PD-ABL-012

ISN 63204

**AGENCY FOR INTERNATIONAL DEVELOPMENT**

**Washington, D. C. 20523**

# PROJECT PAPER

PAKISTAN: Shelter Resource Mobilization Program (391-HG-001 and 391-0507)

June 1, 1989

UNCLASSIFIED

AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON, D.C. 20523

# PROJECT PAPER
# PAKISTAN - SHELTER RESOURCE MOBILIZATION PROGRAM
391-HG-001 AND 391-0507

JUNE, 1989

UNCLASSIFIED

AGENCY FOR INTERNATIONAL DEVELOPMENT

# PROJECT DATA SHEET

1. TRANSACTION CODE: A (A = Add, C = Change, D = Delete) — Amendment Number

DOCUMENT CODE: 3

2. COUNTRY/ENTITY: PAKISTAN

3. PROJECT NUMBER: 391-HG-001 / 391-0507

4. BUREAU/OFFICE: ASIA/NEAR EAST

5. PROJECT TITLE (maximum 40 characters): SHELTER RESOURCE MOBILIZATION PROGRAM

6. PROJECT ASSISTANCE COMPLETION DATE (PACD): MM 06 DD 30 YY 94

7. ESTIMATED DATE OF OBLIGATION (Under 'B.' below, enter 1, 2, 3, or 4)
A. Initial FY 89 B. Quarter 3 C. Final FY 94

8. COSTS ($000 OR EQUIVALENT $1 = )

| A. FUNDING SOURCE | FIRST FY 89 B. FX | C. L/C | D. Total | LIFE OF PROJECT E. FX | F. L/C | G. Total |
|---|---|---|---|---|---|---|
| AID Appropriated Total | | | | | | |
| (Grant) | ( 2,000 ) | ( ) | ( 2,000 ) | ( 5,000) | ( ) | ( 5,000 ) |
| (Loan) | ( ) | ( ) | ( ) | ( ) | ( ) | ( ) |
| Other U.S. 1. Housing Guaranty Loan | 25,000 | | 25,000 | 100,000 | | 100,000 |
| Other U.S. 2. | | | | | | |
| Host Country | | 25,000 | 25,000 | | 100,000 | 100,000 |
| Other Donor(s) | | | | | | |
| TOTALS | 27,000 | 25,000 | 52,000 | 105,000 | 100,000 | 205,000 |

9. SCHEDULE OF AID FUNDING ($000)

| A. APPROPRIATION | B. PRIMARY PURPOSE CODE | C. PRIMARY TECH. CODE 1. Grant | 2. Loan | D. OBLIGATIONS TO DATE 1. Grant | 2. Loan | E. AMOUNT APPROVED THIS ACTION 1. Grant | 2. Loan | F. LIFE OF PROJECT 1. Grant | 2. Loan |
|---|---|---|---|---|---|---|---|---|---|
| (1) ESF | 720 | 860 | 810 | 2,000 | | 2,000 | | 5,000 | |
| (2) | | | | | | | | | |
| (3) | | | | | | | | | |
| (4) | | | | | | | | | |
| TOTALS | | | | 2,000 | | 2,000 | | 5,000 | |

10. SECONDARY TECHNICAL CODES (maximum 6 codes of 3 positions each)

11. SECONDARY PURPOSE CODE

12. SPECIAL CONCERNS CODES (maximum 7 codes of 4 positions each)

| A. Code | BU | BR | EQTY | PART | | | |
|---|---|---|---|---|---|---|---|
| B. Amount | 1,500 | 1,500 | 1,000 | 1,000 | | | |

13. PROJECT PURPOSE (maximum 480 characters)

The purpose of the program is to create the policy environment which will promote the establishment of market-oriented shelter finance institutions. A second purpose is to initially support, through local currency equivalent amounts, GOP shelter programs affordable to low income families during the period of policy change.

14. SCHEDULED EVALUATIONS
Interim MM 07 YY 90 | MM 07 YY 91 | Final MM 07 YY 94

15. SOURCE/ORIGIN OF GOODS AND SERVICES
☐ 000 ☐ 941 ☐ Local ☐ Other (Specify)

16. AMENDMENTS/NATURE OF CHANGE PROPOSED (This is page 1 of a ____ page PP Amendment.)

17. APPROVED BY
Signature: James A. Norris
Title: JAMES A. NORRIS, MISSION DIRECTOR
Date Signed: MM 06 DD 01 YY 89

18. DATE DOCUMENT RECEIVED IN AID/W, OR FOR AID/W DOCUMENTS, DATE OF DISTRIBUTION
MM DD YY

AID 1330-4 (8-79)

GUARANTY AUTHORIZATION

Project No. 391-HG-001
(Authorization No. 391-HG-001)

PROVIDED FROM: Housing Guaranty Authority

FOR: Pakistan - Shelter Resource Mobilization Program

Pursuant to the Foreign Assistance Act of 1961, as amended (FAA), and the Delegations of Authority issued thereunder, and the specific delegation of Authority to the Mission Director, USAID/Pakistan, contained in 88 State 409241, I hereby authorize the issuance to eligible U.S. investors (Investors) acceptable to A.I.D. of guaranties pursuant to Section 222 of the FAA of not to exceed Twenty Five Million United States Dollars ($25,000,000) in face amount. The guaranties shall assure against losses (of not to exceed one hundred percent (100%) of loan investment and interest) with respect to loans, including any refinancing thereof, made to support the generation of domestic resources for shelter in Pakistan. These guaranteed loans shall be made to the Ministry of Finance of Pakistan or such other financial institution as A.I.D. may otherwise agree, (Borrower) to provide long-term financing for the development of a market-oriented shelter finance system in Pakistan and to support Government of Pakistan shelter programs which benefit the urban poor.

These guaranties shall be subject to the following terms and conditions:

1. Term of Guaranty: The loans and any refinancing thereof shall extend for a period of up to thirty (30) years from the date of disbursement and may include a grace period of up to ten (10) years on repayment of principal and may include such terms and conditions as shall be acceptable to A.I.D. The guaranties of the loans shall extend for a period beginning with the first disbursement of the loans and shall continue until such time as the Investor has been paid in full pursuant to the terms of the loans.

2. Interest Rate: The rate or rates of interest payable to the investor pursuant to the loans shall not exceed the allowable rate of interest prescribed pursuant to Section 223 (F) of the FAA and shall be consistent with rates of interest generally available for similar types of loans made in the long term U.S. capital markets.

3. Government of Pakistan Guaranty: Prior to disbursement of any loan amounts pursuant to this guaranty authorization, a written guaranty to indemnify A.I.D. against all losses arising by virtue of A.I.D.'s guaranties to the Investor or from non-payment of the guaranty fee shall be provided in a form satisfactory to A.I.D. by the Government of Pakistan or a financial instituton authorized by the Government of Pakistan to provide such a guaranty and approved by A.I.D.

4. Fee: The fee of the United States shall be payable in dollars and shall be one-half percent (1/2%) per annum of the outstanding guaranteed amount of the loans plus a fixed amount equal to one percent (1%) of the amount of the loans authorized or any part thereof, to be paid as A.I.D. may determine upon disbursement of the loans.

5. Other terms and conditions: The guaranties shall be subject to such other terms and conditions as A.I.D. may deem necessary.

James A. Norris
Director
USAID/Pakistan

June 1, 1984
Date

Clearances:

A/DD:PDavis PD
PRO:FWTate FW Tate
FM:ADPratt
RLA:TCarter
PDM:LMailloux
RHUDO/Asia:DPainter (draft)
GC/PRE:MKitay (draft)

# PROJECT AUTHORIZATION

Name of Country/Entity: PAKISTAN

Name of Project: Pakistan Shelter Resource Mobilization Program - Technical Assistance and Training

Project No. 391-0507

1. Pursuant to Section 531 of the Foreign Assistance Act of 1961, as amended, I hereby authorize the Pakistan Shelter Resource Mobilization Program - Technical Assistance and Training for the Islamic Republic of Pakistan involving planned obligations of not to exceed U.S. Dollars Five Million (U.S. $5,000,000) in grant funds over a five (5) year period from the date of authorization, subject to the availability of funds in accordance with the A.I.D. OYB/allotment process, to help in financing foreign exchange and local currency costs for the Project. The planned life of the project is five years from the date of initial obligation.

2. The Project will assist the Government of Pakistan to finance the technical assistance, including evaluation services and logistical support, and related training necessary to create the policy environment which will promote the establishment of market-oriented shelter finance institutions. The Project is an integral part of the Pakistan Shelter Mobilization Program (A.I.D. Project 391-HG-001).

3. The Project Agreement(s) which may be negotiated and executed by the officer(s) to whom such authority is delegated in accordance with A.I.D. regulations and Delegations of Authority shall be subject to the following essential terms and covenants and major conditions, together with such other terms and conditions as A.I.D. may deem appropriate.

Source and Origin of Goods, Services and Shipping

Goods and services financed by A.I.D. under this Project shall have their source and origin in the Cooperating Country or in the United States except as A.I.D. may otherwise agree in writing. Ocean shipping financed by A.I.D. under the Project shall, except as A.I.D. may otherwise agree in writing, be financed only on flag vessels of the United States.

Approved: James A. Norris
Director
USAID/Pakistan

Date: June 1, 1989

Clearances:

PDM: LMailloux:
PRO: FWTate:
FM: ADPratt:
DD(A):PDavis:

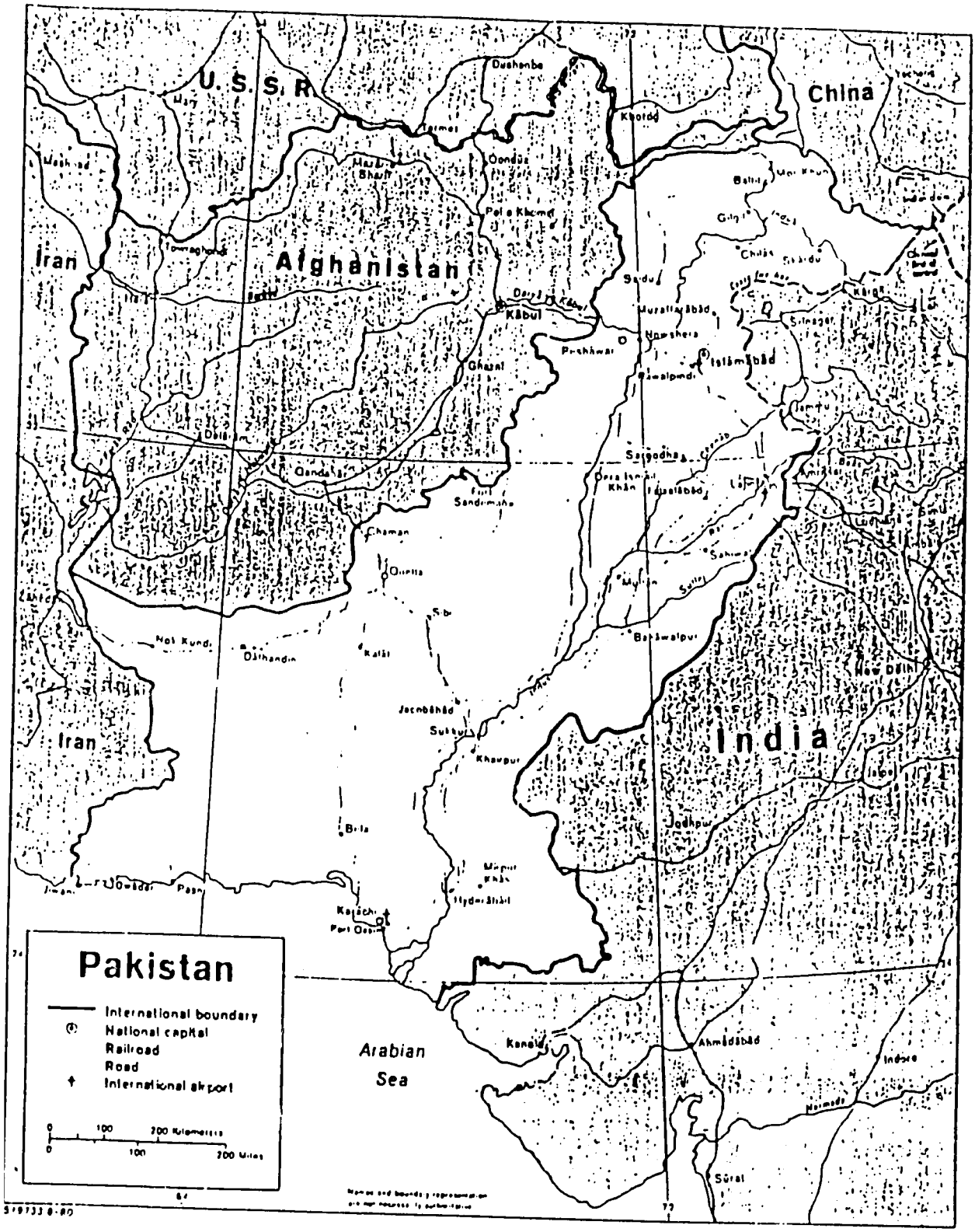
RLA:TBCarter:mh:5/24/89
2576R

## PRINCIPAL ACRONYMS

| | |
|---|---|
| AID | Agency for International Development |
| ADB | Asian Development Bank |
| ADP | Annual Development Program |
| ADBP | Agricultural Development Bank of Pakistan |
| ANE | A.I.D. Asia and Near East Bureau |
| CDSS | Country Development Strategy Statement |
| BEL | Bankers Equity Limited |
| DFI | Development Finance Institutions |
| FSAL | Financial Sector Adjustment Loan |
| FY | Fiscal Year |
| GOP | Government of Pakistan |
| HBFC | House Building Finance Corporation |
| HFC | Housing Finance Company |
| HG | Housing Guaranty |
| IA | Implementation Agreement |
| IBRD | International Bank for Reconstruction and Development (World Bank) |
| ICP | Investment Corporation of Pakistan |
| IDBP | Industrial Development Bank of Pakistan |
| IFC | International Finance Corporation |
| KDA | Karachi Development Authority |
| KMC | Karachi Metropolitan Corporation |
| MOF | Ministry of Finance |
| MDP | Ministry of Planning and Development |
| MOHW | Ministry of Housing and Works |
| NBFI | Non-Banking Financial Institutions |
| NCCC | National Credit Consultative Committee |
| NCB | Nationalized Commercial Banks |
| NDFC | National Development Finance Corporation |
| NIT | National Investment Trust |
| NHA | National Housing Authority |
| OECD | Organization for Economic Cooperation and Development |
| PAP | Policy Action Plan |
| PICIC | Pakistan Industrial Credit and Investment Corporation |
| PBC | Pakistan Banking Council |
| PID | Project Identification Document |
| PLS | Profit and Loss Sharing |
| PRE/H | AID Office of Housing and Urban Programs |
| RHUDO | AID Regional Housing and Urban Development Office for Asia |
| Rs | Rupees |
| SBP | State Bank of Pakistan |
| SDP | Special Development Program |
| TA | Technical Assistance |
| USAID | AID Mission to Pakistan |
| WAPDA | Water and Power Development Authority |

Exchange Rate, March 1989 - U.S. $1.00 = Rs. 19.28

Marla = 225 square feet (25 square yards)


U.S.S.R.
China
Iran
Afghanistan
India
Arabian Sea
Dushanbe
Khorog
Qondūz
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Kābul
Ghazni
Peshāwar
Rawalpindi
Islāmābād
Srinagar
Sargodha
Lahore
Amritsar
Chaman
Quetta
Kalāt
Bahāwalpur
New Delhi
Jacobābād
Sukkur
Khairpur
Jodhpur
Bela
Mirpur Khās
Hyderābād
Karāchi
Port Qasim
Gwādar
Kandla
Ahmadābād
Indore
Sūrat
Pakistan
International boundary
National capital
Railroad
Road
International airport
0 100 200 Kilometers
0 100 200 Miles

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<u>Project Design Team</u>

USAID/Pakistan: F. Wayne Tate, Abid Hussain
RHUDO/Asia: David Painter, Earl Kessler, Thomas Johnson
Abt Associates: John Miller, Sally Merrill, Harry Garnett
Consultant: Donald Gardner

# 1. SUMMARY AND RECOMMENDATIONS

## 1.1 Introduction and Program History

The Government of Pakistan (GOP) is about to undertake a major reform of the financial sector, the objectives of which are to introduce a market oriented financial system and to increase domestic resource mobilization. This restructuring is based upon studies undertaken jointly by the World Bank (IBRD) and the Government. A $150 million financial sector adjustment loan was negotiated with the IBRD in February 1989. General structural adjustment loans of $100 million and $800 million have been signed with the IBRD and the IMF respectively.

Over the past year, Asian Development Bank (ADB) consultants have prepared a report on the main public sector housing finance institution, the House Building Finance Corporation (HBFC). A program to implement the ADB recommendations has been incorporated as one of the conditions for the World Bank loan. Those recommendations were reviewed by HBFC and the Government, and by the Bank, ADB, and USAID in January 1989.

As part of this restructuring of the financial sector, USAID has taken responsibility for housing finance, in particular the introduction of private or joint sector, market oriented housing finance institutions. USAID prepared a report in May 1988 entitled "Policy and Institutional Study of Housing Finance in Pakistan" that identified problems and recommended reforms deemed necessary to stimulate housing finance activities in Pakistan.

The Government is also planning to introduce policies and programs to address its severe shelter sector problems. An expert group prepared a National Housing Policy in 1986. This policy is now being revised to reflect the Pakistan People's Party manifesto's housing sector proposals. The World Bank prepared a Shelter Sector Review in June 1988 and the ADB produced a report on Preparatory Technical Assistance for Low Income Housing in October 1988. The Government has indicated its agreement that USAID focus on supporting reform of the housing finance component of the financial and shelter sectors, as presented in the USAID Concept Paper that the Government approved.

The reform of the financial and housing sectors forms the basis for the proposed Housing Guaranty Program.

## 1.2 Summary of Problems to be Addressed

The proposed HG Program will address problems in the financial and shelter sectors. These problems are intersectoral. There is a need to mobilize resources from households and institutions to support the establishment of private and joint sector housing finance companies (HFCs). These HFCs will assist in developing a market oriented financial system and in expanding the supply of shelter to a rapidly growing population as well as make up for past housing deficits.

Pakistan faces a serious resource mobilization problem. The private savings rate is exceptionally low at a time when the need for domestic resources is growing rapidly and the Government's budgetary capacity to fund economic development is overstretched.

To encourage better domestic resource mobilization, as well as improve allocative mechanisms, the Government is committed to the development of market oriented financial institutions. A market oriented system would mobilize and enhance savings by providing savers with financial assets that are more convenient to hold, and less risky and more liquid than the underlying real assets.

Housing finance has a very important role to play in such a financial system. Housing is an important investment good and a significant source of savings. Housing typically accounts for between one quarter and one half of the capital stock in most developing countries.

However, housing finance has not performed well in Pakistan. Housing investment only contributes 2.7 per cent to GNP, well below the average for low income countries, and the proportion has been falling over the past 30 years. According to official statistics housing as a proportion of gross capital formation is only 9 per cent, less than half the figure for comparable developing countries. There is very little savings mobilization by formal sector financial institutions directly from households.

