INDIAN MORTGAGE FINANCE MARKET JUNE 2019

Tough operating environment to impact housing credit growth and asset quality in FY2020

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Executive Summary

HIGHLIGHTS

- Overall market size of Rs. 19.1 lakh crore as on March 31, 2019; YoY growth slows down to 15% due to liquidity crunch in H2 FY2019
- Non-housing loan growth slows down to a greater extent
- Asset quality deteriorates marginally; could weaken further
- Securitisation, resumption of commercial paper (CP) rollovers and funding from banks support liquidity in Q4 FY2019
- Share of CP borrowings in overall funding mix drops to 6% as of March 2019 from 10% as of September 2018
- Higher upfront income softens impact of slower growth; helps maintain good profitability

OVERVIEW

As per ICRA's estimates, the on-book housing loan portfolio growth for housing finance companies (HFCs) and non-banking finance companies (NBFCs) reduced to 9% YoY for the year ended March 31, 2019 owing to the tight liquidity environment in H2 FY2019, which drove HFCs to lower their disbursements and augment their portfolio sales (through securitisation). Banks availed of this opportunity to increase their retail home loan portfolios and therefore, their growth increased to 19% in FY2019 (13% in FY2018) leading to overall market growth of 15% (17% in FY2018). Consequently, a modest shift in the market share was seen between the key lender segments in FY2019, with the market share of banks increasing to 64% as on March 31, 2019 from 62% as on March 31, 2018. This trend could continue for a couple of quarters. ICRA estimates that the total housing credit outstanding stood at around Rs. 19.1 lakh crore as on March 31, 2019.

Tight liquidity conditions, which have prevailed in the market since September 2018, impacted the growth plans of most HFCs with the on-book portfolio growth in FY2019 being low at 10%. Some HFCs witnessed a decline in their portfolios as well, owing to a significant decline in fresh disbursements and the high volume of securitisation required for the repayment of debt obligations.

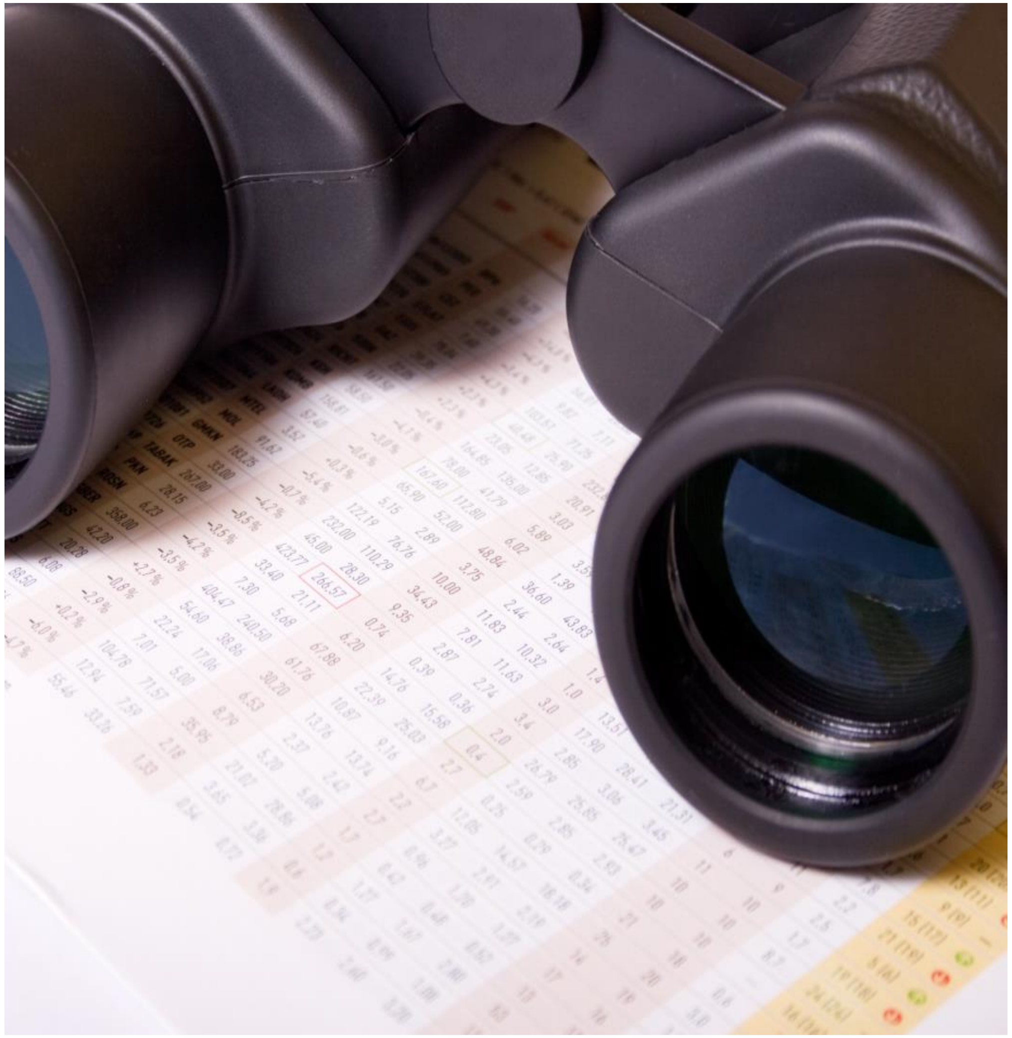
Unlike most of the previous financial years, when the non-performing assets (NPAs) declined in the last quarter through enhanced recovery efforts, gross NPA (GNPA) increased to 1.5% as on March 31, 2019 (1.4% as on December 31, 2018) from 1.1% as on March 31, 2018. Some reduction in the NPAs was seen in the affordable new housing segment, to 4.6% as on March 31, 2019 from 5.0% as on December 31, 2018. However, this improvement was largely due to write-offs and the sale of NPAs by some HFCs.

