

# Evolution of the Regulatory Framework In Pakistan

Presented at 4th Global Conference on  
Housing Finance in Emerging markets  
May 26-27, 2010,  
World Bank, Washington

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# South Asia: Population Trends

| Country    | Total Population (mn) 2007 | Population Growth % 2007-2015 | Urban Population (mn) 2007 | Urban Population % of Total | Urbanization Growth % | GDP Growth Rate % 2000-07 |
|------------|----------------------------|-------------------------------|----------------------------|-----------------------------|-----------------------|---------------------------|
| India      | 1,125                      | 1.3                           | 329                        | 29                          | 2.5                   | 7.8                       |
| Pakistan   | 162                        | 2.1                           | 58                         | 36                          | 3.3                   | 5.6                       |
| Sri Lanka  | 20                         | 0.3                           | 3                          | 15                          | 0.2                   | 5.3                       |
| Thailand   | 64                         | 0.5                           | 21                         | 33                          | 1.6                   | 5.3                       |
| Indonesia  | 225                        | 1.0                           | 113                        | 50                          | 4.3                   | 5.1                       |
| Bangladesh | 158                        | 1.6                           | 42                         | 27                          | 3.7                   | 5.7                       |

# Pakistan: Demographic Snapshot

- Population: 160,000 million
- Population: 2/3<sup>rd</sup> rural, 1/3<sup>rd</sup> urban
- Poverty Rate: 24%
- Access to formal finance: 14%
- Total Housing Stock 20.48 million units
- Urban Housing Backlog 2.5-3.0 million units
- Candidate for micro-housing: 20% of population
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- Average household size: 6.6
- Major metropolitans cities like Karachi are facing high rate of urbanization, Karachi needs 100,000 new housing units per year to meet natural growth, address backlog & urbanization pressure

# Overview of Housing Shortage contd..

- Candidate for micro-housing: 20% of population
- Candidate for small-housing: 40% of population
- Min wage rate: Rs 7,000 (\$84) / month
- Total housing backlog 7.6 mn units
- Urban housing backlog: 2.5 to 3.0 mn units
- Persons/Room Density (Urban): 3.5
- Average household size: 6.6

# National Housing Policy 2001

- Government's as facilitator and regulator to stimulate housing sector.
- It outlines the improvement and development of financial and legal measures to facilitate the housing sector.
- Provides policy guidelines for Katchi Abadis (slum settlements) as
- Housing is declared as a Priority industry
- Housing Finance Companies are allowed to issue secondary market Bonds.
- **National Housing Authority** for Monitoring the implementation of the National Housing Policy

# Stakeholders: Housing Supply & Demand

## ■ Housing Supply:

- Public Sector: PHA, NHA, MoH, and MoF
- Private Sector: Builders and Developers

## ■ Housing Finance:

- Commercial Banks
- Development Financial Institutions (HBFC)
- Microfinance Institutions

## ■ Regulators:

- SBP for Commercial Banks and DFIs
- SECP for Housing Finance Companies (HFC)
- SBP for Micro Finance Institutions

# Regulation & Supervision of the Mortgage Finance Sector

- **SBP (Commercial Banks & HBFC):**
  - Enforcement of Prudential Regulations (PRs)
  - Housing finance is a part of Consumer Finance PRs, until housing specific PRs are framed
  - Annual On-site inspections (by Banking Inspection Department)
  - Off-Site Supervision through Off-Site Supervision & Enforcement & Banking Surveillance Departments
- **SECP:**
  - Housing Finance by NBFCs and HFCs are regulated by SECP under NBFIs Rules
  - Housing specific regulations are being framed

# SBP's Initiatives in Housing Sector

- Infrastructure and Housing Finance Department
- Setting up Housing Advisory Group
- Roadmap of immediate and short term goals
- Close coordination with Association of Builders and Mortgage Bankers Association
- Mechanism to bring on board the Urban Planners at the Federal and Provincial level



# SBP's Initiatives in Housing Sector contd..

- Implementation of HAG Recommendations
- Housing Finance Guidelines
- Housing Finance Prudential Regulations
- Guidelines on Risk management
- Long-Term Liquidity Facility Institution
- Capacity Building Program
- Product Development (Risk and Income Profile)
- Public Awareness Programs
- Involving Stakeholders

# SBP's Initiatives in Housing Sector contd..

- **Short-term:**
  - Large-Scale Developers' Finance Model
  - Enhancing Outreach of Housing/Mortgage Finance
  - Housing Observatory
  - Low-Cost Housing Finance Model
  - Low-Cost Housing Supply Models
  - Expansion of housing finance outreach (Geographical and Faith-Based)
  
