaces, premiumization as well as other factors such as low interest rates, stamp duty rebates resulted into an up-cycle in residential real estate market. These forces are set to sustain housing demand over the medium to long-term. Since the pandemic, housing demand has surged, further supported by low interest rates and beneficial policy measures, leading to sales of residential units reaching a decade-high of 470,424 units in CY23, with 467,449 new launches. Despite the Reserve Bank of India's cumulative repo rate increase of 250 basis points from May 2022 to February 2023, residential demand has remained robust.

Figure 1: Residential Sales & Launches

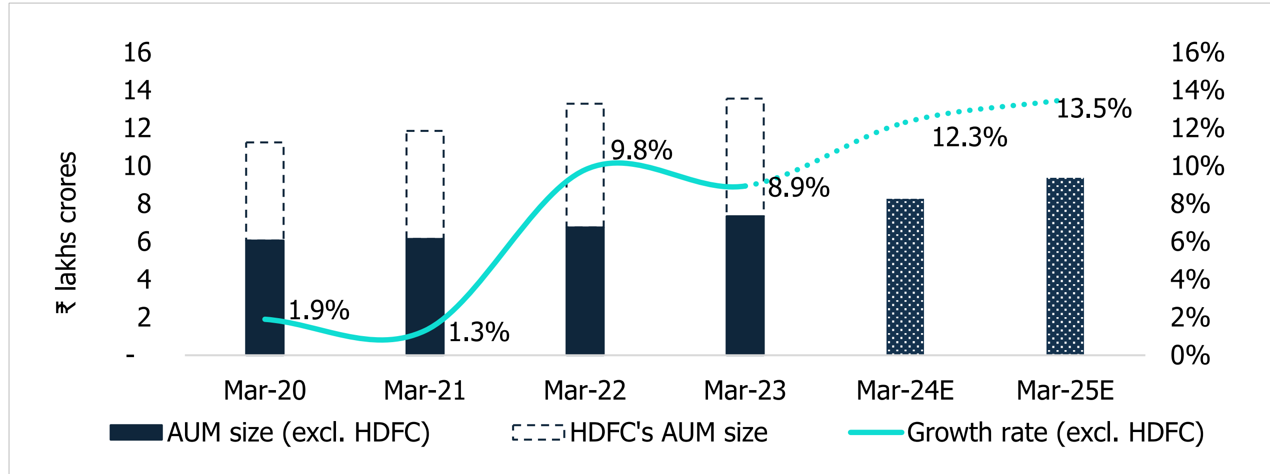


Source: Liases Foras & CareEdge Ratings

HFCs AUM growth gaining momentum propelled by retailisation

In sync with a rebound in the residential real estate market, retail loans started witnessing an uptick from FY22. Consequently, the AUM gnbrowth has been led by retailisation. During FY23, the overall AUM of HFCs grew by roughly 9% with the housing segment growing by 13% while the non-housing portfolio including the developer finance book contracted marginally. The total outstanding portfolio of HFCs as of March 31, 2023, stood at Rs. 7.4 lakh crore (excluding HDFC Ltd) of which housing loans comprised Rs. 5.5 lakh crore vis a vis housing loans by SCBs amounting to Rs.19.4 lakh crore.

