State Bank of Pakistan

Development of Strategic Goals for Housing Finance in Pakistan

Infrastructure and Housing Finance Department

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The Infrastructure and Housing Finance Department of State Bank of Pakistan presents 'Development of Strategic Goals for Housing Finance in Pakistan'.

This paper is in fulfillment of one of the development project approved for FY 2008-09.

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Introduction

According to the UN-Habitat, half of humanity now lives in cities, and that the urban population will increase to 60% within next two decades. Developing world with highest growth rate of urban population absorbs on an average about 5 million new urban residents every month and thus accounts for 95% of the world's urban population growth. Urban growth is a result of a combination of factors namely geographical location, natural population growth, rural-to-urban migration, infrastructure development, national policies, corporate strategies and other major political, social and economic forces.

The population of Pakistan is estimated to be over 166 million[1]; approximately increasing at the rate of 2% per annum[2]. Urban population as a percentage of total population has been recording a growing trend with a 23.7% share in total population during 1995 and 34.9% share during 2007. This proportion of urban population is greater than that of India (29.2%), almost similar to Maldives (35%) but less than China (46%). There are approximately 10 urban centers in Pakistan and the two biggest centers (Karachi and Lahore) alone constitute 62% of the total population of these 10 cities. Of this highly concentrated urbanization trend, over 45% of the total urban population is believed to be living in slums. This high concentration of slum households in Pakistan can be associated with a variety of factors, including lack of investment in infrastructure, critical shortage of housing units, poverty and instability.

The need for the government and financial institutions to respond adequately and timely to this resultant increase in housing demand perhaps has never been more critical. The ability of financial institutions to meet this demand in turn hinges on the overall institutional and regulatory framework of a country relating to housing and financing the housing needs.

Although the role of financial institutions in providing adequate credit to the housing sector is only part of a bigger puzzle, the inability of financial institutions to adequately respond to housing finance needs, poses as a significant supply side constraint. This paper sets out to establish goals that need to be achieved in order to create an enabling and sustainable housing finance system in Pakistan. It is pertinent to mention that this paper serves as an extension to the Housing Advisory Group (HAG)'s recommendations made in 2007 and establishes clear goals that particularly fall under the ambit of State Bank of Pakistan.

[1] The Federal Bureau of Statistics, Pakistan
[2] Key Indicators for Asia and the Pacific 2008

Establishing Goals

In order to create an efficient housing finance system in Pakistan, the economic, social and political context needs to work in tandem with the housing policy environment. In the policy environment objectives need to be clearly defined, goals need to be established keeping in view constraints posed by the country's institutional framework and strategies then need to be laid out to achieve these goals. It is important to set goals that serve both the short and long term objectives; that is of the 'creation of an enabling and sustainable housing finance system in Pakistan'.

The Objective – 'Create an Enabling and Sustainable Housing Finance System'

An *enabling* action is one that sets boundaries and gives support while relinquishing control[3]. To enable a housing finance system to work efficiently it is important that steps are taken to develop a market based financial sector which is adequately governed under regulations that define boundaries and set limits to risk on one hand, while encouraging competition through innovation on the other. Of course there are other factors external to the financial sectors that play an equally important role in allowing the system to function efficiently e.g., political system, legal system that can efficiently enforce contracts etc. However, for the purpose of this paper we limit the scope to highlighting factors that are internal to the housing finance system in Pakistan.

A *sustainable* system is one that is capable of being maintained at length without interruptions, weakening or loss in power or quality[4]. Housing finance systems as part of a financial system is known to be in a perpetual state of flux and transformations, either due to external or internal imbalances. In order to make the housing finance system sustainable, the housing policy environment should be such that the kind of housing finance system instilled should not be capable of impeding its own performance endogenously, even in the absence of unanticipated events.

Goals

Being at a nascent stage, housing finance in Pakistan still requires the right set of policies to make it sustainable in the long run. It is important that these set of policies give impetus to housing finance now and in the future too by continuously evolving to ensure that it is able to expand in the long run. Figure 1 illustrates constituents of an enabling and sustainable housing finance system in Pakistan. This framework has been developed as an extension to HAG's recommendations that pertained to the financial sector. These areas, requiring policy intervention have been defined in 5 broad areas, namely;

1. Improvements in housing finance regime
2. Presence of long term funding source
3. Enhanced outreach
4. Capacity building initiatives
5. Growth of large scale developer finance

[3] Angel (2000)
[4] Center for Sustainable System. http://css.snre.umich.edu/index.php

Figure 1

Creating an Enabling and Sustainable Environment for Housing Finance System

MAJOR GOALS				
Improve Housing Finance Regime	Establish Long-Term Funding Mechanism	Enhancing Outreach	Continue Capacity Building Initiatives	Promoting Large Scale Developer Finance
Sub-Goals	Sub-Goals	Sub-Goals	Sub-Goals	Sub-Goals
Improving Effectiveness of Foreclosure Laws	Creation Of Secondary Mortgage Market	Provision of Low-cost Housing	Developing Mortgage Banking Industry	Credit Rating
Improvements in Prudential Regulations	Utilization of Long-term Investors Funds (Pension Funds, Insurance Etc)	Reduce Credit Rationing Of Mortgage Lending	Developing Housing Market Information System (HMIS)	Simplification of Loan Documents
		Encouraging Competition	Establishment of a Housing Observatory	Standardization f Valuation Methodology
		Encourage Innovative Solutions For Product Delivery		
		Awareness Campaign For Borrowers		

Each of these 5 major goal areas has been further divided into components (sub-goals) that collectively represent a particular major goal.

