State Bank of Pakistan

For the Quarter ended September 30, 2014

Quarterly Housing Finance Review

Infrastructure, Housing and SME
Finance Department,
State Bank of Pakistan.

The Team

Team Leader

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Members

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Executive Summary

The Infrastructure, Housing & SME Finance Department of State Bank of Pakistan presents its Quarterly Housing Finance Review to reflect data on housing finance, collated on quarterly basis from public sector banks, private banks, foreign banks, and DFIs. It portrays trend of different parameters like disbursements, outstanding and recoveries.

At present, twenty seven commercial banks, House Building Finance Company Limited (HBFCL) and one microfinance bank are catering to the housing finance needs. HBFCL is the only specialized housing bank in the country providing housing finance since 1952, while commercial banks entered the mortgage business in 2003. HBFCL is still the only institution with mandate to cater to the lower-middle and low-income groups.

During current quarter, an increase of Rs 268.20 million was witnessed in gross outstanding of housing finance (0.51 percent). The continued growth in housing finance portfolio is an encouraging sign. Overall housing finance portfolio currently stands at Rs. 52.9 Billion. HBFCL remained the largest shareholder, in terms of gross outstanding, with the share of 24 percent. However, based on category, Private Banks remained the largest players with 37 percent share in gross outstanding. Fresh disbursement for the quarter accounted for Rs. 2.88 billion with 708 new borrowers. NPLs, however, in terms of their ratio to outstanding, remained unchanged at 30 percent during current quarter. HBFCL, being the largest player in the housing finance market, accounted for 48.60 percent of new borrowers and contributed 15.54 percent of the new disbursements equivalent to Rs. 447 million. Islamic banks disbursed Rs. 1.54 billion as of September 30, 2014. Furthermore, major chunk of total outstanding remained directed towards "outright Purchase" category as 61 percent of total outstanding was used to finance "outright purchase" housing loans. It was followed by "Construction" and "Renovation" products with 28 and 11 percent respectively.

For the quarter ending September 30, 2014, Islamic banks remained active in extending housing finance; however, conventional commercial banks have not pursued housing finance products actively. Reasons behind the sluggishness in growth of mortgage portfolio are numerous; ranging from difficulties related to foreclosure law & titling issues to overall financial environment. Another reason hindering the growth of housing finance in Pakistan is reluctance of banks for lending outside few big cities. Moreover, the lack of effective institutional framework, secondary mortgage market, high transaction costs, unorganized real estate sector, inadequate property development framework and long term funding arrangements are also the major constraints towards the growth of housing and housing finance in the country.

Keeping in view growth in housing finance during the last two quarters, housing finance has started picking up after 2008. It is expected that SBP's stance of reducing policy rate will further help in enhancing affordability and demand for housing finance in Pakistan. All this will be instrumental to increase economic growth through positive changes in 40 allied industries to housing sector.

Contents

State of Housing Finance

There was shortage of around 8 million housing units in Pakistan in 2009, which has been accumulating by 0.34 million units every year (World Bank, 2009). As of today, housing units' shortage can be estimated more than 9 million units. As for property finance, most of the housing finance is arranged through personal resources. The formal financial sector caters to only 1 to 2 percent of all housing transactions in the country, which is quite lower compared to regional countries, whereas the informal lending caters up to 10-12 percent of such transactions.

The property development industry suffers from low public confidence. Financial weaknesses and the absence of clear and fair business practices have affected its credibility, contributing to the reluctance of financial institutions in providing development and construction finance. There is a strong need to strengthen the property titling and land administrative procedures including improvements of the legal provisions, standardization of processes, and computerization of all relevant revenue records. These steps will enhance the financing by the formal sector.

Weakness in the existing legal framework also impedes the financing opportunities of the formal financial sector. The Financial Institution Recovery Ordinance, 2001 empowered financial institutions in case of default to foreclose a mortgage property without recourse to the court of law. However, Section 15 of this Ordinance has been declared "ultra vires" to the constitution by Honorable Supreme Court of Pakistan. This has made foreclosure of mortgaged property tedious and time consuming.

Although the regulatory framework for land registration and transfer regime exists in Pakistan, the process by which land is acquired and registered is cumbersome at times, because of number of institutions and registration procedures required to execute property transactions. Land records are manually maintained leading to errors and omissions and resultantly they have modest commercial value for the mortgagee financial institutions especially in rural and some urban areas. The lack of efficient and reliable system of ascertaining the bona-fide of property titles has forced banks to limit the access of housing finance to a certain number of urban localities within the urban centers.

In addition to this, national and local master plans for town planning and housing facilities are either inadequate or poorly enforced, which leads to inefficient allocation of land and uncontrolled urban development. Over-restrictive building codes and laws on subdivision limit the efficient use of urban land and increase the price to consumers, especially in zones having relatively higher prices of lands. Moreover, the large scale projects often get delayed due to failure of utility companies in connecting new housing developments in time.