- **Medium to Long Term:**
  - Enhance Mortgage Debt to GDP Ratio at 1% per annum
  - Promote Pro-Poor Housing by encouraging Low-Cost Housing Supply and microfinance institutions

# Housing Advisory Group of SBP

SBP formulated a Housing Advisory Group (HAG), drawing membership from different stakeholders. Its recommendations, given below, are being actively pursued by SBP:

- Reforming Legal Framework affecting Foreclosure, Transfer, Tenancy, Rent Control and Credit bureaus etc.
- Rationalization of Transaction Costs.
- Establishing an integrated land registration information system
- Increasing supply of land for affordable housing.
- Structuring and streamlining large scale developer's finance.
- Facilitate low-cost/low-income housing models and products.
- Facilitate Real Estate Investment Trusts (REITs)
- Provision of long term funding for housing loans.
- Housing Observatory (housing market information system).
- Capacity building of the mortgage banking industry in Pakistan.

# Development of Prudential Regulations for Housing Finance by SBP

- Currently Housing Finance regulations are covered under Consumer Finance Prudential Regulations.
- Since Housing Finance has its distinct nature and scope, there has been growing demand from all stakeholders to separate Housing Finance from Consumer Finance and to launch full-fledged Housing Finance Prudential Regulations.
- SBP is currently developing Guidelines on Housing Finance to cover Conventional Mortgages, Sharia-Compatible Mortgages.
- SBP intends to announce Housing Specific Prudential Regulations in in 2010-11.

## Prudential Regulations Cont'd

- Though permissible LTV is 85:15, normal practice is 70:30.
- Once the Mortgage Insurance is introduced ( under study), LTV may not exceed 80:20, since Sharia compliance calls for sharing of ownership and risk.
- Ratio of Mortgage Advances to Total Advances was relaxed from 5% to 10%, and currently there is no cap.
- Only Islamic banks have housing portfolio exceeding 10%, while conventional banks average around 5%.

# Prudential Regulations Cont'd

Central bank has recently tightened some PRs relating to Provisioning and Write-Offs:

- Benefit of Forced Sale Value
- Ageing of Overdue Repayments
- This has resulted in rise in reported NPLs in during 2008-09.
- Another reason for rise in NPLs is interest rate hike during the same period.

Guidelines on Risk management:

- Banks/FIs in mortgage finance need to have Risk Management and Compliance Functions
- Risk management and Compliance Functions periodically report to the Board of Directors, and send periodic reports to the Central bank on a prescribed format.
- Risk-weightage Guidelines for mortgage backed instruments of finance

# Large Scale Builder Finance Model

- SBP is working to develop financing models to facilitate large-scale builders/ developers' access to formal financial sector.
- The models are being developed in consultations with the *Association of the Builders and Developers (ABAD)*, *Investment Bankers and Association of Mortgage Bankers (AMB)*.
- Key challenges include:
  - Corporatization of large-scale developers.
  - Bankable financial statements
  - Credit rating (Entity and Instrument Ratings)
  - Fiscal issues relating to Book Value and Market Value, declared income and wealth etc

# Builder Finance Model Cont'd

- Financial Model are being developed in consultation with the Builders and Mortgage Bakers.
- Models to form basis for assessing project cost, cash flow streams, income etc, by the Banks, Tax and Municipal authorities.
- For builders not ready for Entity Rating, projects may be floated on Instrument Rating under SPV mechanism.
- Fiscal incentives to be designed based on Entity Rating, Instrument rating, Target Market segment based on income or geographical location.
- Extensive consultations are on with Association of Builders and Mortgage Bankers for development of financial and business model.



# Setting up of Pakistan Mortgage Refinance Company (PMRC)

- Major impediment in growth of HFCs is absence of LT Liquidity.
- Even Commercial banks are running tenor mismatch on housing portfolio.
- PMRC is being sponsored by Central bank, the financial institutions, insurance companies and Pension Funds.
- IFC is providing Technical Assistance and will possibly take 20% equity.
- Hybrid Business Model aims at covering both Sharia-Compatible and Conventional Mortgages.
- Since Islamic Banks are likely to be among sponsors and beneficiaries, it will be a unique model if successfully developed.