Goal 1- Improve Housing Finance Regime

The kind of housing finance system that is prevalent is, to a large extent, determined by the finance regime (state or condition) it operates under. This finance regime reflects on the policy environment; i.e. it reflects on the set of financial rules, regulations and policy interventions that motivate, enable, and constrain housing finance. Both the ECE review and Angel (2000) identify regulatory instruments that describe and affect the state or condition of housing finance. Common to both are (a) enforceable contracts and foreclosure laws that guarantee secure transactions and (b) prudential regulations that ensure the health of financial institutions and put in place a risk management system. Angel also points to restrictions that aim at controlling mortgage lending by rationing credit, as a third regulatory instrument, often found in a housing finance regime.

Improvement to the existing housing finance regime can be sought by sieving through the existing housing finance regime and identifying factors requiring policy intervention. Two such policy intervention areas are identified, which will collectively aim at improving the housing finance regime in Pakistan.

Sub-goal 1-Improving Effectiveness of Foreclosure Laws

For a sustained housing finance system it is important that lenders (financial institutions) are able to enforce foreclosure law; a law that makes it possible to evict a home owner who fails to meet the contractual obligations towards the mortgage lender[5].

In Pakistan, Section 15 of The Financial Institutions (Recovery of Finances) Ordinance-2001 (Recovery Ordinance, 2001) empowers financial institutions to foreclose and register a mortgage property without recourse to the court of law. However, there is still a void in its implementation as financial institutions have yet to recognize the Recovery Ordinance in its true spirit. Furthermore, there is considerable variability in the legal standing of this Ordinance as recently the Lahore High Court passed a judgment that declared the powers of financial institution to foreclose and register a mortgage property without recourse to the court of law, unconstitutional and without legal effects. Though, subsequently, the Supreme Court of Pakistan suspended the Lahore High Court's judgment, bringing back to life Section 15 of the Ordinance which would once again entitle banks, investment banks and leasing companies to sell mortgaged properties without intervention of the court. However, the Supreme Court has only suspended the Lahore High Court ruling on Section 15, but not annulled it. There will always be danger that foreclosures carried out by Banks under Section 15 could be overturned if the final decision on this Ordinance is not in favor of banks. Therefore, effectiveness of the foreclosure law and its implementation needs to be ensured.

[5] Angel (2000)

Sub-goal 2-Improvements in Prudential Regulations

The prudential regulations of banks are intended to pursue two main goals: investor protection and financial stability. Investor protection aims at preserving the liquidity and safety of deposits. While financial stability aims at keeping systemic risk under control. Both these goals relate to bank failures which explain why preserving the solvency of banks is the overwhelming concern in the practice of prudential regulations[6]. Formulation of such regulations poses a great challenge, as a set of regulations, on one hand, can prove to insulate the financial system and insure its stability whilst stifling growth and innovation by distorting incentives for risk taking[7].

A housing finance system typically adheres to prudential regulation that require minimum capital to be maintained, adequate valuation methods to be followed, maximum loan-to-value ratios and loan-to-income ratios to be maintained. Housing finance in Pakistan was allowed and its regulations were incorporated formally as part of prudential regulations for consumer finance in 2003 by State Bank. Salient features of the prudential regulations for housing finance issued by State Bank of Pakistan are as follows;

- Banks / DFIs shall determine the housing finance limit, both in urban and rural areas, in accordance with their internal credit policy, credit worthiness and loan repayment capacity of the borrowers.
- Total monthly amortization payments not to exceed 50% of the net disposable income of the borrower.
- Banks to extend loans for the purpose of construction, outright purchase and renovation only. Banks / DFIs will not allow housing finance purely for the purchase of land / plots.
- Banks / DFIs may allow Housing Loans in the rural areas provided all relevant guidelines/regulations on the subject are complied with by them.
- The housing finance facility shall be provided at a maximum debt-equity ratio of 85:15.
- The house financed by the bank / DFI shall be mortgaged in bank's / DFI's favour by way of equitable or registered mortgage.
- Banks / DFIs shall either engage professional expertise or arrange sufficient training for their concerned officials to evaluate the property, assess the genuineness and integrity of the title documents, etc.

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[6] Suarez (1998)

[7] Countries with overbearing regulations like India or the Soviet Union enjoy financial stability, but suffer in economic performance, whilst counties with more liberal regulatory regimes suffer from occasional crisis, but do much better economically in the long run (Danielsson 2004).

- The bank's / DFI's management should put in place a mechanism to monitor conditions in the real estate market (or other product market) at least on quarterly basis to ensure that its policies are aligned to current market conditions.

- Banks / DFIs are encouraged to develop floating rate products for extending housing finance, thereby managing interest rate risk to avoid its adverse effects. Banks / DFIs are also encouraged to develop in-house system to stress test their housing portfolio against adverse movements in interest rates as also maturity mismatches.

As housing finance activity expands and in order to seek improvements in the housing finance regime, it will be important to question if these regulations are sufficient and are now not proving to endogenously limit the potential growth of housing finance.

Goal 2- Establish Long-Term Funding Mechanism

The mortgage market in Pakistan is largely being driven by primary mortgage lenders; a role being played by commercial banks. All functions of mortgage lending i.e. origination of house loans, collection and processing of payments from borrowers and performance of risk and portfolio management including funding are all being performed by commercial banks. Although this ability to provide a multitude of services to borrowers creates economies of scope for the banks, it nonetheless poses as a disadvantage. In case of commercial banks, who have higher cost ratios than capital market funded lenders, this ability to provide all services to house loan clients proves to be relatively inefficient. Costs are higher because banks are accounting for both liquidity and interest rate risk that is generated as a result of asset liability mismatching. The availability of long-term fund will help reduce asset liability mismatch which in turn will reduce liquidity risk allowing for increased lending by banks at a relatively lower cost.

