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The World Bank

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Report No: PAD3712

INTERNATIONAL DEVELOPMENT ASSOCIATION

PROJECT PAPER

ON A

PROPOSED ADDITIONAL CREDIT

IN THE AMOUNT OF EUR 75.1 MILLION
(US$85 MILLION EQUIVALENT)

TO THE

ISLAMIC REPUBLIC OF PAKISTAN

FOR THE

PAKISTAN HOUSING FINANCE PROJECT

February 16, 2022

Finance, Competitiveness And Innovation Global Practice
South Asia Region

CURRENCY EQUIVALENTS

(Exchange Rate Effective December 31, 2021)

Currency Unit =	Pakistani Rupees (PKR)
US$ 1 =	PKR 178
US$ 1 =	EUR 0.88347

FISCAL YEAR
July 1 – June 30

Regional Vice President:	Hartwig Schafer
Country Director:	Najy Benhassine
Regional Director:	Zoubida Kherous Allaoua
Practice Manager:	Gabi Afram
Task Team Leader(s):	Namoos Zaheer, Anne Treylane Gapihan

ABBREVIATIONS AND ACRONYMS

AF	Additional Financing
BoP	Bank of Punjab
CAR	Capital Adequacy Ratio
DFI	Development Finance Institutions
E&S	Environmental and Social
EHS	Environment, Health, and Safety
ESMS	Environmental and Social Management System
FBR	Federal Board of Revenue
FM	Financial Management
GDP	Gross Domestic Product
GHG	Greenhouse Gas
GoP	Government of Pakistan
GRM	Grievance Redress Mechanism
GST	General Sales Tax
HBFCL	House Building Finance Company Limited
HFC	Housing Finance Company
IBRD	International Bank for Reconstruction and Development
IDA	International Development Association
IFC	International Finance Corporation
IMF	International Monetary Fund
IRR	Internal Rate of Return
ISR	Implementation Status and Results
KIBOR	Karachi Inter Bank Offer Rate
LoC	Line of Credit
MFB	Microfinance Bank
MPMG	Mera Pakistan Mera Ghar
MSME	Micro, Small, and Medium Enterprises
NAPHDA	Naya Pakistan Housing and Development Authority
NPHP	Naya Pakistan Housing Program
NPL	Non-Performing Loan
NPV	Net Present Value
NRSP	National Rural Support Program
PAHP	Punjab Affordable Housing Program
PBA	Pakistan Bankers Association
PDO	Project Development Objective
PFI	Participating Financial Institution
PKR	Pakistan Rupee
PML	Primary Mortgage Lenders
PMRC	Pakistan Mortgage Refinance Company
PS	Performance Standards
PUC	Portfolio Under Coverage
PULSE	Punjab Urban Land Systems Enhancement
RSF	Risk Sharing Facility
SBP	State Bank of Pakistan
UPB	Unpaid Principal Balance
WB	World Bank
WBG	World Bank Group

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BASIC INFORMATION – PARENT (Pakistan Housing Finance Project - P162095)

Country	Product Line	Team Leader(s)		
Pakistan	IBRD/IDA	Namoos Zaheer		
Project ID	**Financing Instrument**	**Resp CC**	**Req CC**	**Practice Area (Lead)**
P162095	Investment Project Financing	ESAF1 (9284)	SACPK (1539)	Finance, Competitiveness and Innovation

Implementing Agency: PMRC, Ministry of Planning, Development & Reform, Naya Pakistan Housing & Development Authority

Is this a regionally tagged project?
No

Bank/IFC Collaboration	Joint Level
Yes	Complementary or Interdependent project requiring active coordination

Approval Date	Closing Date	Expected Guarantee Expiration Date	Original Environmental Assessment Category	Current EA Category
29-Mar-2018	30-Jun-2023		Financial Intermediary Assessment (F)	Financial Intermediary Assessment (F)

Financing & Implementation Modalities

[ ] Multiphase Programmatic Approach [MPA]	[ ] Contingent Emergency Response Component (CERC)
[ ] Series of Projects (SOP)	[ ] Fragile State(s)
[ ] Performance-Based Conditions (PBCs)	[ ] Small State(s)
[✓] Financial Intermediaries (FI)	[ ] Fragile within a Non-fragile Country
[ ] Project-Based Guarantee	[ ] Conflict
[ ] Deferred Drawdown	[ ] Responding to Natural or Man-made disaster

[ ] Alternate Procurement Arrangements (APA)	[ ] Hands-on Expanded Implementation Support (HEIS)

Development Objective(s)

The Project Development Objective is to increase access to housing finance for households, and support capital market development in Pakistan.

Ratings (from Parent ISR)

	Implementation					Latest ISR
	29-Jun-2018	26-Dec-2018	05-Jul-2019	11-Feb-2020	10-Nov-2020	13-Sep-2021
Progress towards achievement of PDO	S	S	S	S	MS	MS
Overall Implementation Progress (IP)	S	S	S	S	S	S
Overall Safeguards Rating	MS	MS	MS	MS	MS	MS
Overall Risk	S	S	S	S	S	S
Financial Management	S	MS	MS	MS	MS	S
Project Management	S	S	S	S	S	S
Procurement	S	S	S	S	S	S
Monitoring and Evaluation	S	S	S	S	S	S

BASIC INFORMATION – ADDITIONAL FINANCING (Pakistan Housing Finance: Additional Financing - P172581)

Project ID	Project Name	Additional Financing Type	Urgent Need or Capacity Constraints

P172581	Pakistan Housing Finance: Additional Financing	Restructuring, Scale Up	No
Financing instrument Investment Project Financing	Product line IBRD/IDA	Approval Date 10-Mar-2022	
Projected Date of Full Disbursement 30-Jun-2026	Bank/IFC Collaboration No		
Is this a regionally tagged project? No			

Financing & Implementation Modalities

[ ] Series of Projects (SOP)	[ ] Fragile State(s)
[ ] Performance-Based Conditions (PBCs)	[ ] Small State(s)
[✓] Financial Intermediaries (FI)	[ ] Fragile within a Non-fragile Country
[ ] Project-Based Guarantee	[ ] Conflict
[ ] Deferred Drawdown	[ ] Responding to Natural or Man-made disaster
[ ] Alternate Procurement Arrangements (APA)	[ ] Hands-on Expanded Implementation Support (HEIS)
[ ] Contingent Emergency Response Component (CERC)	

Disbursement Summary (from Parent ISR)

Source of Funds	Net Commitments	Total Disbursed	Remaining Balance	Disbursed
IBRD				%
IDA	145.00	138.04	0.59	100 %
Grants				%

PROJECT FINANCING DATA – ADDITIONAL FINANCING (Pakistan Housing Finance: Additional Financing - P172581)

FINANCING DATA (US$, Millions)

SUMMARY (Total Financing)

	Current Financing	Proposed Additional Financing	Total Proposed Financing
Total Project Cost	145.00	835.00	980.00
Total Financing	145.00	835.00	980.00
of which IBRD/IDA	145.00	85.00	230.00
Financing Gap	0.00	0.00	0.00

DETAILS - Additional Financing

World Bank Group Financing

International Development Association (IDA)	85.00
IDA Credit	85.00

Non-World Bank Group Financing

Commercial Financing	750.00
Unguaranteed Commercial Financing	750.00

IDA Resources (in US$, Millions)

	Credit Amount	Grant Amount	Guarantee Amount	Total Amount
Pakistan	85.00	0.00	0.00	85.00
National PBA	85.00	0.00	0.00	85.00
Total	**85.00**	**0.00**	**0.00**	**85.00**

COMPLIANCE

Policy

Does the project depart from the CPF in content or in other significant respects?

[ ] Yes [✓] No

Does the project require any other Policy waiver(s)?