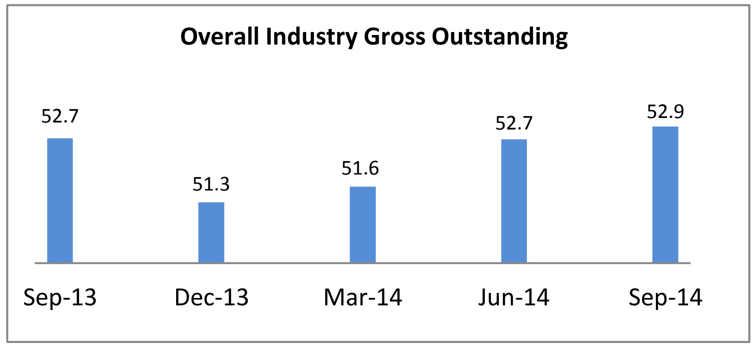
As far as the real estate sector is concerned, majority of real estate builders and developers are working as sole proprietorships or partnerships with limited capital and informal corporate governance structures. Absence of sound governance structure within the housing developer industry creates lack of good practices, illegal construction, unreliable building permits, and legally unprotected advance purchase of units that are required to be built in future. The unstructured and unsupervised nature of business of real estate brokers/ agencies, which could serve as natural arrangers for the provision of financial services, is also a significant constraint to the provision of housing and housing finance. Consequently, it is difficult for financial institutions to verify the character, capital, and capacity of potential clients. Risk assessment and portfolio valuation is also fragile, which is another factor for the lenders' extreme caution for transaction initiated by these venture. As a result, financial institutions are reluctant to enter this market, which in turn causes scarcity of finance and constraints in the supply of housing. Without using a strong regulatory authority to enforce corporate governance and allied standards for this sector, the quality of availability of housing facilities across population spectrum may not improve.

Major Trends

Gross Outstanding

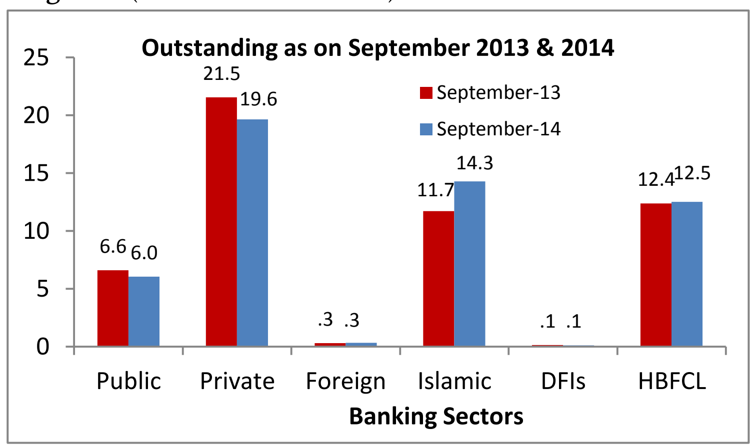
The gross outstanding finance as on September 30, 2014 of all banks and DFIs stood at Rs. 52.9 billion (Figure 1), compared to Rs. 52.7 billion in previous quarter, showing an increase of Rs. 0.27 billion (0.51 percent) over the quarter.

Figure 1 (Amount in Rs. Billion)



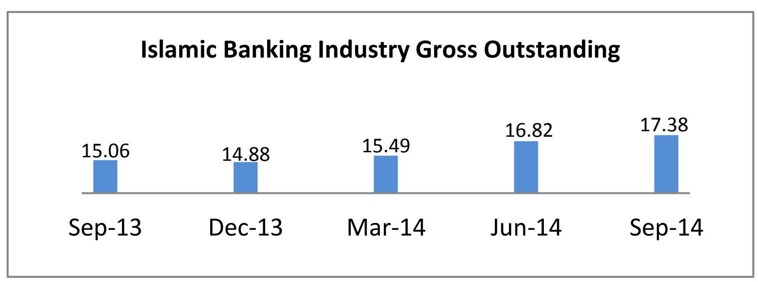
Banking sector-wise gross outstanding on quarters ending September 2014 and 2013 are shown in Figure 2. Of the gross outstanding as of September 30, 2014, commercial banks accounted for Rs. 40.3 billion. Private banks reported Rs. 19.6 billion followed by Islamic banks at Rs. 14.3 billion, public sector banks at Rs. 6 billion and foreign banks with Rs. 0.3 billion. The outstanding loans of HBFCL were Rs. 12.5 billion; up by 0.9 percent over the last year. Other DFIs had a meager share of Rs. 0.1 billion in outstanding loans. The data confirms that primary housing finance market in Pakistan is at nascent stage, which needs to be developed by creating enabling environment and initiatives by public and private sector.

Figure 2 (Amount in Rs. Billion)



Compared to the quarter ended June 30, 2014, gross outstanding of the banking sector decreased over the year except for Islamic Banks and HBFCL. Islamic Banks showed an increase of 3.78 percent from previous quarter and reached to Rs. 14.28 billion by the end of September 2014. HBFCL showed a meager increase of 0.7 percent over the previous quarter.