USAID's Housing Finance Study identified four principal constraints to the achievement of a market oriented housing finance system:

1. There is a lack of confidence on the part of potential investors in housing finance institutions. Lengthy foreclosure procedures have made loan collection difficult for those now in the market, HBFC and the commercial banks. The private sector also fears competition from subsidized lending associated with Government programs.

2. There is a lack of public confidence in private sector financial institutions. Many rich and poor people have lost their savings recently to ineffectively regulated private finance companies. Liquidation and regulatory provisions for licensing and supervising market oriented housing finance institutions do not currently exist.

3. HBFC's past and current operations serve to discourage private investors from establishing competing finance companies. Even though HBFC has made almost all its loans to middle and upper income groups, not its low income target groups, loan delinquencies have been very high. It appears that HBFC would be competing at the margin for some of the same clientele as the more market oriented institutions. In addition, at the moment HBFC has access to Government credit which permits it to offer below market loan terms.

4. There is virtually no short term construction finance. This means that developers and construction companies have to depend on their own savings, advances from clients or informal sector borrowing at very high rates of interest for working capital.

In addition a number of other macroeconomic and credit-related issues emerged during the preparation of this project paper.

5. The availablity of domestic credit to the private sector has been low in comparison with other similar developing countries. Private sector access to credit has been squeezed out by the growing budget deficit and the Government's need to borrow locally.

6. The private sector has played almost no role in financial intermediation, since private banking is prohibited. Private sector leasing companies have only recently been established and private investment companies are only now being approved.

7. Under the system of directed credit, housing has always had a low priority. The supply of credit has not kept pace with demand. However, the Government has not sought credit for the sector elsewhere. As stated above, there are no licensing provisions for market oriented HFCs.

This environment has meant that there is very little financial intermediation in housing finance. According to the ADB household survey, almost all the resources for housing for the majority of the population come from personal savings, the liquidation of assets, and remittances from abroad. Since these funds circulate outside the formal financial sector, they cannot contribute to its development. The balance of the funds applied to housing come from Government budgetary allocations and directed credit. The low level of financial intermediation also means that the "informal" funds cannot be applied to the solution of Pakistan's shelter problems as effectively as they might be if they could be deposited with viable, market oriented housing finance institutions. Such institutions would also prove attractive to long term institutional funds, which would in turn add further to the integration of a liberalized financial sector.

## 1.3 Summary of Program Description

The goal of the Shelter Resource Mobilization Program is to develop the role of housing finance in Pakistan's Financial Sector through the mobilization and application of domestic resources to the shelter needs of Pakistan, especially low-income families.

In order to pursue this goal, one purpose of the program is to create the policy environment which will promote the establishment of market-oriented shelter finance institutions. The Program will establish a process in which policy issues will be studied and actions will be proposed that will lead to significant reform of the housing finance system. The Program will permit the State Bank of Pakistan (SBP) to gradually reduce subsidized credit allocations to HBFC for middle and upper income shelter loans. The Program will assist the GOP in setting up a shelter finance delivery system with clearly defined public and private sector roles, procedures, and support mechanisms.

A related purpose is to initially support, through local currency equivalent amounts, the GOP shelter programs that are affordable to low

income families. Qualified programs would include land and infrastructure development as well as home and community upgrading programs that promote a continuous supply of shelter for low-income families during the period of policy change.

To achieve the program purposes, the GOP will set up the mechanism to address the necessary reforms within the housing finance sector that will promote the establishment of viable private and joint sector housing finance institutions:

1. The GOP will set up a Working Group on Housing Finance, chaired by the Joint Secretary for Internal Finance in the Ministry of Finance, to supervise the introduction of the policy reforms. The Working Group will, together with A.I.D., prepare a Policy Action Plan that will lay out the steps to implement the policy agenda.

2. The Working Group will identify agencies responsible for the formulation and implementation of the housing finance regulatory framework. At some stage it is likely that the SBP will become the regulatory agency, in line with its responsibility to supervise all financial institutions, as agreed under the World Bank's Financial Sector Adjustment Loan (FSAL).

3. Regulations and supervisory procedures will be drawn up that will facilitate the creation and operation of market oriented housing finance institutions by establishing public confidence in such institutions.

4. A body will be identified that will promote and facilitate the creation of housing finance institutions by assisting them to meet regulatory requirements and by acting as an advocate on their behalf to the various government agencies concerned.

5. The role of the public owned HBFC will be clarified. If it is to become a market oriented housing finance institution (as proposed under the FSAL), its funding and lending practices will have to be brought in line with those applicable to the market oriented housing finance companies.

6. The Government will make every effort to establish the first market oriented housing finance company within a matter of months. One such proposal, for a joint sector housing finance company, has already been prepared.

7. The Government will prepare a shelter sector policy statement that clearly segments the housing market between the low income households that will qualify for subsidized programs and those households that will be expected to build and buy housing without any subsidies. The Government is currently redrafting its National Housing Policy.

Each Authorization of the proposed five-year $100 million HG Loan will be associated with progress in studying key policy issues and in implementing proposed policy reforms. Progress will be assessed as part of joint Government and A.I.D. policy reviews.

To assist the Government in establishing a market oriented housing finance system, the HG will be supported by a $5.0 million technical assistance and training grant. This will be used to manage the policy dialogue process; provide the technical and policy analysis needed to advance the policy reform agenda; evaluate progress in the policy dialogue and the impact of the policy changes on low income families; provide training for the public sector staff responsible for the regulatory framework and the promotional activity; and provide training for the staff of the newly established housing finance companies.

## 1.4 Issues Identified During PID Review

The Project Review Committee of the ANE Bureau reviewed the Shelter Resource Mobilization Program PID on November 21, 1988. The PID was approved and the AA/ANE delegated authority to the Mission to authorize the Program, subject to the conditions and guidance contained in the PID review cable (STATE 409241; see Annex 1). The issues raised in that cable included the need: (1) to be more explicit in the Policy Action Plan as to the actual GOP policy and institutional reforms which are expected as a result of this Program, and to indicate GOP agreement, in principal, to the Policy Agenda (see 2.3.2.2. and Annex 13); (2) to present in the PP the first year's policy objectives (see Annex 13); (3) to explain the $100 million funding level in the context of meaningful and irreversible sector policy change (see 2.2.4); (4) to show key indicators that would demonstrate progress toward Program objectives as part of a Program evaluation and monitoring system (see Annex 13); (5) to show GOP intent to continue support of low income housing program activities, especially in areas where the private sector will not meet the need (see 2.2.2); (6) to present how the Mission will determine that low income families can be reached by GOP programs to which HG resources will be attributed (see 2.4); (7) to reflect the efforts to ensure that environmental considerations are being adequately addressed in the implementation of shelter sector programs (see 3.3); and, (8) to present how donor activities can be coordinated and the respective programs serve to strengthen the housing sector and overall Program goals (see 2.2.6).

## 1.5 Recommendations

The Program design team recommends that the Mission Director: (1) approve a $100 million Housing Guaranty Loan Program to support GOP establishment of the enabling and policy environment for a market-oriented shelter finance system; and, (2) authorize the Guaranty of a $25 million loan to the Ministry of Finance in FY89. Subsequent authorizations of the remaining $75 million will be contingent upon evidence of progress made on items included in the Program Policy Action Plan, and on the development of an updated Policy Agenda.

It is also recommended that the Mission Director authorize a technical assistance and training grant in support of the Shelter Resource Mobilization Program in an amount not to exceed $5.0 million, $2.0 million of which will be obligated in FY89. The PACD will be five years from the date of the signing of the Program Grant Agreement.

# 2. PROGRAM RATIONALE AND DESCRIPTION

## 2.1 The Housing Finance Situation in Pakistan

### 2.1.1 The Financial Sector

Pakistan's financial sector is a centrally controlled system of directed credit, dominated by government ownership of the commercial banks and many of the specialized development institutions. At its apex is the State Bank of Pakistan (SBP) which, along with considerable direct involvement of the Ministry of Finance, regulates the financial institutions. Also, as chair of the National Credit Consultative Committee (NCCC), the body charged with making recommendations on monetary and credit expansion and the sectoral distribution of credit, the SBP is instrumental in the division of credit among the government; public enterprises, and the private sector.

Deposit taking institutions are the most important type of financial organization in the financial sector and hold more than 50 percent of the system's total assets (see Figure 1). The Nationalized Commercial Banks (NCBs), especially the three largest (Habib, National, and United) have the great majority of the business. Together, the NCBs account for over 90 percent of banking system deposits and 85 percent of the advances. Seventeen foreign commercial banks also operate; private domestic commercial banking has been prohibited since banks were nationalized in 1974.

Government-owned specialized banks exist for financing agriculture, industry, and cooperatives. Although these banks are treated as deposit-taking institutions, they rely on central bank support for the majority of their funding. These and a number of Development Finance Institutions (DFIs) are classified as non-bank financial intermediaries (NBFIs). The most important of these is the National Development Finance Corporation (NDFC), which is wholly government owned, and lends to public and private manufacturing enterprises; HBFC, which specializes in financing for home purchase and is funded almost entirely from the SBP; and PICIC, which has majority private ownership and provides long-term foreign currency financing to the private manufacturing sector. National Investment Trust (NIT) and Investment Corporation of Pakistan (ICP) are collective investment institutions, which include open-end and closed-end mutual funds. Finally, there are two stock markets (the most important is in Karachi, the other in Lahore). Although market capitalization has increased in recent years, it is still low by comparison with other developing countries in Asia.

Characteristics of the banking and financial sector which are important for understanding the formulation of housing finance policy include: (1) the extremely limited role of private sector institutions; (2) the limited competitive environment; (3) inadequacies in licensing and supervision; and (4) low rates of savings and investment. Stringent legal limits have restricted entry and expansion of private sector institutions; only in the last few years have private leasing companies been established, and, just recently, legislation was enacted for private investment companies.

**Figure 1**

Institutional Structure and Total Assets in Pakistan's Financial Sector

| Institution | Assets 1986 Rs. MN | % of Total Assets |
|---|---|---|
| SBP (State Bank of Pakistan) | 141,137 | 30.7% |
| Commercial Banks | 243,323 | 52.8% |
| Specialized Banks | 27,658 | 6.0% |
| ADBP (Agricultural Development Bank of Pakistan) | 16,193 | |
| IDBP (Industrial Development Bank of Pakistan) | 6,639 | |
| FBC (Federal Bank for Cooperatives) | 1,840 | |
| Cooperative Banks | 2,986 | |
| Development Finance Institutions | 31,482 | 6.8% |
| PICIC (Pakistan Industrial Credit and Investment Corporation) | 6,596 | |
| NDFC (National Development Finance Corporation) | 12,849 | |
| HBFC (House Building Finance Corporation of Pakistan) | 8,900 | |
| Pak-Kuwait | 550 | |
| Pak-Libya | 1,460 | |
| Saudi-Pak | 722 | |
| Other | 405 | |
| SLIC (State Life Insurance Corporation) | 8,000 | 1.7% |
| Collective Investment Institutions | 8,000 | 1.9% |
| ICP (Investment Corporation of Pakistan) | 2,492 | |
| NIT (National Investment Trust) | 3,704 | |
| BEL (Bankers Equity Limited) | 2,714 | |
| TOTAL | 460,510 | 100.0% |

Source: Pakistan Financial Sector Review, Volume II, December 11, 1987, The World Bank.

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This situation has concentrated market share in the NCBs and discouraged competitive and efficient operation of the financial system. Also, inadequacies in licensing and regulation contributed to two episodes of failure and scandals in private finance companies. Finally, savings and investment rates (now around 9 percent and 16 percent, respectively), are quite low. Below-market interest rate policies, designed to encourage investment in sectors such as industry and agriculture, may, in fact, have depressed savings propensities. Other reasons include weak capital markets and flows of black money and remittances outside the formal intermediation system.

Despite its problems, however, the financial sector displays characteristics which lend a more sanguine view to establishment of new institutions. The sector is relatively large and dynamic compared to other countries and the banking sector is reasonably deep. The DFIs, in particular, have developed innovative new products; these are the institutions most likely to be involved in joint sector HFCs.1/ The rapid growth of deposits in the GOP's National Savings Schemes suggest that deposits can be quickly mobilized at favorable rates. Finally, Islamization of the banking system has provided incentives for innovation as well as more market-oriented rates.

### 2.1.2 The Housing Finance Sector

Like other elements of the financial sector, housing finance is dominated by government rather than private credit. Furthermore, formal sector sources of finance, taken together, have only been able to supply about 20 percent of the needed credit. Thus, the majority of households must rely on informal borrowing and personal asset liquidation.

The House Building Finance Corporation (HBFC) is the dominant government institution, supplying about 80 percent of total formal housing credit. HBFC was established in 1952; with its share capital fully subscribed by the GOP and SBP. HBFC receives almost all its resources from SBP and has not attempted to mobilize other resources. In 1987-88 HBFC received Rs.1,450 million from the SBP and financed about 20,000 units.

HBFC domination of housing finance is costly and inefficient and, moreover, represents a missed opportunity to contribute to financial deepening and stability. HBFC lends through the Profit and Loss system at rates ranging from 6-3/4 to 15 percent. The average return is well below what it would have to pay for funds in the market.

1/ As discussed in Section 3.1.2, proposals for housing finance companies have been developed by PICIC and NIT.

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In addition, HBFC has a large volume of delinquent loans on which it "accrues" interest in its income statement and balance sheet. Thus, the profits on which it bases its payments to SBP are illusory; the real return to SBP is only about 3 to 4 percent. Such subsidization of interest rates is highly inefficient; it produces distortions in the money market, contributes to poor loan recovery, and most importantly, inhibits private sector involvement. The private sector has no reason to enter a sector dominated by an institution with nation-wide coverage which is lending at negative real rates of interest. Finally, failure to mobilize domestic resources constrains overall housing investment, which is only 9 to 10 percent of fixed capital formation in Pakistan compared with 18 to 25 percent more typically.

Other formal sector institutions supplying housing credit include the NCBs, government and SBP loans to employees, and housing cooperatives. Funds allocated by NCCC in 1987-88 to the NCBs amounted to only Rs.190 million, which is insignificant compared to total NCB lending. (As an example, HABIB received Rs.69.5 million, which is about a tenth of one percent of its advances of Rs.50 billion). NCBs tend to lend housing credit to bank employees and customers; rates appear to be somewhat less than market. Government loans to employees are estimated to be Rs.300 million, according to the 1987/89 NCCC credit plan. Loans are interest free to non-gazetted civil servants, and close to market for higher level officers. Finally, the cooperatives have primarily assisted in financing sales of land and serviced lots.1/

## 2.2 Program Strategies and Objectives

### 2.2.1 Government of Pakistan Resource Mobilization Policies

USAID's goal of establishing a framework to foster market-oriented housing finance institutions comes at an extremely propitious time in the evolution of GOP financial sector policies.

As in many other developing economies, Pakistan has relied on direct credit controls to enhance monetary and credit policy in the face of large public sector fiscal deficits and relatively underdeveloped money and capital markets. However, the price of stringent credit controls can be inefficient allocation of credit and discouragement of financial sector mobilization of resources. The GOP has decided, therefore, to amplify its strategy of liberalization and reform of the financial sector. Over the last ten years the GOP has undertaken efforts to deregulate the economy. These included liberalization efforts in industrial policy, public investment programs, tariffs, and exchange rate management. Liberalization of the financial sector began with Islamization of the banking system and the gradual freeing-up of interest rates.

1/ ADB Consultant Report Paper 2

The Pakistan Peoples' Party Manifesto now proposes "institutional and policy reforms to remove shortcomings in the structure of the domestic financial system." The PPP plans to increase financial intermediation and create an environment that would stimulate innovations in financial institutions. The Manifesto also indicates that the regulatory framework would be strengthened to increase public confidence.

To this end, the GOP, in conjunction with the World Bank and the International Monetary Fund, has developed a series of medium and long-term reforms that will substantially alter the operation of financial and monetary policies in Pakistan. The overall goal of the structural adjustment program is to deepen financial markets and expand private investment and savings. Also, it should be stressed that development of a market-oriented system of housing finance is one of the most effective ways of contributing to financial deepening (see Annex 10). The financial system will undergo a major shift toward market-oriented operations through gradual dismantling of the system of directed credit; strengthening of capital markets; increasing the competitiveness of the banking system; and strengthening and consolidating in SBP supervisory and debt recovery procedures.1/ These reforms will structure the framework in which housing finance companies operate and compete, and encourage the entrance of market-oriented institutions.

These reforms extend far beyond previous GOP expressions of policy regarding financial sector liberalization for the purpose of mobilizing resources. For example, while previous National Plans encouraged private sector participation through creation of specialized, market-oriented savings institutions, GOP policies actually employed remained in conflict with this objective.

### 2.2.2 Government of Pakistan Shelter Policies

The new Government of the Pakistan Peoples' Party (PPP) has stated that shelter and financial sectors reforms are high priorities.

The Pakistan Peoples' Party Manifesto recognizes that a large proportion of the population has inadequate shelter. The Government aims to ensure that half a million homes are constructed each year. Better incentives will be provided for the private sector to make a major contribution. The Manifesto also admits that the savings rate is one of the lowest in Asia and that it cannot support the development program without resorting to external borrowing.

The new Government is now designing measures to implement its shelter objectives. A new housing policy document is now under review. It has been based upon the 1986 Draft National Housing Policy that was prepared by a committee of experts assembled by the Ministry of Housing and Works.

1/ World Bank FSAL Report and Recommendation.
See Section 3.1.3 and Annex 15.

Ongoing programs were designed by the previous Government. Many are likely to continue in similar form. Each is outlined below.

The previous Government had announced a Shelter for the Shelterless Program. In 1987-88, the first phase of the program, 75,000 nucleus houses for the very poor were to be constructed using Pakistan's religious welfare fund, or Zakat funds. Three sub-programs were to be financed from existing national and provincial budgets: 20,000 houses costing Rs 25,000 will be built in rural areas and allocated to shelterless plot owners, the loans to be repaid over 20 years without interest; 20,000 interest free rural home improvements loans of Rs 20,000 each were to be disbursed; and 15,000 interest free new construction loans of Rs 10,000 for urban households were to be made, the balance being provided by the beneficiary. Under a separate subprogram, HBFC is to provide 20,000 loans of Rs 10,000 for urban house construction, with recovery according to their normal PLS formula.

The previous Government also outlined a program to construct one million homes. This program, which would cost the Government Rs 5 billion, planned to provide finance for 300,000 houses over the period 1989-91. The Rs 15,000 loans would cover construction and upgrading. Loans would be recovered over 23 years with a nominal profit of 6 per cent. Disbursements and collections would be through a commercial bank.

The Government is also implementing the 1985 Five Points Program, for which Rs 23 billion had been allocated for FY 1987-88. This program includes upgrading katchi-abadis, providing three marla plots for the urban poor, and seven marla plots for the rural poor.

The World Bank's Shelter Sector Review identifies three issues raised by the last Government's programs. Many of the same issues were identified earlier by the team that prepared the 1986 National Housing Policy.

First, there are serious constraints to housing supply. The process of normalizing tenure for the katchi-abadi dwellers has proved to be more difficult than expected due to institutional rigidities. In addition, it has proved difficult to supply serviced land at the rate required. The plot allocation system does not in practice allocate plots to those in need. There is also an inadequate supply of serviced residential land in rural areas.

Second, the institutional capacity to administer these programs has proved to be inadequate. Related to this is the high risk of political interference in the program.