[ ] Yes [✓] No

INSTITUTIONAL DATA

Practice Area (Lead)

Finance, Competitiveness and Innovation

Contributing Practice Areas

Urban, Resilience and Land

Climate Change and Disaster Screening

This operation has been screened for short and long-term climate change and disaster risks

PROJECT TEAM

Bank Staff

Name	Role	Specialization	Unit
Namoos Zaheer	Team Leader (ADM Responsible)		ESAF1
Anne Treylane Gapihan	Team Leader		SLCUR
Syed Wajahat Ali Shah	Procurement Specialist (ADM Responsible)		ESARU
Haider Raza	Procurement Specialist		ESARU
Noureen LNU	Financial Management Specialist (ADM Responsible)		ESAG1
Babar Naseem Khan	Social Specialist (ADM Responsible)		SSAS1
Ekaterina Grigoryeva	Environmental Specialist (ADM Responsible)		SAEE2
Ahmad Imran Aslam	Environmental Specialist		SSAEN
Andrey Milyutin	Team Member		EFNLT
Ifedolapo Mary Borisade	Team Member		ESAF1
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Olivier Hassler	Team Member		ESAF1
Rafay Khan	Team Member		ESAF1
Raja Muhammad Nasir	Team Member		SACPK
Victor Manuel Ordonez Conde	Team Member		WFACS
Yan F. Zhang	Team Member		SSAU1

Extended Team

Name	Title	Organization	Location

I. BACKGROUND AND RATIONALE FOR ADDITIONAL FINANCING

A. Introduction

1. **This project paper seeks approval of the World Bank Board of Executive Directors to provide a credit in the amount of EUR 75.1 million (US$85 million equivalent) for a proposed Additional Financing of the Pakistan Housing Finance Project (parent project—P162095).** The Additional Financing (AF) is being proposed to increase access to housing finance for low- and middle-income households and to support the development of capital markets in Pakistan. The AF will fund the initial capitalization of a sub-trust (Risk Sharing Facility-phase 2) of the pilot Risk Sharing Facility (RSF) under the parent project, which provided the initial capitalization of this RSF. This is aligned with the Government of Pakistan's (GoP) increased policy focus on this area. The proposed AF will be directly channeled through the Recipient, but the operation of the RSF will continue to be managed by the existing implementation agency, the Pakistan Mortgage Refinancing Company (PMRC). The proposed AF does not entail changes to the original Project Development Objective (PDO) nor the safeguard policies applicable to the parent project. The AF does, however, include a level-2 restructuring of the parent project, which is expected to entail the cancellation of one component and revisions to the results framework, including the revision of one PDO indicator, the addition of an intermediate indicator, and revision of end targets. The proposed restructuring is also expected to include the dropping one implementing agency (Planning Commission) and cancelling leftover funds (SDR 419,627) due the proposed cancellation of one component.

2. **This AF is one of the three complementary projects that are being proposed as a package of integrated interventions in the land and housing sectors to support the GoP in addressing constraints across the housing sector value chain.** Punjab Urban Land Systems Enhance Project (PULSE, 172945) will finance the digitization of land records in urban and rural areas of Punjab and create a province-wide parcel-based cadaster. PULSE will strengthen systems that will help increase the security of records on land rights and facilitate the identification of developable land in urban areas. The second operation, the Punjab Affordable Housing Program (PAHP, P173663), will help strengthen housing institutions and systems and enhance housing supply, including affordable housing for lower-income households in Punjab. This AF, which is the third operation, will support the scale-up of the credit risk sharing facility that was developed in 2018 under the parent project to promote access to mortgage loans for low- and informal-income households.

B. Economic Context

3. **Pakistan has made significant progress over the last two decades towards reducing poverty.** Nonetheless, challenges remain. Human capital outcomes are poor and stagnant, with high levels of stunting at 38 percent and learning poverty at 75 percent. Per capita GDP growth has also been low, averaging only around 1.8 percent annually. Economic growth in Pakistan has historically been fueled by private and government consumption, with productivity enhancing investment and exports contributing relatively little. Consumption-led growth has been associated with frequent macroeconomic imbalances. Achieving sustained higher economic growth is important for Pakistan to reduce inequality and increase shared prosperity.

4. **Economic activity contracted in FY20 due to COVID-19 but has recovered in FY21.** Due to low-

base effects and recovering domestic demand, real GDP growth (at factor cost) is estimated to have rebounded to 3.5 percent in FY21 from a contraction of 0.5 percent in FY20.[1] However, considering emerging external imbalances and higher domestic inflation, fiscal and monetary tightening are expected to resume in FY22. Output growth is therefore projected to ease to 3.4 percent in FY22 but strengthen thereafter to 4.0 percent in FY23 on reform dividends such as those from sustaining macroeconomic stability and increasing competitiveness. Inflation is projected to edge up in FY22 with domestic electricity tariff hikes and higher oil and commodity prices before moderating in FY23. The current account deficit is projected to widen to 2.5 percent of GDP in FY23 as imports expand with higher economic growth and oil prices. Despite fiscal consolidation efforts, the deficit (excluding grants) is projected to remain high at 7.1 percent of GDP in FY22 and widen to 7.2 percent in FY23 due to pre-election spending. Implementation of critical revenue-enhancing reforms, particularly the harmonization of the General Sales Tax (GST), will support a narrowing of the fiscal deficit over time. Public debt will remain elevated in the medium term, as will Pakistan's exposure to debt-related shocks. This outlook assumes that the International Monetary Fund (IMF) Extended Fund Facility program will remain on track.

C. Project Background and Performance

5. **The parent project was conceived and designed to address structural gaps in Pakistan's financial system that have historically impeded the growth of affordable housing finance.** The GoP and the State Bank of Pakistan (SBP) began to take active steps to unlock the housing finance ecosystem in 2014. Relevant prudential frameworks were developed, amendments to the mortgage recovery law were made, and, in 2016, the Pakistan Mortgage Refinance Company (PMRC) was established. PMRC's objective is to address several market failures to improve mortgage affordability. It was in this context that the GoP and SBP sought WB support to operationalize PMRC to further their efforts to promote access to affordable housing finance. The project was approved by the International Development Association (IDA) Board of Executive Directors in March 2018 and became effective in June 2018.

6. **The parent project, funded at US$145 million, was comprised of three synergistic and mutually reinforcing components.** *Component 1 (US$60 million)* entailed the establishment and operationalization of PMRC. The project supported the injection of US$60 million in long-term subordinated debt to help strengthen PMRC's capital base and support it in meeting the SBP's minimum capital requirements for Development Finance Institutions (DFIs).[2] *Component 2 (US$80 million)* of the project entailed extension of US$70 million in concessional, long-term, and fixed rate finance to primary mortgage lenders (PMLs) through PMRC, along with the establishment and operationalization of a pilot US$10 million RSF to provide partial credit risk cover for lenders to incentivize mortgage financing for low- and informal-income groups. *Component 3 (US$5 million)* entailed capacity building for housing policy and analytics.

7. **Component 1 and 2 of the parent project stand fully disbursed and it currently has a closing date of June 30, 2023.** All major PDO level indicators are on track to being achieved before the project closing date. Under *Component 1* the US$60 million Tier II capital injection buttressed PMRC's capital base

1 World Bank estimate. The government's preliminary growth estimate for FY21 is 3.9 percent. The government's revised growth estimate for FY21 is 5.4 percent (constant basis prices of 2005–06, January 2022).
[2] PMRC could commence operations with paid up capital of PKR 3.8 billion (US$22.4 million) rather than the prescribed PKR 6 billion (US$35.3 million) due to an exemption allowed by the SBP. The SBP gave PMRC five years to build up its capital; they have until June 2023 to meet the minimum capital requirements.

and allowed PMRC to undertake a series of capital market transactions. PMRC has successfully executed seven capital market transactions to date, raising PKR 11.8 billion (US$69.4 million). These transactions have directly supported the development of Pakistan's capital markets, which is also a key element of the PDO for this operation. Under *Component 2*, the project sought to expand the size of Pakistan's mortgage market, specifically by enhancing access to housing finance for those traditionally excluded. PMRC has fully disbursed the US$70 million Line of Credit (LoC) to 17 PMLs as of October 2021, including microfinance providers. PMRC's total portfolio stands at PKR 23.9 billion (US$140 million) as of December 2021. Much like the LoC, the advent of the pilot RSF in the market also supports the development of the mortgage market. The pilot RSF is designed to share partial credit risk with PMLs and provides a 40 percent first loss risk cover for eligible mortgage portfolios at a premium. Thus, by providing a 40 percent credit risk guarantee (to be paid in the event of borrower default), the pilot RSF gives banks some comfort as they lend to segments that are not their traditional client base. The RSF in the parent project has been designed as a pilot to be leveraged tenfold (up to US$100 million) and has the potential to give risk cover to 7,700 mortgages. At present, 11 banks have signed agreements for coverage under the pilot RSF; six banks have portfolios ready for coverage (see Annex 1 for details of the performance of RSF under the parent project). *Component 3* aimed to build technical capacity within the Planning Commission of Pakistan for coordinated and evidence-based housing policy. This component was not implemented as the government established and funded the Naya Pakistan Housing and Development Authority in 2019 with the same mandate.

8. **The project Mid-term Review in June 2021 concluded that the PDO and project design remain relevant, with a high level of commitment from the GoP.** According to the latest Implementation Status and Results (ISR) (September 2021), the PDO rating is Moderately Satisfactory, and the Implementation Progress rating is Satisfactory. The Financial Management (FM) and Procurement performance of the Project are Satisfactory. The overall rating for Environmental and Social Safeguards compliance is also Moderately Satisfactory. The project remains compliant with all legal covenants.

9. **The parent project has had a significant developmental impact on the housing finance market in Pakistan.** Availability of the longer-term, fixed rate wholesale funding that PMRC brought to the market not only made mortgages more affordable, but also created an enabling environment for new PMLs to enter the market. Four housing finance companies (HFCs) have been registered in Pakistan since PMRC began its operations (there were no HFCs at the time the project became effective) and 12 microfinance banks now actively lend in this space. There has been a 180 percent increase in the number of housing loan clients in the microfinance sector since July 2019. Forty-two percent of PMRC's portfolio is for low- and middle-income borrowers and 26 percent of the loans are to females (as sole mortgagers or with a female as a joint mortgager).

