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Affordable housing finance segment gaining strength, higher interest rates unlikely to hit profitability

After posting muted growth in the financial year 2020-21, the affordable housing finance space grew 20% on-year in the fiscal year ending March 2022.

Written by Kshitij Bhargava
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CareEdge pointed out that the overall, higher NIMs along with controlled credit costs boosted the profitability profile of sector companies.

After posting muted growth in the financial year 2020-21, the affordable housing finance space grew 20% on-year in the fiscal year ending March 2022, a report by CareEdge said. Experts believe that the segment will continue to expand and post a growth rate of around 18% in the current fiscal year. "Overall, CareEdge expects affordable HFCs to continue to report healthy profitability metrics with RoTA of around 3%. Any impact of a decline in NIMs is expected to get largely offset by improved operating efficiency and controlled credit costs," CareEdge said in their report.

Holding interest rates aids profitability

Affordable Housing Finance Companies were relatively slow in passing on the benefit of lower interest rates to their customers, during the previous fiscal year, said CarEdge. This, analysts believe, helped improve the profitability of the companies. Despite the declining interest rate environment, yields remained largely in line with the pre-Covid levels (yields in FY21 were higher due to the cautious stance taken by most of the HFCs)," the report said. Funding costs for affordable HFCs, however, benefitted from the rising share of low-cost National Housing Bank funding along with the low-interest rate regime. NIMs of the affordable housing finance segment were improved to 7.4%.

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CareEdge pointed out that the overall, higher NIMs along with controlled credit costs boosted the profitability profile of sector companies. Affordable housing finance firms reported a RoTA of 3.1% — higher than the pre-Covid level

Improved asset quality

Bad loans of the affordable housing finance sector have moved southward as well as the segment improves its asset quality. Gross NPA ratio was down to 3.4% at the end of March 2022, from 4.1% earlier. Experts said that the segment reported strong recovery performance in the second half of FY22 as the economic activity picked up and the unorganised sector flourished.

Will higher interest rates hurt?

As the Reserve Bank of India (RBI) started hiking interest rates in this fiscal year, it would be taking the cards away from affordable housing finance companies that did not pass on the benefit of lower interest rates to customers. "With the change in the interest rate scenario, the lending spreads may come under pressure. Affordable HFCs have also started to pass on the rate hike to their customers, though at a relatively slower rate," experts at CareEdge said.

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The impact of the higher rates is believed to only be visible in the financial year 2024. "However, the spreads charged by lenders on these companies over benchmarks are generally getting compressed with improvement in the balance sheets of the companies," the report said. Overall, CareEdge expects affordable HFCs to continue to report healthy profitability metrics with RoTA of around 3%. The impact of a decline in NIMs is expected to be largely tackled by improved operating efficiency and controlled credit costs.

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