Sub-goal 1-Creation of a Secondary Mortgage Market

In many countries a form of secondary market institution exists that can help portfolio lenders manage liquidity and interest rate risks that arise as a result of asset liability mismatching. These institutions referred to as liquidity, rediscounting or secondary mortgage market, issue general obligation bonds in the capital markets and use the proceeds to refinance the portfolios of primary market lenders. They provide funds to primary market or retail lenders through collateralized loans or recourse to purchase. The absence of a secondary mortgage market in Pakistan is a seriously limiting factor for its housing finance sector.

Sub-goal 2-Utilization of Long-Term Investors Funds

A secondary mortgage market will draw from institutions that manage household savings (e.g. EOBI, SLIC) and provide asset liability matching required for a sustainable housing finance system. This arrangement between the primary lender, the secondary mortgage market and institutional investors will provide the system with requisite liquidity.

Goal 3- Enhancing Outreach

An increase in volume of house loans will not only bring economies of scale for banks but will also bring down the cost of lending for housing, ultimately benefit the borrower. An increase in outreach can be targeted in a number of ways including an increase in geographical dispersion, encourage competition and through innovation. Greater outreach is also an interplay of these three elements. As much as these three elements serve as targets to be achieved for greater outreach, they collectively affect the ability of financial institutions to expand their housing finance facilities.

Sub-goal 1-Provision of Low-Cost Housing

At present, by and large, financial institutions are not seriously working to find solutions for addressing the acute shortage of low cost housing facilities because of the following reasons:

- Intermediation costs for the provision of housing loans to low income groups are higher than that for middle and upper income groups due to smaller loan size, lack of documented income, higher incidence of circumstantial defaults due to negative propensity to save;

- Property titling in low income areas is comparatively more difficult as representative of mortgagee financial institution needs to visit at least five (5) different offices for the verification of title documents;

- Initiation and successful closure of low income residential projects are also marked with barriers to site permits, environmental clearance, and lack of infrastructure and utilities connections. Resultantly, the residential ownership has remained predominantly equity financed and capitalization of housing sector has not been able to realize its true potential.

Sub-goal 2-Reduce Credit Rationing of Mortgage Lending

Another component of the housing finance regime is the presence of restrictions that control mortgage lending by rationing credit. The reason for adopting this in our context is because in the case of housing finance in Pakistan, there is a likelihood of some form of credit rationing taking place. Angel elaborates on this by identifying three types of rationing (a) limiting mortgage lending to specific types of housing, (b) limiting lending to specific segments of the population or (c) placing ceilings on deposits and mortgage interest rates that, in effect, ration credit to the housing sector as a whole. Angel points out that although some of these restrictions may be well-intended and other discriminatory, such restrictions nonetheless, depress the development of a healthy housing finance sector.

Currently, the financial institutions’ lending is highly skewed towards high-income population. Lending is further restricted towards urban centers with banks clearly demarcating areas that they approve for lending. The goal here will be to first see what forms of rationing exist; both implicit and explicit and to reduce the distortionery effect that they may have on the housing finance regime.

There needs to be a clear and conscious effort to encourage banks to expand their lending both across regions and income group.

Sub-goal 3-Encouraging Competition

Expansion and the resultant increase in volumes will only take place if a competitive environment is instilled. More competition among banks will motivate them into altering their long-term business strategies by expanding into untapped regions and penetrating into existing markets by serving to a broader spectrum of income groups.

Sub-goal 4-Encourage Innovative Solutions for Product Delivery

Increased competition not only involves motivating banks into expansion, as explained above, it also forces them to formulate innovative solutions for product delivery.

Sub-goal 5-Initiate an Awareness Campaign for Borrowers

Easily and accurately available information is crucial for all stakeholders involved in a particular initiative. As much as complete information on the borrowers is important for the lender, easy access to and a complete understanding of mortgage process to borrowers, is equally important. In Pakistan where literacy rates are low and potential borrowers are hesitant in approaching financial institutions to tap formal lending options, a campaign to educate borrowers will help induce a sense of comfort and commitment in the borrowers towards their lenders.

These five sub-goals in tandem lead to an increased level of outreach.

Goal 4- Continue capacity building initiatives

A change in market dynamic always generates a need for specialized human resource and investment in information technology.

Sub-goal 1-Developing Mortgage Banking Industry

Realizing the fact that housing finance be institutionalized simultaneous efforts to develop human capital needs to take place. The training should continue to cover aspects of mortgage lending, e.g., product development, loan marketing/distribution and origination to loan underwriting, servicing and risk management.

Sub-goal 2-Developing Housing Market Information System (HMIS)

Estimation and provision of credit to the housing sector are a function of sufficient, timely and reliable information relating to new home starts, existing home sales and causative factors that impact housing demand, i.e. incomes, demographics, consumer spending etc.

Lack of sufficient information impedes the ability of financial institutions to form an informed opinion about the demand and supply of housing units and the need of credit arrangements thereupon. At present some data on housing sector is being covered by census relating to type of structure, housing facilities, construction period etc.; however, it is insufficient. In order to streamline and consolidate housing market information, there is a need of developing a Housing Market Information System (HMIS). An information portal relating to Housing Market Information System (HMIS) should be designed to, inter-alia, cover the various facets of the construction projects financed by mortgage lenders, which are either at the stage of marketing or in the process of construction. It should also cover the availability of the plots in housing schemes, as well as the individual plots and houses for sale and purchase.

Sub-goal 3-Establishment of a Housing Observatory

A Housing Observatory should also be established with an aim to produce authentic, timely, transparent and integrated data relating to housing sector in Pakistan, which should be compatible with the needs of economy and socio-economic development. This Observatory will be on a much broader scale and will cover greater information than an HMIS; where the HMIS will fulfill short term needs.