D. Rationale for Additional Financing and Restructuring

10. **The improved policy environment and revitalized market conditions around the supply of housing and demand for housing finance have resulted in unprecedented growth of the sector.** The current administration came into office two months after the parent project became effective and launched an ambitious affordable housing program in early 2019 (i.e., the Naya Pakistan Housing Program—NPHP). The Naya Pakistan Housing & Development Authority (NAPHDA) was established in

2019 to implement the NPHP. NAPHDA has wide ranging powers to promote and foster growth in affordable housing. It initially developed four distinct housing products to promote:

(a) **Tier 0:**[3] houses up to 1,250 ft^2, built on public or private land, specifically targeted to microfinance sector with loans up to PKR 2.0 million (US$12,763).

(b) **Tier 1:** 850 ft^2 houses, built on public or private land, with mortgage loans up to PKR 2.7 million (US$17,230).

(c) **Tiers 2 and 3:** 1,250 to 2,000 ft^2 houses, built on private land, with mortgage loans up to PKR 6.0 million or PKR 10 million (US$38,290 or US$63,816) respectively.

11. **The GoP has announced several complementary fiscal and policy measures to promote both the supply and demand for affordable housing and to stimulate economic recovery in response to COVID-19:**

(a) **Construction stimulus package:** This package was announced in April 2020 and has a dual purpose: it serves as an economic stimulus package as part of COVID-19 recovery, but it also includes additional tax and regulatory incentives specific to affordable housing. This is part of the government's push to create an enabling environment for private sector driven growth in the supply of affordable housing.[4]

(b) **Housing and construction lending targets:** Anticipating the increase in supply of housing and pre-empting the risk that banks will fail to meet the demand, in July 2020 the SBP set mandatory targets for housing and construction loans for commercial banks. By December 2021, all commercial banks were to have the equivalent of 5 percent of their outstanding credit to the private sector devoted to housing and construction loans (failure to comply results in hefty fines).[5] There has been an 84 percent increase in the volume of housing and construction finance in the last 12 months due to this measure. Directed lending of this nature is not deemed good practice but the SBP has highlighted that given the risk averse lending practices of banks in Pakistan, there would be no meaningful movement in housing finance without these mandatory targets.

(c) **Down payment subsidy:** In March 2020, the GoP announced an up-front subsidy of PKR 300,000 (US$1,764) to beneficiaries of the Tier 1 housing typology of NPHP to enhance the affordability of the units supplied under the program.[6]

(d) **Interest rate subsidies:** Even with the lower cost housing and the up-front subsidy, affordability will remain a challenge for lower quintile households. As such, an interest rate subsidy program was announced and launched by the SBP in December 2020 to complement NPHP. Known as the Mera Pakistan, Mera Ghar program (MPMG—My Pakistan, My Home), the program is a tier-based structure that aims to enhance the affordability of housing loans down to households in the 2nd quintile. The tier structure of MPMG is aligned to the four housing typologies being promoted by the NPHP. It offers highly subsidized loans to beneficiaries for the first 10 years of their mortgage

[3] Tier 0 property size is larger than Tier 1 as it is expected these will likely be rural constructions.

[4] A total of 2507 projects worth PKR627 billion (US$3.5 billion) have been registered with the Federal Board of Revenue (FBR) under this package till date.

[5] This re-pivoting would mean that the banking sector's consumer housing finance and developer finance portfolio must reach PKR 300 billion (US$1.8 billion) by December 2021 (the outstanding loans to the sector stood at PKR 166 billion [US$976 million] in September 2020). This measure has seen remarkable results, housing and construction finance stands at PKR 305 billion (US$1.8 billion) as of September 2021, a year-over-year growth of 84 percent.

[6] PKR30 billion (US$176 million) has already been allocated to NAPHDA to fund the up-front subsidy for the first 100,000 developed under NPHP.

loan.[7] Within the current lending targets, banks have monthly sub-targets specifically for MPMG loans. Microfinance banks have also been given targets under the program based on the quality of each institution's balance sheet (see Annex 2 for details of the salient features of MPMG).

12. **The proposed AF has been conceived to complement and support the government's ambitious housing program and will entail an initial capitalization of US$85 million equivalent into a sub-trust of the RSF under Component 2 of the parent project.** The need for a larger RSF has become critical given the government's policy priorities, especially given the mandatory targets under MPMG—which has a borrower segment that is not the traditional client base of PMLs. The SBP has imposed lending targets on banks based on the tacit understanding that, through the RSF, the GoP will share some of the risk of this rapid expansion into an untested market segment. Direct lending targets complemented by such deep subsidies can potentially be distortive; however, given the very small size of Pakistan's mortgage market (0.3 percent of GDP) and the very narrow focus of MPMG on lower-income households, the risk of a systemic distortion is quite limited at this stage of market development. The RSF (both the pilot and phase 2) will only provide risk cover to mortgages being originated under the MPMG. While banks have made steady progress in meeting their broader targets, their progress on MPMG targets has been somewhat muted. Since its inception one year ago, there have been applications of value PKR 276 billion— (US$ 1.62 billion) under MPMG and only applications of value PKR 117 billion (US$688 million) have been approved (indicating only a 42 percent approval rate). Disbursements are still lower at PKR 38 billion (US$223 million). The proposed AF to fund capitalization of a sub-trust of the RSF will give banks comfort as they move towards lending to an untested market segment and will have a direct impact on the rate of approvals and disbursements going forward. The AF will flow into a new sub-trust (as phase 2) under the existing Master Trust Agreement under which the pilot RSF operates.[8] Since the pilot RSF (US$10 million equivalent) in the parent project became operational after the MPMG program was announced, it has also been realigned to meet the needs of the MPMG program (i.e., only loans under this scheme qualify for coverage).

13. **The proposed AF is aligned with the World Bank Group's Pakistan Country Partnership Strategy FY2015-19.** The strategy was discussed by the Board of Executive Directors on May 1, 2014 and subsequently extended to FY20 under the corresponding May 2017 Performance and Learning Review. The Project also responds to Pillar 3 (Ensuring Sustainable Business Growth and Job Creation) and 4 (Strengthening Policies, Institutions and Investments for Rebuilding Better) of the WBG COVID-19 Crisis Response Approach Paper.

II. DESCRIPTION OF ADDITIONAL FINANCING

A. Project Development Objective

14. **The PDO remains unchanged.** The PDO is to increase access to housing finance for households, and support capital market development in Pakistan.

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[7] The GoP pays the differential between the market rates and the subsidized rates (banks have agreed to Karachi Inter Bank Offer Rate (KIBOR) linked margins). The SBP has also set lending targets for MPMG; each bank must have a mandated proportion of their housing portfolio devoted to this program.

[8] Details of the Master Trust and Sub-Trust structure are provided in the Project Description section of the document.

B. Project Beneficiaries

15. **The primary project beneficiaries continue to be low- and middle-income households in Pakistan, (specifically 1st, 2nd, 3rd, and 4th quintile income households reliant on informal incomes).** A household, as defined by the Pakistan Bureau of Statistics, may be either a single-person or multi-person household. An intermediate indicator to directly track how the AF benefits lower quintile households (Tier 0 and 1 loan beneficiaries) has been added to the project results framework.

16. **AF will make it possible for financial institutions to move down-market.** The project will enable PMLs to move from the very upper end of the households in the 5th quintile to lower quintile income groups. Therefore, the financial sector at large will also benefit greatly as the project will help deepen the primary mortgage market, in addition to supporting capital market development.

C. Project Description, Components, and Financing

17. **The AF, under Component 2 will entail the provision of financing for the purpose of an initial capitalization of the Sub-Trust of the RSF for the Eligible Participating Financial Institutions (PFIs), to cover partial loss in case of borrowers' defaults on their Eligible Mortgage Loans**. As such, the pilot RSF (US$10 million) will now be complemented by a new sub-trust RSF (US$85 million equivalent). Like the pilot RSF, the salient features of the scaled up RSF (RSF-phase 2) will be fully aligned with the government's MPMG program. The capitalization of RSF-phase 2 will take place in two tranches.

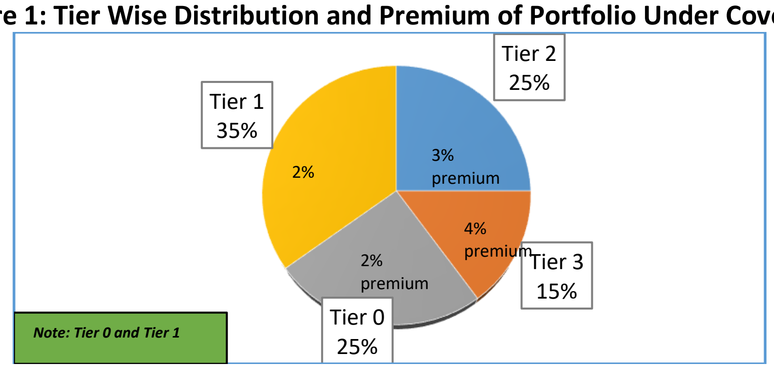
18. **The rationale for a tranche-based approach is twofold.** Firstly, both the mortgage market and the MPMG program are at a very nascent stage in Pakistan. As such, the salient features of the RSF-phase 2 are based on simulations and assumptions about how the market will develop. Significant deviations from these assumptions will require a recalibration of the features of RSF-phase 2. As such, the RSF-phase 2 needs be implemented incrementally. Secondly, given the recent growth trajectory of housing and construction finance in Pakistan (84 percent growth in 12 months), there is a strong indication that the market will require a much larger credit risk sharing facility going forward. The government does not have the fiscal space to meet these growing needs. The RSF-phase 2 has been designed to be scalable so that additional funding can be injected to increase its leverage if required. The second tranche of the capitalization will be timed such that any potential private capital injection can be sequenced into the structure, where the coverage model can be expanded beyond MPMG to help develop the "middle market."