Figure 3 (Amount in Rs. Billion)



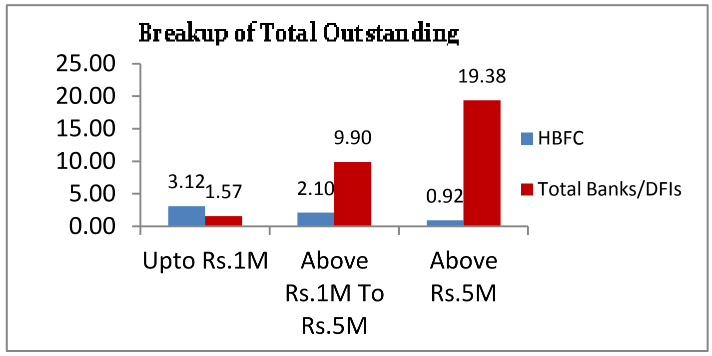
The gross outstanding housing finance as on September 30, 2014 of Islamic Banking Industry (Five Islamic Banks (IBs) & 14 Islamic Banking Divisions (IBDs) of Conventional Banks) stood at Rs. 17.38 billion. Compared to quarter ended June 30, 2014, gross outstanding of Islamic banking Industry increased by 3.34 percent as shown in Figure 3. This is a positive sign and reflects significant potential in Islamic banking.

Of the gross outstanding in Islamic housing finance, Islamic banks accounted for Rs. 14.28 billion; an increase of 3.77 percent over the quarter. IBDs of conventional banks posted Rs. 3.1 billion. Islamic bank's aggressive efforts for pursuing housing finance have yielded such a growth in their outstanding portfolio.

Figure 4 shows the breakup of total outstanding in terms of loan size. As of September 30, 2014, HBFCL and All Banks & DFIs reported outstanding loans net of NPLs in the category 'Up to Rs. 1 million' as Rs. 3.12 billion and Rs. 1.57 billion against 12,022 and 4,968 borrowers respectively. In second category 'Above Rs. 1 Million to Rs. 5 Million', HBFCL reported Rs. 2.10 billion and all Bank & DFIs reported Rs. 9.90 billion outstanding. In the third category 'Above Rs. 5 Million', HBFCL reported Rs. 0.92 billion and all Banks DFIs reported Rs. 19.38 billion outstanding. This reflects that major chunk of total outstanding in housing finance is inclined towards category "Above Rs. 5 M". Furthermore, it also shows that HBFCL has large portion of its portfolio in small-sized loans (Up to Rs. 1 M) compared to other Institutions that are tilted towards larger loan size (Up to Rs. 5 M & above).

This confirms that banks are focusing on high-end customers. However, to increase primary mortgage market, banks have to extend their services to low income and salary class customers as well.

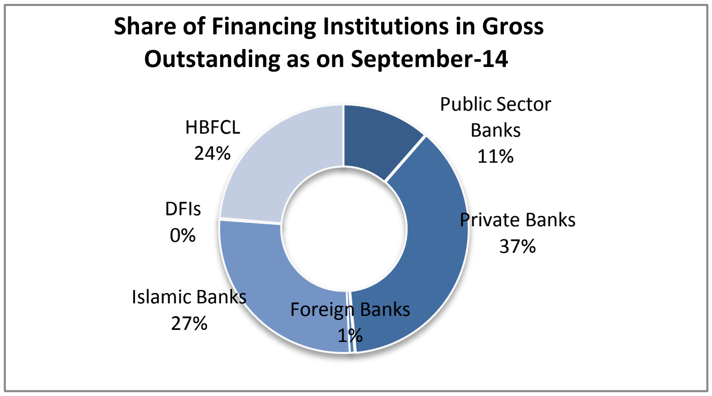
Figure 4 (Amount in Rs. Billion)



Share of Banks

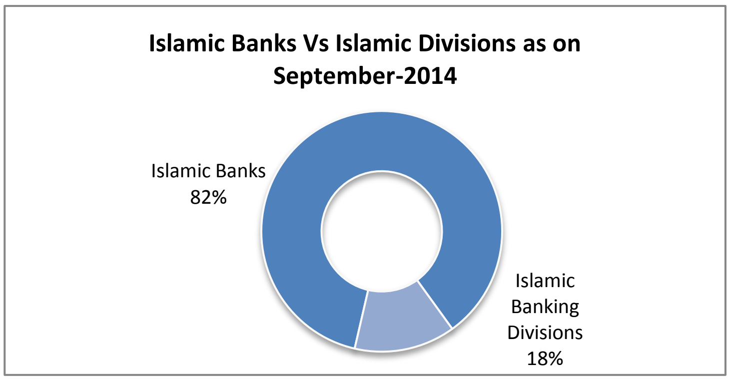
The share of private banks decreased by one percent to 37 percent and that of Islamic Banks increased to 27 percent over the quarter. Share of public sector banks decreased by 1 percent to 11 percent. However, share of foreign banks and HBFCL remained unchanged over the quarter. It is worth mentioning that Islamic banks have surpassed HBFCL with respect to gross outstanding. This is in line with consumer's preference for Islamic banking over conventional banking. Islamic banking has huge potential in housing finance market which is still untapped.