Figure 2: AUM SIZE & Growth: HFCs

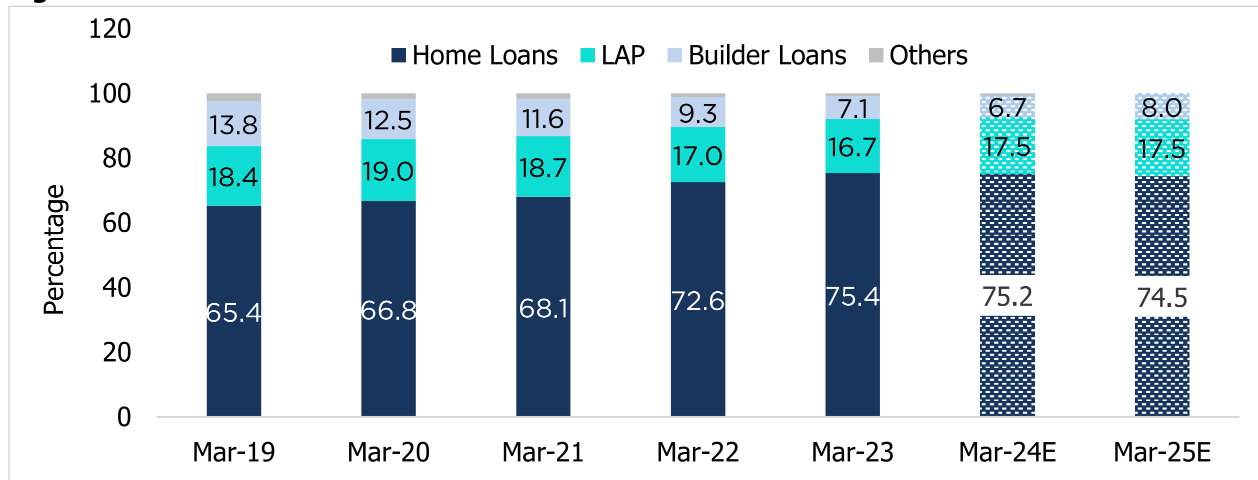


Source: Reserve Bank of India, CareEdge Ratings, based on top 15 leading HFCs in India

Wholesale books continuously declining, however, expected to cautiously pick up going forward

The share of builder loans has shown a declining trend while retail loans have been rising in the overall portfolio mix. Post 2019 developer and NBFC/ HFC crisis, developer finance portfolios of HFCs witnessed stress thereby resulting in conscious curtailment. Apart from issues in developer financing, the growth in retail loans was also contributed by higher disbursements post regulatory guidelines on the principal business of HFCs.

Figure 3: Portfolio Mix OF HFCs



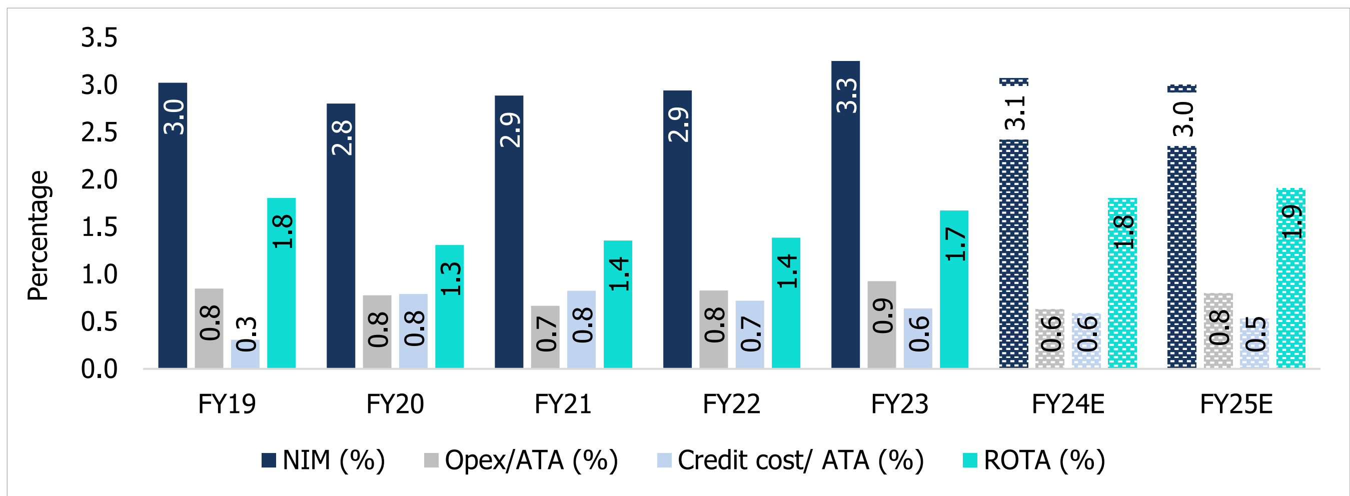
Source: CareEdge Ratings, based on top 15 leading HFCs in India

However, going forward, in the backdrop of strong residential sales, a shrinking pool of stressed developers and progressive resolutions/ recoveries within the developer financing book, the share of developer financing is expected to gradually pick up in the medium term.

Credit costs receding, profitability expected to remain robust

Given the rebound in the residential real estate market, growth, and receding credit costs; profitability indicators for HFCs inched up during FY23. The majority of prime-housing-focused HFCs passed on rate hikes to customers in tandem with the rising cost of borrowings. With the yield on advances rising faster than the cost of borrowings, HFCs saw an improvement in margins during FY23. Improving margins coupled with waning credit costs have resulted in better profitability.