19. **The government's capitalization through this AF can have a significant demonstration effect for the market. Its success will serve as a signal which crowds in private capital (such that the current structure can be transitioned to a more market-based Mortgage Guarantee Fund).** This model of incremental growth is widely accepted as best practice and been successful in similar markets. The premium structure, investment policy, and coverage model of the RSF-phase 2 is designed to ensure it remains a sustainable fund that will remain part of the housing finance market infrastructure well beyond the life of the project; but it includes the flexibility to scale it up through further capital injections as the housing finance market grows. Furthermore, the AF design considers the government's tight fiscal

position and, as such, the salient features and governance of the RSF-phase 2 have been developed to limit the government's fiscal exposure.

20. **The RSF-phase 2 will provide a 50 percent credit risk cover, as opposed to 40 percent in the pilot RSF.** The increase in risk coverage is based on extensive consultations with the regulator, PMLs, and other key stakeholders. Like in the parent project, a premium will be charged by the RSF-phase 2 for coverage. However, going forward the premium will be priced higher for the higher income groups and will range between 2–4 percent. The premium structure is currently designed to cross subsidize coverage between tiers; more affluent borrowers (under Tier 2 and 3) will be charged a higher premium. The premium structure, like the coverage, will be reevaluated as more empirical data becomes available to inform the operations and sustainability of the RSF-phase 2. The coverage model will also carry indicative targets (i.e., tier-wise allocation of the number of loans covered) to ensure that the RSF-phase 2 predominantly benefits lower- and middle-income households (see Annex 3 for details of the salient features of RSF-phase 2). The proposed distribution of the portfolio under coverage and premium charge by tier is laid out in Figure 1.

Figure 1: Tier Wise Distribution and Premium of Portfolio Under Coverage



** This distribution is contingent on there being enough supply of loans by tier.
Prevailing market conditions may require the Trustee and the GoP to realign the allocation.

21. **A Master Trust Agreement, which is grounded in local Trust Laws, will continue to underpin the operation of the RSF-phase 2.** The pilot RSF in the parent project was established under a Trust structure to ensure segregation of funds and to ring-fence the contingent liabilities that may result from the guarantees issued. This Trust structure is underpinned by the Master Trust Agreement, which has been signed by the GoP, as the owner of the Master Trust, and by PMRC, as the designated Trustee. The new Sub-Trust Deed will once again stipulate that PMRC will administer RSF-phase 2 on behalf of the government for a fee. The pilot RSF operates as a sub-trust of this Master Trust. The Master Trust and Sub-Trust Deed lay out clear guidelines for the operation of the pilot RSF. This includes details of the reporting requirements, financial management protocols, the investment policy of the pilot RSF, liability of the Trust and Trustee, auditing requirements, and governance. The RSF-phase 2 will replicate this model and will operate under a new sub-trust under the existing Master Trust Agreement. All other implementation arrangements remain as is (i.e., PMRC will act as Trustee of both the sub-trusts—for the pilot RSF and the RSF-phase 2).

22. **The notable difference between the RSF-phase 2 and the pilot RSF is that the US$85 million (equivalent) allocated under the AF will be the GoP's initial capital injection into the RSF**; the funds will not be on-lent to PMRC as was the case in the parent project. The additional funding will flow into the

sub-trust as the GoP's initial capitalization of the RSF-phase 2. Like in the pilot RSF, the GoP will backstop all guarantees issued. However, to keep the fiscal exposure of this backstop in check, like in the parent project, the contingent liability of the government will be capped in the Sub-Trust Deed, with an initial allocation of PKR 7 billion with a commitment to increase the allocation as required on the recommendation of the Oversight Committee (details on role of the Committee are given below). The government's capital along with the accumulated fees and income from investment (additional capital) generated by RSF-phase 2 will be leveraged such that the portfolio under coverage (PUC) can reach up to PKR 270 billion (US$1.5 billion). Details of the stress testing performed to keep the government's contingent liability in check are at Annex 4.

23. **A robust monitoring and evaluation framework will be put in place to ensure the RSF-phase 2 meets its developmental objective whilst also ensuring the government's fiscal risks are contained.** As the RSF-phase 2 is designed to support the government's efforts to promote affordable housing finance for lower income households, it will be important to monitor how it is rolled out and managed, particularly regarding distribution across tiers. The Operating Manual will include controls to ensure the implementation of the RSF-phase 2 continues to meet the objectives of the operation. Additionally, the overall operation of the RSF-phase 2 and any burgeoning contingent liability risks will be monitored closely. Scenario-based stress testing based on key financials and the implied leverage indicates that only in a catastrophic scenario, one underpinned by a wider economic meltdown, would there be any meaningful contingent liability implications for the GoP. The capital and recognized income of the RSF-phase 2 are projected to be sufficient to meet payment claims as they come due even under the stressed scenario. To ensure the efficient functioning of the RSF-phase 2 and to mitigate any fiscal risks, an Oversight Committee (with representatives from the Ministry of Finance, SBP, Securities and Exchange Commission (SECP), NAPHDA, and Pakistan Bankers Association (PBA), amongst others), will be constituted two months after project effectiveness to oversee any emerging risks emanating from coverage models. This Committee will receive quarterly reports from PMRC as the Trustee managing the RSF-phase 2. The Oversight Committee will have significant powers to adjust the operations, policies, and procedures of the RSF-phase 2, up to and including stoppage of issuing guarantees in case of a severe market deterioration.

24. **Private Capital Mobilization: The US$140 million IDA funding of the parent project is on track to mobilize an additional US$192.5 million of private capital for housing finance.** The parent project mobilized private capital through multiple angles, including:

- The subordinated debt and LoC were leveraged by PMRC to raise additional funding of US$69.4 million from the domestic capital markets.
- WB's lending made PMRC a viable investment for the IFC, which became an equity partner in 2020 with a US$3.1 million investment (IFC's investment has also served as a signal to other private sector players that have expressed interest in investing in PMRC).
- PMRC's advent has allowed for three private Housing Finance Companies to enter the market and has also enabled the microfinance sector to also start lending in this space (there has been an additional US$20 million in lending from the microfinance sector due to PMRC's funding).
- The pilot RSF under the parent project will be leveraged tenfold—the US$10 million equity will cover a portfolio up to US$100 million.

25. **Thus, like the parent project, the AF is expected to mobilize significant private capital.** The additional funding into the RSF-phase 2 will also be leveraged significantly to mobilize private capital. At its peak, the RSF-phase 2 with initial capital of US$85 million equivalent has the potential to have a portfolio under coverage (PUC) up to PKR 270 billion (US$1.5 billion – of this, it is expected that approximately US$750 million will be additional capital mobilized from private sector financial institutions). This represents approximately 70,000 loans. The RSF-phase 2 by its charter documentation (Sub-Trust Deed) is designed to remain within the agreed PUC limit. Additionally, the RSF-phase 2 will maintain capital reserves of no less than 8 percent to keep the fiscal risks within agreed limits. Notably, premiums and investment income will also contribute to reserves over time and thus to its financial sustainability. The risk-weighted leverage ratio of the GoP's initial capital contribution is estimated at eightfold. This represents unprecedented crowding in of private capital into the affordable housing finance space—a segment that has historically struggled to attract private capital.

26. **Additionally, the design of the RSF – phase 2 includes space for injection of additional private capital injection in due course.** An independent actuarial review of the performance of the RSF-phase 2 will be undertaken 18 months after project effectiveness. This provides enough time for the RSF's portfolio (pilot and phase 2) to mature to a level where credible data and market intelligence can be extracted. Any scope for additional private capital to increase the leverage and scope of the RSF-phase 2, along with any needs to recalibrate the coverage model due to changing market dynamics, will be identified at this stage. The second tranche of the capitalization will be disbursed once the independent actuarial review is complete and any recommendations for recalibration of RSF-phase 2 have been incorporated into the Operating Manual. As agreed during project preparation, the International Finance Corporation (IFC) will work with other private sector players to explore avenues to increase leverage if market development warrants it at that stage.

