An Analysis of Profitability and Key Hurdles for the Housing Finance Sector in India

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There is a fear of recession worldwide as is evident from the decline in the economic activities in all major economies of the world. As per the prediction of the IMF, the Indian economy looks somewhat better placed compared to other major economies for the current financial year. The real estate sector has always been a significant contributor to the process of growth of India and depends on the soundness of the Housing Finance sector to a great extent. The study tries to examine the profitability of the housing finance sector as well as identifies significant hurdles, especially in the post Covid period when the fear of global recession looms large. Three leading housing finance companies based on market capitalization are taken as the sample companies and one-way Anova is used as a significant tool of analysis. The study points that the favourable time ahead for housing finance sector in near future.

Keywords: profitability, return on assets, return on equity (ROE), housing finance, assets quality

INTRODUCTION

Since the beginning of the current financial year, there has been discussion about the risk of a global recession all around the world. It is measured as a decline in global per capita GDP caused by the rapid worsening of growth prospects, increasing inflation, and tightening financial conditions. Forecasts for global growth in 2022 and 2023 have been significantly revised downward. The risk of a worldwide recession shortly is increased by at least two developments, which have either already occurred in recent months or maybe in the works, according to experience from prior recessions, even though their estimates do not indicate one in 2022–2023. First, every worldwide recession that has occurred since 1970 has been preceded by a considerable slowdown in global growth the year before, as has been the case most recently. Second, every prior global recession was accompanied by severe slowdowns or complete recessions in several important economies. Despite the present downturn in the global economy, inflation rates in many nations have reached multi-decade highs. Many nations are removing monetary and fiscal support to reduce the risks associated with persistently high inflation and in the context of constrained budgetary flexibility.

The IMF projects a meager 1.6% growth for the United States this year, down 0.7 percentage points from its prediction in July, and a paltry 1% growth for 2019. The IMF predicts 3.1% growth in Europe this year and just 0.5% growth in the following year. In contrast to the pandemic's impact on the global economy in 2020, when China's growth countered slowdowns elsewhere, its economic issues are escalating the downturn globally. China's economic growth is now projected by the IMF to be 3.2% this year and 4.4% in 2019. That is far slower than anticipated, for instance, from India, whose economy is developing at the quickest rate; the IMF anticipates 6.8% growth this year and 6.1% in 2023. Given the current scenario of growth of the Indian economy, the housing sector deserves special mention as one of the important drivers of growth. The true measure of a nation's development is not the height of its metropolitan cities but rather the increase in real estate development in its smaller towns, villages, and second and third-tier cities. As India marks its 75th year of independence, a significant milestone is being reached. The brilliant emergence of India's towns and villages, which are being bolstered by strong infrastructure, is the pinnacle of our nation's development. Additionally, the real estate market is being utilized to the fullest extent due to the growing demand from individuals. India has one of the world's fastest-growing major economies, and the real estate industry contributes to overall economic growth as the second largest employer in the country and also as the third largest sector in terms of the flow of FDI. By 2024, the real estate industry is anticipated to reach Rs 65,000 crore, and by 2025, it is anticipated that this sector will account for 13% of the nation's GDP. The real estate industry is unmistakably on a growth trajectory and is already charging into its next adventure. The real estate industry has been transforming over the past few months with cutting-edge initiatives in the residential, commercial, and retail sectors. The Indian real estate market has been adaptable and robust to meet the changing needs, and a variety of asset classes have been developed or are in the process of being developed. This market has developed as a result of shifting lifestyles, demographics, and enterprises.