Finally, the Bank believes that the program is too costly and involves excessive and often unnecessary subsidies. This is a particularly serious problem at a time when the Government has undertaken to reduce the budget deficit as a proportion of GDP. The whole program has to be put onto a more self-financing basis.

The 1986 National Housing Policy team linked many of these issues to the fact that there was "no mechanism to attract personal savings for investment in housing". The report pointed out that the land acquisition process was unfair to landlords and procedurally difficult. Since the public was unable to capture any of the increase in land values, the potential for financing further land development was reduced. Rent controls were identified as a constraint to private sector rental construction.

The ADB, in its preparatory assistance, has concluded that the "evident lack of improvement in housing conditions over the last 27 years, have to do more with the policy and institutional framework for the sector than with the programs themselves". This Shelter Resource Mobilization Program directly supports the GOP's ambitious shelter and financial sector goals by promoting the introduction of a policy and institutional framework that will mobilize the resources necessary for housing finance.

### 2.2.3 Program Goal and Purpose

The goal of the Shelter Resource Mobilization Program is to develop the role of housing finance in Pakistan's Financial Sector through the mobilization and application of domestic resources to the shelter needs of Pakistan, especially low-income families.

In order to pursue this goal, one purpose of the program is to create the policy environment which will promote the establishment of market-oriented shelter finance institutions. The Program will establish a process in which policy issues will be studied and actions will be proposed that will lead to significant reform of the housing finance system. The Program will permit the SBP to gradually reduce subsidized credit allocations to HBFC for middle and upper income shelter loans. The Program will assist the GOP in setting up a shelter finance delivery system with clearly defined public and private sector roles, procedures, and support mechanisms.

A related purpose is to initially support, through local currency equivalent amounts, the GOP shelter programs that are affordable to low income families. Qualified programs would include land and infrastructure development as well as home and community upgrading programs that promote a continuous supply of shelter for low-income families during the period of policy change (see Logical Framework, Annex 4).

### 2.2.4 Program Strategies and Objectives

To achieve the Program's goals and purpose, A.I.D. will assist the GOP set up the mechanism to address and to adopt necessary reforms within the overall financial sector. These reforms will support domestic resource mobilization for shelter and put mortgage and improvement lending on a market-oriented basis. Figure 2 presents the Program's objectives as they relate to identified constraints and Program actions. Many of these constraints are reflected in recent articles in the press (see Annex 5).

FIGURE 2

Program Objectives, Constraints, and Actions

| Constraints | Objectives | Actions |
|---|---|---|
| 1. Lack of confidence in housing finance institutions | Develop policies for market-oriented housing within the context of both structural reform in financial and capital markets and overall shelter policies | Finalize responsibility for development of market oriented housing finance with the Joint Secretary for Internal Finance in the Ministry of Finance<br>Establish a Housing Finance Working Group |
| o Inadequate foreclosure procedures | Develop instruments and procedures to facilitate the growth of housing finance and to remove barriers and disincentives to market growth | Review current foreclosure procedures and establish an appropriate subcommittee to recommend revisions |
| o Lack of licensing and supervisory procedures specific to housing finance | Establish regulatory and supervisory provisions appropriate to market based housing finance institutions | Review the merits of establishing special provisions for licensing and supervision for housing finance institutions |
| 2. Lack of confidence in private sector institutions | Develop policies for market-oriented housing finance within the context of both structural reform in financial and capital markets and overall shelter policies | Establish roles for NCBs, DFIs, and HBFC consistent with formulation of market oriented housing finance institutions |
| o Ineffective regulation and supervision of private finance companies | Develop a legal framework appropriate to the creation of private and joint sector housing finance companies | Coordinate the process for review of licensing and supervision with GOP efforts for reform and consolidation of efforts under SBP |
| o Economy-wide debt recovery problems | | Coordinate recommended actions for foreclosure and arears with GOP reforms in all sectors |
| 3. Inadequacies in HBFC operations and non-performing loans | Rationalize the GOP role in financing shelter | Focus GOP subsidies to low income families through NHA programs |
| o Competition from HBFC's lending at subsidized inherent rates | Develop instruments and procedures to facilitate the growth of housing finance and to remove barriers and disincentives to market growth | Coordinate efforts to recapitalize HBFC and restructure the institution and its housing finance policies |
| o Substantial delinquencies | | Coordinate foreclosure and arrears recommendation with GOP measures in all sectors |
| 4. Lack of short-term construction finance | Foster the development of market-oriented construction finance | Assess alternative arrangements for construction finance by the NFCs, NCBs, and DFIs<br>Consider the need for special supervisory provisions for construction finance |
| 5. Lack of experience by the private sector | Develop policies for market-oriented housing finance within the context of both structural reform in financial and capital markets and overall shelter policies | Promote the concept and purpose of market oriented housing finance through the Housing Finance Working Group |
| o Lack of private sector experience in banking and other financial institutions | Develop a legal framework appropriate to the creation of private and joint sector housing finance companies | Coordinate housing finance policy development with overall GOP reform and liberalization of the private sector |
| o Lack of private sector experience in investment | Develop instruments and procedures to facilitate the growth of housing finance and to remove barriers and disincentives to market growth | Monitor the status of reform and consolidation of financial sector licensing, supervision and regulation |
| o Lack of GOP mobilization of private sector resources for housing | | Review the desirability of safeguards to increase public confidence; instruments to facilitate long-term lending; mobilization of long-term funds; review of rent control, land titling. |



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The strategy will support GOP development of a more efficient operation of financial markets in general by addressing the role of shelter finance in the financial sector, the system through which private capital will be brought to finance shelter i. particular; and the targeting of GOP subsidies for shelter for the poor. A Program Concept Paper was presented to the GOP for its comments, and the GOP has reiterated its support for involving the private sector in shelter finance.

A.I.D.'s strategy is to make $100 million available through the HG loan program to support GOP policy changes that will create the enabling and regulatory framework for a market-oriented shelter finance system and thereby deepen Pakistan's financial market. The $100 million level is deemed necessary over the five year life of the Program to complement the level of resources other donors are bringing to the financial and shelter sectors and to effect the complex medium and long-term changes in policy being proposed. The World Bank will be providing $150 million to the financial sector and the ADB will be providing $132 million to the shelter sector through the HBFC over the next five years. In addition, the $100 million HG program represents unrestricted foreign exchange that the GOP could use as required to manage its balance of payments problems. USAID's interest is to provide support for the balance of payments in connection with a policy dialogue with the GOP in areas which include deregulation, improved climate for private investment, and reform of financial sector policies.

By creating the regulatory framework for a market oriented housing finance system the strategy will also address the issues of public confidence crucial to domestic resource mobilization and risk mitigation necessary for private capital to be made available for long-term mortgage lending. The strategy will promote the creation of an inter-institutional working group under the leadership of the Ministry of Finance to coordinate efforts between the financial and shelter sectors and oversee the analysis and development of the proposed market-oriented housing finance system.

By offering technical assistance of $5 million over the five year life of the Program, funding will be available to the Working Group to promote the formation of private and joint sector housing finance companies. TA funds will also be used to carry out specific studies of issues important to the development and functioning of the shelter finance system. Such studies would include the special regulations shelter finance companies may require because of the nature and terms of their lending and modification to the existing foreclosure laws and practices. Grant funding will also be available for management training for regulatory and supervisory staff as well as for primary lenders.

A.I.D. will develop jointly with the GOP a Policy Action Plan that will confirm the operation of an interim process and the development of a long-term process to license, regulate and supervise private and joint sector shelter finance companies. By confirming the extent to which the current laws and regulations can accommodate current requests for approval to form and operate a shelter finance company, this interim process will license only those companies that comply to MOF criteria. The interim process will thereby improve the image and operation of new housing finance companies, while the long-term policy changes are developing.

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The Policy Action Plan for the first tranche of HG funds will be negotiated with the GOP and confirm, at least, the operation of an interim process to regulate the housing finance system. Progress against this Policy Action Plan will be evaluated on a yearly basis, and a new plan negotiated before the next tranche of HG funds is authorized. This process will be repeated until $100 million in guaranties have been authorized. In the event that the GOP policy actions do not meet agreed targets, the Mission retains the option to reduce, postpone, or cease funding HG authorizations.

2.2.5 Relationship to the CDSS and Current Mission Action Plan

The FY 88-93 CDSS identifies ten development problems that USAID programs should address, three of which are related to the policy reforms that will be promoted as part of the HG Program. They are balance of payments pressure, inadequate domestic resource mobilization, and the need for quality improvements in key institutions. This program will provide balance of payments support, promote the development of private and joint sector finance institutions that will mobilize domestic resources, and provide technical assistance and training to key financial sector institutions.

The CDSS identifies four challenges, each of which applies to the proposed program: reform of the policy environment, rehabilitation and expansion of physical infrastructure, development of human capital, and improved institutional performance.

The CDSS singles out domestic resource mobilization as the "most serious problem" and the liberalization of the financial sector as the most important objective. The very goal of the HG Program is to encourage the mobilization of domestic resources.

The February 1989 Action Plan points out that USAID's own programs complement many of the main themes that the Pakistan People's Party emphasized in the fall election campaign. The Action Plan refers to the HG as a new initiative under the 1988-93 program. The Action Plan further endorses the HG as follows: "If GOP accepts the policy packages that would come with the HG program, a private industry providing financing for house construction and mortgages should begin to emerge."

The Action Plan identifies several structural problems: the budget deficit, low national savings, trade imbalances, and monetary controls. The HG Program has important contributions to make to each of these. The development of private or joint sector housing finance institutions will reduce the need for government to subsidize housing. Informal savings will find a profitable outlet in the housing finance institutions. The HG disbursements will provide foreign exchange. And finally, the financial reforms will in general improve monetary controls within the context of a market-oriented rather than directed system of credit allocation.

### 2.2.6 Relationship to Other Donor Programs

#### 2.2.6.1 Introduction

The World Bank and the Asian Development Bank are undertaking significant programs with the GOP in the finance and shelter sectors. As the PID cable rightfully suggests, the effectiveness of this HG Program depends on the continuing collaboration among the three donors on a consistent approach to both sectors vital to Pakistan's development programs. RHUDO and Mission staff have established the necessary working relationship with ADB and IBRD staff. Importantly, the timing of the three donors' discussions with GOP institutions has made it possible to present a consistent and integrated approach to a policy agenda. The $100 million HG loan in combination with the IBRD $150 million FSAL loan, the approximately $100 million IBRD Shelter/Urban Loan, and the $132 million ADB Housing Loan serves to maximize each donor's influence on GOP policies. The most recent donor discussions confirmed that A.I.D.'s shelter finance policy interests are supported by the FSAL and the ADB loans, and that A.I.D.'s local currency program is supported by the IBRD Shelter/Urban project activities dealing with land as a constraint to low income housing provision, as well as the ADB's housing project.

#### 2.2.6.2 World Bank

The World Bank is preparing two loans that are related to the HG Program: the Financial Sector Adjustment Loan (FSAL) and the Housing Sector Loan.

The objectives of the FSAL are to improve credit allocation and economic growth, increase resource mobilization, reduce disintermediation, support capital market development and reduce information and negotiation costs in financial markets through measures to deregulate financial markets.

The program is supported by an IMF/IBRD Structural Adjustment Facility and an IMF Standby Agreement, for a total of about $900 million. The IMF's December 1988 "Staff Report" on Pakistan and its paper "Pakistan: Recent Developments" endorse the objectives of the FSAL.

The negotiations for the World Bank Financial Sector Loan took place in February 1989. The following policy changes and actions that will have a direct impact on housing finance were agreed upon.

HBFC loans are to be accessible by all income groups. HBFC is to introduce market based lending rates. In order to become financially viable, HBFC is to introduce commercial procedures, market oriented lending rates, and raise its own resources. A corporate action plan is to be prepared by FY 90; due account should be taken of the ADB recommendations. Before the second tranche of the loan is advanced, there is to be a portfolio audit.

A number of general conditions will also have an important impact on the housing finance sector. The capital-liability ratio of the commercial banks is to be 3 per cent by the end of 1991. Prior to the presentation of the loan to the Board (of the World Bank), the Government will submit a copy of draft legal documents to provide SBP with authority to supervise Modarabas, leasing companies and investment banks. In addition, by that time at least one investment company shall have received all the necessary authorization, licenses, and permits.

The Government's letter to the President of the World Bank agrees to these conditions and to other recommendations of the Financial Sector Review. The Government agrees that credit should be allocated in response to market determined rates of return through a system of intermediation. The Government plans to promote healthy financial institutions providing a wide menu of credit and financial services in a competitive manner. It is stated to be Government policy to abolish all sectoral credit targets. An early step in the process will be to phase out all concessionary rates of return. By 1990 the rates on all concessionary credit programs are to exceed the rate of inflation; the letter specifically includes housing in this. Financial institutions are to be free to negotiate fees and rates for syndicated advances. The incidence of directed credit is to be reduced as financial institutions gain experience. SBP is to start to supervise the financial institutions by July 1989. It is anticipated that the specialized financial institutions will eventually graduate into full scale banks, and be regulated as such by SBP.

The World Bank is also preparing a Housing/Urban Sector Loan. The Bank undertook a Shelter Sector Review in 1988. The Bank proposed a four part program:

1. A national community improvement program covering 5.5 million katchi abadi dwellers in five years. This would include home improvement loans.

2. A national land and shelter development program, including materials and improvements loans.

3. A rural land and shelter program.

4. Reform of the housing finance sector.

2.2.6.3 <u>Asian Development Bank</u>

The ADB also plans to be active in both the housing and financial sectors. Project preparatory technical assistance in low income housing was undertaken in 1988. A project was proposed that will help to provide essential inputs for house construction through self help and mutual help by the poor; develop community based institutions necessary to improve housing for the poor; and strengthen the policy and institutional framework for the sector. The program's four components are: house construction and improvement loans; small plot development; extension services, research and information; and training and technical assistance. The 5-year program will cost $319 million, towards which ADB will provide a loan for $132 million.

This program includes Rs 25 million of technical assistance to HBFC, to be undertaken in 1990 and 1991.

ADB consultants have just completed a major study of HBFC. The consultants recommended that HBFC become a commercially viable mortgage bank, paying particular attention to the lower-income end of the commercial market. A three-year $840,000 program of technical assistance in management, training, computing, and accounting is proposed.

## 2.3 Program Description

### 2.3.1 Overview of the Program

The Shelter Resource Mobilization program will consist of two closely related components. The first component is the HG funded capital assistance. The second component is the grant funded technical assistance and training.

Under the HG, the GOP will borrow up to $100 million from the U.S. capital market under an A.I.D. guaranty. This private U.S. capital can be used by the GOP as unrestricted foreign exchange. In consideration for the A.I.D. loan guaranty, the GOP with A.I.D. would develop and implement a package of policy reforms that are consistent with the financial and shelter sector policies now being developed. The Program will actively promote the participation of the private sector both as investors and as depositors that will draw resources from the large pool of cash available in the informal sector. The Program will create the policy and regulatory environment which would expand the role of shelter finance in the financial sector and encourage the development of a market-oriented shelter finance system.

A.I.D. will pursue the jointly developed Program policy agenda with the GOP by negotiating a Policy Action Plan acceptable to both parties for the first tranche of HG funds. The A.I.D. guaranteed dollar loans would ultimately lead to an increase in domestic resources mobilized for shelter through private and joint sector housing finance companies this program will promote.

In view of the necessity to continue to provide resources to the shelter sector while policy changes are carried out, the rupee equivalent of the dollar loans will continue to be provided by the GOP to programs that are affordable to low income families and that A.I.D. has pre-qualified for purposes of this Program. These investments will be monitored through the review of GOP expenditure reports of HG eligible programs.

The HG component of the program will be supported by a $5 million technical assistance and training component grant used to: (1) manage the policy dialogue process; (2) provide technical and policy analyses necessary to advance the policy reform agenda through the Working Group and implementing institutions; (3) evaluate the Policy Action Plan process and the impact of policy changes on the financial and shelter sectors and low-income families; and (4) provide training for Pakistanis in the public and private sectors who will be critical to the development of a market-oriented shelter finance system.

### 2.3.2 Program Structure

2.3.2.1 Institutional Arrangements. The institutional framework which is proposed for the development of market oriented housing finance in Pakistan is structured upon the current policy and regulatory roles of the Ministry of Finance, Ministry of Housing, Planning Commission and the State Bank. A Working Group on Housing Finance, chaired by the Ministry of Finance, will be formed which will assume responsibility for formulation of policy, promotion of private sector housing finance organizations, and attention to problems and issues identified as major barriers to public and investor confidence. Figure 3 characterizes the organizational framework and summarizes the key actions that are necessary for development of the market-oriented system. These actions include:

(1) formulation of housing finance policy within the context of both overall housing policy and financial sector reform;

(2) formulation of the legislation and/or regulations underlying the formation and licensing of market-oriented housing finance institutions;

(3) promotion of the market-oriented housing finance concept and reduction of legal or operational barriers to formation and successful operation of housing finance institutions; and

(4) regulation, monitoring, and supervision of housing finance institutions with attention to the specific characteristics of long-term mortgage lending and construction financing.

The functions and responsibilities of each of the designated institutions and committees are briefly discussed below in the context of these roles.

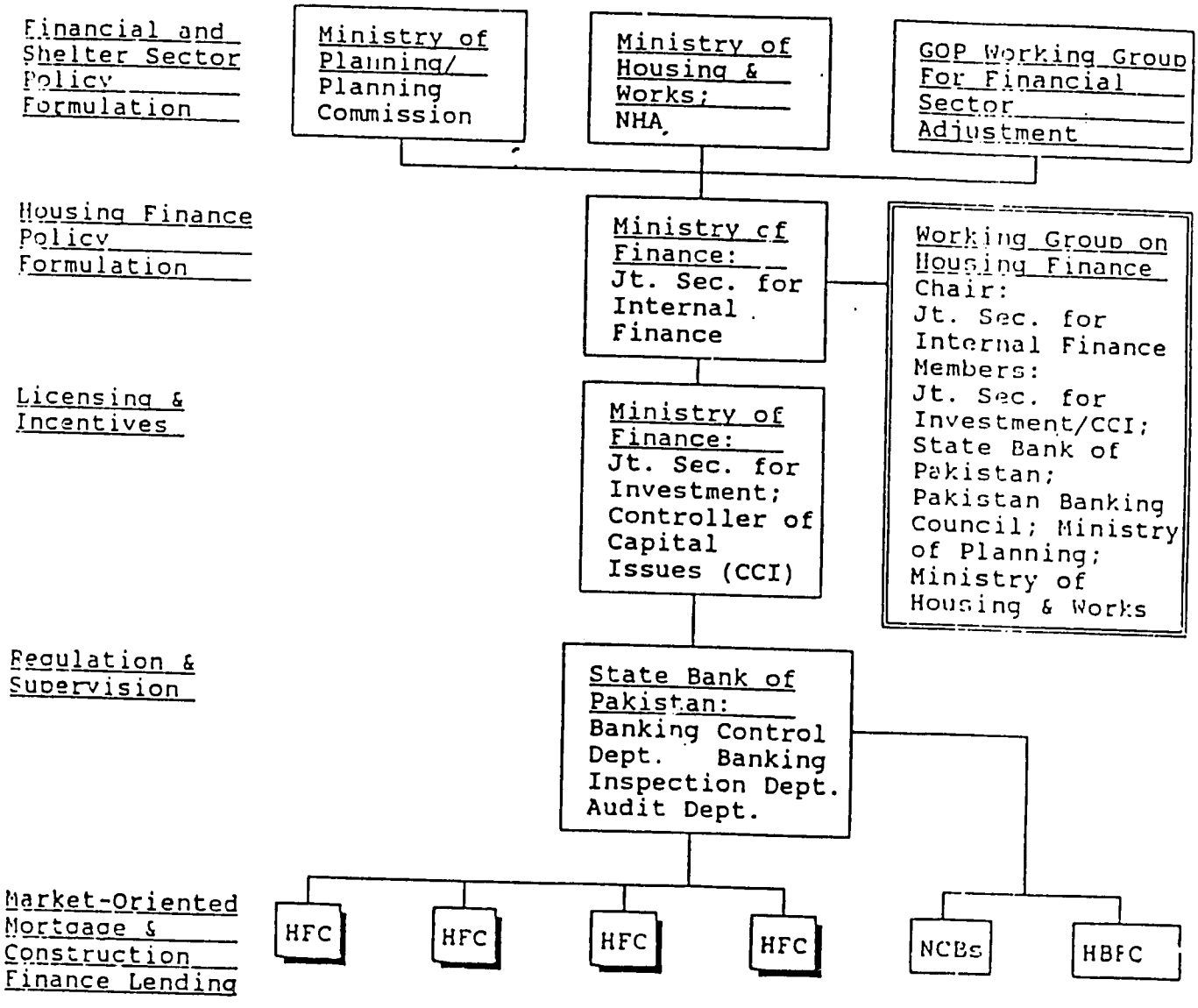
#### Ministry of Finance

Within the framework of financial sector and shelter sector policies, the Ministry of Finance has been designated as the institution responsible for development of the framework for the market-oriented shelter finance system. Within the Ministry of Finance, responsibility has been assigned to the Joint Secretary for Internal Finance. The Joint Secretary will assume the lead role in:

- establishment of the Working Group on Housing Finance and preparation of its agenda and timetables;
- development of legislation and/or regulations necessary for the licensing of the housing finance companies;
- development, in conjunction with the State Bank, of regulatory procedures specifically applicable to housing finance; and
- coordination of GOP financial and shelter policies with housing finance policies in order to establish a mutually supportive environment.

