



ICRA
RESEARCH SERVICES

Lower interest rates and interest subvention to support housing loan growth, HFCs' competitive positioning may decline

Financial Sector Ratings

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Summary

The recent reduction in home loan rates by lenders is likely to improve the affordability of borrowers and could potentially spur demand. In ICRA's opinion, the reduction in lending rates could also lead to increased competition and balance transfers in the highly competitive housing loan market, especially in the prime salaried segment. While the lower rates are applicable only for new loans and loans linked to Marginal Cost of Funds based Lending Rate (MCLR), usually borrowers are given the option to shift to a lower interest rate by paying a fee which could lead to dilution in yields for the lenders.

In ICRA's opinion, while banks and larger HFCs would still be able to make reasonable returns, as banks currently have substantial funds parked in lower yielding investments, and realigning these funds for housing loans, would effectively have a positive impact on their profitability. Further, HFCs would also benefit from the reduction in MCLR by various banks and should be able to reprice a portion of their liabilities. Nevertheless, given that around 60% of the borrowings for HFCs are at fixed rates of interest, and the assets are largely floating, spreads could shrink over the medium term. In ICRA's opinion, the smaller HFCs are likely to get impacted more on account of their relatively higher operating cost ratios. Given that only a few HFCs would be able to match the interest rates being offered by banks, this could lead to some balance transfers from HFCs to banks and hence an increase in banking sector market share.

The Government of India has extended the Credit Linked Subsidy scheme under the Housing for All by 2022 to loans of value upto Rs. 12 lakh (from the Rs 6 lakh earlier)¹ and also added the middle income category to the economically weaker section (EWS) and lower income group (LIG) recognised as eligible earlier. This action is likely to expand the eligible borrower base for Credit Linked Subsidy Scheme, and also improve affordability of the borrowers owing to lower equated monthly instalments (EMIs) and hence debt burden ratios. While this could create a wider set of borrowers with access to formal credit channels leading to higher growth potential in the affordable housing segment, the extent of growth would hinge on the supply of such houses as well. Initiatives taken by the state governments and urban local bodies to provide land to keep the prices affordable while ensuring adequate returns for the developers would be critical to ensure adequate supply of affordable houses.

¹ Detailed guidelines on revised income criteria for the middle income segment are yet to be communicated by Ministry of Housing and Urban Poverty Alleviation

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