Goal 5- Promoting Large-Scale Developer Finance

The large scale developer sector is a small but a burgeoning one in Pakistan. According to the Association of Builders and Developers (ABAD), there are around 600 construction companies that are members of the this association. This is almost 33% increase in construction companies since 2007[8]; reflective of the growing needs of large scale development projects especially in major cities. However, despite growing needs, the capacity of large scale housing projects by developers is limited due to fragmented and unstructured nature of property development business. This limitation in turn translates into financial institutions extending inadequate financing facilities to these developers. This lack of financing limits the growth of large scale housing projects; a cause that adds on to the existing housing backlog in the country. Some of the initiatives that need to be taken up by the financial sector include improvement in the effectiveness of credit ratings of builders and developers, simplification of loan documentation process and standardization of valuation methodologies adopted for projects.

Sub-goal 1-Effectivess of Credit Ratings of REBADs and REPs

Presently a majority of real estate builders and developers (REBADs) are working either as sole proprietors or as partnership concerns, therefore, making it difficult for all builders and developers to get themselves rated, thereby necessitating the need of credit rating of Real Estate Projects (REPs) sponsored by them. It will also be beneficial if financial institutions establish a business relationship with builders based on their (builders') past performance and the commercial and financial viability of their projects.

Sub-goal 2-Simplification of Loan Documentation

There is a need to simplify and standardize the set of documentation required from builders by financial institutions to ease and shorten the process of credit approvals.

Sub-goal 3-Standardization of Valuation Methodology

The property valuation process of large scale developers in Pakistan is currently marked with lack of standardization, which leads to variance in estimating a proxy market price of the same property by different valuers. This valuation methodology needs to be standardized so that all financial institutions follow a standard screening procedure thus reducing the time of credit approvals.

[8] According to HAG's study which was completed in 2007, there were around 450 builders and developers under ABAD. The 33% increase to 600 builders and developers is a figure quoted on ABADs website.

Strategic Initiatives

As mentioned in earlier sections, this paper serves as an extension to the HAG's recommendations that pertain to the financial sector. This section discusses initiatives that have been planned or already taken towards fulfillment of overall objectives. The table below summarizes the action plan devised against each sub-goal.

<table>
<tr><th colspan="2">Improve Housing Finance Regime</th></tr>
<tr><th>Sub-Goal</th><th>Strategic Initiative</th></tr>
<tr><td>Improving Effectiveness of Foreclosure Laws</td><td>Implementation of Recovery Ordinance 2001
To ensure effective implementation of the Recovery Ordinance 2001, legal advice is being sought to mitigate the risk emerged due to recent decision of the Lahore High Court that declared the powers of financial institution to foreclose and register a mortgage property without recourse to the court of law, unconstitutional and without legal effects. Though the decision has been suspended by the Supreme Court, there is still a risk as it has not been annulled.

Amendment to Recovery Ordinance 2001
Advice has been sought from the General Council's Office for the process to be followed for introducing the proposed amendment in Recovery Ordinance 2001 including the following;
To maintain sanctity of owner tenant relationship by protecting the interest of the bona fide tenant at the time of Foreclosure by Financial Institutions without intervention of the court., i.e., to avoid premature termination of tenancy agreements at the time of foreclosure.
Reserve price fixing through surveyors approved by SBP. Sales conducted by financial institutions without fixation of a reserve price are likely to be looked at by courts with suspicion.
Wider publicity (English, Urdu and local newspapers) of proposed sales by financial institutions</td></tr>
<tr><td>Improvements in Prudential Regulations</td><td>It is proposed that as a first step, separate Guidelines on Housing Finance will be issued.

It is also proposed that a review and an assessment for the need of separate regulations for housing finance will be conducted in consultation with BPRD. The review here will include, review of the definition of classification of default mortgage loans.</td></tr>
</table>

Establish Long-Term Funding Mechanism	
Sub-Goal	Strategic Initiative
Creation of a Secondary Mortgage Market	The World Bank had submitted a proposal to assist SBP in the establishment of a Mortgage Refinance Company (MRC). To take the initiative further, a presentation to stakeholders was also made and a formal Expression of Interest has been solicited from the Ministry of Finance. As an immediate step, business model of MRC will be developed which will pave the way for implementation of subsequent strategic steps, necessary for establishment of the MRC.
Utilization of Long-term Investors Funds	Equity contributions of long term investors including EOBI, SLIC will be solicited. Successful models of MRC around the globe emphasize the significance of tapping long term investors' funds which will help reduce asset liability mismatch and in turn help reduce liquidity risk.
Enhancing Outreach	
Sub-Goal	Strategic Initiative
Provision of Low-Cost Housing	The World Bank had also submitted a proposal to assist SBP in the provision of low-cost housing. A formal Expression of Interest has been solicited from Ministry of Finance. Once an EoI is issued, dialogue will be initiated with World Bank to seek their technical assistance in the area of low cost housing finance models. Furthermore, to strengthen linkages with government a study is proposed to be conducted aiming to analyze various initiatives taken by the government towards provision of low cost housing.
Reduce Credit Rationing of Mortgage Lending	The action plan will be to study what forms of rationing exist and to identify the suitable strategic initiatives to reduce them. As a first step it is proposed that a study will be conducted that will aim to collate information on instances of credit rationing based on the following factors; • Gender • Occupation/Profession • Geographical location • Income
Encouraging Competition	Subsequent to the establishment of a secondary mortgage market, the option of setting indicative targets for the financial institutions can be explored.
Encourage Innovative Solutions For	Once the secondary mortgage market is successfully established,