Figure 3

Institutional Structure for Development of a Market-Oriented Housing Finance System



The Joint Secretary for Investment, who is also the Controller of Capital Issues, plays an important role with regard to housing finance policy, and particularly with regard to enabling regulations. Applications to operate in the capital market require approval of the Controller for Capital Issues. In the short run, applications by housing finance companies will be reviewed by the Joint Secretary for Internal Finance in conjunction with the Joint Secretary for Investment to determine what functions the applicant will perform (as a banking or non-banking financial institution) and thus what legislative modifications to present regulations, if any, are necessary. In the long run, it is recognized that the entire licensing function must be reviewed by the Working Group in the context of reform and consolidation of regulatory functions. (See Section 3.I.1).

Working Group on Housing Finance. The Working Group on Housing Finance will support the MOF in the formulation of housing finance policy, the resolution of constraints to implementation of a market-oriented system, rationalization of GOP shelter policy with housing finance policy, development of licensing and regulating procedures, and coordination with the Working Group for Financial Sector Adjustment.

The Chairman of the Working Group on Housing Finance is the Joint Secretary for Internal Finance. Its members include the Joint Secretary for Investment and representatives of the State Bank of Pakistan, the Pakistan Banking Council, the Ministry of Housing and Works, and the Ministry of Planning (see Annex 17).

The Working Group will deal with overall policy and promotion as well as with technical issues that impact the development of public confidence and the return on investments in housing finance for both improvement and mortgage lending and construction finance.

The Planning Commission, and the Ministries of Planning, and, Housing and Works, and the Working Group for Financial Sector Adjustment. In order to ensure that policy development for housing finance is formulated within the context of the national policy agenda, the Ministries of Planning and Housing and Works will communicate overall shelter policy goals to the Ministry of Finance/Joint Secretary for Internal Finance. This is especially important to assure a financial environment conducive to the entry of the private sector, particularly with regard to rationalizing GOP policies on market pricing and targeting beneficiaries for GOP supported programs.

It will also be important to coordinate housing finance policy with policy developments being proposed for the financial sector as a whole. The GOP is developing these policies together with the World Bank and the IMF. A yet-to-be-created working group, the "Working Group for Financial Sector Adjustment," will coordinate its efforts with the Ministry of Finance and the Working Group on Housing Finance.

The State Bank of Pakistan. As agent of the Ministry of Finance, the State Bank of Pakistan will regulate and supervise the housing finance companies. Legislation now being developed consolidates under SBP regulatory and supervisory functions for both bank and non-bank institutions. Authority will rest within the Banking Control Department or a new department to be created. In the interim, the SBP, specifically the Banking Control Department, will coordinate development of regulatory procedures for housing finance companies, and, regulations specific to encouraging and safeguarding housing finance will be prepared.

Housing Finance Companies. The institutional framework described above is designed to encourage the formation of private sector and joint (private and public sector) housing finance companies. A proposal for a joint sector company has been submitted for approval by PICIC; another proposal from the National Investment Trust and the Dawood Group has also been formulated. In order to proceed with licensing of such groups in a timely manner, interim procedures for their licensing and regulation will be developed by the Working Group on Housing Finance. The HFCs will, however, be subject to the final form of the licensing and regulatory procedures when they have been instituted.

House Building Finance Company. The future role of HBFC is currently under discussions by the GOP, HBFC, the World Bank, USAID, and the Asian Development Bank (see Section 3.1.4). One suggestion is that HBFC pursue a dual role with regard to the housing market: on one hand, as an implementor of GOP-financed low income housing projects, and, on the other hand, as a supplier of mortgage loans at market rates (mortgages and/or construction financing). Another suggestion is that HBFC provide only market-oriented loans and gradually eliminate all SBP credit for its operations. Whatever mode is ultimately chosen, the market aspects of HBFC's program must be subject to regulation and review by MOF and SBP and be consistent with market-oriented housing finance company development.

Nationalized Commercial Banks. At present, mortgage and construction finance lending by the NCBs has been limited. Recent policy directives have apparently lifted the credit ceiling on housing lending by the NCBs, however, so the potential exists for expanded activity. In any event, the housing finance component of the NCBs portfolio should be subject to the specific SBP regulations developed for housing finance.

2.3.2.2 Policy Action Plan

The GOP, with A.I.D. support, will pursue a jointly developed Policy Action Plan (PAP) that presents and details the objectives of this Program. During project paper preparation, the Joint Secretary for Internal Finance, the responsible GOP office for the development and implementation of this program, has developed and reviewed with A.I.D. the PAP presented below. Progress against the PAP will be evaluated annually, and the PAP will be updated to reflect the next steps necessary to meet the policy objectives before the next tranche of HG resources is authorized. The process will be repeated until $100 million in guaranteed loans have been authorized. Figure 4 presents the Policy Action Plan Schedule.

Figure 4

POLICY ACTION PLAN (PAP) SCHEDULE

| | Agreement | Year 1 | Year 2 | Year 3 | Year 4 |
|---|---|---|---|---|---|
| GOP Adoption of PAP | GOP R&A | | | | |
| **OBJECTIVE NO. 1: Develop Policies for Market-Oriented Housing Finance** | | | | | |
| Establish Working Group on Housing Finance | GOP R&A | | | | |
| Formalize Responsibility for Policy Development | GOP R&A | | | | |
| Coordination of Housing Finance Policy Development | ON-GOING | | | | |
| **OBJECTIVE NO. 2: Rationalize GOP Role in Financing Shelter** | | | | | |
| Focus GOP Shelter Subsidies | STUDY | | | | |
| Establish Proper Roles for NCBs DFIs, and HBFC | STUDY | | | | |
| Monitor Saving Schemes' Deposit Rates | STUDY | GOP R&A | | | |
| **OBJECTIVE NO. 3: Develop Legal Framework to Create Market-Oriented HFCs** | | | | | |
| Review Existing Process for Licensing of HFCs | STUDY | | | | |
| Monitor Status of Draft Legislation on Financial Institutions | STUDY | | | | |
| Review Merits of Establishing of Special Provision for HFCs | STUDY | GOP R&A | | | |

NOTE:
(R&A) - "Review and Approval"

Estimated Initial Loan Authorization Date of June 1, 1989

Figure 4

POLICY ACTION PLAN (PAP) SCHEDULE

| Agreement | Year 1 | Year 2 | Year 3 | Year 4 |
|---|---|---|---|---|
| OBJECTIVE NO.4: Establish Regulatory and Supervisory Provisions Appropriate to Market-Oriented HFCs | | | | |
| Review Existing Regulatory and Supervisory Procedures | STUDY, GOP R&A | | | |
| Coordinate Development of Housing Finance Regulatory Framework | STUDY, GOP R&A | | | |
| Evaluate Current Review and Audit Procedures | STUDY | | | |
| OBJECTIVE NO. 5: Develop Instruments and Procedures to Facilitate the Growth of Housing Finance | | | | |
| Review and Recommend Improvements to Exist. Foreclosure Legislation | STUDY | GOP R&A | | |
| Review Use of Mortgage and Deposit Insurance as an Interim Measure | STUDY, GOP R&A | | | |
| Investigate Use of Adjustable Mortgage Instruments | STUDY | | | |
| Review HFC Short-Term Liquidity Requirements | STUDY, GOP R&A | | | |
| Assess Use of Long-Term Institutional Funding for HFCs | STUDY, GOP R&A | | | |
| Review of Items That May Adversely Affect the Development of a Housing Market | STUDY, GOP R&A | | | |

NOTE:
(R&A) - "Review and Approval"

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Figure 4

POLICY ACTION PLAN (PAP) SCHEDULE

| | Agreement | Year 1 | Year 2 | Year 3 | Year 4 |
|---|---|---|---|---|---|
| OBJECTIVE NO.6: Foster the Development of Market-Oriented Construction Finance | | | | | |
| Assess Alternative Arrangements for the Provision of Construction Finance | STUDY | GOP R&A | | | |
| Consider the Need for Special Licensing and Supervision Criteria for Construction Finance Lending | STUDY | GOP R&A | | | |
| ANNUAL POLICY IMPACT EVALUATIONS | | ***** ***** | ***** ***** | ***** ***** | ***** ***** |
| ANNUAL LOAN AUTHORIZATIONS | X | | X | X | X X |

NOTE:
(R&A) - "Review and Approval

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The initial PAP will confirm the operation of an interim process, working within the existing institutional structure and regulatory framework to review, license and regulate proposed market-oriented housing finance companies. The initial PAP will also begin the studies of institutional, legal and regulatory reforms necessary to address the constraints identified above and reflected in this program's objectives. The Policy Action Plan below presents the policy objectives and a menu of actions that sets the course and charts the progress on overall policy objective achievement. The implementing steps, benchmarks, and estimated timing of these activities are listed in Annex 13. The estimated timing dates are indicative and considered as guidelines for Working Group planning. These dates will be reviewed as part of the Implementation Agreement negotiations and will ultimately depend upon the effectiveness of the process this Program proposes to establish.

Policy Action Plan

Objective No. 1: Develop policies for market-oriented housing finance within the context of both structural reform in financial and capital markets and overall shelter policies.

1. Establish a Working Group on Housing Finance to address the housing finance policy objectives, the promotion of the concept and purpose of market-oriented housing finance institutions, the necessary legal and regulatory framework, the role of the GOP in housing finance, and the elimination of barriers to the flow of funds to mortgage and improvement lending.

2. Within the framework of shelter policy, formalize responsibility for formulation of market-oriented housing finance policies in the Ministry of Finance, and specifically with the Joint Secretary for Internal Finance.

3. Coordinate housing finance policy development with shelter policy as directed by the Ministry of Housing and Works, and reform of the financial sector as determined by the GOP in conjunction with the financial sector adjustment loan.

Objective No. 2: Rationalize the GOP role in financing shelter.

1. Focus GOP subsidies for shelter to low income families through programs implemented by the NHA and/or HBFC. Eliminate GOP subsidization of interest rates in segments of the market where the private sector can finance shelter needs at market interest rates.

2. Establish roles for the NCBs, DFIs and HBFC consistent with the formulation of market-oriented private and joint sector institutions.

3. Coordinate efforts to recapitalize HBFC and restructure the institution and its housing finance policies.

4. Monitor the returns to deposits in savings schemes to ensure their consistency with market competition.

Objective No. 3: Develop a legal framework appropriate to the creation of private and joint sector housing finance companies.

1. Confirm the interim process for review and licensing of housing finance institutions within the context of current procedures of the MOF and State Bank of Pakistan and the proposed reforms and consolidation efforts.

2. Monitor the development of the newly drafted law that would consolidate the regulatory and supervisory functions of banking and non-bank finance institutions in the State Bank of Pakistan.

3. Review the merits of establishing special provisions for housing finance within the proposed framework of legislation and regulations for establishing banking and non-bank finance institutions.

Objective No. 4: Establish regulatory and supervisory provisions appropriate to market-oriented housing finance institutions.

1. Confirm the interim process for supervision and closure of housing financial institutions with the current procedures of the MOF and SBP.

2. Coordinate development of the housing finance regulatory framework with GOP efforts to consolidate regulatory functions for banking and non-bank financial institutions within the State Bank of Pakistan.

3. Evaluate current review and audit procedures and information systems employed by the current regulatory system and make recommendations to strengthen them.

Objective No. 5: Develop instruments and procedures to facilitate the growth of housing finance and to remove barriers and disincentives to market growth.

1. Review the legal and administrative steps of the current foreclosure laws and make recommendations to reduce the bottlenecks and delays in the present foreclosure process.

2. Coordinate review of foreclosure and arrears with GOP measures to improve debt recovery in all sectors.

3. Review the desirability of mortgage and deposit insurance as procedures designed to enable risk reduction and mobilization of private capital.

4. Investigate the applicability of adjustable mortgage instruments designed to assist in long-term lending in an environment of uncertainty and inflation.

5. Review the adequacy and applicability of the State Bank's line of credit to finance institutions for short-term liquidity requirements.

6. Assess the utilization in housing finance of long-term funds such as those available in life insurance or pension schemes.

7. Review rent control, land titling, standards, and the revenues such as the stamp tax that may adversely affect the development of the housing market.

Objective No. 6: Foster the development of market-oriented construction finance.

1. Assess alternative arrangements for the development of construction finance by the housing finance companies, the NCBs, DFIs, and HBFC.

2. Consider the need for special licensing and supervision criteria for construction finance lending.

2.3.2.3 Program Outputs

The Program's Outputs will support the overall Program goal of encouraging the mobilization of domestic resources for housing and shifting the burden of providing shelter resources from the national budget to private financial markets.

Output 1: More Efficient Financial Markets Through the Establishment of a Market-Oriented Shelter Finance System

This Output is the prime objective of the Policy Action Plan described in 2.3.2.2. The system, based on market-oriented rates of return, will be more efficient than the current GOP approach that relies on directed credit and subsidies. To achieve this Output the following elements are required:

- extension of national shelter policy to specifically address the consistency of overall shelter policy with regard to the role and promotion of market-oriented housing finance;

- coordination of housing finance policy formulation with structural reform efforts in monetary and financial policy, debt recovery, supervision and regulation by the SBP, efficiency of the nationalized banking system, and rationalization of interest rate structures;

- establishment of the focus of responsibility for housing finance within the office of the Joint Secretary for Internal Finance together with the Ministries of Planning and Housing. The Joint Secretary will coordinate policy development and promote the establishment of the system;

- establishment of a broad-based, policy-oriented Working Group on Housing Finance to provide ongoing support to the Joint Secretary of Internal Finance in the formulation of housing finance policy, and the resolution of problems constraining the development of the system, such as foreclosure, and the development of incentives and instruments to further the system;

- establishment of a housing finance regulatory and supervisory function within the Banking Control Department of the State Bank of Pakistan, in coordination with efforts to consolidate regulation of banking and non-banking financial institutions in SBP;

- development of a revised HBFC role in the shelter sector, consistent with a market-oriented system of housing finance and resources available to the GOP for development of low-income shelter programs;

- development of shelter and financial sectoral policy on the appropriate use of subsidies in which they become more efficient and equitable through explicit targeting to the very low-income households.

Output 2: Increased level of Financial Intermediation Leading to Stronger, More Stable Economic Growth

Through the establishment of a viable shelter finance system, financial resources will be mobilized and be made available for economically productive purposes. While informal household savings in Pakistan may be reasonably high, they are not productive if held as cash outside the banking system. Household participation in the overall formal financial system increases financial intermediation, resulting in a more effective utilization of savings and stronger economic growth.

Output 3: Shelter Services Valued at the Equivalent of $100 Million, Which are Affordable to Below Median Income Urban Households

This Output would be the rupee expenditure for shelter services represented under the pre-qualified GOP programs, described in Section 2.4. It is proposed that these expenditures will be for Katchi Abadi upgrading, water supply and sanitation projects and area development schemes.

2.3.2.4 Program Inputs

This Program will consist of three discrete inputs:

(A) The Policy Action Plan

The Policy Action Plan (PAP), developed jointly with the GOP, will constitute a set of actions that would be followed in order to achieve the Program's overall policy objectives. The PAP consists of a menu of actions, implementing steps, and benchmarks that set the course and chart the progress of the overall range of sectoral objectives, especially the development of a market oriented shelter finance system in Pakistan. The PAP will be reviewed and refined with the GOP before it is incorporated into the Program Implementation Agreement (see Section 4.5). On-going discussions will be held with the GOP Working Group on Housing Finance to review progress made on the PAP and determine which actions in the PAP need modification to reflect changing conditions. An evaluation of progress on the PAP will be carried out annually to decide which actions should be carried over to the near year's PAP, deleted entirely, or added.

(B) Technical Assistance and Training.

Technical Assistance and Training (TAT), will be provided in support of both monitoring and evaluation of the HG physical outputs, and of the Program's policy objectives. The majority of the TAT input, however, will directly support the implementation of the policy objectives. A comprehensive TAT plan will be developed to structure this support and link it directly to the menu of actions and implementing steps contained in the PAP.

The primary rationale for both technical assistance and training is to advance the Program's Policy Action Plan. In several cases, benchmarks that are directly linked to the implementing actions are the provision of technical assistance or training, i.e., in order for the PAP to advance, technical assistance and training must be utilized.

The achievement of technical assistance and training objectives will depend on the presence of two resident advisors. Short-term consultancies averaging six person-months per year for five years will complement the work of the resident advisors. As the need for special studies, training, and other assistance is identified by the resident advisors, USAID, RHUDO, and the GOP, appropriate technical specialists will be provided along with required logistical and financial support.

A description of the long and short-term technical assistance and training components follows:

Long-Term Advisory Support for the program will consist of a long-term team of two resident experts. The team will provide technical assistance as needed through the entire Program period.

The Chief Technical Advisor, will be a Shelter Finance System Advisor. This position may be staffed by a full-time contractor or A.I.D. Direct Hire, and will be based in USAID/Pakistan's Program Office (PRO). PRO and the Advisor will serve as the liaison to RHUDO, and will help coordinate the TAT component of the Program, as well as to identify policy development and TA needs, and support the policy dialogue. This Advisor will also be responsible for Program monitoring duties.