Both the housing and home financing industries have experienced significant upheaval as a result of changes in monetary policy, COVID-19, and several other circumstances. They are intricately linked. The housing finance industry in India had a recovery in disbursements over the prior three quarters despite the second wave of the pandemic having an impact on business volumes. A formal evaluation determined that the growth was somewhat higher than the forecasted growth rate of 8–10% for FY22. The second wave of the pandemic reportedly had an impact on business volumes in the first quarter of FY22, which led to an increase in disbursements during the final three-quarters of FY22, according to the statement. Additionally, the sector's Gross Non-Performing Assets (GNPAs) decreased in the fourth quarter of FY22 after rising in the third. The Reserve Bank of India's notification, Prudential norms on Income Recognition, Asset Classification, and Provisioning Relating to Advances Clarifications, dated November 12, 2021, which tightened the standards for the identification and upgrading of GNPAs, led to an increase in GNPAs in the third quarter of FY22. However, the sector did experience a drop in GNPAs in the final quarter of the previous fiscal year as a result of the stronger recovery. The typical restructured book decreased to roughly 1.7% of AUM as of March 31, 2022, as a result of excellent recoveries from the restructured book and a rise in the assets under management. According to the agency, asset quality indicators will likely continue to rise in FY23 along with increased delinquent account collections. The study aims to analyze the profitability of the housing finance companies and examine the growth challenges of the sector post-covid-19 in India.

LITERATURE REVIEW

Reinhart and Rogoff (2008) contend that housing cycles have a considerable impact on economic activity by affecting wealth-related variables including consumption and investment in private residential projects. This is mostly a result of profitability swings and how they affect demand and employment in businesses involved in real estate. They went on to say that if housing prices deviate from fundamentals, the country's economic and financial stability may be in jeopardy, primarily due to the macro-financial connections that empirical research has shown to exist. One of the most significant causes of the financial crisis was the decline in real estate property values.

Ashwani et al., (2009) investigated the effects of a wide range of independent variables on the profitability of several HFCs, including interest revenue, interest expenses, non-interest income, operating and administrative costs, and personnel costs. The number of various variables that were correlated was examined using a bi-variate correlation study. They concluded that the overall profitability of housing finance organizations had decreased, as evidenced by the declining trend in return on capital invested.

Manoj (2010) assessed the operational efficiency for each of these businesses based on Return on Equity, using the operational efficiency of a sample of 10 well-known HFCs in India as represented by their respective cost-to-income ratios and ROE. Several statistical analytical approaches, including trend analysis, correlation analysis, and regression analysis, were used to evaluate the significant change. The study discovered considerable variations in the operational effectiveness of the most important HFCs in India, which are partially attributable to the fact that each HFC has been utilizing a distinctive price system.

Manoj (2010) examined the financial stability of home financing companies in India and factors that affect profitability using the "CAMEL method" and ROE Decomposition Analysis for a sample of the top 10 HFCs. Common financial analysis techniques like ROE Decomposition Analysis were used to analyze the profitability of the HFCs, and the "CAMEL" method was used to determine their financial soundness and classification into different groups. The relative financial soundness of HFCs in India varies noticeably, however it has been noted that all HFCs are consistently under pressure from rising costs. Monitoring costs carefully is necessary to increase ROE and increase their returns on investment.

Allen and Carletti (2010) claim that several real estate bubbles, not just in the United States but also in many other countries including Spain and Ireland, were the primary cause of the most recent global financial crisis.

Guruswamy (2012) conducted a comparison study on four Indian mortgage lenders: Housing Development Finance Corporation Ltd. (HDFC), LIC Housing Finance Ltd., Can Fin Homes Ltd., and Vysya Bank Housing Finance Ltd. (2012). Secondary data for ten years, from 1991-1992 to 2000-2001. That investigation found HDFC. and LIC Home Finance Ltd. was an outstanding house finance company that dealt with genuine competition in the housing finance industry. The following are important reasons fuelling the growth of the housing financing markets, according to Peppercorn (2013):

- Value for money, or maximizing the results of public resources through partnering with the private sector on government programs to achieve a greater multiplier;
- To increase the efficiency and efficacy of the programs, ensure collaboration between administrations and the public and private sectors.
- The public sector's role should shift from being a provider of housing to one of enabling it.
- Poorer households have a propensity for higher rates of borrowing from unofficial sources, according to Peppercorn.

Meghna Sarda & Ramesh Chandra Babu (2018) examine the financial standing of the NBFCs involved in home finance in their report, "Financial Performance Analysis of Selected Indian NBFCs in House Finance." The subject of the study is the famous stock exchange's listed companies. The camel parameters are represented via calculated, tabulated, and graphically displayed ratios. The hypothesis that compares the performance of the companies has also been looked at using statistical techniques like the ANOVA (f-test). GIC Housing Finance, Dewan Housing Finance Ltd., and GRUH Finance are placed second and third, respectively.