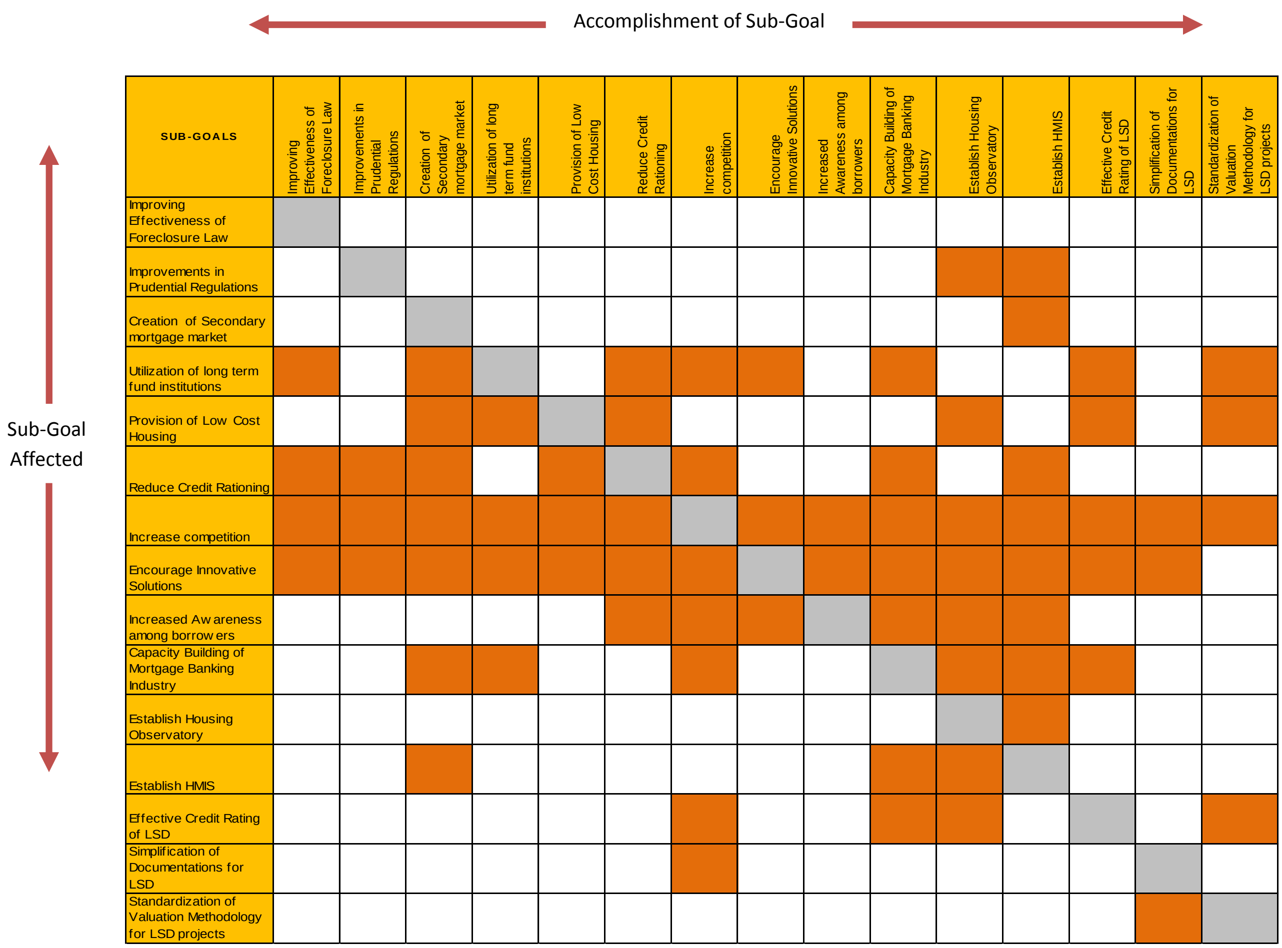
Product Delivery	banks can be encouraged to work on innovative and new products including fixed/semi-fixed rate products and/or other hybrid products for housing finance.
Awareness Campaign for Borrowers	Answers to Frequently Asked Question (FAQs) will be developed with the intention to create awareness among and educate potential borrowers on mortgage financing. It is proposed that these FAQs will be in both English and Urdu and its circulation will be made through BSC offices. Moreover, possibility of conducting awareness workshops through BSC in far flung areas will also be explored.
Capacity Building Initiatives	
Sub-Goal	Strategic Initiative
Development of Mortgage Banking Industry	SBP has been playing an active role in the capacity building of mortgage bankers. This initiative will be continued and a greater number of mortgage bankers will be targeted.
Developing Housing Market Information System (HMIS)	As agreed with Pakistan Banks Association (PBA), Association of Mortgage Bankers (MBA) has been asked to present to SBP a set of recommendations on the contents of the HMIS portal, by August 16, 2009. The portal will be developed to serve as a focal point of information on the housing finance sector.
Establishment of a Housing Observatory	The World Bank had also submitted a proposal to assist in the establishment of a housing observatory in Pakistan. A formal Expression of Interest has been solicited from Ministry of Finance. The establishment of the Observatory will address the information needs of both borrowers and lender on the housing sector as a whole and cover greater information than an HMIS.
Promoting Large Scale Developer Finance	
Sub-Goal	Strategic Initiative
Credit Rating	In order to put in place structured financing for large-scale developers through the formal sector, it was agreed with PBA that a capacity building initiative for rating agencies is required. This capacity building initiative has been proposed as one of the projects in TABS II.
Simplification of loan documents	PBA has been requested to take this initiative with the mutual consent of Association of Builders and Developers (ABAD). A feedback is expected by August 16, 2009
Standardization of Valuation Methodology	As agreed with PBA, AMB has been requested to share recommendations on standardization of property valuation mechanism by August 16, 2009 for streamlining the provision of credit to REBADs.