The second technical advisor, a Finance Systems Specialist, will be placed in the Ministry of Finance with the Office of Internal Finance. The Specialist will also work with the State Bank of Pakistan and coordinate Program activities between the two institutions. The responsibilities of this Advisor will include coordination of the GOP actions contained in the PAP, assessment of Ministry TAT needs, assisting in the coordination of Ministry TAT activities, monitoring of PAP progress, participation in policy negotiations, and assisting with Program monitoring and evaluation. Responsibilities will also include expert advice on the structure and content of the legal and regulatory framework to be established for the market-oriented shelter finance system. This Advisor's background should include professional training and experience in financial regulation, with specific experience in housing finance.

These Advisors will be supported by the RHUDO staff on TDY from Bangkok, and by PRE/H backstopping as necessary.

Short-Term Consultancies and Special Studies will supplement and support the work of the long-term advisory team through a variety of short-term consultancies totalling approximately 30 person months. The purpose of this assistance will be to add more specialized knowledge of technical areas, and to work with GOP officials to design, conduct, and analyze special studies and projects. The determination of the use of short-term advisory services and the need for specially focused studies and analyses will be made by the GOP and long-term advisory team, in consultation with the USAID Program Manager and RHUDO.

Training Activities will consist of three types of training: U.S. long-term training; U.S. and regional short-term training; and, local workshops and seminars. RHUDO's Regional Training Advisor will be responsible for developing an initial training needs assessment with input from the long-term Advisors and involved GOP institutions. The assessment will result in a detailed training plan that will match training needs with resources. As with technical assistance, training activities will be managed by RHUDO.

Long-term training opportunities in the specific field of housing finance are limited, although degree programs in the general fields of accounting and finance are available. Specifically tailored training or exchange programs with U.S. housing finance institutions should prove to be more effective. Participants in long-term training programs would be selected by the GOP from involved ministries, and by USAID in the case of private sector entities.

Short-term training opportunities in shelter finance are more prevalent. They will be offered to GOP senior-, mid-, and technical-level officials, and to potential private sector lenders in the form of short courses, policy seminars, study tours, and observation visits both outside and inside Pakistan.

(C) The Housing Guaranty Loan

The Shelter Resource Mobilization Program is planned for a total of $100 million in A.I.D. guaranteed loans over a five-year period. The first tranche would consist of a $25 million authorization in U.S. FY 89.

The dollar proceeds of the HG loans can be used by the GOP as unrestricted foreign exchange. A.I.D. will not track the use of the dollars, but will only verify the use of rupee equivalent to finance shelter programs affordable to families earning below the urban median family income level (including water supply, sanitation, drainage, road/paths, housing, and community facilities). (See Section 2.4)

2.3.2.5 HG Disbursements

HG loan authorizations will be based on the GOP's agreement to pursue a jointly negotiated Policy Action Plan. HG disbursements are projected to occur at the time the loan is contracted based upon the GOP's presentation of eligible expenditures as approved by A.I.D. in local currency equivalent to the amount of the HG guaranteed dollar loan. Should it be deemed appropriate by A.I.D., the dollar loan disbursement may be provided on an advance basis to be liquidated by the GOP presenting eligible expenditures before the next disbursement would occur.

Prior to the disbursement of the first tranche, eligible expenditures will be submitted by the GOP and approved by A.I.D. The date from which eligible expenditures may be accrued is the GOP's FY 1989. Subsequent loan guaranty authorizations will be derived from the annual PAP review process described in Section 2.3.

## 2.4 Local Currency Support

### 2.4.1 Utilization of Local Currency

Over the five-year life of the Program the GOP will continue to provide support to national and local shelter and urban development institutions. Such entities are responsible for implementing shelter and urban development projects that are affordable to families earning below the median family income that generate eligible expenditures for this Program. The GOP will provide these entities with local currency at least equivalent to the $100 million HG Program loans. Eligible expenditures in the amount of approximately Rs. 482 million will be presented for A.I.D. approval to justify the disbursement of the first tranche of US$25 million.

HG related local currency will be attributed to pre-qualified programs described below that now finance the development of raw land for residential plots, community upgrading in Katchi Abadi and other low-income neighborhoods with inadequate services, and new shelter programs. These local currency expenditures are to be funded from current GOP resource allocations. The HG program will not require additional resources from the GOP to finance other shelter projects. The local currency component of this program will support the GOP's interest in better targetting resources for shelter to those unable at this time to receive a loan from the private sector.

The criteria for the kinds of projects to which HG related local currency funds may be attributed is affordability, that is the executed projects must be affordable to low income households. Ongoing and programmed GOP projects that meet this criterion are identified in Section 2.4.2 below as Pre-qualified Shelter Programs. A.I.D. will coordinate with other donors on development issues related to those programs that are pre-qualified. As the Program progresses, additional projects may be qualified as sources of local currency expenditures as well.

### 2.4.2 Pre-qualified Programs

The Program proposes to pre-qualify GOP shelter activities funded through the Special Development program (SDP) and the Annual Development Program (ADP) and attribute HG eligible expenditure to SDP and ADP shelter activities.

The SDP budget, a complement to the GOP's Annual Development Program budget, is intended to reflect pressing developmental needs in "lagging areas". The projects included in the SDP budget represent priority areas of attention under the current GOP Five-Year Plan, both in terms of content and geographic focus. There is US$10.5 million worth of qualified expenditures for local currency attribution in the 1988-89 SDP alone (see Annex 14).

Total allocations under the ADP in the urban sector over the Five-Year Plan period are Rs. 15.411 billion (US$811 million) at the provincial level. Of this amount, some Rs. 5 billion (US$263 million) is earmarked for nationwide Katchi Abadi improvement programs. Taken together, eligible projects in both the SDP and ADP budgets are well in excess of the US.$100 million in local currency needed to justify disbursement of the HG loan. 1/

1/ This figure is based on the Seventh Five-Year Plan's Katchi Abadi improvement target population of 5 million, and the GOP's budgeting formula of Rs. 1,000 per capita. Using this last figure, the Rs. 212 million allocated in the SDP for Katchi Abadi improvements in Sind alone should benefit 212,000 persons.

The priorities for attribution will be the provision of infrastructure and Katchi Abadi improvements. The development of land, including its servicing, was identified by the IBRD as the single most significant sectoral constraint. The IBRD's program focus, which A.I.D. supports, is on land tenure, planning, and taxation issues, and will be well complemented by support for infrastructure provision even as this HG Program focusses on the other key sectoral constraint of access to credit.

Local currency attribution to infrastructure priorities also supports the GOP's stated intention of introducing user fees to increase cost recovery, and modifying infrastructure standards to increase affordability. Infrastructure provision is consequently supportive of the establishment of a viable housing finance system in Pakistan. Trunkline infrastructure programs will benefit Katchi Abadis as the tenure status of residents is resolved. In addition, A.I.D.'s support of World Bank objectives to assist the GOP address tenure issues will be enhanced.

Based on the analysis of GOP budget expenditures and specific shelter activities the following shelter activities are prequalified for the generation of local currency eligible expenditures under the Shelter Resource Mobilization Program.

Katchi Abadi Upgrading Programs

Katchi Abadi programs improve streets, install water, sewerage, drainage works, and electrical lines and provide land for facilities such as schools and health clinics.

The very limited new formal housing that is produced each year is for the most part beyond the price range of low income families. With no other source of housing, the urban poor in Pakistan are housed in essentially two ways:

- They live in severely crowded, deteriorating housing with inadequate services in old inner city slums; or,
- They reside in informal settlements, on land owned by the government or private landowners (usually on the city outskirts) with little or no urban services. Katchi Abadis are home to an estimated 25 percent of the urban population, with the proportion considerably higher in the major cities such as Karachi where the estimated incidence is 38 percent.

According to the World Bank Shelter Sector Review, households in the Katchi Abadis of Karachi earn a wide range of incomes with well over half (62%) earning below the urban median family income of Rs. 2,100. Thus the improvement of Katchi Abadis is an especially effective means of targeting shelter resources to the urban poor. Annex 11 provides a more detailed discussion of affordability.

| Monthly Household Income | Percent |
|---|---|
| Up to Rs. 500 | 2.4 |
| Rs. 501 - 1000 | 19.1 |
| Rs. 1001 - 1500 | 21.9 |
| Rs. 1501 - 2000 | 18.7 |
| (Approximate urban median income cut off) | |
| Rs. 2001 - 3000 | 18.5 |
| Rs. 3001 - 4000 | 8.2 |
| Rs. 4001 - 5000 | 4.5 |
| Rs. 5001 and above | 5.5 |
| TOTAL | 100.0 |

As noted in the World Bank report, slum upgrading has proven, in Pakistan as elsewhere, to be a very effective way of meeting the priority needs of low income groups. Unlike some land and shelter programs, the beneficiaries are readily identifiable as poor. After employment, their priorities are usually public services. In addition, slum upgrading programs usually have a high economic rate of return. For all these reasons, A.I.D. support of GOP programs addressing the backlog in improvement and regularization of Katchi Abadis in cities of all sizes is justifiable.

Serviced Plots

The second type of program to which local currency will be attributed will be 3 marla serviced plots schemes on which families construct their homes in urban area development plans. Many of these households are currently living in unimproved Katchi Abadis and have been allocated plots using a ballot system, since demand far exceeds supply. Others are residents of the approximately five to ten percent of Katchi Abadi units slated for removal due to the improvements made under upgrading projects. There is every indication that local planners will continue to ensure minimal dislocation for these purposes. Households in this group have incomes with a narrower range than those in the Katchi Abadi group listed above, and a lower overall average income. Once again, the majority have income below the urban median so this program also qualifies for A.I.D. support.

2.4.3 Affordability

The urban median family income for Pakistan is calculated to be Rs. 2,100. ADB affordability calculations indicate that assuming market interest rates (12%), a loan term of 15 years, and use of no more than 15% of the household income for monthly payments, a loan of Rs. 36,000 can be afforded by a household earning the urban median family income.

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Katchi Abadi Upgrading

The GOP has used the figure of Rs. 1,000 per capita for budgeting improvements in Katchi Abadi. An average household therefore might expect to borrow between Rs. 5,000 - 6,000. A recent upgrading project was costed at Rs. 35 per sq. yard, or roughly Rs. 5,600 for an averaged-sized 120 sq. meter plot. Using either measure, Katchi Abadi upgrading projects are affordable to A.I.D.'s target group.

3 Marla Plots

Area development schemes in Punjab have recently produced 3 marla plots costing Rs. 7,821, while in Peshawar plots presumably involving land of higher cost or with higher infrastructure standards have been priced at an average of Rs. 32,000. In the Hyderabad Development Authority's incremental development scheme, 80 sq. yd. plots cost a total of Rs. 9,600. A 20 percent downpayment and Rs. 50 (increasing with time to Rs. 110/month) payments ensure affordability to households earning as little as Rs. 1,000 per month (less than one-half the urban median).

As indicated above, the GOP shelter programs described are affordable by households earning below the median income, and their funding is consequently regarded as attributable local currency expenditures.

2.4.4 A.I.D. approval of local currency attribution

Supporting shelter and related infrastructure projects through the SDP and ADP funding mechanism (or similar ones as A.I.D. may agree) is intended to be straightforward. It should not require extensive coordination with other donors to avoid duplication of funding. The HG Program Implementation Agreement will include a list of Pre-qualified Shelter Programs and projected eligible expenditures for each. Site visits would be carried out on a sample of projects in each Program type to verify implementation and determine the proportion of total Program expenditure that is suitable and affordable to low income families.

The HG Program Implementation Agreement will also specify that a GOP Program Manager will be responsible for gathering, analyzing and presenting for A.I.D.'s approval the eligible expenditures for qualified projects before each HG disbursement. The GOP Program Manager will present the SDP/ADP expenditures for each Pre-qualified Program along with an analysis supporting the calculation of expenditures eligible for attribution to the HG. RHUDO working with the GOP Program Manager will determine the final level of eligible expenditures acceptable.

# 3. PROGRAM ANALYSIS

## 3.1 The Institutional Framework for Housing Finance

Introduction: The proposed HG Program is considered institutionally feasible for two major reasons: (1) the basic institutional mandate and elements of a regulatory framework for supervision of financial institutions are established in Pakistan; and (2) the GOP has undertaken reforms of its institutional framework that will be conducive to improved supervision and the effective establishment of market oriented companies. These reforms will be supported by the World Bank's Financial Sector Adjustment Loan and a medium term macroeconomic adjustment program to be implemented with the assistance of the Bank and the IMF. The proposed A.I.D. HG Program support in housing finance will itself be supplemented by ADB assistance to HBFC and the World Bank's own shelter sector program. An interim process for developing housing finance companies can be established within the current regulatory and supervisory procedures of the institutions analyzed below.

Reforms to the institutional framework will be required however, since the authority to supervise and regulate housing finance companies has been applied ineffectively and has not created an environment conducive to the establishment of market oriented companies.

First, the private sector has had relatively little financial experience. As indicated in section 2.1, there has been virtually no private sector provision of housing finance in the formal sector, either mortgage and improvement loans or construction financing. Furthermore, domestic private sector banking is prohibited and provision of credit by and to the private sector overall has been extremely low, especially when compared with levels in similar developing countries.

Second, the licensing and regulatory system has twice shown itself unable to respond decisively to new financial initiatives. The failure of the private finance companies in the late 1970s, in which substantial public savings were lost, was a failure of the regulatory and supervisory function rather than the fact that the companies were private. Another surge of private investment companies, and subsequent loss of depositor's funds, has occurred since 1987 and although SBP filed criminal complaints, the existing regulations did not always allow action to be taken. Thus a special set of regulations for finance companies was issued in July 1987. Foreclosure procedures are another regulatory stumbling block. There is strong agreement among the NCBs that residential lending is too risky because of high delinquencies and the inability to pursue these delinquencies in a timely manner. Also, HBFC's delinquencies are substantial and are caused at least in part by administrative delay in addressing nonpayment. Although Special Banking Tribunals were created in 1978 under the Banking Companies Recovery of Loans Ordinance, a shortage of expert judges and negative social attitude about foreclosure have prevented much improvement.

Finally, the overall financial sector will be undergoing substantial liberalization carried out by the GOP in consultation with the World Bank and International Monetary Fund. While these adjustments will benefit the growth of private housing finance in the long run, in the current environment the institutional capacities of the major financial institutions (MOF and SBP) are no doubt stretched. Uncertainties over the role of HBFC in a market environment adds to the reform burden. The Working Group on Housing Finance will coordinate its efforts with committees established by the GOP to undertake related financial reforms.

The sections below discuss the key functions which must be undertaken in developing the housing finance framework -- licensing, regulation, and supervision -- and issues concerning the overall financial context such as structural adjustment, formation of market oriented housing finance companies, and solution of disincentives such as ineffective foreclosure.

### 3.1.1 The Institutional Structure for Housing Finance

To maximize the impact of housing finance on the development of the financial sector, a regulatory system is required that will (1) encourage new lenders to enter the market and (2) protect depositors. The objectives of such a system are as follows:

- protect the public from the consequences of fraudulent bankruptcies;
- foster growth and diversification;
- insure the financial integrity of the housing finance institutions;
- establish net worth requirements for the safety of depositors
- restrict conflict of interest; and
- insure the proper management of risks;

The major regulatory functions encompass licensing (granting of charter), supervision (including audit), and the establishment of regulations which underlie supervision. Ownership and appointment of directors is also an important matter of control. At the present time, there is extensive diffusion of regulatory activity across the SBP, the MOF (both the Joint Secretaries for Internal Finance and Investment), and the Pakistan Banking Council. Much of the delineation occurs between banks and Non-Banking Financial Institutions (NBFIs), but lines of responsibility still cross these institutions. Finally, although a number of statutes exist for granting charter, it is likely that regulatory and/or legislative actions will ultimately be necessary for the emergence of HFCs, especially if any of them wish to accept general deposits.

#### 3.1.1.1 Licensing

Governing legislation for the NCBs includes the Banking Companies Ordinance (1962), the Banking Reform Act (1972), and the Banks Nationalization Act (1974). (Foreign banks are also governed by the Foreign Private Investment Act, 1976.) NBFIs are chartered under either the Companies Ordinance of 1984 (PICIC, BEL, NIT, and the private leasing

companies, for example) or under special governing legislation unique to the institution (HBFC, IDBP, NDFC, and ADBP). Also, a special set of Statutory Notifications were issued in 1987 setting forth the terms and conditions for private investment finance companies beyond provisions in the Companies Act.

The situation for granting Charter to private and joint sector HFCs is currently very unclear. The Joint Secretary of Internal Finance has stated that Pakistan's financial sector institutions would be separated into two segments: banking and NBFIs, with banking institutions under the purview of Internal Finance and NBFIs under the Joint Secretary for Investment. Presumably the Controller of Capital Issues (Joint Secretary for Investment) will continue to have licensing power for companies registered under the Companies Act and the Special Regulations for Finance Companies. However, HFCs (since they can be either banks or non-banks) have no obvious "home" in this structure and there is no law or regulation governing their establishment: (1) the Bank Nationalization Act does not permit private banks; (2) the Companies Act does not permit investment in real estate; and (3) the current interpretation by MOF of the special finance regulations has been that they too would not permit companies that engage in mortgage lending. The Deputy Managing Director of PICIC, who has prepared PICIC's proposal for a joint sector HFC (see Appendix 9), suggests that approval will be granted under the special regulations. In any event, the Joint Secretary for Internal Finance, as the government official responsible for the development of the housing finance framework, has assumed responsibility for clarifying the licensing process and will introduce the matter to the Working Group on Housing Finance.

There are at least three reasons why the licensing structure for housing finance companies should be considered as quickly as possible within a broad, long-term context: Finance companies can assume many bank and non-bank forms. There is also the possibility of "shifting" from a NBFI to a bank (that is, taking general deposits from the public as well as mobilizing resources from the capital market). Finally, pressures now exist to consolidate the regulatory system for all financial institutions under SBP.

Private housing finance companies may be structured as savings institutions (savings and loans, building societies, mutual savings banks, credit unions, housing cooperatives); mortgage banks, commercial banks, or credit financiers.1/ There are two basic types of models: the British and U.S. type of thrift institution which takes general deposits and the Continental European, non-bank financial institutions. There is great diversity around the world and both types can exist in one country. Also, as they gain experience, NBFIs whose resources were mobilized on the capital market (or from government) begin to seek general deposits. The Housing Development Finance Corporation in India is evolving in this manner. Thus, ultimately the GOP may wish to modify both the Bank Nationalization Act and the Companies Ordinance to permit bank and non-bank HFCs, or establish special regulations for HFCs which supplement other governing legislation.

1/ Bertrand Renaud, Housing and Financial Institutions in Developing Countries. p.65; Mark Boleat, National Housing Finance Systems.

Finally, licensing regulations must be considered in the context of suggested reforms of the regulatory function. As indicated, the Financial Sector Adjustment Loan (FSAL) calls for consolidating regulation and supervision in the SBP and unifying the regulations. This consolidation does not appear to include licensing, which presumably remains within the MOF. Following this thrust, however, it may be appropriate to consolidate the chartering function for all types of HFCs within one segment of the MOF. As already mentioned, this will be taken up by the Working Group on Housing Finance.

3.1.1.2 Regulation and Supervision

While the major regulatory provisions and procedures are fairly well established, problems of both organization and process have been identified. Also, some of the regulations are not felt to be adequately stringent. Specific issues include: (1) diffusion of responsibility; (2) uniformity and adequacy of regulations; (3) inadequate numbers of skilled personnel in the SBP; and (4) the need for improved SBP research and reporting systems. In addition, regulatory procedures specific to housing finance will need to be introduced into the system.

