Housing Finance

Welcome Address on the occasion of the inauguration of Housing Finance Conference at Karachi on 11th December 2002

I would like to dwell on the rationale for the Central bank of the country to organize a Conference on Housing Finance and bring together all the various stakeholders involved in the housing and construction industry.

First, the broad-based financial system reforms which involve restructuring of the financial institutions, liberalization of financial markets, introduction of financial engineering and new products and services, improvement in the quality of assets, provisioning of bad loans, mergers and acquisitions and a new model of non-bank financial companies have led to a partial cleansing up of the system. Although there is much to be achieved, the financial system has acquired strength and some space to diversify and branch into new areas of business.

Second, the competitive forces, reduced borrowing demand from the government, lower interest rates, upsurge in rupee deposit mobilization, de-dollarisation of the economy and rising inflows of remittances have created an excess supply of loanable funds at the disposal of the banking system. For the first time in many decades the banks have embarked on aggressive marketing to sell their loans. The beneficiaries of this excess supply of funds are the well established corporate sector firms who are able to obtain credit at very thin margins thus squeezing the profitability of the banking system.

Third, the increased awareness of risk management and the traditional reliance on security and collateral of loan can be employed profitably to develop asset-based lending and housing finance provides a major opportunity in this regard. The recovery rates in mortgage housing markets and profit margins have been on average, higher than project and corporate lending.

Fourth, Pakistan is one of the few countries which is blessed with billions of investment locked – up in the existing stock of residential as well as commercial properties that can be recycled for similar class of assets. This leveraging on bankable properties could unfreeze immense amount of investment funds for households. Virtually every major city of the country has fully bankable assets locked up in the commercial and residential areas. The challenge for the banking industry is to develop home equity products which can put cash in the hands of these property owners for consumption and investment purposes.

Fifth, during the last three years the enabling environment has been made conducive to attract and facilitate investment in housing. The restrictions on commercial banks to lend for housing and other consumer durables have been removed, the upper limits on mortgage loans have been raised to Rs 5 million, foreclosure loans have been revised so that the banks can repossess the properties without recourse to the courts, interest payments upto Rs 100,000/- on mortgage loans have been rationalized, banks have been allowed to float long term bonds to match their mortgage assets, special purpose vehicles have been allowed to develop pools of asset backed securities which can be traded in the market and off-loaded from the balance sheets of the originating banks. The SBP and SECP are open to suggestions for bringing about further changes in the regulatory environment to make it amenable and friendly for mortgage financing.

Despite the above favorable developments, the housing finance sector has not yet taken off. There are many constraints and difficulties in the way of this take-off. Our initial consultations with the various stakeholders have identified a set of constraints which need to be resolved.

The first constraint is the complex legal framework, lack of clarity of the title deed and problems in registration, enforcement of contracts, difficulties in eviction of tenants at the expiry of leasing period, frozen rent control laws, prolonged litigation in the courts of law, bias in favour of possession of the property to the chagrin of owners and related problems. We have to simplify, streamline and strengthen the legal framework, establish a clear system of title deeds of property and procedures whereby dispute about these deeds are resolved amicably, and take other actions to provide fair treatment to the creditors and borrowers, the owners and tenants.

The second constraint is the taxation of property transactions, stamp duties and like. These are estimated to be about 10 percent of the value of the transaction and are real deterrent for developing a well functioning. This high cost is further compounded by corruption, delays and obstacles that push the buyers and sellers into resorting to misuse of power of attorney and benami transactions. The Provincial and local governments will earn higher revenue yield if they make the taxation, assessment, registration, recording and retrieval system customer friendly. The shift to benami and informal housing markets will be averted if the tax rates and duties are lowered.

The third constraint is that the provision of requisite sites and services is not only inadequate but the attitude of utility companies is a hindrance in new housing development. There are cost overruns because the basic services such as telephone lines, water, electricity, sewerage, gas are not provided on time. It is in the business interest of these companies that they should expand their customer base and income by reaching out to these new housing schemes. On the contrary, collusion, nepotism and under-hand dealings by some unscrupulous elements have marred the orderly growth of these housing schemes. There is an urgent need for these utility companies to re-examine their strategy and thus maximize their revenue streams.

The fourth constraint is that institutional investors such as insurance companies, provident funds, pension funds etc. have not actively explored real estate development and housing markets as an investment vehicle. There is a natural fit between their appetite for long term assets and the middle class income groups' aspirations to acquire housing and pay their installments over a long period of time. The institutional investors should invest in real estate related equities, long term lending or mortgage-backed securities. There is a natural alliance whereby the retail distribution of mortgage loans is handled by the commercial banks through their network while the wholesale business is the domain of the institutional investors.