Figure 5



The share of Conventional Banking (excluding HBFCL), Islamic Banking Industry and HBFCL in the total outstanding was 43 percent, 33 percent and 24 percent respectively as on September 30, 2014. IBDs (12 windows) and IBs (05 banks) have 18 percent and 82 percent share respectively in housing finance portfolio of Islamic Banking Industry (Figure 5.1). Compared to previous quarter, market share of Conventional Banking (excluding HBFCL) decreased by one percent over the last quarter. The share of Islamic banking industry, however, increased by one percent to 33 over the previous quarter. On the other hand, market share of HBFCL remained unchanged since June 2014.

Figure 5.1:



Non-Performing Loans (NPLs)

NPLs increased from Rs. 15.66 billion (September 30, 2013) to Rs. 15.93 billion (September 30, 2014); 1.75 percent increase during the quarter as shown in Figure 6. Figure 7 compares NPLs as a percentage of outstanding portfolios at the end of quarters on September 30, 2014 and 2013. Figure 8 shows a comparison of existing NPLs status of different banking sectors with last year.

HBFCL's NPLS showed a marginal increase of Rs. 18 million (0.28 percent) over the yester quarter ended June, 2014. Furthermore, its percentage share in its total outstanding is greatest after Foreign Banks' NPLs. At the end of current quarter, 51 percent of its total outstanding constitutes NPLs (Figure 7). HBFCL's percentage share in total NPLs is 40 percent.

Excluding HBFCL, NPLs for all banks and other DFIs have decreased by 2.74 percent over the quarter. The percentage share of NPLs of all banks and other DFIs (excluding HBFCL) was 60 percent in total NPLs as on September 30, 2014.

Among banks, as shown in Figure 8, non-performing finances (NPFs) of Islamic banks witnessed a decrease of 11.04 percent during the year, from Rs. 1.7 billion to Rs. 1.5 billion. Their NPFs constitute 9.23 percent, as on September 30, 2014, of total industry NPLs. NPLs of the public sector banks decreased by 2.67 percent from Rs. 1.8 billion to Rs. 1.7 billion, over the year, which were 28.63 percent of their gross outstanding as of September 30, 2014. Private Banks' NPLs decreased by 7.35 percent, from Rs. 6.5 billion to Rs. 6 billion. NPLs of foreign banks as a percentage of their outstanding portfolio remained at 78.18 percent. NPLs of DFIs (excluding HBFCL) increased from Rs. 53.14 million to Rs. 56.98 million; a 7.22 percent increase over the year.

NPFs for Islamic Banking Industry (IBs & IBDs) shown in Figure 9 were reported as Rs. 1.91 billion on

Figure 6: (Amount in Rs. Billion)

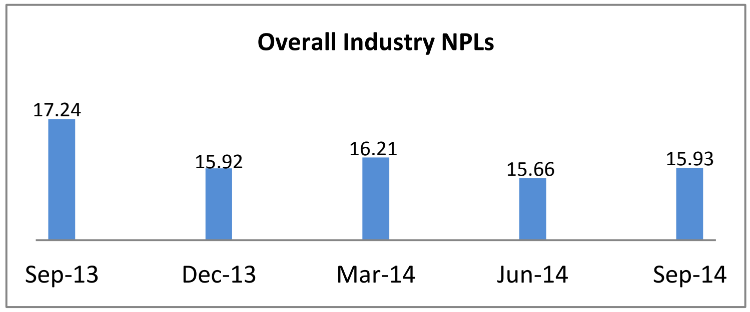


Figure 6.1: (Amount in Rs. Billion)

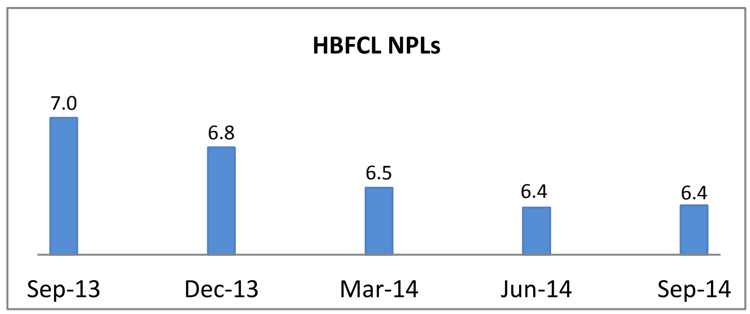
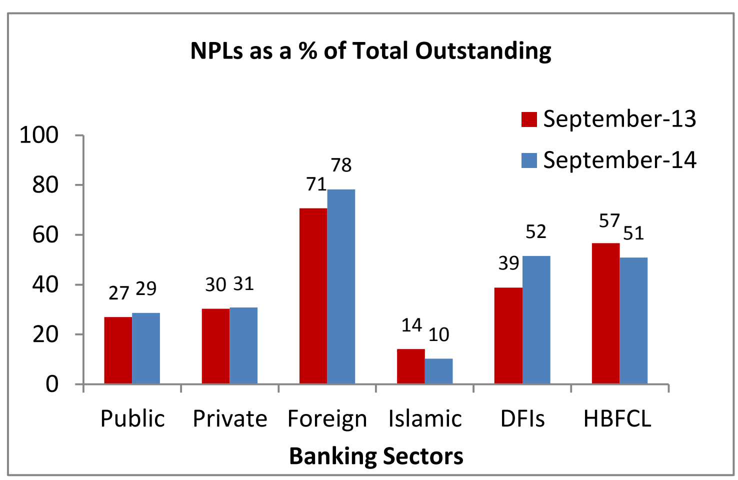