Diffusion of Responsibility. The commercial banks and specialized banks are supervised by SBP while the NBFIs are supervised by MOF (notably HBFC and NDFC). However, this split is complicated by the fact that SBP issues regulations for all banks and some, but not all, NBFIs. For example, HBFC is governed by the Housing Building Finance Corporation Act of 1952 which establishes its regulatory framework. Although direct supervision rests with MOF, little supervision actually takes place, apparently because of staff limitations. Furthermore, the PBC shares some aspects of supervision with SBP for some, but not all, banks. SBP conducts on-site inspections of all banks in Pakistan but PBC conducts inspections of foreign offices of NCBs. In addition, PBC conducts its own audits of NCBs' domestic operations. Finally, PICIC and BEL are regulated by SBP but inspected by the CLA (Corporate Law Authority) as well as by SBP.

Uniformity of Regulations. Partly as a result of the fragmented supervisory structure and partly because of intent, different institutions have different regulations. For example, (1) tax treatment differs for banks and non-banks and among non-banks only leasing companies are tax free; (2) reserve requirements apply only to banks and not to deposit-taking non-banks such as modarabas and investment companies; and (3) banks cannot advertise for deposits at guaranteed rates whereas private listed companies can. Non-uniform incentives can result in distortions to the intent of finance policies. Thus, consistent review of regulations across institutions would clarify whether uniformity was desired, or whether incentives are indeed warranted for given institutions as a matter of development policy.

Adequacy of Regulations. Regulatory provisions may encompass all the following parameters: capital structure, management experience, asset quality, liquidity ratios, repayment performance, accruals of interest on non-performing loans, earnings, and net interest margins. These regulatory parameters are also generally employed in Pakistan. The World Bank has found that SBP appraisal procedures and collateral valuation are satisfactory. However, for some parameters, the target ranges may not be stringent enough. Moreover, reporting procedures need improvement, and issues involving early warning systems and the changing structure of financial systems need further strengthening.

A particularly important example is capital adequacy, which, because of its importance, is a highly debated issue worldwide. For example, OECD regulators are now trying to formulate uniform definitions and target ranges for capital adequacy; assets are rated according to risk and liquidity and classified into five general categories ranging from zero (least risk) to one hundred percent (most risk). A minimum weighted average of 10 percent has been suggested.

Relative to these standards, the present capital adequacy status in Pakistan is considered to be neither sufficiently stringent nor adequately specified for calculating a risk adjusted asset base.

A number of other regulatory shortcomings have been identified by the World Bank, including prudent exposure limits, restructuring of insolvent banks, the implied deposit insurance of the NCBs, and the clarity of reporting requirements. The World Bank has suggested formulation of review committees on these issues.

Strengthening the State Bank of Pakistan. In addition to problems in the structure of the regulation, the ability of SBP to carry out supervision and inspection requires review. In the last two decades, SBP's ability to supervise the financial system, manage monetary policy, and give the GOP advice on macroeconomic policy, has been significantly impaired because of personnel policies.1/ Recruitment of high quality professional staff has been impaired by salary policy and union pressure to recruit all professional staff from clerical levels. As part of the FSAL, GOP has agreed to improve SBP staffing and personnel policies, set up a subsidiary for inspection (free from salary and recruitment limitations). In the longer term the SBP will improve its research capacity and establish a credit bureau to pool information from all financial institutions to assist in credit decisions. Again the Working Group on Housing Finance will coordinate its recommendations with actions taken for SBP reforms.

1/ World Bank. Pakistan Financial Sector Review; Report No. 7049-Pak; December, 1987.

Regulation of Housing Finance. Although, in the first instance, housing finance companies would be supervised according to the procedures established for banks and other financial institutions, the special nature of denomination and maturity intermediation in housing finance dictates certain specialized rules. Housing finance requires special management skills and local market expertise. Capital adequacy is crucial because of the long term nature of real estate loans. For the same reason, housing finance is extremely sensitive to inflation; indexation procedures are used in some countries. Underwriting procedures replace the notion of prudent exposure limits. Finally, loan recovery procedures must be quickly and stringently enforced, especially since many small borrowers are involved.

### 3.1.2. Market Oriented Housing Finance Companies

The types of organizations that may undertake improvement, mortgage and/or construction lending are not easily predictable at this time. The discussion of institutional arrangements (see Section 2.3.2.1) assumed that lending would be undertaken by newly-formed, private and joint sector HFCs, the National Commercial Banks, and, perhaps, by a restructured HBFC. The following section discusses these alternatives.1/

#### 3.1.2.1 Private and Joint Sector Housing Finance Companies

Joint public-private sector as well as private sector HFCs should be encouraged to undertake improvement, mortgage and construction finance lending at the present time. Several GOP officials, and private bankers, however, have suggested that only private sector organizations should be promoted. Their argument is that joint sector companies, especially if the public sector is the majority owner, are really under the control of government and do not bring enough net, new resources into the system. Although the ultimate objective is to stimulate private investment and commercial activity, the issue of confidence is so great that the first few HFCs will probably need public sector support in terms of partial ownership and even some financial guarantees. In addition, the private sector has played a relatively small role in the financial sector to date. Management expertise in the private sector is a relatively scarce commodity and joining forces with the DFIs may be extremely useful in the short-term. DFIs have been responsible for innovations in both organization and financial instruments.

It is difficult to suggest guidelines for defining joint sector companies; determination of actual public and private "shares" is not always straightforward. The PICIC proposal, for example, claims that the majority of the shares would be held by the private sector. However, only 30 percent would actually be held by the "general public." The rest would be from IFC and privately registered companies with large public sector shareholders (such as PICIC). Also, the proposed chairman of the Corporation is the Governor of SBP; and SBP guarantees have been requested.

1/ The PICIC proposal for a joint sector Housing Finance Corporation is described in Annex 9. A proposal by NIT and the Dawood group, apparently not yet finalized, is described in the USL International report.

Thus, care will have to be taken so that partial public ownership will not lead to a "non-market" orientation and consequent loss in public confidence. State owned enterprises, even those registered as private limited companies, often become unprofitable because they are forced to meet social goals that detract from profitable operations. It would probably be best to eliminate all such social objectives from the joint sector (or fully public sector or fully private sector) HFCs in order to give them the best possible opportunity to establish good reputations as financially viable companies. This will be the best way to attract savers, and long term investors. It may even be unwise to force such companies to cross subsidize from high to low income borrowers in the early years or to operate low income windows on a contract basis for Government programs. The single-minded pursuit of financial viability would probably be the best way for the HFCs to assist in the establishment of an integrated, market oriented financial sector.

Ultimately, it may be desirable to stress private ownership; certainly, it is desirable to maximize private sector equity participation. Also under the terms of the FSAL, Pakistan will be moving gradually toward increased private representation in the NCBs and the transition of private non-banks (in this case the newly proposed private investment banks) to full-fledged banks. Whether or not it is advisable for housing finance companies to follow this route or remain as specialized institutions is a matter of debate. Nevertheless, in the interim, private sector resource mobilization may be best accomplished in conjunction with joint sector resources and skills.

#### 3.1.2.2 The Role of The Nationalized Commercial Banks in Housing Finance

At the present time, the five NCBs can lend for housing. As noted in Section 2.1.2, funds allocated by the NCCC in 1987-88 to the NCBs amounted to only Rs. 190 million. USAID's study of housing finance indicated that it was not clear whether this was a ceiling or a mandated target; in any event it is a very small percentage of housing finance requirements and tends to be allocated to bank employees, bank customers, military personnel, and so forth.

The 1988-89 NCCC credit plan apparently allocates Rs. 900 million to the NCBs for housing.1/ This is a substantial increase over the Rs. 190 million allocated in 1987-88 (it represents about 6 percent of housing finance needs as estimated by the ADB). Again, it is not clear, however, whether NCB policy will dictate increasing their mortgage lending. Somewhat different perspectives have been voiced by the Pakistan Banking Council and the NCBs. Also, it must be finally established whether the NCCC ceilings are currently in effect for NCB mortgage lending.

1/ ADB Consultant Report, Paper 2.

First, the low level of NCB lending in mortgage finance may be more an issue of bank policy rather than the availability of funds for lending. The team preparing the housing finance study discussed mortgage lending with several NCBs and it was universally felt that it was too risky, given the delinquency and foreclosure problems, and the consequent inability to attract private investors in the business. The Habib Bank was contacted again during preparation of the project paper and this view was reiterated. The foreclosure issue is, indeed, a bottleneck. There is another perspective, however: the general unwillingness (worldwide) for commercial banks to engage in mortgage lending. Given the problems of denomination and maturity intermediation involved for commercial banks in long-term mortgage lending and the generally more profitable (or at least familiar) nature of their commercial and mercantile lending, many commercial bankers do not believe housing finance is worth the risk.

Second, under current NCCC policy, however, the NCBs may increase mortgage lending as an interim second best policy. The GOP has suggested that at the present time commercial banks remain outside the NCCC limits for mortgage lending. (A representative of PBC did not realize that this adjustment was currently in effect, so clarification is needed.) In any event, if NCBs mortgage lending were to fall outside the ceiling he felt they would undertake increased mortgage lending merely to mop up excess liquidity. The NCBs now have substantial amounts of excess liquidity. Because they have no other avenues, these funds are invested with the SBP at 6 percent. Given that their cost of operations is around 10 percent, mortgage lending at 13 to 14 percent seems a more lucrative alternative (even 12 percent was mentioned, since a 2 percent spread was quite acceptable). In summary, the PBC made it clear that while the NCBs preferred lending for industry and trade, housing finance was a viable option in the current context of excess liquidity.

One likely outcome of the NCB situation may be that, at the most, mortgage lending by NCBs is viewed as: (1) preferential treatment for employees and customers; and (2) a short-run expedient in asset/liability management under the current NCCC system. In the long-term, two events will alter this situation: the gradual replacement of the NCCC limits with market oriented monetary policy and the development of specialized housing finance institutions.

As discussed in Section 3.1.3, the GOP has agreed under the FSAL to gradually liberalize its interest rate and directed credit policies. This is recognized to be a long-term endeavor; while limits on directed credit schemes take place in phase one, final abolition of credit targets occurs with "potential future loans" (see Annex 15). At that time, NCBs will presumably base credit allocations on market criteria and may not be faced with the excess liquidity of the present directed credit system, which may push them toward (second best) mortgage lending.

Mortgage lending in developing countries may be more suitably handled by specialized institutions in any case. An active debate exists on the merits of universal banking versus specialized financial institutions.1/ Multipurpose institutions are expected to provide long-term financing, increased competition, and lower cost intermediation. In the case of housing finance in developing countries, however, Renaud thinks the verdict on universal banking is far from clear and that housing would lose out because of the serious long-term intermediation problem compared with other forms of commercial banking. This view, along with the specialized and local knowledge required to be a successful mortgage lender, suggests continued promotion of specialized HFCs in Pakistan. Finally, the Joint Secretary for Investment has indicated that the NCBs preferred to operate in and from Karachi; thus, their branches may not push for housing lending without more emphasis from headquarters.

3.1.2.3 The Role of House Building Finance Corporation

A number of different roles have been proposed for HBFC.

First, the GOP and the World Bank have agreed that HBFC should be a commercial, market oriented lending institution that will move rapidly towards raising its own resources. This is an important condition of the FSAL. Within the next few months, HBFC has been instructed to prepare a corporate plan that will address its new goal. The market orientation is clear, as is the World Bank and IMF case for reducing government expenditure by minimizing subsidies.

Second, the ADB, which considered a number of options, has proposed a two window approach: one fully commercial, the other for subsidized finance for low income groups.

Third, the view has also been put forward that HBFC be only the Government's window for subsidized finance for low income groups. A market oriented window would run the risk of competing unfairly with the very housing finance institutions A.I.D.'s program is seeking to promote.

There may be a case for HBFC staying out of subsidized programs altogether (as was probably the intent of the World Bank conditions, although the Bank did give support to the implementation of the ADB recommendations which do permit the possibility of subsidized finance) and becoming one of the housing finance companies to be promoted by the GOP policy reforms.

The case for a purely market oriented HBFC is as follows. There is only one organization with any, albeit imperfect, experience with housing finance: HBFC. HBFC is indeed unprofitable (partly because it has been forced into non-viable "social programs") and it has no experience of

1/ Bertrand Renaud, Housing and Financial Institutions in Developing Countries, p.104.

raising deposits or selling bonds. Its management may need strengthening and its collections records may be poor. But HBFC does have the experience of making tens of thousands of loans, some of them commercial, in the housing sector. The only other potential housing finance institution (the PICIC proposal) has no experience with the unique characteristics of housing sector borrowing and lending operations. Other institutions that have tried housing finance, the commercial banks, have not made significant inroads into the market, despite their excess liquidity.

It might be claimed that HBFC would compete unfairly with the HFCs because of its access to Government credit. However, according to the agreement with the IMF, sectoral credit allocations are to be eliminated. And the PICIC proposal also requests special Government support: SBP guarantees, as well as an immediate line of credit from IFC.

The initial public support for the first proposal for a housing finance institution is not unreasonable. Support will be required to build up public confidence. HBFC could be gradually transformed into a market oriented mortgage bank or mutual society and attract private ownership.

As a current member of Pakistan's financial sector, which is about to be liberalized, HBFC should probably not be asked to limit itself to low income, subsidized finance. It would probably also be unwise to add to HBFC's management problems by asking it to operate two windows. According to its chairman, HBFC's experience to date of two windows has not been good; clear separation of the two activities has not been possible.

The best policy, in the context of financial liberalization and integration, would probably be to make market lending operations quite separate from subsidized low income housing. Low income housing that does require subsidies should be made the clear and distinct responsibility of federal and provincial governments, probably under policies formulated by the National Housing Authority. HBFC should not be given responsibility for subsidized programs, nor should the institution proposed by PICIC, even though it has included low income programs in its proposal.

HBFC could be one of the first two market oriented housing finance institutions. As such, HBFC and PICIC's Housing Finance Corporation will initially find it profitable to aim fairly high up the market, at least above the 40th percentile. For them to have that target will begin to establish that housing finance is a profitable activity, which will in turn attract new entrants. It may be possible for HBFC, the corporation and others to have fully profitable home improvement loan programs that would be attractive to low income groups that are outside subsidized government programs. Gradually the competing institutions will move down market, in a financially viable manner.

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### 3.1.3 Structural Adjustment of the Financial Sector

The GOP is currently developing reform policies designed to liberalize the financial sector.1/ The key reform areas are:

- o revision of government debt management policies in order to introduce a greater role for market rates;
- o revision of interest rate and directed credit policies as pa of a gradual move towards dismantling of credit ceilings;
- o improvement in bank supervision, bank restructuring, and deb recovery; and
- o increased autonomy, accountability, and competition in the banking system;

These reforms are, indeed, major transitions for Pakistan. Financial sector liberalization will generally impact housing finance po in a number of ways, including the role of the NCB's, interest rate structure, and reformulation of monetary policy away from directed credi and toward a market oriented system. Several of the detailed steps, however, will have direct and immediate impact on the Policy Action Plan proposed here, especially with regard to bank supervision, debt recovery and the role of the SBP.

Because of their importance to the housing finance Policy Action Plan several specific reforms and their implications for the program are summarized in Figure 4. The Working Group on Housing Finance will coordinate its recommendations and actions with those of the GOP working groups assembled to implement the FSAL reforms.

### 3.1.4 Other Issues in the Development of Housing Finance

#### 3.1.4.1 Constraints and Incentives

A number of constraints and incentives for the development of a housing finance system have been identified, some unique to Pakistan and others with worldwide relevance to public confidence and resource mobilization.

1/ These reforms are being designed in conjunction with the World Bank and the IMF under the Financial Sector Adjustment Loan. Refer to Sections 2.2.1, 2.2.6, and Annex 15, which provides a summary of the major steps.

Figure 5

SELECTED AGREEMENTS OF THE FINANCIAL SECTOR ADJUSTMENT LOAN AND RELATIONSHIP TO POLICY ACTION PLAN

| FSAL Area of Agreement | Specific FSAL Reforms | Implication for Policy Action Plan |
|---|---|---|
| I. Strengthening SBP | 1. Unify supervision of financial institutions under SBP. | This policy is in accordance wtih the recommendations of the Policy Action Plan. |
| | 2. Set up a subsidiary of SBP to supervise modarabas, leasing companies and new investment banks. | This step appears to isolate certain private sector companies. Regulation of NBFIs and the consolidation effort under SBP needs to be carefully studied; bank and non-bank HFCs should be treated uniformly. |
| | 3. Review of SBP organization with a view to strengthening and increasing autonomy. | This is in accordance with the plan for consolidating under a strengthened SBP. |
| | 4. Establish a Credit Bureau. | Analysis of bank portfolios and publication of results for assistance in risk assessment; this could ultimately help HFCs as well as NCBs. |
| Improved System for Debt Recovery | 1. Improved procedures (Special Courts; legislation departments). | In accordance with goals to restore public confidence, and improve debt recovery. |
| | 2. Program to recover arrears on publicly guaranteed debt and arrears of private lenders. | Foreclosure is a special component of this, with crucial importance to mortgage lending. A subcommittee to the Working Group on Housing Finance on Foreclosure is recommended. |
| | 3. Increased numbers of Banking Tribunals | Special Banking Tribunals for Foreclosure may be recommended. |
| Privatization of Financial Institutions | 1. Two private investment banks to be selected now. | This is in accordance with policies to stimulate the involvement of the private sector. |
| | 2. Disinvestment of NCBs, up to 20 percent initially. | This is in accordance with policies to introduce increased competition and private resources into banking. |
| | 3. Strategy for allowing private banks, including graduation of investment banks, into full-fledged banks. | HFCs may also graduate from NBFIs to banks. The regulations must accommodate this shift. |
| | 4. Policy to allow HBFC to become a profitable, efficient organization. | HBFC's future role is under discussion. (See Section 3.1.2.3) Must coordinate this effort with those to eliminate the competition of publicly-owned institutions with HFCs and rationalization of GOP shelter policy. |
| | 5. Phase out of automatic SBP credit lines to PICIC, and other DFIs and parastatals. | Review in conjunction with PICIC role in proposed HFC. PICIC has requested a line of credit for the Housing Finance Corporation. This policy reform excludes only automatic lines of credit. |

Loan delinquency and foreclosure are major problems in Pakistan. The HBFC, for example, has an enormous amount of past due loans.1/ Part of the problem may be administrative, that is, timely recognition and response. HBFC has recently instituted two reforms: an improved collection system (with Muslim Commercial Bank) and mortgage insurance for the "partner" (or guarantor, if the guarantor's income was used to guarantee the partner).

Improved administrative procedures and mortgage insurance are not solutions to lack of effective foreclosure, however. Lack of foreclosure contributes to payment abuse and undermines administrative reforms.2/ An effective legal system is crucial to the operation of a financial system. Even though Special Banking Tribunals have been established, shortages of judges and lawyers have limited the effectiveness of these tribunals.3/

As noted above, debt collection is a topic under the FSAL and foreclosure should be considered as one aspect of the broader reforms. The Working Group on Housing Finance may consider establishing a special subcommittee on foreclosure, including legal experts and representatives of the tribunals, to develop solutions specific to housing.