Satyanarayana & Ramu (2019) compare and contrast the financial results of five public HFCs and five private HFCs in India from 2009 to 2018 in their work titled "a comparative analysis between public and private housing finance companies (HFCs) in India." They accomplish this by utilizing a student t-test, some financial measures, and descriptive statistics that are based on means. They found that, as a result of regulatory changes and policy reforms, profitability and operational ratios had a considerable impact on the financial performance of both public and private HFCs.

Objectives of the Study

The main objectives of the study include the following:

i. To assess and compare the profitability of the housing finance sector in India
ii. To identify the challenges and suggest measures to over those challenges

RESEARCH METHODOLOGY

Sample

The sample companies are India Bulls Housing Finance Ltd. (IHFL), Can Fin Home Ltd. (CFHL), and PNB Housing Finance Ltd. (PHFL)

Key Variable

The variables which have been considered in the study return on equity and return on assets. Return on assets (ROA) and return on equity (ROE) are used for measuring the profitability position of the firm.

Time Period

The period of study is from 2017-18 to 2021-22.

Source of Data

The data on key variables is compiled from the annual reports of the firm. Stock Prices were collected from the NSE website.

The Hypothesis of the Study

H01: *There is no sign in the ROA among the sample companies.*

H02: *There is no sign in the ROE among the sample companies.*

Statistical Tools

The statistical tools that have been used in this study include arithmetic mean, standard deviation, compounded annual growth rate (CAGR), and one-way analysis of variance.

DATA ANALYSIS AND INTERPRETATION

Return on Assets

The return on assets ratio demonstrates how well a business can recoup its asset investment. In other words, ROA demonstrates the effectiveness with which a business can turn the capital spent on asset acquisition into net profits. A higher ratio is thought to be more advantageous to investors since it demonstrates how well the business is managing its assets to generate more net income. A rising trend in the company's profits is typically indicated by a positive ROA ratio. The return on assets of some representative corporations is shown in the following table-1:

TABLE 1
RETURN ON ASSETS (ROA)

Year	IHFL	CHFL	PHFL
2017-18	2.91	1.81	1.33
2018-19	3.14	1.58	1.42
2019-20	2.13	1.78	0.81
2020-21	1.28	2.06	1.3
2021-22	1.43	1.68	1.27
Average	2.18	1.78	1.23
S.D	0.84	0.18	0.24

Table 1 shows that IHFL has the highest return on assets on an average basis during the period of study followed by CHFL and PHFL. When it comes to variability, it is IHFL that has the highest variation in ROA followed by PHFL and CHFL. Now it can be tested whether there is a significant difference between the Return on Assets of sample companies based on the following ANOVA table-2:

TABLE 2
ONE-WAY ANOVA FOR ROA

Variation Source	*SS*	*df*	*MS*	*F*	*P-value*	*F crit*
Between Groups	1.35	2.00	0.67	2.42	0.14	4.26
Within Groups	2.50	9.00	0.28			
Total	3.85	11.00				

Interpretation

As the calculated value (2.42) is lower than the tabulated value (4.26) at a 5% level of significance, the null hypothesis is accepted, and concluded that there is no significant difference between the return on assets of the sample companies.

Return on Equity

This ratio calculates a company's earnings about the capital the owners of the business have invested. Earnings after taxes are split by owner equity to determine it. Shareholders in equity companies prefer higher returns on net worth. We may get a sense of the ROE of some companies from the table-3 below:

TABLE 3
RETURN ON EQUITY (ROE)

Year	**IHFL**	**CHFL**	**PHFL**
2017-18	28.66	19.24	12.8
2018-19	24.81	16.65	15.79
2019-20	14.15	17.49	8.08
2020-21	7.44	17.47	10.42
2021-22	7.06	15.36	8.47
Average	16.42	17.24	11.11
S.D	9.92	1.41	3.22

The above table shows that CHFL has a marginally higher ROE as compared to IHFL. However, the highest variability is noticed in the case of IHFL only. Now it can be tested whether there is a significant difference between the Return on Equity of sample companies based on the following ANOVA table-4:

TABLE 4
ONE-WAY ANOVA FOR ROE

Variation Source	*SS*	*df*	*MS*	*F*	*P-value*	*F crit*
Between Groups	73.59	2.00	36.80	1.34	0.31	4.26
Within Groups	247.29	9.00	27.48			
Total	320.89	11.00				

Interpretation

As the calculated value (1.34) is lower than the tabulated value (4.26) at a 5% level of significance, the null hypothesis is accepted and hence concluded that there is no significant difference between the return on assets of the sample companies.