Figure 7 (Percentage)



September, 2014, which were Rs. 1.89 billion at the end of June 30, 2014, showing a marginal increase of 1.15 percent.

Figure 10 shows the breakup of NPLs in terms of Loan disbursed i.e. up to Rs. 1 million, above Rs. 1 million to Rs. 5 Million and above Rs. 5 million. As of September 30, 2014, Rs. 5.47 billion of 41,218 borrowers were recorded as NPLs in the category of 'up to Rs. 1 Million' out of which Rs. 5.15 billion belonged to HBFCL and Rs. 0.32 billion was reported by All Banks & DFIs. In the second category 'Above Rs. 1 million to Rs. 5 million', total defaulters were 2,074 with the amount Rs. 4.37 billion, as on September 30, 2014, out of which Rs. 0.96 against 675 borrowers were reported by HBFCL and Rs. 3.41 billion against 1,399 borrowers were reported by All Banks & DFIs. In the third category 'Above 5 Million', total NPLs were Rs. 6.08 billion against 863 borrowers. Out of these, 108 defaulters with the amount of Rs. 0.25 billion were of HBFCL and Rs.5.83 against 755 borrowers belonged to All Banks & DFIs.

Figure 8 (Amount in Rs. Billion)

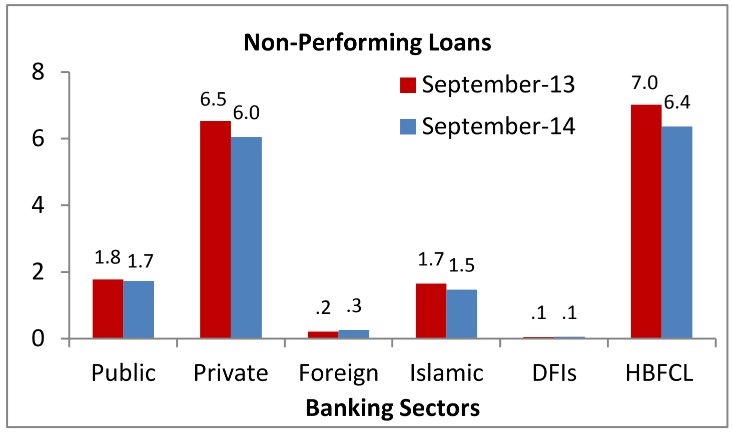


Figure 9 (Amount in Rs. Billion)

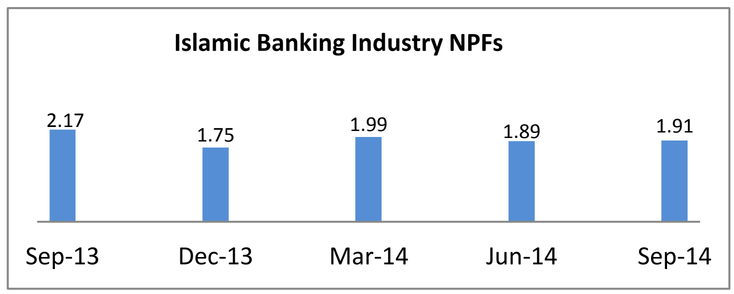
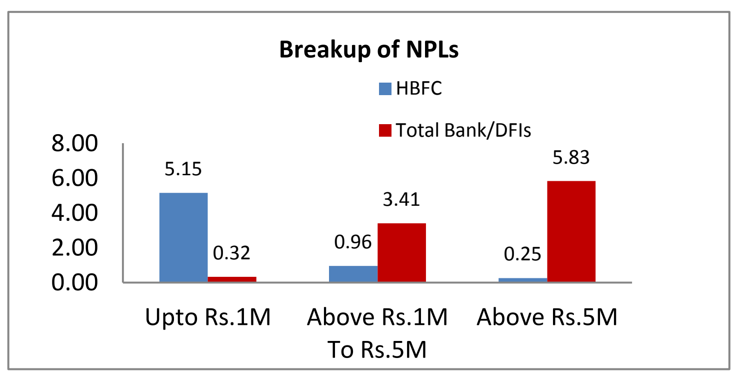


Figure 10 (Amount in Rs. Billion)



Number of Borrowers

Number of borrowers decreased from 78,275 to 74,465 since September 30, 2013; a decline of 4.87 percent. As shown in Table 1, there was a decrease in number of borrowers in each category except in Islamic Banks. It may be inferred that borrowers, currently, prefer Islamic banking over conventional banking and find it more attractive in terms of product and structure.