Goal Matrix

It is recognized that all the sub-goals identified and discussed in earlier section affect each other, both directly and indirectly. And in doing so, it is expected that the accomplishment of some goals have a greater affect on the accomplishment of others. We highlight the existence of cross-cutting issues by constructing a 'Goal Matrix'- the objective of which is to see how accomplishment of one initiatives/sub-goal will strongly contribute in the accomplishment of others. This is not to prioritize initiatives/sub-goal based on their importance, but the objective is to assess the impact of consciously achieving one initiative/sub-goal on the achievement of others without any form of intervention.

For this purpose, a small survey, in the form of an opinion poll was conducted. The respondents were selective and from the mortgage industry[9]. The matrix below shows the responses collected at the end of the survey.

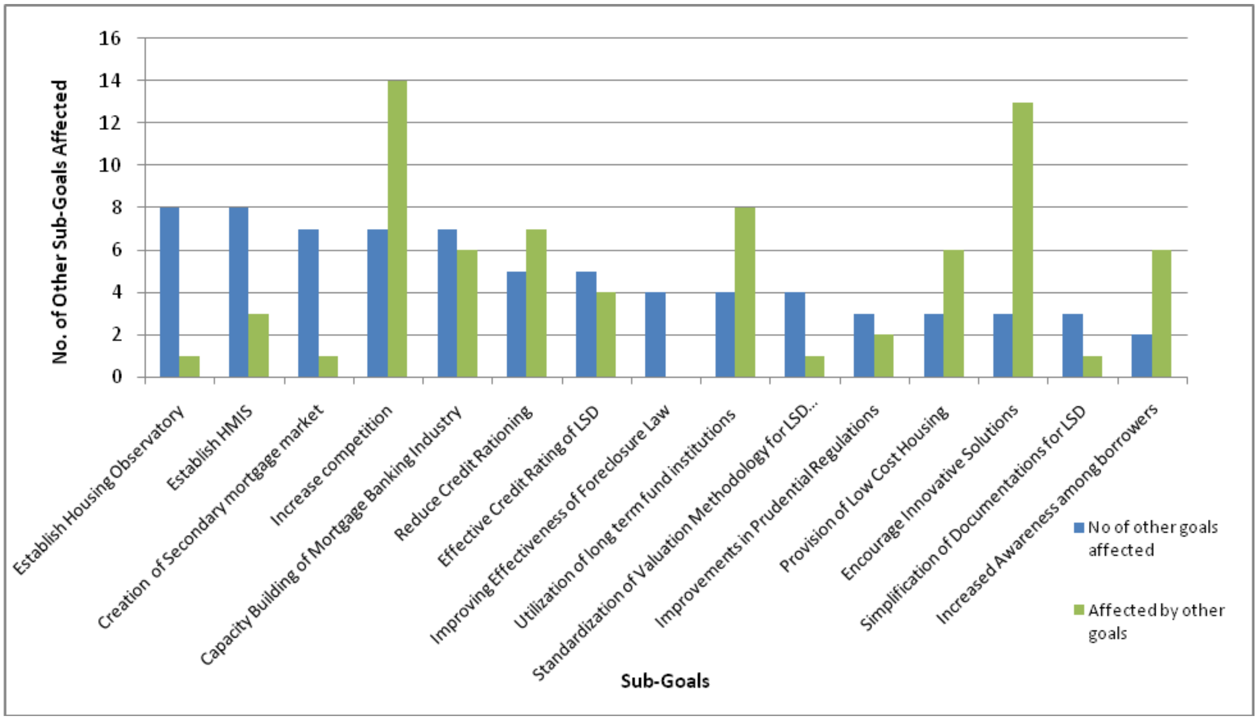
Goal Matrix



[9] Respondents were from IFC, commercial banks and Infrastructure and Housing Finance Department.

The responses (highlighted in deep orange) mark the perception that the accomplishment of a particular sub-goal (on horizontal axis) has a *direct* impact on the accomplishment of other sub-goal (along vertical axis). Direct impact here implies that achievement of a particular targeted goal causes accomplish one or more than one sub-goal to follow suit. The results of this experiment have been graphed below.

Results of the Goal Matrix



According to the results collated, establishment of a Housing Observatory and a Housing market Information Systems (HMIS) directly affects 8 other sub-goals out of a total of 15 sub-goals. This is the greatest impact a sub-goal is perceived to have on others. The matrix shows that if only a Housing Observatory is established, the accomplishment of the following other sub-goals will follow suit including, provision of low-cost housing, increased competition, more innovation, increased awareness among borrowers, increased capacity of mortgage bankers, establishment of a Housing Market Information Systems and an effective credit rating of large scale developers will be stimulated. The next greatest perceived impact is seen to be caused by the creation of a secondary mortgage market, increased competition and capacity building of mortgage bankers that affects seven other sub-goals (see matrix for individual areas affected).

Results also highlight areas that are most affected by all sub-goals. Any initiative taken is perceived to be impacting competition the greatest, followed by innovative solutions in the housing finance sector.

As much as all the sub-goals are important initiatives for the development of housing finance sector, this experiment applies a technique to identify the perceived impact value of each initiative and aid in a more tactile judgment.