Challenges of Housing Finance Companies in India

The lockdown due to Covid-19 had a significant impact on the Housing Finance Companies (HFCs) not only in India but also worldwide and is further expected to pose several challenges for the sector in the time to come. These challenges can be highlighted under the following heads:

Growth Rate in Credit

According to estimations from the industry and the pattern of new customer acquisitions following the moratorium, it appears that the sector is ready for a moderate increase in the credit of between 2 and 4 percent as compared to the previous fiscal year. The top quartile of HFCs is currently posting the same monthly amounts that they were during the time before the shutdown. The sale of new homes has suffered because those who have lost their jobs are experiencing a reduction in their cash flow. People are delaying making judgments about buying a property until their financial flows start to stabilize. The predicted credit growth in the industry would also be challenging to get given the loss of revenue during the lockdown and the limited recovery following the moratorium. The on-book portfolio of the housing financing companies grew by 15% year over year in the first quarter of FY23, according to a performance review of the current financial years. The significant growth in the first quarter was caused by the same period last year's sluggish growth, nevertheless. At the end of June 2022, home finance businesses' on-book portfolio was 12.7 lakh crore, up from 11 lakh crore the previous year. The solid industrial demand and rising level of economic activity were the driving forces behind the rise. Demand should continue to be strong in the future.

Quality of Assets

In addition to managing the existing loan book while dealing with client cash flow difficulties, the HFCs must also develop a high-quality portfolio that will stand the test of time. While the gross non-performing assets of affordable housing firms increased by 140 basis points, the gross NPAs of other housing finance companies increased from 3% in September 2021 to 3.3% by December 31, 2021. According to Crisil Ratings Agency, this is mostly due to the circular on the recognition and computation of NPAs from November 12, 2021, rather than any actual mark-down in asset quality. Due to this, the new criteria have had a 70-bp impact on their overall asset quality; otherwise, their gross NPAs would have been 2.6% in December.

Liquidity Management

Liquidity management has assumed top importance due to the decreased cash flows during the moratorium phase and the potential impact on the cash flows because of restructuring relief provided to the customers. The goal for smaller HFCs is to have enough cash to meet debt repayment commitments on time and to keep the new customer acquisition engine operating in an environment where bank lines are limited. Many of them are selling their portfolios as direct assignments to preserve funds on hand for this.

Profitability

The revenue line is already strained among the HFCs as lesser interest income is booked during covid. This is accompanied by higher provisioning needed to cover COVID-19 moratorium benefit cases, restructuring benefit cases, and an overall rise in NPA. Overall, keeping the bottom line figures becomes quite stressful.

FINDINGS AND DISCUSSION

The financial analysis of the sample companies in the housing finance sector in India highlights the following significant points:

- The return on assets of the sample companies was not found to be significantly different.
- Return on Equity differed significantly, CHFL has got better ROE.
- The Covid-19 had posed several challenges to the sector as far as credit growth and asset quality is concerned.

India is currently one of the economies in the world that is expanding the fastest, and it is anticipated that this trend will continue for the foreseeable future. On the other hand, other significant EM economies, including China, Turkey, and Brazil, have not yet been able to sustain a robust or consistent recovery. This tells us that the Indian economy is more advantageously situated in terms of growth prospects, opportunities, and risk and return profiles. The residential real estate market in India appears bright. In many developed and emerging economies, home sales and prices are declining below their previous peak; China's real estate market problems are well known. In India, however, real estate activity and prices have surged significantly since 2021 following several years of inventory and housing price stabilization. For several reasons, including improved governance, transparency laws, and other governmental changes, better affordability, developer consolidation, and stronger financial sheets, the real estate market is now much healthier. These all point to a favourable period for India's housing finance industry.

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