27. **Promote greater access to housing finance for women:** Women constitute only 15 percent of borrowers and account for a mere 10 percent of the gross loan portfolio in Pakistan's overall housing finance market. Compared to men, women in Pakistan earn less and have fewer formal income sources as well as limited access to credit services and property titles, making it more difficult for them to meet standard loan approval requirements. Like the parent project, the RSF-phase 2 provides credit risk cover to mortgages provided under the GoP's MPMG scheme. MPMG has eligibility provisions to support loans made to applicants with informal sources of income—this is particularly significant for women, the majority of whom work and earn informally in Pakistan. To incentivize PMLs to originate more loans where a female is a borrower (as sole or joint borrower), coverage accorded by the RSF-phase 2 to mortgages taken out by women will be higher at 60 percent, against standard coverage of 50 percent—at the same premium. This incentive is based on the objective that, at minimum, around 20 percent of the portfolio covered by the RSF-phase 2 will be comprised of mortgages taken out either solely or jointly by women. The revised project results framework also includes an indicator to measure progress on the portfolio under coverage disaggregated by gender.

28. **Climate Co-Benefits ("CCB"): The AF is also designed to promote climate friendly housing by incentivizing banks to give more mortgage loans to lower income households that transition to formal housing with greater energy and resource efficiency.** Pakistan is one of the most urbanized countries in the South Asian Region—one third of the population lives in urban centers. This urbanization has resulted in increasing urban sprawls, with growing concerns about air pollution, waste generation, and lack of

housing. Informal settlements are mushrooming across urban centers and these settlements are most vulnerable to the impacts of climate change. The lowest income households (Tier 0 and Tier 1 under NPHP) mostly reside in informal settlements and are thus very vulnerable to climate change, as they are unable to secure housing units that can adapt to the increasing climate risks in Pakistan. Like the incentive to promote greater gender equity, the RSF-phase 2 will increase the risk cover (i.e., from 50 percent to 60 percent) for these Borrower Groups. The bulk of the financing for these segments facilitates resettlement out of informal housing and many of these loans finance on-site production of renewable energy in new homes (solar panels). For loans to qualify for increased coverage based on energy efficiency and on-site renewable energy, stringent screening criteria will be developed and the PML will have to provide sufficient evidence that the underlying loan qualifies. This may result in a paradigm shift in lending practices. At present, housing finance providers do not look at their loans from a “green” lens. Building the capacity of banks to understand what loans qualify as climate resilient and energy/resource efficient will mainstream lending practices that do not currently exist. This will directly influence the norm and, in the medium to longer term, will change behaviors of both lenders and borrowers. Further details on the project’s CCB assessment are recorded in the Bank’s operations portal and can be made available to Executive Directors upon request.

D. Details of Project Restructuring

29. In addition to the AF, this Project Paper proposes a level 2 restructuring in three areas:

(i) **The proposed restructuring entails cancellation of Component 3: Capacity Building for Housing Policy and Analytics (US$5 million) from the original project design.** Given the new government’s strong policy focus on housing and with the establishment of the new housing authority (NAPHDA), the government has devoted sufficient resources to build the institutional capacity to promote affordable housing in Pakistan. Additionally, the two complementary supply side projects (Punjab Affordable Housing Program - P173663 and Punjab Urban Land Systems Enhance Project - P172945) have strong technical assistance components and as such this capacity gap no longer remains. The cancellation of this component will also include dropping the implementing agency (Planning Commission) and cancelling the leftover funds (SDR 419,627).

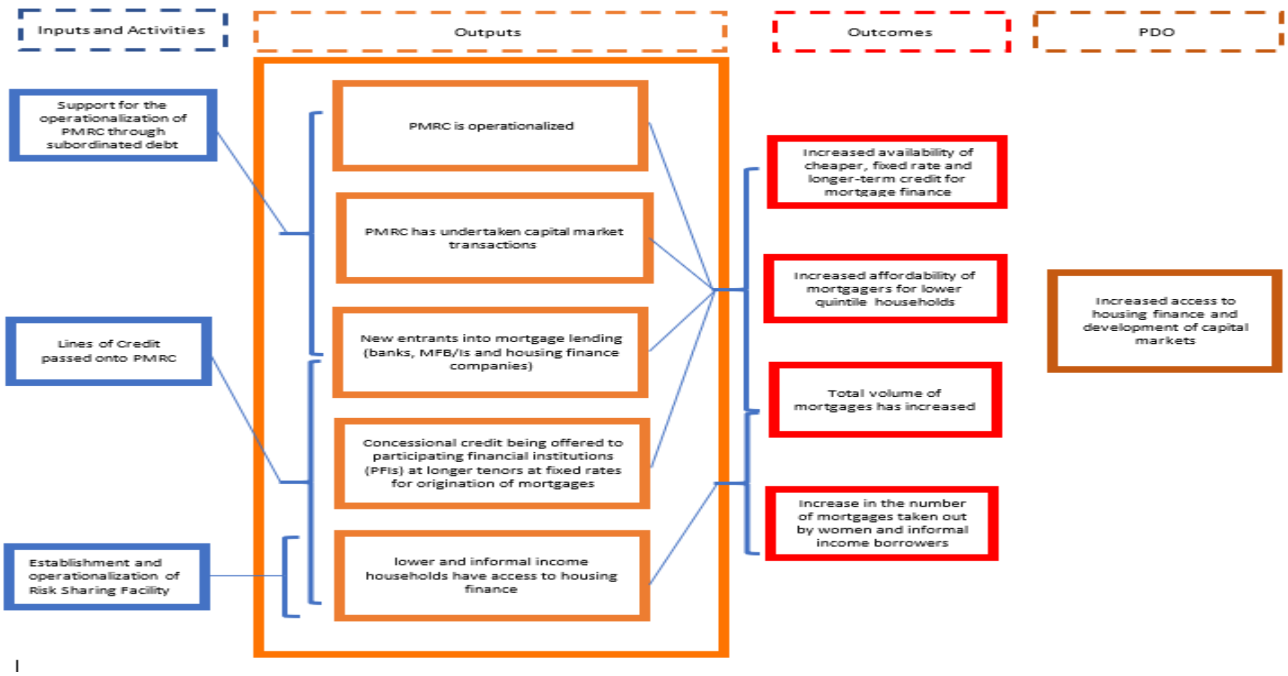
(ii) **The proposed restructuring is expected to entail revisions to the results framework.** Changes mainly refer to higher end target value changes for several indicators, introduction of one new indicator (“Portfolio under coverage of RSF”) and the drop of one indicator earlier included to monitor progress under Component 3, which is now proposed to be dropped. Details can be found in Section VIII below.

(iii) **The proposed restructuring also entails an extension of the Project Closing Date.** It is proposed that the project closing date is extended from June 2023 to June 2026.

E. Theory of Change

30. **The revised theory of change, incorporating all the changes being proposed in the AF and restructuring, is presented below:**

Figure 2: Revised Theory of Change



III. KEY RISKS

31. The overall risk rating for project design and implementation remains **Substantial.**

32. **Political and Governance (Substantial):** Housing is a significant policy imperative for the government but focus on this area may become muted if there is a change in leadership. The AF supports the MPMG program and with elections approaching in 2023 there may be a risk of policy shift. Nevertheless, the SBP is implementing MPMG and has given assurances to the banking sector that the program is independent, and the central bank has access to the government's accounts with it to pay the interest rate subsidies as they fall due.

33. **Macroeconomic (Substantial):** Macroeconomic risk is likely to remain Substantial, as fiscal and monetary tightening is expected to resume in FY22. After contracting in FY20 due to the adverse impact of COVID-19, economic activity recovered in FY21. Due to low-base effects and recovering domestic demand, real GDP growth (at factor cost) is estimated to have rebounded to 3.5 percent in FY21 from a contraction of 0.5 percent in FY20. However, considering emerging external imbalances and higher domestic inflation, fiscal and monetary tightening are expected to resume in FY22. Public debt will remain elevated in the medium term, as will Pakistan's exposure to debt-related shocks. This outlook assumes that the IMF Extended Fund Facility program will remain on track. The subsidies embedded in MPMG may

become fiscally unsustainable if the macro environment deteriorates. While loans already originated under the program will be grandfathered, new loans may not be fiscally viable. To mitigate this risk, the project design includes space to revise coverage model in case the MPMG program is halted. Additionally, to manage any burgeoning fiscal risks, the contingent liabilities arising from the RSF will be tracked as part of project design.

34. **Other: COVID-19 (Substantial):** The impact of the COVID-19 pandemic poses risks to at least the start of implementation, including restrictions on mobility. The design of the project aims to mitigate these risks by requiring adherence to COVID-19 standard operating procedures. The virus-related risks are expected to be reduced as the scaling up of vaccinations advances.

IV. APPRAISAL SUMMARY

A. Economic and Financial Analysis

35. **The economic analysis undertaken for the AF suggests an internal rate of return (IRR) of 118 percent over the life of the project, in addition to a net present value (NPV) of US$225 million.** The economic analysis was undertaken based on the additionality of the project (i.e., additional financial flows generated attributable to the RSF-phase 2). **The key assumption employed was that at any point in time, 30 percent of the portfolio under coverage would be attributable directly to the RSF-phase 2—that is, this portfolio/these loans would not have been originated in** the absence of the risk cover accorded by the RSF-phase 2. The NPV was calculated using a discount rate of 15 percent.[9] It is also important to note that the relatively large IRR is a function of the leverage ratio and coverage of the RSF-phase 2.