Compared to previous quarter, number of borrowers decreased by 0.57 percent. Furthermore, excluding HBFCL, 12.84 percent of total borrowers of housing loans have been classified as non-performing.

Figure 11 (Number of Borrowers)

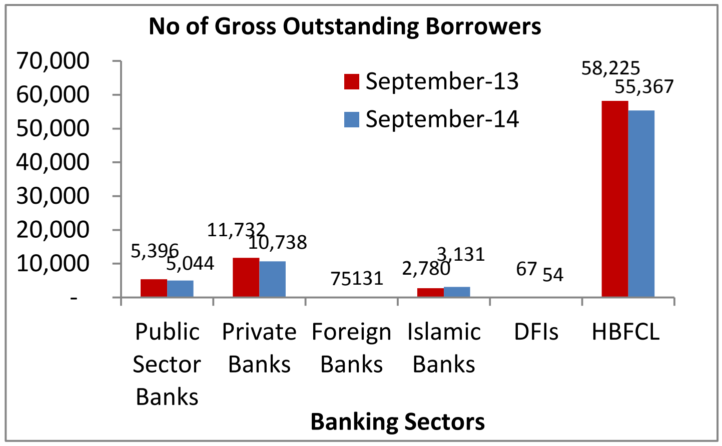


Table 1

	September – 14			September – 13		
Banks/ DFIs	**No. Active Borrowers**	**No. of Borrowers classified as NPLs**	**Total O/s Borrowers**	**No. Active Borrowers**	**No. of Borrowers classified as NPLs**	**Total O/s Borrowers**
Public Sector	4,405	639	5,044	4,732	664	5,396
Private Banks	8,908	1,830	10,738	9,780	1,952	11,732
Foreign Banks	21	110	131	27	48	75
Islamic Banks	2,852	279	3,131	2,465	315	2,780
DFIs	40	14	54	58	9	67
HBFCL	14,084	41,283	55,367	14,047	44,178	58,225
Total	30,310	44,15	74,465	31,109	47,166	78,275

Disbursements

Fresh disbursements of Rs. 2.88 billion (Figure 12) were made to 708 borrowers during the quarter ending September 30, 2014 (Table 2). Islamic banks extended new disbursements with Rs. 1.54 billion followed by private banks with Rs. 857.94 million and public sector banks with Rs. 33.47 million. HBFCL's fresh disbursements (Figure 13) for the quarter were reported to be Rs. 447 million. Among commercial banks, the number of new borrowers totaled 364, with private banks serving 161 new borrowers and Islamic banks 189 customers. HBFCL extended loans to 344 new borrowers during the quarter under review.

Fresh disbursement for Islamic Banking Industry was Rs. 1.71 billion to 217 new borrowers during the quarter ending September 30, 2014. This includes new disbursements of Rs. 172.5 million to 28 customers by IBDs of conventional banks.

Figure 14 shows the disbursement break-up in terms of loan size. Commercial banks disbursed Rs. 1.80 billion (144 borrowers) in terms of loans above Rs. 5 million and Rs. 0.05 billion (31 borrowers) against the category up to Rs. 1 million.

Figure 12: (Amount in Rs. Billion)

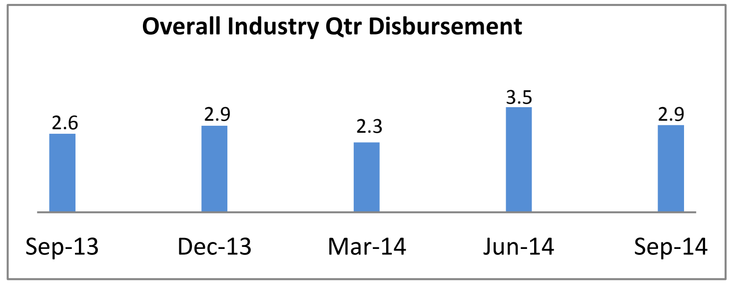


Figure 13: (Amount in Rs. Billion)

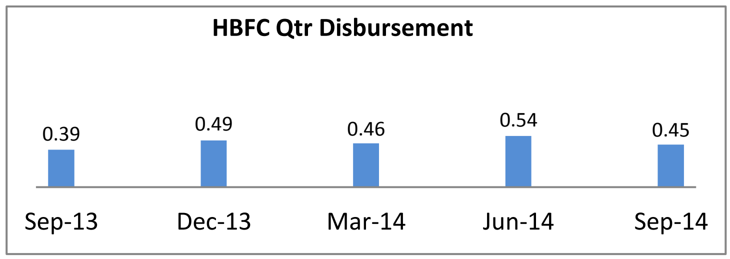


Figure 14 (Amount in Rs. Billion)