# Sharia-compliant Housing Finance

- In 2004 IBs share in total outstanding mortgages was 2% (Rs 0.7 bn). In 2009 it was 12% (Rs 9.0 bn) - a growth rate of 68% per year
- For CBs, it moved from 44% (Rs 16.0 bn) to 67% (Rs 49.6 bn) - a growth rate of 25%
- The NPLs as %age of total outstanding moved from:
  - Comm. Banks: 10% in 2008 to 17% in 2009
  - Islamic Banks: 3% in 2008 to 10% in 2009
- The main reasons for rise in NPLs were:
  - Rise in profit rates
  - Enforcement by SBP of more stringent Prudential Regulations on NPLs and Provisioning.

# Role of Sharia-Compliant Housing Finance

- Makes Housing Finance accessible by faith-based clientele (expansion of outreach)
- Islamic Housing Finance grew more faster than Conventional Banks
- Housing Finance Portfolio as percentage of overall bank financing:
  - 2.5 to 3% for Conventional Banks
  - 10% for Islamic Banks
- Housing Portfolio is among the most favored and secure asset class on Islamic principles of finance.
- Risk sharing and management ( joint ownership), and not Risk elimination
- Financing instruments are asset backed, not paper backed (Derivatives)

# Pro-poor Housing: Main Issue of Asia-Pacific Region

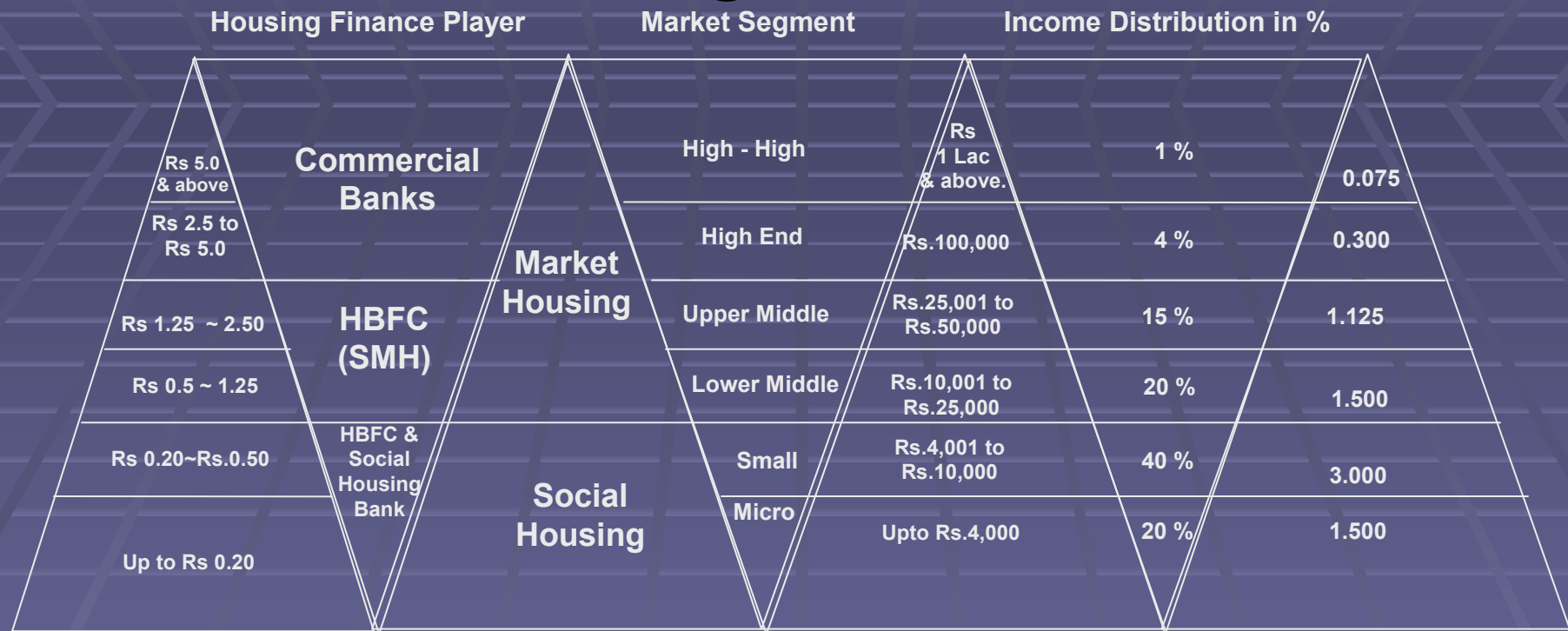
- Asia-Pacific Union for Housing Finance (APUHF): A regional platform has been set primarily to address Pro-Poor Affordable Housing Issues.
- APUHF needs your support and cooperation.

