Box 3.1.1: Growth Issues in Consumer Finance and SBP Measures

Consumer finance (CF) in Pakistan is one of the financially underserved segments of the credit market. It has not been able to grow steadily and achieve some level of maturity despite witnessing historic growth during CY03-07. In recent years, the growth in CF has been robust but financing to additional consumers appears quite moderate.[134]

Moreover, CF to GDP ratio of Pakistan is considerably lower than other emerging market economies (**Table 1**). One of the factors is weak mortgage financing which contributes only 17.83 percent to total CF. This is in sharp contrast to other emerging market economies where mortgage finance generally contributes around half of the CF.[135]

Table 1

Consumer Finance as Percentage of GDP - Cross Country Comparison

Country	FY14	FY15	FY16	FY17
	Percent			
Pakistan	1.15	1.17	1.20	1.29
India	7.71	8.05	8.72	9.86
Indonesia	38.43	38.53	38.60	39.20
Malaysia	34.05	35.16	35.11	33.69
Mexico	2.99	3.10	3.31	3.34
Philippines	7.14	7.96	8.78	9.44
Thailand	28.12	29.05	29.11	28.78

Source: SBP & Haver Analytics

As a result, unlike other jurisdictions, from stability point of view, CF poses meager threat to Pakistan's economy at present. Given its importance for economic growth and limited stability risk concerns, SBP has made mortgage financing one of its top priorities.

Over the past few years, CF has picked up momentum with an average annual growth of 12.47 percent during CY13-17. Particularly in CY17, CF has grown by 20.62 percent (YoY basis), highest since CY07. This is largely driven by growth in auto loans (34.61 percent) followed by mortgage loans (29.82 percent). Other than the secured nature of auto loans, banks' growing attraction towards auto industry, in recent years, is the increase in demand of automobiles.[136]

Table 2

Component-wise distribution of Consumer Finance

	CY13	CY14	CY15	CY16	CY17
	PKR Billion Outstanding				
Credit Cards	21.4	22.8	24.7	28.3	34.2
Auto Loans	55.8	70.9	95.1	125.9	169.5
Consumer Durable	0.2	0.3	0.3	0.3	0.7
Mortgage Loan	53.1	52.3	54.4	61.6	80.0
Other Personal Loans	142.6	147.7	161.1	155.7	164.1
Consumer Finance	273.2	294.0	335.6	371.8	448.5
Total Advances	4,505.5	4,930.0	5,330.1	6,013.1	7,029.4
Consumer Finance as %age of Total Advances	6.06	5.96	6.30	6.18	6.38

Source: SBP

Historically, low interest rates have encouraged the banking sector to increase CF due to *search-for-yield* motive. With easy monetary policy in vogue recently, banks have opted to take on more risk to maintain their interest income.[137] Moreover, ease in repayment capacity of the borrowers (induced by low interest rates) has led to higher demand for CF as well. Resultantly, as the CF has increased the infection ratio has come down to 6.21 percent in CY17 from 8.11 percent in CY16. Lower credit risk has provided further impetus to banks to take on more exposure in CF.

Despite recent momentum in CF, there are numerous impediments that the banks face. Consumer's low level of income discourages them to extend CF beyond a small pool of salaried individuals.

[134] The number of CF customers has increased by an average of 2.88 percent during CY14-17 as opposed to 13.30 percent increase in amount of CF.

[135] Analysis reveals that by removing mortgage finance, total CF declines by around half in case of India, Malaysia, Philippines and Turkey.

[136] According to the data published by Pakistan Automotive Manufacturers Association (PAMA), in CY17, the total number of automobiles produced has increased by 19.04 percent (39.97 percent in CY16), whereas, the number of automobiles sold has increased by 19.05 percent (40.67 percent in CY16).

[137] Spread of the banking sector declined to 2.18 percent in CY17 from 2.52 percent in CY16.

Moreover, structural problems in housing industry have hindered the potential growth of mortgage finance in Pakistan. Weak foreclosure standards, lengthy judicial procedures and non-automation of documentation are dis-incentivizing banks from going into mortgage financing. Moreover, prevailing real estate prices along with unfavorable terms and conditions of existing mortgage products make mortgage finance affordable only for high net worth individuals.[138]

In light of the aforementioned issues in CF, within its domain, SBP is playing an active role to facilitate CF in Pakistan.

1. In CY17, SBP with the support of World Bank has established Pakistan Mortgage Refinance Company (PMRC) to improve access of housing finance in Pakistan. Besides dealing with the existing market failures, the purpose of PMRC is to encourage fixed rate mortgages and longer maturity loans to allow lower-middle and middle class households to have access to mortgage finance.

2. SBP has revised Prudential Regulations (PRs) for housing finance. The main purpose was to increase the extent of additional housing finance and remove restriction on the frequency of property revaluation.[139]

3. The regulatory retail portfolio (including CF) limit under Basel Capital Framework has been enhanced to PKR 125.0 million from PKR 75.0 million. This development is expected to support the growth of credit to the retail sectors as well as SMEs.[140]

4. SBP also takes into account customer complaints in order to retain consumer confidence in the financial system. For this purpose SBP has launched Consumer Grievances Handling Mechanism (CGHM) and a dedicated helpline for banking customers.[141,142]

5. Following the international best practices, SBP has developed *Product Disclosure Requirements* and *Know Your Rights and Responsibilities as a Banks' Consumer*.[143,144] This will assist consumers in making informed decisions over diversified and complex financial products.

6. SBP in collaboration with Pakistan Banks Association (PBA) established the Electronic Credit Information Bureau (e-CIB). SBP collects and consolidate the monthly information of individual borrowers, which is accessible on request to any bank. This facilitates assessment of the credit worthiness of borrowers.

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[138] The World Bank: Pakistan Housing Finance Project (P162095): http://documents.worldbank.org/curated/en/277261492752441488/pdf/ITM00184-P162095-04-21-2017-1492752439147.pdf
[139] IH&SMEFD Circular No. 3, 2017
[140] BPRD Circular No. 08, 2017
[141] BC&CPD Circular No. 01, 2016
[142] BC&CPD Circular No. 04, 2017
[143] BC&CPD Circular No. 2, 2016
[144] BC&CPD Circular No. 1, 2017