36. **The cascading and catalytic economic impact of the project is expected to be just as large as the financial impact.** While difficult to quantify, the catalytic economic impact of the RSF-phase 2 is expected to be large because the construction sector is directly and indirectly linked to 40 other sectors of the economy. Greater flows of finance towards housing leading to the construction of houses and apartments across the country, and hence to an increase in the demand of construction materials and services, can all reasonably be expected to lead to an increase in aggregate output and associated increase in jobs and investment.

B. Technical

37. **The RSF-phase 2 has been designed to be a sustainable fund, which, failing a very significant economic scenario, will not require a contingent capital injection from the government.** In the base case scenario, where the market and the portfolio perform in a non-stressed environment, this initial capital could be leveraged to guarantee a maximum PUC of up to US$1.5 billion (PKR 270 billion). Notably, RSF premiums and investment income also contribute over time to reserves and thus to RSF financial sustainability. There is also an 8 percent capital reserve ratio. However, given the identified substantial macro-economic risks, it is reasonable to expect that there will be uncertainties about mortgage loan origination and demand for RSF coverage, and such maximum portfolio will accumulate at a significantly slower rate. Based on these assumptions, and to remain prudent in managing the contingent liability risks,

[9] The WB has not traditionally calculated a discount rate and has used 15 percent as a notional figure for discounting the flows.

the risk-weighted leverage ratio of the GoP's initial capital contribution is estimated at eightfold. Such maximum PUC size is expressed as per the Sub-Trust Deed both in the number of covered loans (70,000 loans) and in PKR terms (PKR 270 billion) with the provision that loan guarantee provision will stop once either of these limits is reached.

C. Financial Management

38. **The FM arrangements to manage the AF are adequate and there is no change from the parent project.** PMRC will continue to manage these funds under the existing Master Trust Agreement, supplemented with a Subsidiary Trust Deed for the RSF-phase 2. Controls embedded in the Operating Manual and the ongoing monitoring by the Oversight Committee further mitigate risks of funds not being used for intended purposes. The FM staffing, budgeting, internal controls, auditing, reporting, accounting, and fund flow arrangements of PMRC are adequate for this AF.

39. **The funds will be moved from the designated account (DA) into the sub-trust account (RSF-phase 2) as per the financial management rules of the GoP.** Separate Interim Unaudited Financial Statements (IUFRs) are not required. This AF will be included in the IUFRs of the parent project. The annual audit of the parent project will also cover the AF.

D. Procurement

40. **The AF will not involve any procurement.** Component 3 under the parent project was the only component that included any procurement and this has been cancelled after the proposed restructuring. The project does not therefore require the preparation of a Project Procurement Strategy for Development by the borrower/implementation agency. Nor does it require a Procurement Plan to be prepared by the implementation agency.

E. Social and Environment (including Safeguards)

41. **The E&S risks and rating for the AF remains the same as the parent project, based upon the AF supporting only the additional injection of funds into the RSF, without a change to the supported activities, for which there is an established, functional, and active ESMS at PMRC.** The AF is categorized the same as the parent project—as FI-2—in accordance with OP/BP 4.03 based on the review of the prospective project activities and an expectation that, in accordance with BP 4.03 paragraph, potential adverse environmental and social risks or impacts will be few, generally site-specific, largely reversible, and readily addressed through mitigation measures.

42. **PMRC has performed satisfactorily in the implementation of the ESMS.** Through the parent project, PMRC has set up an ESMS guided by their E&S Policy, which follows the IFC Performance Standards[10] (in line with OP4.03) and sets WBG approved procedures for E&S risk management. Head of Risk at PMRC is supervising E&S aspects, while Head of Products supports as E&S coordinator for customer interaction. The E&S Policy has been mainstreamed throughout PMRC activities and is an integral part of its lending activities.. PMRC espoused the same ESMS and E&S standards in its role as Trustee of the RSF. Since PMRC relies on its participating financial institutions (PFIs) to conduct primary due diligence on their mortgage portfolios presented to PMRC for refinancing, PMRC also has processes to assist PFIs in building

[10] https://pmrc.com.pk/wp-content/uploads/2021/04/PMRC_Environmental_and_Social_Policy.pdf.

their E&S capacity through training and counseling. PFIs lacking adequate ESMS are required to prepare and implement Action Plans. The first training session for PFIs was held in September 2019 at the SBP with 26 participants from 13 banks. A second virtual training session was conducted in June 2021 with 20 participants from 14 PFIs. Some challenges remain where PMRC works with microfinance institutions, which still have comparatively weak E&S systems and capacity, and the AF will focus on ramping up targeted training and technical support for MFIs. PMRC has in place a Grievance Redress Mechanism (GRM) Policy, which is also present on their website.[11]

V. WORLD BANK GRIEVANCE REDRESS

43. **Communities and individuals who believe that they are adversely affected by a WB supported project may submit complaints to existing project-level grievance redress mechanisms or the WB's Grievance Redress Service (GRS).** The GRS ensures that complaints received are promptly reviewed to address project-related concerns. Project affected communities and individuals may submit their complaint to the WB's independent Inspection Panel which determines whether harm occurred, or could occur, because of WB non-compliance with its policies and procedures. Complaints may be submitted at any time after concerns have been brought directly to the WB's attention, and Bank Management has been given an opportunity to respond. For information on how to submit complaints to the WB's corporate GRS, please visit http://www.worldbank.org/en/projects-operations/products-and-services/grievance-redress-service. For information on how to submit complaints to the World Bank Inspection Panel, please visit www.inspectionpanel.org.

[11] https://pmrc.com.pk/reports/complaint-management/.

VI. SUMMARY TABLE OF CHANGES

	Changed	Not Changed
Implementing Agency	✓	
Results Framework	✓	
Components and Cost	✓	
Loan Closing Date(s)	✓	
Cancellations Proposed	✓	
Reallocation between Disbursement Categories	✓	
Project's Development Objectives		✓
Disbursements Arrangements		✓
Safeguard Policies Triggered		✓
EA category		✓
Legal Covenants		✓
Financial Management		✓
Procurement		✓
Other Change(s)		✓

VII. DETAILED CHANGE(S)

IMPLEMENTING AGENCY

Implementing Agency Name	Type	Action
PMRC	Private Sector	No Change
Ministry of Planning, Development & Reform	Line Ministry/Ministerial Department	Marked for Deletion
Naya Pakistan Housing & Development Authority	Parastatal/Independent Government Institute	Marked for Deletion

COMPONENTS

Current Component Name	Current Cost (US$, millions)	Action	Proposed Component Name	Proposed Cost (US$, millions)
Support to PMRC in Strengthening its Capital Base	60.00	No Change	Support to PMRC in Strengthening its Capital Base	60.00
Supporting Expansion of Mortgage Loans	80.00	Revised	Supporting Expansion of Mortgage Loans	915.00
Capacity Building for Housing Policy and Analytics	5.00	Marked for Deletion	Capacity Building for Housing Policy and Analytics	0.00
TOTAL	**145.00**			**975.00**

LOAN CLOSING DATE(S)

Ln/Cr/Tf	Status	Original Closing	Current Closing(s)	Proposed Closing	Proposed Deadline for Withdrawal Applications
IDA-62070	Effective	30-Jun-2023	30-Jun-2023	30-Jun-2026	30-Oct-2026

CANCELLATIONS

Ln/Cr/Tf	Status	Currency	Current Amount	Cancellation Amount	Value Date of Cancellation	New Amount	Reason for Cancellation
IDA-62070-001	Disbursing	XDR	99,600,000.00	419,627.00	27-Oct-2021	99,180,373.00	REVISE VALUE DT(WHEN CHNG VAL DT SELEC.)