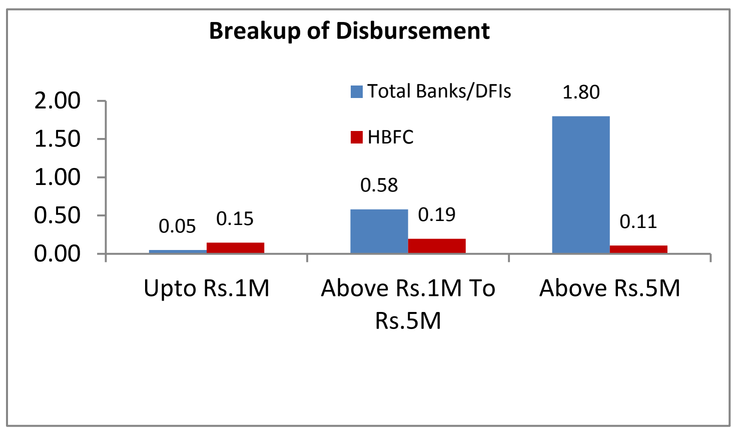


Table 2

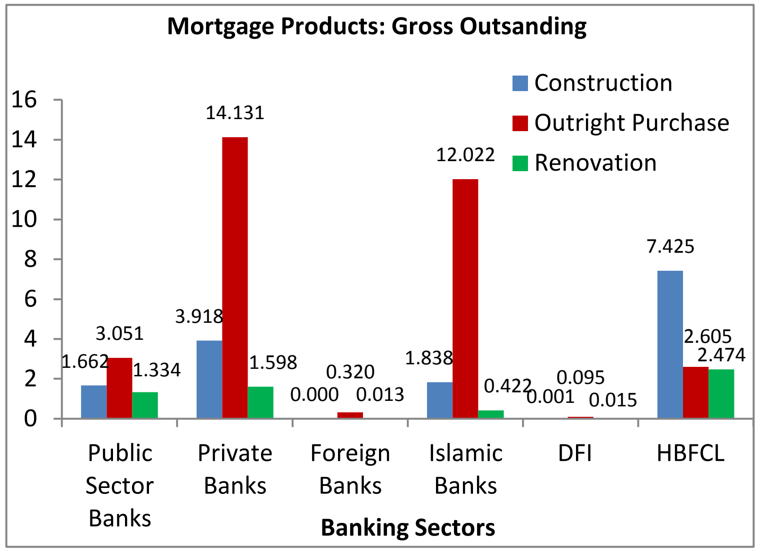
New Disbursements during the quarter ending June 30, 2014		
	Amount (Rs. Millions)	**No. of Borrowers**
Public Sector Banks	33	14
Private Banks	858	161
Foreign Banks	-	-
Islamic Banks	1,538	189
All Banks	2,429	364
DFIs	-	-
HBFCL	447.0	344.0
Total	2,876	708
Islamic Industry	1,710	217

Products Category-Wise Share

The biggest share of housing finance continued to be attracted towards outright purchase (Figure 15).

The gross outstanding for 'outright purchase' stood at Rs. 32.2 billion as on September 30, 2014; a 61 percent share in total outstanding of Rs. 52.9 billion. This is followed by the 'construction' category where gross outstanding reported at quarter-end stood at Rs. 14.84 billion and that of 'renovation' stood at Rs. 5.86 billion. Active portfolio shows that private banks took a lead in financing for outright purchase at 45 percent followed by Islamic banks that have the share of 37.31 percent in outright purchase financing. HBFCL has taken lead in financing two sectors i.e. construction category 50 percent and renovation category 42.25 percent.

Figure 15 (Amount in Rs. Billion)



Analysis of Financing Variables adopted by Banks/DFIs and HBFCL

Tables 3 to 6 summarize financing variables across all banking sectors including weighted average mark-up rate, average maturity period, Loan-to-Value ratio (% financing by banks) and average loan size.

Weighted average Markup rate

The overall weighted average Markup rate was 13.1 percent at the end of the current quarter as shown in Table 3. Highest weighted average profit rate was reported as 14 percent by HBFCL and foreign banks. Islamic Bank's rate stood at 13.4 percent and Private Sector banks at 10.8 percent.

Table 3

	Weighted Average Interest Rate (%)				
	Sep-14	Jun-14	Mar-14	Dec-13	Sep-13
Public Sector Banks	**13.7**	14.0	14.0	10.8	11.3
Private Banks	**10.8**	11.7	13.2	13.8	13.8
Foreign Banks	**14.0**	14.0	14.0	14.7	14.7
Islamic Banks	**13.4**	13.2	13.1	12.9	12.9
All Banks	**12.2**	12.4	13.3	13.3	13.3
DFIs	-	-	-	-	-
All Banks & DFIs	**12.2**	12.4	13.3	13.3	13.3
HBFCL	**14.0**	14.0	14.0	13.0	13.0
Total Average	**13.1**	13.2	13.7	13.1	13.1

Average maturity periods

Average maturity period of outstanding loans as on September 30, 2014 was 12.8 years. HBFCL's average maturity period was 12.8 years, while that of Public Sector Banks is 10 years. Table 4 shows that among commercial banks, Private Banks extended housing finance loans for average tenure of 13.6 years followed by Foreign Banks with 12.5 years and Islamic Banks with 11.2 years.