Figure 4: Profitability Metrics



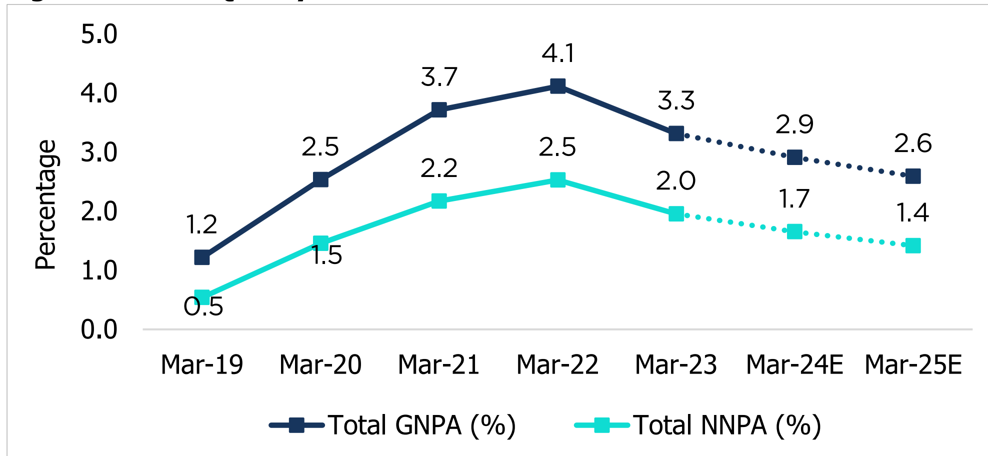
Source: CareEdge Ratings, based on top 15 leading HFCs in India

Going forward lenders are expected to adopt a calibrated approach between growth and asset quality. Further, anticipated interest rate cuts in FY25 are also expected to lead to downward pressure on margins as portfolios reprice faster vis a vis borrowing. While net Interest Margins (NIM) are expected to remain under pressure, overall profitability is expected to improve largely supported by declining credit costs. For FY24, CareEdge Rating expects the ROTA of HFCs to be near or marginally exceed pre-covid levels.

Waning asset quality stress

While developer financing portfolios of HFCs started showing signs of stress post-FY18, retail asset quality metrics witnessed deterioration led by pandemic-induced economic slowdown which largely impacted self-employed customers. However, with FY23 being the first full year of recovery in economic activity and improving demand, NPA levels have shown improvement which is expected to continue.

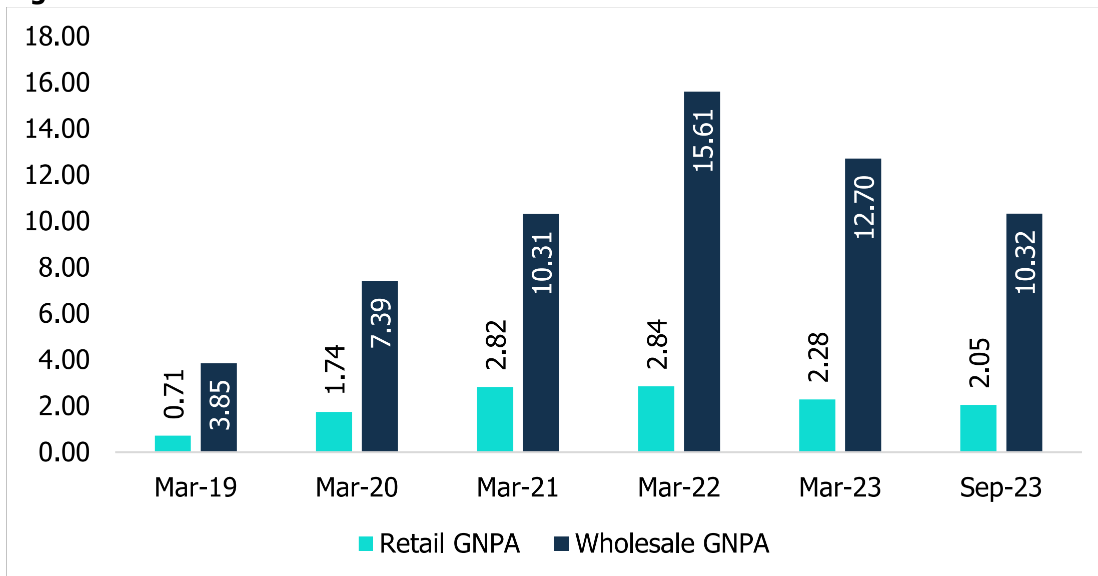
Figure 5: Asset Quality



Source: CareEdge Ratings, based on top 15 leading HFCs in India

FY23 has seen a significant reduction in both retail and wholesale NPA levels, after rising consistently for the past three years (FY20-FY22).