REALLOCATION BETWEEN DISBURSEMENT CATEGORIES

Current Allocation	Actuals + Committed	Proposed Allocation	Financing % (Type Total)	
			Current	Proposed

IDA-62070-001 | Currency: XDR

iLap Category Sequence No: 1 Current Expenditure Category: SUBORDINATED LOAN UNDER PT. 1

41,214,000.00	41,242,405.47	41,266,449.00	100.00	100.00
iLap Category Sequence No: 2A	Current Expenditure Category: MORTGAGE REFINANCING PT. 2A			
48,083,000.00	49,727,161.86	50,644,897.00	100.00	100.00
iLap Category Sequence No: 2B	Current Expenditure Category: CAPITALIZ'N RISK SHARING FCLTY P.2B			
6,869,000.00	0.00	7,269,027.00	100.00	100.00
iLap Category Sequence No: 3	Current Expenditure Category: GDS, NON-CS, CS, TR/WS, IOC PT.3			
3,434,000.00	0.00	0.00	100.00	100.00
Total **99,600,000.00**	**90,969,567.33**	**99,180,373.00**		

Expected Disbursements (in US$)

Fiscal Year	Annual	Cumulative
2018	88,400.00	88,400.00
2019	4,050,165.00	4,138,565.00
2020	6,844,115.00	10,982,680.00
2021	9,906,155.00	20,888,835.00
2022	11,934,255.00	32,823,090.00
2023	11,840,415.00	44,663,505.00
2024	13,690,525.00	58,354,030.00
2025	14,173,750.00	72,527,780.00
2026	12,472,220.00	85,000,000.00

SYSTEMATIC OPERATIONS RISK-RATING TOOL (SORT)

Risk Category	Latest ISR Rating	Current Rating
Political and Governance	Substantial	Substantial
Macroeconomic	Moderate	Substantial

Sector Strategies and Policies	Moderate	Moderate
Technical Design of Project or Program	Moderate	Moderate
Institutional Capacity for Implementation and Sustainability	Moderate	Moderate
Fiduciary	Moderate	Moderate
Environment and Social	Moderate	Moderate
Stakeholders	Moderate	Moderate
Other	Moderate	Substantial
Overall	Substantial	Substantial

LEGAL COVENANTS – Pakistan Housing Finance: Additional Financing (P172581)

Sections and Description
No information available

Conditions

Type	Financing source	Description
Effectiveness	IBRD/IDA	(a) The Trust Deed has been registered in accordance with the legal requirements of the Recipient.
Effectiveness	IBRD/IDA	(b) (i) The Sub-Trust Deed has been executed between the Recipient and the Project Implementing Entity. (ii) The Project Operations Manual for the Sub-Trust which has been approved by the Recipient and acceptable to the Association, has been adopted by the Project Implementing Entity.
Disbursement	IBRD/IDA	Under Category (2) for the second tranche of the Capitalization of the Sub-Trust of a risk sharing facility under Part 2 (c) of the Project, unless and until: (i) an independent actuarial review of the performance of the Sub-Trust has been undertaken; and (ii) the Project Operations Manual for the Sub-Trust has been revised and approved by the RSF Oversight Committee and the Association, reflecting recommendations from the review referred to in (i) above.

VIII. RESULTS FRAMEWORK AND MONITORING

Results Framework
COUNTRY: Pakistan
Pakistan Housing Finance: Additional Financing

Project Development Objective(s)

The Project Development Objective is to increase access to housing finance for households, and support capital market development in Pakistan.

Project Development Objective Indicators by Objectives/ Outcomes

Indicator Name	PBC	Baseline	Intermediate Targets									End Target
			1	2	3	4	5	6	7	8	9	
To increase access to housing finance for households and Capital market development in Pakistan												
Number of Total Mortgage Loans Refinanced by PMRC (Number)		0.00	1,000.00	2,600.00	2,000.00	3,800.00	2,600.00	3,400.00	5,000.00	5,000.00	4,600.00	30,000.00
Action: This indicator has been Revised												
Value of Total Outstanding Mortgages (Amount(USD))		627,142,857.00										3,529,411,764.00
Action: This indicator has been Revised												
Percentage of Refinanced		0.00	0.00	3.00	4.00	6.00	8.00	10.00	13.00	17.00	19.00	20.00

Indicator Name	PBC	Baseline	Intermediate Targets									End Target
			1	2	3	4	5	6	7	8	9	
Mortgages Taken out by Women (Percentage)												
Action: This indicator has been Revised												
PMRC bond issuance volume (Amount(USD))		0.00										261,000,000.00
Action: This indicator has been Revised												

Intermediate Results Indicators by Components

Indicator Name	PBC	Baseline	Intermediate Targets									End Target
			1	2	3	4	5	6	7	8	9	
Support to PMRC in Strengthening its Capital Base												
Amount of PMRC-Refinanced Mortgage Loans (Amount(USD))		0.00	10,000,000.00	25,000,000.00	70,000,000.00	100,000,000.00	120,000,000.00	150,000,000.00	150,000,000.00	150,000,000.00	100,000,000.00	800,000,000.00
Action: This indicator has been Revised												
Supporting Expansion of Mortgage Loans												

Indicator Name	PBC	Baseline	Intermediate Targets									End Target
			1	2	3	4	5	6	7	8	9	
Number of PMRC financed/refinanced Mortgage Loans of PKR 3 million or less (Number)		0.00	250.00	1,600.00	1,700.00	1,450.00	2,000.00	3,000.00	3,000.00	2,000.00		15,000.00
Action: This indicator has been Revised												
Direct project beneficiaries that feel that project investments reflected their needs (Percentage)		0.00	80.00	80.00	80.00	80.00	80.00	80.00	80.00	80.00	80.00	80.00
Action: This indicator has been Revised												
Scaled up RSF has been operationalized (Yes/No)		No										Yes
Action: This indicator is New												
Portfolio under coverage of RSF (Amount(USD))		0.00										1,588,235,294.00
Action: This indicator is New												
of which Tier 0 and Tier 1 mortgages (Amount(USD))		0.00										952,941,176.00

Indicator Name	PBC	Baseline	Intermediate Targets									End Target
			1	2	3	4	5	6	7	8	9	
Action: This indicator is New												
of which mortgages taken out by women (Amount(USD))		0.00										317,647,058.00
Action: This indicator is New												
Capacity Building for Housing Policy and Analytics *(Action: This Component has been Marked for Deletion)*												
New low income strategy prepared and adopted (Yes/No)		No	No	No	Yes	Yes	Yes	Yes				Yes
Action: This indicator has been Marked for Deletion												

Monitoring & Evaluation Plan: PDO Indicators					
Indicator Name	Definition/Description	Frequency	Datasource	Methodology for Data Collection	Responsibility for Data Collection
Number of Total Mortgage Loans Refinanced by PMRC		Annual	PMRC financial reports		PMRC
Value of Total Outstanding Mortgages		Annual	SBP		PMRC

Percentage of Refinanced Mortgages Taken out by Women	The target to be achieved is 20 percent by the end of the project	Annual	PMRC		PMRC
PMRC bond issuance volume		Annual	PMRC		PMRC

Monitoring & Evaluation Plan: Intermediate Results Indicators					
Indicator Name	**Definition/Description**	**Frequency**	**Datasource**	**Methodology for Data Collection**	**Responsibility for Data Collection**
Amount of PMRC-Refinanced Mortgage Loans		Annual	PMRC		PMRC
Number of PMRC financed/refinanced Mortgage Loans of PKR 3 million or less	Reference to the amount of mortgage loan is in constant PKR	Annual	PMRC		PMRC
Direct project beneficiaries that feel that project investments reflected their needs		Annual	Survey tools		PMRC and Planning Commission
Scaled up RSF has been operationalized			PMRC		PMRC
Portfolio under coverage of RSF			PMRC		PMRC
of which Tier 0 and Tier 1 mortgages			PMRC		PMRC
of which mortgages taken out by women		Annual	PMRC		PMRC
New low income strategy prepared and adopted		Annual	Planning Commission		Planning Commission

ANNEX 1. PILOT RSF

Table A2.1. Tier-wise Distribution of Loans Requested for RSF Coverage (loan amount in PKR million and US$ equivalent)

	PFIs	No. of loans requested to be covered	Cumulative Loan Amount	Tier-wise Details			
				Tier 2		Tier 3	
				No. of Loans	Loan Amount	No. of Loans	Loan Amount
1	HBL	122	323.3 (US$1.9)	96	239.8 (US$1.4)	26	83.6 (US$0.5)
2	JS Bank	38	144.9 (US$0.8)	31	97.5 (US$0.6)	7	47.4 (US$0.3)
3	Meezan	104	301.6 (US$1.7)	59	163.2 (US$1.0)	45	138.5 (US$0.8)
4	NBP	294	463.6 (US$2.7)	163	233.6 (US$1.4)	131	230 (US$1.3)
5	Bank of Punjab	43	175.4 (US$1.0)	23	66.72 (US$0.4)	20	108.71 (US$0.6)
6	Bank Alfalah	270	1,224.8 (US$7.2)	170	593.52 (US$3.5)	100	63.12 (US$0.4)
	Total	**871**	**2,633.6 (US$15.5)**	**349**	**734.1 (US$4.3)**	**209**	**499.5 (US$2.9)**

Table A2.2. Banks Signed up for Risk Sharing Facility

	Name
1	The Bank of Punjab
2	Habib Bank Limited
3	Faysal Bank Limited
4	BankIslami Pakistan Limited
5	Meezan Bank Limited
6	JS Bank Limited
7	Soneri Bank Limited
8	Bank Alfalah Limited
9	Dubai Islamic Bank Pakistan Limited
10	United Bank Limited
11	National Bank of Pakistan
12	Askari Bank Limited
13	Habib Metropolitan Bank