Table 4

	Average Maturity Period (Years)				
	Sep-14	Jun-14	Mar-14	Dec-13	Sep-13
Public Sector Banks	**10.0**	12.0	6.3	9.0	9.0
Private Banks	**13.6**	13.7	11.5	13.7	13.7
Foreign Banks	**12.5**	12.5	12.5	10.8	10.8
Islamic Banks	**11.2**	11.2	9.9	10.7	10.7
All Banks	**12.2**	12.7	10.5	12.1	12.1
DFIs					-
All Banks & DFIs	**12.2**	12.7	10.5	12.1	12.1
HBFCL	**12.8**	12.5	11.5	12.2	12.2
Total Average	**12.8**	12.5	11.5	12.2	12.2

Loan to Value ratio (LTV)

The percentage of financing (Loan to Value ratio) extended by banks and DFIs remained 37.2 percent during the year (Table 5). Average LTVs of commercial banks remained 41 percent over the quarter. The average LTV for HBFCL was reported at 33.4 percent at the end of quarter July-September, 2014.

Table 5

	Loan to Value Ratio (%)				
	Sep-14	Jun-14	Mar-14	Dec-13	Sep-13
Public Sector Banks	**46.7**	46.7	46.7	46.7	46.7
Private Banks	**33.2**	30.4	28.7	41.6	41.6
Foreign Banks	**45.3**	45.3	45.3	44.0	44.0
Islamic Banks	**38.9**	42.1	39.0	41.3	41.3
All Banks	**41.0**	41.1	39.9	43.4	43.4
DFIs	-	-	-	-	-
All Banks & DFIs	**41.0**	41.1	39.9	43.4	43.4
HBFCL	**33.4**	40.3	44.2	44.6	44.6
Total Average	**37.2**	40.7	42.1	44.0	44.0

Average loan size

Average loan size for disbursements made during the quarter ending September 30, 2014 (Table 6) was Rs. 3.8 million. The average loan size for HBFCL was Rs. 2.5 million. Private Banks reported an average financing size of Rs. 5.8 million, Foreign Banks 5 million and Islamic Banks reported an average financing size Rs. 5.1 million. Public sector bank's average loan size stood at Rs. 3 million.

Table 6

	Average Loan Size (Rs. Millions)				
	Sep-14	Jun-14	Mar-14	Dec-13	Sep-13
Public Sector Banks	**3.0**	6.5	2.2	3.6	3.6
Private Banks	**5.8**	8.6	8.9	4.4	4.4
Foreign Banks	**5.0**	5.0	5.0	5.0	5.0
Islamic Banks	**5.1**	6.0	4.6	5.1	5.1
All Banks	**5.1**	7.5	6.9	4.5	4.5
DFIs	-	-	-	-	-
All Banks & DFIs	**5.1**	7.5	6.9	4.5	4.5
HBFCL	**2.5**	2.6	2.2	2.0	2.0
Total Average	**3.8**	5.0	4.5	3.3	3.3

Housing Finance Business of Microfinance Banks:

Gross Outstanding

The outstanding housing finance of Microfinance Banks (MFBs) was Rs. 218.56 million as on September 30, 2014 which was Rs. 217.89 million at the end of previous quarter. It registered an increase of 0.31 percent, over the last quarter.

Number of Borrowers

The number of outstanding borrowers increased from 2,158 to 2,177 over the quarter; an increase of 0.8 percent.

Non-Performing Loans

NPLs for MFBs were reported nil for the current quarter.

Mortgage to GDP Ratio:

While calculating mortgage to Grand Domestic Product (GDP Nominal), following figures were taken in to account.

- Outstanding finances of Commercial Banks, DFIs and Microfinance banks were Rs. 52.9 Billion as of September 30, 2014.
- Amount of finance availed by employees of the banks and DFIs was Rs. 61.710 Billion as of September 30, 2014.
- Nominal GDP for FY14 was Rs. 25,401.895 billion

Mortgage to GDP Ratio = Total Mortgages/GDP

Mortgage to GDP ratio was **0.45%** as of September 30, 2014.

Acronyms

ABAD	Association of Builders and Developers
DFI	Development Finance Institution
GDP	Gross Domestic Product
HAG	Housing Advisory Group
HF	Housing Finance
HBFCL	House Building Finance Company Limited
HFCs	House Finance Companies
IB	Islamic Bank
IBD	Islamic Banking Division
LSDF	Large Scale Developer Finance
LTV	Loan to Value Ratio
MRC	Mortgage Refinance Company
NPL	Non Performing Loan
NPF	Non Performing Fund