**Pro-Poor Housing:**  
**Issues We Know**  
**Answers We Need**

**Thank You!**

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# Housing Continuum



**Mortgage Affordability**  
(Rupees in Million)

- Per Capita Income
- Minimum Wage Rate

**Housing Market**

Rs.7,500 per month  
Rs.7,000 per month

**Income Distribution**

**Housing Shortage \***  
(In Million)

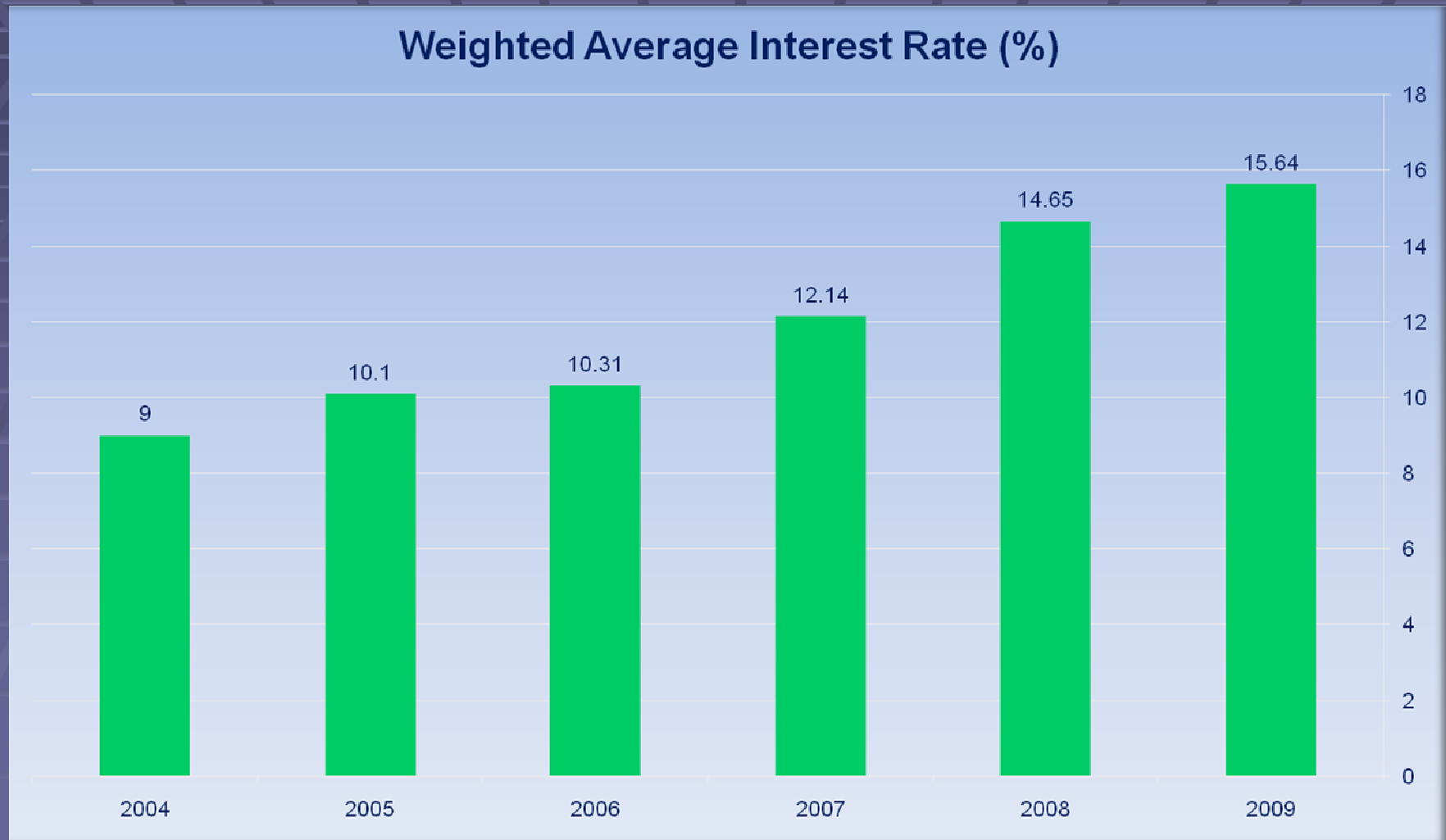
Total existing backlog is estimated at 7.5 Million units. The shortage in various income segments is assumed in the same proportion as per income distribution pattern. However, actual shortage is much higher in low income segments as opposed to higher income segments.

# Outstanding Mortgage Portfolio

Housing Finance Portfolio (Rs million) (end-Dec figures)



# Recent Interest Rates Hikes





## Outstanding Housing Finance Portfolio