Deposit insurance is another policy quite common in developed country financial markets. In Pakistan, however, there is an implied insurance scheme for the NCBs, rather than an explicit guarantee and funding mechanism.4/ The Bank Nationalization Act included a provision that all depositors were fully guaranteed by the federal government.

Deposit insurance has now proved to be a mixed blessing in the U.S. It is clear that a major "moral hazard" problem can only be avoided if the regulatory function is thorough and effective. If not, weak institutions undertake risky lending for their survival because they do not have to face angry depositors (especially under full guarantee).

1/ USL International.

2/ The idea of GOP-provided mortgage "insurance", applicable for failure to foreclose after nonpayment because of abuse as well as death, does not seem warranted. It raises problems of moral hazard (HFCs would simply collect from the GOP), dilutes pressures to improve foreclosure procedures, and might be extremely expensive.

3/ Financial Sector Review, World Bank, Volume II.

4/ ibid.

The issue of deposit insurance in Pakistan should be addressed for all deposit-taking institutions. There are a number of issues involved. First, with regard to the NCBs, the GOP charges no risk premium for its implicit guarantee and it is therefore underfunded. Second, as the NCBs are gradually privatized and as private sector institutions such as the investment companies or, in the future, the HFCs, evolve into deposit-taking institutions, no provisions for insurance now exist. This would put them at a distinct disadvantage with banks that remain government owned. Although it is not clear whether a deposit insurance system is warranted at present, at least treatment of institutions should be uniform. Finally, if a deposit insurance system were to be created, problems of moral hazard would increase as privatization went forward. The World Bank has suggested a review of this issue and the Working Group on Housing Finance should collaborate.

Effective procedures for restructuring insolvent banks is another issue that can have major impact on public confidence. The NCBs, and HBFC as well, are not assumed to be allowed to "fail". However, HBFC is technically bankrupt because of non-performing loans. Recommendations for improved roles for both non-performing loans and capital adequacy are needed for all financial institutions; again, the need will become greater as the system has more private sector involvement. These reforms and decisions regarding restructuring HBFC (and other organizations in the future) should also be an agenda item for donor/GOP cooperation.

Finally, the role of an apex housing bank is an issue explicitly raised by the ADB. This institution would assume the role of "banker" to the housing finance sector and would mobilize funds on a wholesale scale. At the present time in Pakistan, this recommendation seems somewhat premature. It is an issue that needs to be discussed, however, since numerous countries have found it desirable to establish such apex institutions. The National Housing Bank of India has been recently chartered, for example, under a similar financial system of directed credit tempered by increasing privatization and privately capitalized institutions. Apex banks can offer lines of credit; technical assistance in numerous areas, including development of flexible mortgage instruments; well-focused supervision; and system-wide research and analysis. Apex banks may assist the housing finance sector access insurance and/or pension funds. Under centrally directed systems, governments often require life insurance companies and pension funds to earmark some portion of their funds for housing. While this does indeed increase the flow of resources into housing finance, it raises difficult issues. For example, the cost of resources is generally higher than the return provided and the implicit subsidies are not adequately studied. Moreover, mandatory allocations may not be consistent with current liberalization procedures in Pakistan.

The Working Group on Housing Finance will discuss these issues with the SBP; it is anticipated at present that SBP will assume some or all of the roles of an apex institution.

### 3.1.4.2 Islamization of the Banking System

Since 1979, GOP has been undertaking reforms to bring Pakistan's financial system closer in line to Islamic principles.1/ These changes essentially shift transactions from an interest bearing basis, for both deposits and loans, to a profit and loss sharing basis (PLS), essentially equity participation. The operations of certain NBFIs were first to be reoriented, including HBFC, and subsequently new financial instruments were introduced and PLS was extended to the NCBs. There are a variety of lending mechanisms, including term finance certificates; modarabas (conceptually an investment fund for which resources are obtained through sale of certificates); musharikas (temporary partnerships for providing working capital requirements); leasing and hire purchase (also for financing fixed industrial investment); lending with a service charge; and mark-up lending. In view of the difficulty of establishing non-interest based instruments for financing deficits, government borrowing continues on a interest-based approach. However, the provision of SBP finance to banks is on a PLS or mark-up basis.

Overall, Islamization is considered to have a positive and liberalizing effect on the system. The financial instruments created under the new system have probably facilitated financial deepening; also, some deregulation has occurred which allowed market forces a greater role.2/

The impact of Islamization on modes of lending for housing finance is not yet entirely clear. Since 1979, all of HBFC's new lending has been converted to a non-loan (PLS) basis. Under this mode, HBFC becomes a co-owner of the real estate rather than a lender charging interest. HBFC charges no fees during the construction period and is paid a proportion of an imputed rental income to reduce equity after construction is completed. HBFC, as co-owner, shares proportionally in capital gains.3/ HBFC began simplifying its system in 1987 and has now actuarially worked out a system with 180 equal installments.

Utilization of the PLS method for real estate lending has, however, met with problems by other actual or potential lenders. Essentially, the calculation of the value of the investment, needed in order to determine capital gains, makes the PLS approach difficult in this context. The NCBs recently dropped the PLS formula for real estate lending because of its complications; clients were disputing the method of calculation of investment. The NCBs now lend on a mark-up basis, based on a reducing balance method of calculating rate and utilize equal payments over the life of the loan. The PICIC proposal also advocates the mark-up basis. Finally,

1/ This section draws on Pakistan: Recent Economic Developments, International Monetary Fund, December 19, 1988, Appendix V.
2/ Financial Sector Review, Volume II.
3/ Pakistan: Recent Economic Developments, December 19, 1988 and USL International.

the ADB has recommended to HBFC that the mark-up basis, or even a leasing system, are preferable to PLS.1/ The ADB's argument is that the rate of return must be based on the costs and profits of HBFC and not those of the borrower.

In summary, the major problems of PLS for real estate lending are: (1) ascertaining the value of the house, and therefore the capital gain at the end of the lending period, and (2) determining what refinancing options should be employed if, at the end of the term, the borrower does not want to move but cannot pay the lender his share of the capital gain without additional borrowing. Clearly, the nature of the real estate market long-term appreciation, market specific idiosyncracies and the consumption as well as investment nature of housing, all exacerbate the problem.

## 3.2 The Economic Effects of the HG Program

The policy reforms associated with the HG program will have an important impact on the development of the financial sector and in meeting housing sector goals.

### 3.2.1 Financial Sector

Pakistan faces a serious resource mobilization problem. Savings are low at a time when the need for domestic resources is growing.

Formal savings and investment rates are so low that the country risks consuming existing public and private capital. This will result in reduced rates of economic growth in the future. The investment rate of 17 percent for FY86 was much lower than the average for low income countries of 25 percent. The formal savings rate of 5 to 10 percent in recent years is well below the low income country average of 23 percent.

The growing trade deficit, increased debt servicing requirements and falling levels of donor assistance are forcing the Government to draw down reserves and resort to short-term borrowing. The budget deficit is about 8 percent of GDP and domestic debt is growing at a rapid 20 percent per annum, with domestic interest payments rising by 27 percent per annum. Most of the debt is being financed by non-bank borrowing, now 34 percent of GDP, which is diverting resources from the private investment required to generate economic growth.

To encourage better domestic resource mobilization, the Government is committed to the development of market-oriented financial institutions. A market-oriented financial system would mobilize and enhance savings by providing savers with financial assets that are more convenient to hold, and less risky and more liquid than the underlying real assets. The system would assist in the allocation of the resources provided by savers into higher yielding investments. The financial system would therefore enhance growth by increasing the savings ratio and reducing the capital to output ratio.

1/ ADB Consultant Report, Paper 3.

Housing finance has a very important role to play in such a financial system.1/ Housing is important as an investment as well as consumption good, and it is a significant source of savings. It is usually the largest single form of household wealth and accounts for between one quarter and one half of the capital stock in most developing countries. Housing finance corporations and building societies that do not depend upon directed credit as their source of funds can be major depositories of personal savings; for example, UK building society deposits represent over a third of all savings; the figure for US savings and loans is about one quarter. Housing finance institutions in developing countries have proved to be able to mobilize most of their resources domestically and to be effective promoters of savings (much better than other types of development finance institutions). Housing finance institutions have also proved to be effective in reducing the borrowing governments' contingent liabilities.

The housing finance system in Pakistan has not performed well. Housing investment typically contributes 3 to 8 percent to GNP; in Pakistan the contribution has fallen from 4.8 percent in 1960/61 to 2.7 percent in 1986/87. By comparison even the proportion for India, which has also pursued policies that have suppressed housing demand, is 3.4 percent. Housing as a proportion of gross capital formation is typically 18 to 25 percent; the proportion is only 9 percent in Pakistan. There is now very little financial intermediation in the housing sector in Pakistan. There is virtually no savings mobilization for housing by formal sector financial institutions directly from households. The financial institutions provide credit for only a very small proportion of the population.

A well designed, market oriented housing finance system could assist greatly in the mobilization of domestic resources. Housing is one of the safest assets in the economy. Financial institutions will become more stable if they are allowed to diversify their portfolios into housing. Saving for housing is particularly appealing to households in developing countries. House values keep pace with inflation and tend not to fluctuate and little financial sophistication is required to save through ownership of a house.

### 3.2.2 Shelter Sector

A broad based housing finance system is needed to assist in the achievement of shelter goals. The increase in the numbers of people per room or per housing unit over the past twenty years is indicative of the growing shelter crisis. Meeting the incremental demand for housing of about 270,000 new households each year will require improved access to credit as well as to land and infrastructure.

Considerable investment will be needed. The team of experts that prepared the 1986 National Housing Policy estimated that the annual cost of construction and land to accommodate increments in the urban population and contribute to the backlog in housing demand was Rs 28 billion. This

1/ For a more detailed analysis, see Annex 10, "The Role of Housing Finance in the Development of Pakistan's Financial Sector."

represents 31 percent of 1985's total investment, or 6 percent of GDP. Using a housing demand model, the ADB team estimated the 1988-89 financing need for all new housing to be Rs 15 billion. According to the report, only about one third could be provided by HBFC, the commercial banks, and cooperatives. The balance would have to come from remittances, personal savings, and informal borrowing.

The objective of the HG program is to introduce policy reforms that will encourage private and joint sector housing finance institutions to organize the financing of this substantial formal sector shortfall.

There are personal, informal savings that could be attracted to housing finance institutions. The ADB sponsored survey estimated that over 60 percent of the finance required for land and housing is funded from the personal savings and the liquidation of assets. Only 17 percent of the households surveyed obtained finance for housing from HBFC; none received any formal sector finance for land. It should be noted that this survey under represented the lowest quartile of the household income distribution. They probably provide all their own financing from personal sources. The survey also found considerable willingness to participate in savings and loan schemes.

### 3.2.3 Other Impacts

Considering Pakistan's good record of economic growth and its ability and potential for economic reform, the GOP should have the capacity to service the $100 million HG loan. The Country Risk Analysis prepared for the PID (see Annex 8) reflects current economic conditions.

Through its impact on resource mobilization and shelter sector investment, the policy reforms associated with the HG loan will have an impact on the housing and construction sectors. Construction employment will grow even more rapidly than in the past. According to the 1980 census, there are 1.5 million workers in the construction sector (4.9 percent of the labor force), of which 655,000 are in house building. This part of the workforce has been growing at about 5 percent per annum during the 1980s.

Through interindustry linkages, investment in construction will generate growth in other sectors. The ADB consultants estimated that Rs 1 million investment in building construction would result in an increase in final demand of Rs 2.6 million.

## 3.3 Environmental Considerations

The PID approval cable requests USAID/Pakistan to address the environmental aspects of GOP shelter programs. The Mission was urged to pay attention to "host country environmental protection procedures to ensure that environmental considerations are being adequately addressed in the implementation of housing sector programs". This could include "supporting institutional capability of relevant host country institutions to conduct appropriate environmental reviews of proposed low-income shelter programs, including associated basic infrastructure". The Initial Environment Examination (IEE) has been approved (see Annex 16).

### 3.3.1 Environmental Impacts Associated with Human Settlements

Environmental impacts to be considered in association with human settlements, and in particular low-income housing, can be divided into two broad classes.

First are impacts upon the residents of the settlement themselves. These are most often manifested as health related problems, and can usually be linked to often inter-related causes, including:

- o inadequate waste collection and disposal;
- o inadequate drainage; and
- o inadequate and/or contaminated drinking water.

Another type of environmental problem of this first class can arise from the siting of these settlements. Since in many cases low-income settlements are located on marginal, ie., inexpensive land, the location can expose residents to pollution and toxic substances from industries, waste dumps, and major transportation infrastructure.

The second class of environmental consequence are not felt so much by the residents as by the larger public as a whole. These impacts are caused by settlements and include: degradation of water supplies; loss of arable land; subsidence and related problems resulting from depletion of groundwater supplies; and, flooding and drainage problems due to reduced surface infiltration of rainwater and construction in floodplains and drainage channels.

While the impact upon a single individual may not be as great as under the first type of environmental consequence, the cumulative impact upon the public as a whole can be quite large. Some types of impacts, such as degradation of water supplies, affect both the responsible individual directly, and the larger public.

The Environment and Urban Affairs Division of the Ministry of Housing and Works is primarily concerned with the second type of impact, and most importantly with the question of water quality. Annex 12 provides detailed information about environmental conditions in urban areas of Pakistan.

### 3.3.2 Environmental Protection Regulations

An environmental protection ordinance was passed in 1983, the fundamental objective of which was to "provide for the control of pollution and preserve the living environment". The Ordinance provided for the creation of a Pakistan Environmental Protection Council and a Pakistan Environmental Protection Agency, which will implement the objectives of the act.

During the Seventh Plan period the following actions are planned:

- o Environmental Protection Agencies will be opened at the provincial level;

- all public sector projects which are submitted for processing will be required to explicitly state the impact the project is likely to have on the natural environment; and

- general as well as sector-specific guidelines will be prepared for the sponsoring agencies, to enable them to prepare an environmental impact statement.

Although GOP shelter programs consider environmental issues, actual environmental impact assessments are not normally conducted. Environmental issues are addressed at the sectoral level, rather than on a project-by-project basis.

The environmental nature of katchi abadi improvement programs that stress water supply and sanitation provision will be continued. A GOP emphasis is on potable water quality and sewage disposal/treatment. The GOP is investigating alternatives to traditional methods that require high capital and maintenance costs, such as "indigenous" technologies, including pour-flush latrines and primary treatment of wastes using aerobic lagoons.

### 3.3.3 Response to Environmental Issues in the Shelter Sector

The most pressing environmental issues associated with low-cost shelter development in Pakistan are clearly the related problems of waste disposal and domestic water quality. The evolution of GOP policy in the areas of infrastructure standards and the adoption of user fees is supported by A.I.D. Not only do both these relate to environmental problems associated with shelter, but their adoption would support the key objective of the Program - to establish a market-oriented housing finance system.

A covenant in the Implementation Agreement will support the continued GOP implementation of the Environmental Protection Ordinance. In addition, as part of the technical assistance provided under the Program, an assessment of specific assistance to environmental issues will be made. Such assistance could be offered in concert with that provided under the proposed ADB water and sanitation program.

## 3.4 Social Soundness

Pakistan's population has been growing rapidly: in rural areas at the rate of 2.3 percent, while urban population is growing at 4.4 percent. In certain urban slum areas the rate is double the average urban growth rate. Such high urban population growth is the result of high natural population growth rates, compounded by migration from rural to urban areas by families seeking economic opportunity. By 1981, the urban population of 24 million totaled 28 percent of Pakistan's total population and the proportion is continuing to rise to 36 percent by 2000.

The consequence of these demographics in terms of housing needs are great. In addition to the requirement to improve the living conditions of existing households, there is also a need to accommodate newly formed households which in urban areas alone are increasing at an estimated rate of about 140,000 per year.

Quite often the residents of Katchi Abadis rely on community participation to organize and implement improvement projects, as they are only now receiving assistance from governmental entities. In some cases, such as the Orangi Pilot Project in Karachi, this approach has been very successful. Even so, without access to formal credit the residents have no option but to capitalize their physical assets or borrow money from informal sources at high rates of interest. Neither approach is economically efficient nor socially sound.

The ultimate direct beneficiaries of the proposed Program are thus those households who will be able to improve their living conditions by participating in a market oriented shelter finance system. The growth in loans for shelter is expected to bring significant numbers of low income families into the formal shelter finance system. These families will be able to obtain loans for new plot purchase, for building materials for home improvements and additions, and for new house construction. These families will become the client group of a housing finance system in which private finance companies provide long-term financing for housing.

In addition, low-income households will directly benefit from the Program by improvements in the Katchi Abadis and other under-serviced urban areas. The work that will be undertaken with local currency includes provision of water and sewerage services, street paving, drainage, and other environmental improvements.

The Program's technical assistance and training will also directly contribute to improvements in shelter conditions. Several research and study topics will address some of the obstacles to infrastructure provision, and how the structure of loans can better serve Katchi Abadi residents and new plot owners.

## 3.5 Program Impact on Women

The position and role of women in Pakistan is complex, and changing. Although under traditional Islamic laws discrimination against women with regard to property rights, inheritance rights, etc., is justified, there are no overt civil housing-specific discriminatory laws against women. However, it is perhaps significant that the (draft) National Housing Policy nowhere discusses women's needs, requirements, or access to shelter. This is in contrast with India's recently adopted policy that identifies widows, single women, and women-headed households among the "priority groups" to be provided access to shelter.

Legally, women are entitled to own or rent any housing; however, social practices may differ from civil law, making it difficult for single or widowed working women to access housing finance. Civil laws relating to inheritance and attestation are primarily Islamic in nature. Though subject to exceptions, women generally inherit only half the inheritance of their male counterparts, thereby making it more difficult to assemble required collateral for housing finance.

The Program proposed here cannot directly address the underlying causes of these problems, but it can ensure that women, whether married or not, have equal access to the benefits of the Program. As noted above, there is no overt evidence that institutions - and primarily HBFC - discriminate against women in determining credit eligibility. Nevertheless, the Policy Action Plan includes a provision that addresses these issues in the establishment of a nationwide market-oriented housing finance system. Specifically, regulatory laws pertaining to the system should mandate that: a woman's (wife's) income will be considered in determining credit eligibility; the option of joint titling of the property is offered, and that the woman, if widowed, is thus entitled to full inheritance of the property as stated in the title Documents; and, that single women are eligible to apply for mortgages and that if granted the loan, the title to the property would be in their name.

# 4. PROGRAM IMPLEMENTATION, MONITORING, AND EVALUATION

## 4.1 Implementation Strategy

Implementation of the Shelter Resource Mobilization Program will be carried out by the Ministry of Finance, Internal Finance Wing, under the guidance of the Working Group on Housing Finance. They will coordinate and monitor the necessary actions of other Ministry of Finance offices as well as the SBP, the Ministries of Planning and Housing, and the National Housing Authority. Assistance to the Internal Finance Wing will be provided by the Grant-funded resident advisor as well as the short-term analytic and institutional technical consultancies. A.I.D. management will be provided by RHUDO/Asia and a Mission contractor or direct hire who will maintain the necessary sustained dialogue on the Policy Action Plan. The following sections detail the plans and requirements for the Program Agreements, A.I.D.'s management and the Program implementation schedule. Figure 3 in Section 2.3.2.2 presents the implementation schedule as it relates to the Policy Action Plan.