With tight liquidity being witnessed in the debt markets since September 2018, HFCs began focussing on raising longer-tenure funds as well as on raising funds through the assignment route. The share of CPs declined significantly to 6% as on March 31, 2019 from 10% as on September 30, 2018.

Consequently, the liquidity profile of the HFCs in the short-term buckets improved Q3 FY2019 onwards with gaps in the up to 1-year bucket reducing to around 3% as on March 31, 2019 (3% as on December 31, 2018) from around 6% as on September 30, 2018. Further, most of the HFCs continued to maintain on-balance sheet liquidity buffers for meeting near-term debt obligations and overcoming any sudden market disruptions.

The Reserve Bank of India (RBI), through its circular released on May 29, 2019, extended the dispensation on the relaxed minimum holding period (MHP) requirement for which the asset needs to reside on the books of the seller before it becomes eligible for securitisation. The period was extended to December 31, 2019 vis-à-vis May 2019 earlier (originally relaxed on November 29, 2018 for a period of six months). In ICRA's view, this would benefit HFCs and NBFCs offering mortgage loans where the loan tenure is typically more than five years. A greater proportion of their loan book would now become eligible for securitisation. Accordingly, these entities can raise more funds through the securitisation route, which will provide them with an additional funding source in a tight liquidity scenario. As per ICRA's estimates, based on the portfolios of HFCs and NBFCs as of March 2019, an additional Rs. 40,000 crore would become eligible for sell-down due to this change.

The overall profitability indicators for HFCs moderated marginally in FY2019 owing to some squeeze in the interest spreads because of the additional liquidity buffer maintained by many entities and the repricing of debt. Going forward, as most of the HFCs have increased their lending rates by 20-30 bps, the overall impact on net interest margins (NIMs) could be lower at around 15-25 bps. Further, a slowdown in growth is likely to impact the operating expense ratios.



OUTLOOK

Given the tough operating environment, ICRA expects housing credit growth in FY2020 to be in the range of 13-15% (lower than the last three years' CAGR of 17%). Banks are expected to grow at a faster pace than HFCs. As some HFCs aim to go slow on construction finance to conserve liquidity, given the lumpy nature of these loans, the growth in non-housing loans is expected to be even lower. However, given the low mortgage penetration levels in the country, the long-term growth outlook for the sector remains good and ICRA expects housing credit growth to recover as the operating environment improves.

The pressure on the asset quality owing to the tough operating environment is expected to continue. One of the emerging risk factors, which would need to be watched out for, is the stress faced by many developers with delayed under-construction projects. Further, under-construction properties sold by builders under subvention schemes or buyback/assured return schemes could be more vulnerable as some of the builders are facing a liquidity crunch and their ability to honour these obligations would be limited. In ICRA's opinion, GNPAs in the HFC home loan segment are likely to increase to around 1.1-1.3% over the medium term from the current level of 1.0%. Further, given the tight liquidity faced by some developers with delayed projects, the reduced fund availability to these developers could lead to some stress on the construction finance portfolio of the HFCs, leading to an increase in the overall gross NPAs for HFCs to around 1.5-2.0% over the medium term.

As for FY2020, ICRA expects the HFCs to report similar profitability indicators unless a prolonged slowdown in growth impacts the operating expense ratios and asset quality, which could lead to further moderation in the profitability indicators. The profitability indicators for FY2020 are likely to remain at 14-15%. However, upfront income booking on assignments could support profitability.

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