Way Forward

This paper established a clear objective i.e. to create an enabling and sustainable housing finance system. It then sought factors that constitute such a system; housing finance regime, long-term funding, continued capacity building, outreach and promotion of large scale developers. Establishing these five as broader goals, factors were identified and explained why they were important to a housing finance system. These broad goals were further broken down to sieve through elements that individually affected the state of these five broader goals. These elements were named sub-goals. Strategic initiatives already taken or planned were also presented. Cross-cutting issues were then discussed and interdependence of these sub goals was recognized. It was highlighted that most of these sub-goals would independently contribute towards our greater objective; to create an enabling and sustainable housing finance system. Lastly, an assessment of the impact that each sub-goal is expected to have on the achievement of other sub-goals, was also conducted. It was concluded that as much as these sub-goals were interdependent, the fulfillment of some clearly had a greater ripple/stimulating effect on the fulfillment of other sub-goals.

This section as part of a forward looking approach, will present a structure of a proposed 'Impact Assessment Strategy'.

Impact Assessment Strategy

An Introduction

Subsequent to establishing goals, the next phase which is proposed, will entail detail analysis of underlying factors of each sub-goal. For example in the case of targeting to improve the housing finance regime it was recognized that improvements in the prudential regulations will be sought and foreclosure laws will have to be made more effective. Similarly, in order to enhance outreach, provision for low-cost housing will have to be made, instances of credit rationing will have to be reduced, competition and innovation will have to be encouraged and an awareness campaign will have to be run.

The impact assessment strategy will involve gauging existing level of performance of each of the key underlying factors contributing towards these sub-goals. This will be achieved through a quantitative assessment of each factor. For example, an assessment of the efficiency of foreclosure law will entail using as a proxy the number of days/months it takes before a defaulted case is resolved by the courts in favor of either the lender or the borrower. Here the assessment tool will be the number of days. Once determined, reduction in the number of days to say x days (from y days), will then be set as a target. These targets will be set keeping in view the following;

1. Peer country analysis and their performance on the sub-goal under discussion. For example, research on how long foreclosure proceedings take to resolve in comparable/peer countries like India, Malaysia etc, will be carried out.
2. Other external factors that will continue to pose a constraint on the sub-goal under consideration will have to be accounted for.

3. It is proposed that medium-term targets be set for a period of 5 years for achievement of set goals.

It is imperative to take into consideration these three factors because in the absence of these, establishing targets will become over ambitious and unrealistic. The flow diagram below illustrates the steps involved in conducting an impact assessment.

Impact Assessment- Steps

ASSESSMENT OF GOAL AREAS

Steps	Explanation
Nature of assessment of each goal	Assessment of each goal area will be carried out to establish existing performance levels. Assessment will be either quantitative (where applicable) or qualitative.
Methodology adopted for assessment	Example. For a quantitative assessment on the existing level of efficiency of foreclosure proceedings an index will be constructed using the following information 1. No. of procedures taken to enforce a contract 2. Time to enforce a contract 3. Cost of enforcing contracts (See table titled 'Methodologies-an overview' on the following page)

SETTING TARGETS

Steps	Explanation
Peer country analysis	Collect comparable information and figures on indices of countries like India, Malaysia, China etc.
Establishing time frame by which targets will have to be achieved	It is proposed that targets are set to be achieved within 5 years
Setting targets	Informed judgment will then be used to set targets using the existing performance analysis, the overall economic and institutional context and peer country analysis

STRATEGIC INITIATIVES

Steps	Explanation
Strategy formulation	A step by step strategy will be formulated to achieve the targets set against each goal.

It is also recognized that some targets may be qualitative in nature and indices/ figures may be difficult to construct. Therefore quantitative assessment of each sub-goal will be made where applicable. Some of these goals will require information to be collected via surveys or short interviews with stakeholders.

Proposed Methodology

A summary of the proposed approach is given in table below for sub-goals that can be established quantifiably. Greater details of the exact methodology are given in annexure A to C.

Methodologies- An Overview

Goals/Sub-Goals	Measurement Technique	Proposed Approach	Annexure
Improve Housing Finance Regime			
Improving Effectiveness of Foreclosure Laws	Quantitative	Assessment to be carried out along the following parameters; 1. No. of procedures taken to foreclose/ enforce a mortgage contract. 2. Time to foreclose/enforce a mortgage contract. 3. Cost of foreclosing/enforcing a mortgage contract. 4. Additional parameters to be identified during consultations with stakeholders.	A
Enhancing Outreach			
Reduce Credit Rationing Of Mortgage Lending	Quantitative	Assessment to be carried out along the following parameters; 1. Geographic dispersion of Banks 2. Income groups 3. Demographic	B
Encouraging Competition	Quantitative	Assessment to be carried out using some of the following methodologies; 1. M-Concentration ratio 2. Coefficient of Variation (measuring dispersion in the market) 3. No. of market players 4. Herfindahl-Hirschman Index (HHI)	C

This comprehensive strategy paper on housing finance will serve as a road map for achieving the approved goals. This will also serve as an assessment tool in quantifiably gauging the progress made and impact of initiatives taken by SBP towards creating an enabling and sustainable environment for housing finance system.

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Foreclosure

Suggested Methodology	Nature of Assessment (Quantitative/Qualitative)	Instrument(s)	Source of Methodology
Step 1 Asses the overall efficiency of the legal system in resolving business disputes in Pakistan through; 1. No. of procedures taken to enforce a contract 2. Time to enforce a contract 3. Cost of enforcing contracts	Quantitative	None	The World Bank *Doing Business 2008*[1]
Step 2 Asses the overall efficiency of the legal system in resolving *mortgage* related disputes in Pakistan between banks and borrowers through; 1. No. of procedures taken to foreclose/ enforce a mortgage contract 2. Time to foreclose/enforce a mortgage contract 3. Cost of foreclosing/enforcing a mortgage contract 4. Additional parameters to be identified during consultations with banks.	Quantitative	Survey[2]	The methodology presented in The World Bank *Doing Business 2008*, report will be tailored to focus on assessing the efficiency of the legal system in Pakistan to deal in foreclosures.