Figure 6: Trend in Retail & Wholesale GNPA



Source: CareEdge Ratings, based on top 15 leading HFCs in India

Net NPA to net-worth for HFCs has also improved from 16.6% to 11.7% signifying improving balance sheet strength and provision buffers. Stage 3 provision cover ratio which is estimated at 42% for housing finance companies as of March 31, 2023; is expected to remain healthy in the range of 44-46% in the near to medium term as HFCs continue to hold sufficient provisions to mitigate any credit risks.

Wholesale book stress receding

Stress in wholesale portfolios (including softer delinquencies+ NPA pool) of some HFCs which started to rise post-2018, peaked during FY22 and has started reducing since then. CareEdge Ratings interactions with HFCs as well as management commentaries point to expectations of better resolutions and recoveries of hitherto stranded projects in the scenario of improved sales velocity.

Figure 7: Stress in Wholesale Assets

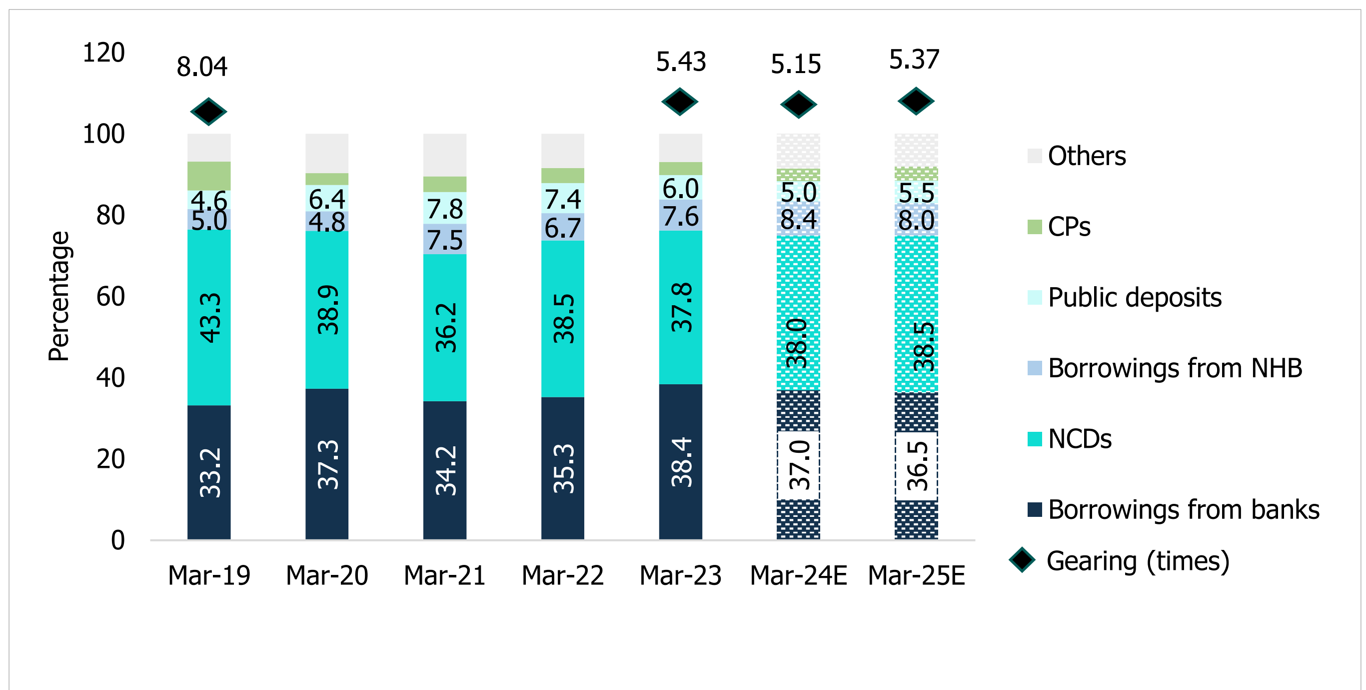
Source: CareEdge Ratings, based on top HFCs with significant wholesale exposures

Further, the overall percentage of HFCs portfolio in stage 2 improved to 5.1% as of March 2023 as against 9.0% as of March 2021 thereby depicting holistic improvement in asset quality.

Bank borrowings continue to be a major source of funding

While bank funding is expected to continue to have a lion's share in the funding profile of HFCs, funding from capital markets which has remained range-bound over the last few years is expected to rise.