ANNEX 2. GOVERNMENT'S MPMG—KEY FEATURES

<table>
<tr><th></th><th></th></tr>
<tr><th>Particulars</th><th>Mark up Subsidy Program</th></tr>
<tr><td>Eligibility Criteria</td><td>• All men/women holding Computerized National Identity Card
• First time homeowner
• An individual can have subsidized house loan facility under this scheme only once</td></tr>
<tr><td>Tiers of the Scheme</td><td>• Financing under Tier 0 is available through microfinance banks for financing of housing units under non-NAPHDA projects
• Financing under Tier 1 is available through banks for financing under NAPHDA projects
• Financing under Tier 2 and Tier 3 is available through banks for financing of housing units under non-NAPHDA projects</td></tr>
<tr><td>Maximum Price of Housing Units</td><td>Maximum price (market value) of a single housing unit at the time of approval of financing, as under:
Tier 1 (T1)—Rs 3.5 million
Tier 0 (T0), Tier 2 (T2), and Tier 3 (T3)—No cap</td></tr>
<tr><td>Maximum Loan Size</td><td>Maximum size of the loan of a single housing unit, as under:
Tier 0 (T0)—Rs 2.0 million
Tier 1 (T1)—Rs 2.7 million
Tier 2 (T2)—Rs 6.0 million
Tier 3 (T3)—Rs 10.0 million</td></tr>
<tr><td>Loan Tenor</td><td>Minimum 5 years and maximum 20 years loan tenor, depending upon choice of customers</td></tr>
<tr><td>Allocation in Budget</td><td>Finance Division shall give authority to SBP to debit GoP account on quarterly basis for the subsidy payment to banks. Payment will be made to the banks on submission of quarterly-consolidated subsidy statement as per format prescribed by State Bank</td></tr>
<tr><td>Pricing</td><td>Pricing for Housing Loans:
<table>
<tr><th><u>Loan Tiers</u></th><th><u>Customer Pricing</u></th><th><u>Bank Pricing</u></th></tr>
<tr><td>Tier 0</td><td>5% for first 5 years &
7% for next 5 years</td><td>KIBOR+700 BPS</td></tr>
<tr><td>Tier 1</td><td>3% for first 5 years &
5% for next 5 years</td><td>KIBOR+250 BPS</td></tr>
<tr><td>Tier 2</td><td>5% for first 5 years &
7% for next 5 years</td><td rowspan="2">KIBOR+400 BPS
(Spread may vary)</td></tr>
<tr><td>Tier 3</td><td>7% for first 5 years &
9% for next 5 years</td></tr>
<tr><td colspan="3">For loan tenors exceeding 10 years, market rate i.e., bank pricing will be applicable for the period exceeding 10 years.</td></tr>
</table></td></tr>
</table>

ANNEX 3. RSF-PHASE 2 SALIENT FEATURES

Reserve contribution by government into the Trust	US$85 million equivalent in PKR, in two tranches. US$65 million initially (in FY22) and US$20 million (within two years)
Maximum PUC	PKR 270 billion—not to be exceeded by the Trustee at any time and to be included in the Deed of Trust
Estimated number of loans comprising such PUC	70,000 loans—may vary by year and depending on the composition of the PUC by Tiers
Estimated yearly number of guarantee policies written (guaranteed loans)	15,000 policies (loans)
Estimated average mortgage loan amount per tiers	Tier 0—PKR 1.5 million Tier 1—PKR 2.0 million Tier 2—PKR 4.5 million Tier 3—PKR 7.5 million
Maximum mortgage loan tenor	20 years
Guarantee coverage	Up to 50% of unpaid principal balance (UPB) at the time of Claim settlement event, 60% for "green" loans or where a female is a sole or joint mortgagor
Assumed PUC claims performance (Claims are lower than prevailing NPLs—more details on this in Annex 6)	Under normal scenario—3% per year Under stress scenario—9% per year Under catastrophic scenario—30% per year
Insured event	Borrower default as declared by the lender pursuant to applicable laws and regulations
Claim settlement event	Lender initiated property foreclosure proceedings pursuant to applicable laws and regulations and subject to mandatory loan restructuring attempt compliant with the RSF Operating Manual
Guarantee premium	Calculated as a percentage of the UPB of the covered Mortgage Loan portfolio as of signing of **RSF Facility Letter** date payable upfront according to Tiers as follows: Tier 0—2%

	Tier 1—2% Tier 2—3% Tier 3—4%
Taxes	Taxes to be borne by PFIs or as per applicable laws
Leverage Ratio	Trust’s net assets should not be less than 8% of the portfolio under coverage as calculated by the aggregate outstanding balance of the Mortgage Loans at each reporting period (quarterly)
Reserves	The Trustee shall make and maintain financial reserves according to the Leverage Ratio, Reserve Investment Policies and other applicable rules and regulations
Trustee fee	0.25 of recognized annual premiums
RSFR prudential recognition	SBP recognizes the RSF coverage via its prudential treatment of the covered Mortgage Loans for Capital Adequacy Ratio (CAR) capital allocation and mandatory provisioning for impaired assets. Thus, the covered portion of the Mortgage Loans receives 0 risk weight for CAR purposes and is deducted from provisioning calculations for impaired assets

ANNEX 4. STRESS TESTING

RSF Sustainability and Government Fiscal Exposure

1. Given that the housing finance market is still at a nascent developmental stage and that the housing finance related risk coverage is novel in Pakistan, there is a need to back-stop the RSF with a government guarantee. The back stop is required to give credibility to the RSF and the GoP commitment to developing housing finance market in Pakistan. This credit risk cover becomes more as critical as the SBP has now given banks mandatory lending targets, with a focus on loans for lower and informal income households. The backstop would imply that the GoP might need to inject capital into RSF under adverse economic conditions. Such additional shareholder capitalization of a mortgage insurer under catastrophic scenario is a normal business practice and is not a particular feature of the RSF.

2. In designing the model of RSF, three different scenarios of portfolio performance have been tested:

(i) **Normal:** which presumes a relatively benign but realistic level of RSF claims of 3 percent per year (the *Normal* scenario is the base case scenario of "business as usual"). This claim level largely correlates with the observed mortgage delinquency for recently originated mortgages. Under this scenario, the RSF is capable to pay all due claims without using its equity, i.e., from recognized premium income and investment income.

(ii) **Stressed:** which presumes a significantly elevated level of claims of 9 percent per year (a *Stressed* scenario would signal significant macro-economic shock). This scenario correlates with a significant impact of the previous mortgage market crisis in Pakistan and lingering NPL effects, which are currently about 10 percent for such legacy portfolio. Under this scenario, some of the RSF reserves are used for claim payment but no additional GoP contribution is needed. Based on the financial modeling, 17 percent is the upper limit of claims that will be sustained by RSF resources (initial capital and accumulated additional reserves from investment and premium income).

(iii) **Catastrophic:** with 30 percent claims per year (the *Catastrophic* scenario is included as a worst case with portfolio delinquencies and RSF claims indicative of a severe prolonged economic crisis and a meltdown of the mortgage market—a very highly unlikely scenario). For comparison, even during past systemic mortgage crises in Central Europe, US Subprime, Columbia, Mexico, and Asia, very high NPL levels (30+ percent) were seen only at some specific lenders (similar to Pakistan's experience with HBFCL, which has had elevated NPLs) and not market wide and did not translate into 30 percent claims. Under this scenario, additional GoP capital contribution may be required to allow RSF to pay the claims: the estimated maximum amount of such conditional exposure is estimated around PKR 30 billion.

3. Note that under all scenarios, the stress testing has been undertaken for the claims to the RSF. Claims are always notably lower than per NPLs, and this will likely be more pronounced for this RSF. The lower level of claims is because there are numerous checks and balances to ensure only eligible defaults can put a claim on the RSF. In the case of this RSF, for example, amongst other measures, a bank must demonstrate it made a clear and in good faith effort to restructure a delinquent loan. Given the target beneficiaries of these loans are low-income households who are benefitting from very subsidized loans,

global experience shows that, where they are given a true opportunity to rectify their delinquent status, they will do so.

4. Additionally, one further mitigating factor in the case of Pakistan is that the RSF only provides credit risk cover to highly subsidized loans, thus the affordability risk is mitigated somewhat. As such, while NPLs in the mortgage sector as a whole may become elevated, the loans covered by the RSF will likely not see NPLs at the same levels. The risk on affordability would be if the government rescinded on the interest rate subsidies, again this risk is mitigated. The SBP has committed that once a loan is originated under the MPMG, it will receive the interest rate subsidy as committed by GoP (for the first 10 years of the loan, which is the same as the coverage period of the RSF). As such, the risk of mass defaults on existing loans due to a lapse in interest rate subsidies is also mitigated.

5. Only under a “catastrophic” scenario would there be a need for the GoP to inject capital into the RSF to maintain its claims payment capacity. To ensure the GoPs fiscal exposure is contained, such contingent liability would remain limited to PKR 30 billion for the RSF-phase 2.

6. Notably, the RSF is not expected to accumulate such maximum PUC of PKR 270 billion immediately, but rather via growth over few years depending on the market demand. Thus, the maximum budget contingent liability will also be increasing over time—time that provides valuable mortgage market and portfolio performance data, which should be used to calibrate RSF features, e.g., adjust pricing, ration coverage towards certain market segments (tiers), perform lender due diligence and practice inspections. In other words, there will be sufficient time to monitor the market and macro-economic situation and prepare accordingly for potentially elevated level of claims.