Setting a Strategy
Step 3 A quantitative analysis will then be carried out by judging foreclosure efficiency (step 2) in the context of the overall legal system (step 1) that prevails in Pakistan. Since comparisons[3] with other countries are available (in step 1) judgment will be used to establish a quantitative target (desired) for improved foreclosure procedures by 2015.

[1] The World Bank Doing Business 2008 project has identified indicators on enforcing contracts that measure the efficiency of the judicial system in resolving a commercial dispute. Three indicators were used to construct an overall index/scoring that ranked (out of 52 countries) the efficiency of contract enforcement in Pakistan. These indicators are;

a) The number of procedures to enforce a contract

   Definition: A procedure is defined as any interaction between the parties, or between them and the judge or court officer. This includes steps to file the case, steps for trial and judgment and steps necessary to enforce the judgment. This year the survey allowed respondents to record procedures that exist in civil law but not common law jurisdictions, and vice versa. For example, the judge can appoint an independent expert in civil law countries whereas both parties in common law countries send a list of their expert witnesses to the court. To indicate the overall efficiency of court procedures, 1 procedure is now subtracted for countries that have specialized commercial courts and 1 procedure for countries that allow electronic filing of court cases.

b) Time to enforce a contract

   Definition: Time is recorded in calendar days, counted from the moment the plaintiff files the lawsuit in court until payment. This includes both the days when actions take place and the waiting periods between. The respondents make separate estimates of the average duration of different stages of dispute resolution: the completion of service of process (time to file the case), the issuance of judgment (time for the trial and obtaining the judgment) and the moment of payment (time for enforcement).

c) Cost of enforcing contracts

   Definition: Cost is recorded as a percentage of the claim, assumed to be equivalent to 200% of income per capita. Only official costs required by law are recorded, including court and enforcement costs and average attorney fees where the use of attorneys is mandatory or common.

Currently only the 2008 figures are available from the *Doing Business 2008* report. As work is initiated on this proposed strategy paper and the 2009 report (*Doing Business 2009*) is published, the new and updated report will be used instead in step 1.

[2] This question will be asked from financial institutions by means of a survey. It is intended that a consultative process with potential respondents (financial institutions) be initiated prior to designing of the survey.

[3] The indicators for Pakistan on the efficiency of the judicial system as estimated in the *Doing Business* report 2008 by The World Bank is as follows;

Nature of Procedure	Indicator
Procedures (number)	47
Duration (days)	976
Filing and service	96
Trial and judgment	580
Enforcement of judgment	300
Cost (% of claim)*	23.8
Attorney cost (% of claim)	16.7
Court cost (% of claim)	5.9
Enforcement Cost (% of claim)	1.2

* Claim assumed to be equivalent to 200% of income per capita

Reduce Credit Rationing of Mortgage Lending

Suggested Methodology	Nature of Assessment (Quantitative/Qualitative)	Instrument(s)	Source of Methodology
Step 1			
Encourage banks to cater to a wider geographical and income groups. Assessment will be carried out on the basis of, but not limited to the following areas; Geographical Dispersion 1. Mortgage financing as a % of total financing 2. No. of branches (Rural/Urban) 3. No. of Islamic banking branches (Rural/Urban) 4. No. of branches within Islamic banking that extend house loans (Rural/Urban) 5. No. of conventional banking branches (Rural/Urban) 6. No. of branches within conventional banking that extend house loans (Rural/Urban) Income groups 1. Measure the extent to which financing is made available to low income groups. Demographics 1. No of Male/ Female borrowers	Quantitative	Survey[1]	

Setting a Target
Step 2 Step 1 will allow construction of quantitative targets specific to housing finance and will aid in gauging efforts made towards encouraging banks to cater to a wider geographical and income groups.

[1] These questions will be asked from financial institutions by means of a survey. It is intended that a consultative process with potential respondents (financial institutions) be initiated prior to designing of the survey.

Encouraging Competition

Suggested Methodology	Nature of Assessment (Quantitative/Qualitative)	Instrument(s)	Source of Methodology
Step 1 The *Financial Stability Review 2007-08* analyses concentration and competition in the banking industry of Pakistan. The review utilizes the following methodologies to gauge level and extent of competition; 1. M-Concentration ratio 2. Coefficient of Variation (measuring dispersion in the market) 3. No. of market players 4. Herfindahl-Hirschman Index (HHI)	Quantitative	None	Financial Stability Review 2007-08, SBP[1]
Step 2 An analysis of competition among banks for housing finance will be conducted by the use of the following; 1. M-Concentration ratio 2. Coefficient of Variation (measuring dispersion in the market) 3. No. of market players 4. Herfindahl-Hirschman Index (HHI)	Quantitative	Research. Computations will need to be carried out.	Financial Stability Review 2007-08, SBP[2] Denmark: Financial Sector Assessment Program-Technical Note-Competition in the Banking Sector[3] 4

Setting a Target
Step 3 The overall competitive environment of the banking industry in Pakistan will first be discussed (Step 1), followed by an analysis on the level and extent of competition among banks in the housing finance sector (Step 2).

[1] "Financial Stability Review 2007-08." Rev. of Financial Stability Department. State Bank of Pakistan.

[2] "Financial Stability Review 2007-08." Rev. of Financial Stability Department. State Bank of Pakistan.

[3] Denmark: Financial Sector Assessment Program-Technical Note-Competition in the Banking Sector. Rep. no. 07/122. Washington, D.C.: International Monetary Fund, 2007.

[4] Fahrer, Jerome, and Thomas Rohling. "Some Tests of Competition in the Australian Housing Loan Market." Economic Research Department, Reserve Bank of Australia 9202 (1992).