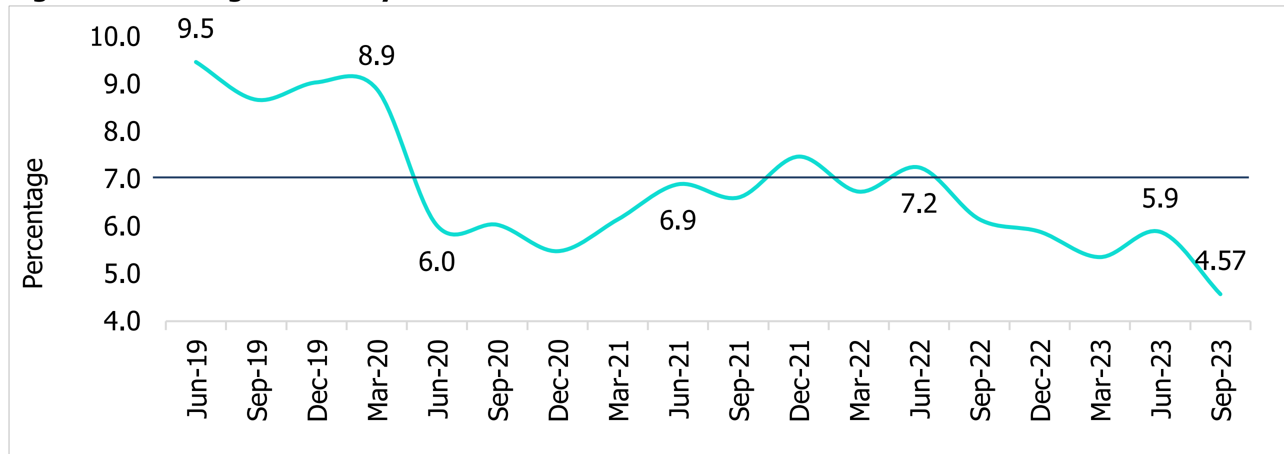
Figure 8: Borrowing Mix



Source: CareEdge Ratings, based on top 15 leading HFCs in India

Within the capital market participants, a look at debt mutual funds exposures to HFCs too shows a declining trend post 2019. While risk aversion within debt mutual funds was already underway owing to the credit crisis, the move gained further traction after the winding up of a few debt mutual schemes as well as significant regulatory changes such as sectoral caps etc. This led to a decline in debt mutual funds exposure to the HFC sector from peak exposure of 9.5% of overall AUM as of June 2019 to 4.5 % as of September 2023.

Figure 9: Funding to HFCs by Mutual Funds



Source: CareEdge Ratings, based on CareEdge Ratings rated debt mutual fund schemes

While the merger of HDFC Ltd into HDFC Bank in the recent past has further exacerbated this decline, the merger has opened sectoral limits for debt mutual funds for further investments in paper issued by HFCs. This along with expectations of rate cuts during FY25, rising spreads, and stronger HFC balance sheets is expected to increase the share of funding from capital markets in the HFC overall borrowings profile in the near to medium term.

Outlook

- As per Mr. Gaurav Dixit (Director – BFSI Rating, CareEdge Ratings) "continued growth momentum in housing loans coupled with an expected revival in developer loans is likely to lead to 12-14% AUM growth for HFCs. Segment-wise, while the share of wholesale financing of HFCs is expected to rise in the medium term, it is broadly expected to remain in the range of 10-12% as financiers embark on cautious growth. Driven by an up-cycle in residential real estate market and waning wholesale credit stress, pool of stressed wholesale assets as a proportion to HFCs net-worth is expected to improve to roughly 10% by March 2024."
- While NIMs may be marginally impacted; profitability during FY24 is expected to remain robust supported by portfolio growth with comfortable asset quality and receding credit costs.
- The downside risks to this outlook are regulatory changes, tighter liquidity, a continuation of elevated interest rates, delayed resolutions/ recoveries with respect to wholesale loans and competition from banks.

Contact

Sanjay Agarwal	Senior Director	sanjay.agarwal@careedge.in	+91 - 22 - 6754 3582 / +91 - 81080 07676
Gaurav Dixit	Director	gaurav.dixit@careedge.in	+91 - 11 - 4533 3235
Geeta Chainani	Associate Director	geeta.chainani@careedge.in	+91 - 11 - 4533 3235
Disha Potagevan	Lead Analyst	disha.potagevan@careedge.in	+91 - 22 - 6754 3447
Shivam Katkar	Analyst	Shivam.katkar@careedge.in	+91 - 22 - 6754 3588 / 580
Mradul Mishra	Media Relations	mradul.mishra@careedge.in	+91 - 22 - 6754 3596

CARE Ratings Limited

Corporate Office: 4th Floor, Godrej Coliseum, Somaiya Hospital Road, Off Eastern Express Highway, Sion (East), Mumbai - 400 022
Phone : +91 - 22 - 6754 3456 | CIN: L67190MH1993PLC071691

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