## 4.2 Conditions and Covenants

### 4.2.1 Housing Guaranty Conditions

In addition to the standard conditions precedent to A.I.D.'s guaranty of a disbursement, the GOP prior to initial investor selection shall inform A.I.D. that the Working Group on Housing Finance has been formed and that its responsibilities to promote and oversee the development of a market-oriented shelter finance system are established. The GOP shall inform A.I.D. as to its agreement with the Policy Action Plan (PAP) for the first tranche of the HG Program, as well as the annual review process which will indicate progress made on activities of the Policy Action Plan and set new Action Plan activities. The GOP shall also present for approval by A.I.D. Eligible Expenditures from the Pre-qualified Programs in the amount of local currency equivalent to the dollar amount of the HG loan to be contracted, unless otherwise agreed to by A.I.D. The GOP agreement to each negotiated PAP will allow subsequent loan authorizations.

### 4.2.2 Program Covenants

In addition to general covenants common to HG projects, the GOP will be asked to covenant the following concerns:

- GOP policy will support the role of the private sector in realizing its economic and social development strategies.
- GOP will accord to the Working Group on Housing Finance the continued responsibility to promote and coordinate efforts to create a market-oriented shelter finance system.

- o GOP policy to implement the Environmental Protection Ordinance of 1983 will continue and sector specific guidelines will be prepared.

## 4.3 A.I.D. Management

Management and administration of the program will be the responsibility of RHUDO/Asia and will be accomplished through periodic visits coordinated with USAID/Pakistan. RHUDO/Asia will discuss progress on Policy Action Plan activities with public and private sector counterpart entities in Pakistan. RHUDO will serve as USAID/Pakistan's technical support office for shelter finance by coordinating with the Mission on policy issues and briefing the Mission on program progress. RHUDO will also undertake the necessary policy reviews as well as expenditure verification analyses needed to justify subsequent HG authorizations and A.I.D. guaranteed borrowings by the GOP pursuant to the PP and Program Implementation Agreement. The Mission has designated the Program Office (PRO) as the Mission's liaison with RHUDO/Asia for this program.

To manage this responsibility, a full-time contractor or direct hire Shelter Finance System Advisor will be required in the Mission's Program Office. PRO and the Advisor will help coordinate the TA/training component of the Program as well as identify policy development and technical assistance needs and monitor and support the annual Policy Action Plan activities. In addition, a long-term advisor will work with the Ministry of Finance and the State Bank of Pakistan to provide and manage the technical assistance and training activities, as well as advise RHUDO and the Mission on HG-related policy negotiations and expenditure reviews with the GOP. These advisors will be supported by the RHUDO staff on TDY from Bangkok and by PRE/H backstopping as necessary.

Preparation of the HG Program Implementation Agreement will be the responsibility of RHUDO/Asia and GC/PRE. A separate Project Agreement will be prepared by the Mission for the TA/training grant and committed at the time of the HG authorization. The Implementation Agreement will be submitted for Mission approval and signature by the Mission Director or Ambassador. Approval of GOP borrowings under this agreement will be the responsibility of RHUDO in consultation with the Mission.

## 4.4 Program Monitoring and Evaluation

The Program's primary monitoring and evaluation objectives are:

- o to support and facilitate the GOP's demonstrated commitment to advance their financial and shelter sector policy objectives; and,
- o to ensure that the proposed HG assistance complies with the Foreign Assistance Act (FAA) affordability criteria.

4.4.1 Monitoring Requirements

The information gained as a result of monitoring will benefit the the GOP implementing institutions, the HG Program's managers at USAID/Pakistan and RHUDO/Asia, the Office of Housing and Urban Programs (PRE/H), and Bureau for Asia and Near East (ANE).

Monitoring is an ongoing process that will take place during program implementation. Annual evaluations will formally measure progress on PAP activities. The ultimate success of the Program is predicated upon achieving selected objectives contained in the PAP, developed during negotiations with the GOP during the initial stage of the Program. Local currency expenditures will also be monitored.

A specific goal for the Program is that the Policy Action Plan ultimately results in greater development of shelter for low-income urban households by market-oriented housing finance companies. While the extent of any such linkage during the early years of the Program is likely to be low, information will be particularly sought in later years that provides evidence that such an outcome is taking place. At that point, local currency disbursements could be directly linked to developments shown to have resulted from the Policy Action Plan.

Each of the Program's principal objectives has specific actions associated with them in the PAP. A Management Information System will be concerned with the benchmarks component under each PAP action. These benchmarks are evidence that the required actions were successfully undertaken, and their completion will be the manager's primary indication that the project objectives are being met.

The nature of the benchmarks indicates that a variety of sources and methods for collecting the required data will be necessary. Among these will be:

1. Administrative records of the counterpart agencies;

2. Reports identified in the PAP

3. Records of A.I.D. Program staff; and,

4. Interviews and other survey techniques.

The key partners in the policy dialogue process include the Ministries of Finance, Planning and Development, and Housing and Works, the NHA, HBFC, and the State Bank of Pakistan. Program monitoring may engage all these entities, and will involve short-term technical assistance designed to advance the policy agenda. The long-term advisor in the Ministry of Finance will be responsible for insuring GOP participation in required information submittals and evaluations. The Shelter Finance

Advisor within USAID/Pakistan will track and manage the information relating to the benchmarks. A file will also be maintained to manage information pertaining to the local currency component of the program. The file will record eligible host-country shelter expenditures against which the HG related local currency may be attributed. The component of the Program involving eligible expenditures may involve a variety of governmental entities at provincial and local levels to verify reports, but will be coordinated through the Working Group for Housing Finance.

4.4.2 Evaluation Requirements

Policy Impact Evaluations (PIEs) are expected to begin approximately a year after the first project authorization, and thereafter precede subsequent authorizations. An approximate timetable for the PIEs follows:

| | | | | |
|---|---|---|---|---|
| #1 - | Fourth | Quarter | U.S. | FY 1990 |
| #2 - | " | " | " | 1991 |
| #3 - | " | " | " | 1992 |
| #4 - | " | " | " | 1993 |

Policy Impact Evaluations will be the overall responsibility of RHUDO/Asia in coordination with the USAID/Pakistan's Shelter Finance Advisor and local short-term consultants. The nature of the PIE is primarily an interim, internal assessment of discrete objectives. It is intended to determine the progress made on the benchmarks associated with the Policy Action Plan since the last PIE. Subsequent authorizations and their associated detailed Policy Action Plans will be based on the results of each PIE.

The final evaluation should take place within six months of the final project disbursement, in approximately the fourth quarter of FY 1994.

The final evaluation will be the overall responsibility of RHUDO/Asia, acting on behalf of USAID/Pakistan. The final evaluation will be conducted by a contract team from the United States, assisted as needed by local consultants. The purpose of the final evaluation will be to determine the overall results of the HG program. In particular, the evaluation will seek to determine the impacts of the PAP in relationship to the Program's original goal and objectives. Where possible, links will be illustrated between sectoral improvements and the completed PAP items.

Information required for evaluation will be gained from data supplied by the Ministry-based advisor and short-term consultants on TA assignments. Information useful to the evaluation could be:

a. A complete list of benchmarks by policy objective, and specific actions required to achieve the benchmarks;

b. List of parties, keyed through responsibility for the achievement of each benchmark;

c. Benchmark dates, as agreed by GOP negotiations;

d. Precedent and subsequent benchmarks (if any);

e. Notes on progress (lack thereof) towards achievement of benchmarks; and,

f. Benchmark completion check-off.

4.5 Borrowing Procedures and Program Agreements

Pursuant to approval of this Project Paper, A.I.D. will authorize a $25 million loan guaranty and send a Letter of Advice to the GOP and the Ministry of Finance, the Program Borrower. A Program Implementation Agreement will then be negotiated and signed with the MOF and, after all Conditions Precedent have been met, the MOF or its approved designee, will seek a U.S. investor. The MOF will seek A.I.D. guidance on the best time to enter the U.S. capital market and inform the Office of Housing of the timing and preferred conditions of its borrowing. The Office of Housing will facilitate the process, and will encourage U.S. lenders to participate in the program.

Once the eligible expenditures have been approved in accordance with the Implementation Agreement (IA), the Ministry of Finance would execute each of the borrowings on behalf of the GOP. Each borrowing would take place in the U.S. capital market. The MOF, representing the GOP, would competitively select a U.S. financial institution. This institution (the Lender) and the MOF would enter into a Loan Agreement. Upon signing, the Lender would disburse the loan in full based upon the Eligible Expenditures approved by A.I.D., and/or as an advance to be liquidated by Eligible Expenditures before the next disbursement. The A.I.D. Guaranty specifies that the "full faith and credit" of the U.S. Government assures the full and timely payment of all amounts due to the Lender. The loan terms usually include a 30 year repayment period, including 10 years grace on repayment of principal, with rates lower than a commercial loan for an equivalent term. The actual rate will depend on capital market conditions in the U.S. at the time of the borrowing.

The MOF would pay A.I.D. a one (1) per cent disbursement fee at the time of the borrowing, which may be financed from the proceeds of the loan, and would repay the U.S. dollar loan according to the terms of the Loan Agreement. Dollar repayment would be made to a Paying and Transfer Agent, currently Riggs National Bank of Washington, D.C., along with the A.I.D. guaranty fee of 0.5 per cent per annum on the outstanding principal of the loan. The Paying and Transfer Agent would arrange for the correct payment to the Lender and A.I.D. on behalf of the GOP.

The GOP executing agency for the **Grant Agreement** to finance the technical assistance and training component of the HG Program would be the MOF. As stated above, the MOF would also be the executing Ministry for the HG borrowing, on behalf of the GOP.

The agreements or contracts to be executed in conjunction with the HG loan and associated Grant include:

1. The **Technical Assistance and Training Project Grant Agreement** between A.I.D. and the GOP.

2. The **Housing Guaranty Implementation Agreement** between USAID and the GOP, specifying the procedures for borrowing, the programs/projects pre-qualified for rupee equivalent expenditures, and the Policy Action Plan.

3. The **Loan Agreement** between the GOP and the U.S. Lender, stating the terms of the U.S. guaranty.

4. The **Contract of Guaranty** between A.I.D. and the Lender stating the terms of the U.S. guaranty.

5. The **Host Country Guaranty** between the GOP and A.I.D. providing for an indemnity to A.I.D. in the event A.I.D. has to make repayments on behalf of the Borrower.

6. A **Paying and Transfer Agency Agreement** between the Riggs National Bank of Washington, D.C. and the GOP for servicing the loan.

## 5. Financial Plan

### 5.1 Financing the Program

The program will be financed by the following institutions:

a. The U.S. Lender(s), which will finance the $100 million of loans to the GOP Ministry of Finance.

b. MOF Internal Finance Wing, which will provide administrative and managerial support for the program's implementation.

c. SBP, which will also provide administrative support, and technical and regulatory input for the program.

d. The participating Housing Finance Companies, which will supply staff time, logistical support and other startup investment to promote the mobilization of household savings and subsequent lending;

e. Individual households will contribute savings and take loans from the housing finance system.

f. Various governmental bodies will be responsible for shelter projects that generate eligible expenditures for local currency attribution. Example: KMC for Katchi Abadi upgrading in Karachi.

g. A.I.D will provide resources to (a) guaranty the HG loan; (b) manage and administer the Program; (c) provide training and TA to the MOF, SBP, participating HFCs, and others involved with the establishment of national housing finance system; and (d) monitor and evaluate the Program

### 5.2 Cost of the Program

a. Housing Guaranty Loan: Over a five year period, the HG loans will provide $100 million in untied foreign exchange in consideration of policy reforms. The GOP will expend the local currency equivalent to the authorized HG loan amounts through their normal budgetary process.

b Long-Term Advisors: Two expatriate advisors will be contracted over the duration of the program (see 2.3.2.4). Both advisors will be required for the entire five year period. Costs per advisor are estimated at $150,000 per year.

Long-Term advisors $1,500,000
(10 person-years)

c. Short-Term Technical Assistance: Illustrative cost of the technical assistance program over the life of the program is as follows:

Technical Consultants

($280K/year) $1,400,000
Expatriate and local experts to prepare studies and analyses on economic, financial and regulatory issues; develop recommendations, guidelines, and strategy; both policy and technical topics.

Policy Seminars/Conferences

($50K/year) $250,000
Supports private and public sector worldwide seminars and conferences; sponsor national conferences and specific interest group policy events on relevant topics.

d. Training

($250K/year)

To address private and public sector issues in shelter finance system development, management and implementation:

| | |
|---|---|
| Policy oriented | $500,000 |
| Technical oriented | $750,000 |

e. Evaluations: To assist A.I.D. and RHUDO evaluate the policy agenda to permit new loan authorizations; to conduct a final evaluation of program:

| | |
|---|---|
| Short-term TA ($100K/year) | $400,000 |
| Final evaluation | $100,000 |

f. Logistical Support $100,000

Support to advisors and Mission to develop contracts, carry out administrative actions, and development materials as needed.

## Summary Cost Estimate and Financial Plan
(US $'000)

| | A.I.D. FX | A.I.D. LC | GOP LC | TOTAL |
|---|---|---|---|---|
| 1. Housing Guaranty loans | 100,000 | | 100,000 | 200,000 |
| 2. Advisors | 1,000 | 500 | | 1,500 |
| 3. Technical Assistance | 1,400 | 250 | | 1,650 |
| 4. Training | 800 | 450 | | 1,250 |
| 5. Evaluations | 400 | 100 | | 500 |
| 6. Logistical Support | | 100 | | 100 |
| TOTAL | 103,600 | 1,400 | 100,000 | 205,000 |

## Projection of Expenditure by Fiscal Year
(US$ '000)

| Fiscal Year | A.I.D. | GOP | HG |
|---|---|---|---|
| 1989 | 100 | - | - |
| 1990 | 870 | 25,000 | 25,000 |
| 1991 | 1,050 | 25,000 | 25,000 |
| 1992 | 1,120 | 20,000 | 20,000 |
| 1993 | 1,040 | 15,000 | 15,000 |
| 1994 | 820 | 15,000 | 15,000 |
| Total | 5,000 | 100,000 | 100,000 |

## Projection of A.I.D. Grant Expenditure by Types per Fiscal Year
(US$'000)

| | FY 1989 | FY 1990 | FY 1991 | FY 1992 | FY 1993 | FY 1994 | Total |
|---|---|---|---|---|---|---|---|
| Advisors | | 300 | 300 | 300 | 300 | 300 | 1,500 |
| Technical Assistance | 70 | 250 | 380 | 450 | 370 | 150 | 1,650 |
| Training | 30 | 200 | 250 | 250 | 250 | 250 | 1,250 |
| Evaluation | | 100 | 100 | 100 | 100 | 100 | 500 |
| Logistics | | 20 | 20 | 20 | 20 | 20 | 100 |
| Total: | 100 | 870 | 1,050 | 1,120 | 1,040 | 820 | 5,000 |

## 5.3 Procurement Plan

### 5.3.1 U.S. Consultants/Contractors

Two U.S. consultants will be hired to assist in program monitoring. One will work with the Office of Program to help coordinate the TA/training component of the Program as well as identify policy development and technical assistance and training needs and monitor and support the annual Policy Action Plan activities. The second will work with the Ministry of Finance and the State Bank of Pakistan to provide and manage the technical assistance and training activities. The consultant will also advise RHUDO and the Mission on the HG related policy negotiations and expenditure reviews with the GOP. Both positions will have a duration of 3 years with an additional two year option. These contracts will be fully competed. If they are PSC positions, the schedule for the acquisition of both is as follows (if the positions are filled by a firm, the Mission estimates 275 days to field the advisors):

| ACTION | ACTION OCCURING ON | NO. OF DAYS BETWEEN EACH ACTION |
|---|---|---|
| PIO/T fully-executed and submitted to the Contracting Officer* | Day 1 | |
| CBD and trade journal synopsis solicitation published | Day 15 | (15 days) |
| Solicitation Closing date | Day 60 | (45 days) |
| Evaluation results submitted to the Contracting Officer | Day 90 | (30 days) |
| Award Contract** | Day 120 | (30 days) |
| Consultant on board | Day 150 | (30 days) |

* The fully-executed PIO/T must have a contractable statement of work and well-reasoned technical evaluation criteria.

** Prior to award of a contract it may be desirable to interview the candidate and conduct past performance reference checks. Also, medical and security clearances will be necessary.

### 5.3.2 Short Term Technical Assistance

Short term expatriate and local advisors will be required to prepare studies and analysis on economic, financial and regulatory issues; develop recommendations, guidelines, and straegies on both policy and technical topics.

These short term advisors can be procured by (1) A.I.D./W through M/SER/OP administered Indefinite Quantity Contracts (IQC); (2) the Mission under small purchase procedures for procurements under $25,000; (3) Mission Technical Assistance Contract; and (4) the Mission under the A.I.D. Acquisition Regulation exception to full and open competition for overseas procurements under $100,000 (see AIDAR 706,302-70 (D)(2).

ANNEXES

Annex 1

UNCLASSIFIED

OUTGOING TELEGRAM

# Department of State

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ORIGIN AID-00

ORIGIN OFFICE ANPD-05
INFO AHEA-02 ANDP-03 ANSA-03 AHAF-04 AHRA-01 PPMS-01 SAST-01
PPR-01 GC-01 GCAN-02 AMIR-06 PRE-06 STAG-02 STFN-01
BAPF-01 BO-07 FPA-02 RELO-01 AMAD-01 HUD-02 /054 A0

INFO LOG-00 CIAE-00 EB-00 DODE-00 NEA-04 EAP-00 /044 R

DRAFTED BY: AID/ANE/PD/SA:HCBOTKIN:LUCI:3593N
APPROVED BY: AID/AA/ANE:CADELMAN
AID/ANE/PD/SA:TRISHOI (DRAFT) AID/ANE/PD/SA:VJEFFERS (DRAFT)
AID/ANE/PD:BODELL AID/ANE/PD:RFVENEZIA
AID/GC/ANE/R:MKITAY (DRAFT) AID/ANE/ENV:GWALEY (DRAFT)
AID/DAA/ANE:THREESE AID/ANE/DP/E:CHERMANN (DRAFT
AID/PRE/R VGELMAN (DRAFT)
AID/GC/PRE/RSONENTHAL (DRAFT)
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E.O. 12356: N/A
TAGS:
SUBJECT: PAKISTAN: SHELTER RESOURCES MOBILIZATION
PROGRAM (391-0587) (391-HG-001)

1. SUMMARY: PRC REVIEWED SUBJECT PID NOVEMBER 21. PID IS APPROVED. AA/ANE DELEGATES TO MISSION AUTHORITY TO AUTHORIZE PROJECT. AT THE END OF TWO YEARS, AN EVALUATION WILL BE REQUIRED PRIOR TO THE LAST TWO AUTHORIZATIONS. PID APPROVAL IS SUBJECT TO THE CONDITIONS AND GUIDANCE PROVIDED BELOW.

2. POLICY AGENDA: THE PID PROPOSES A HOUSING GUARANTEE LOAN OF DOLS 100.0 MILLION TO THE GOP DISBURSED OVER A FIVE-YEAR PERIOD IN RETURN FOR THE GOP UNDERTAKING POLICY AND INSTITUTIONAL REFORMS IN THE HOUSING SECTOR (HOUSING FINANCE SYSTEM). THIS IS A COMPLEX AND HIGHLY AMBITIOUS UNDERTAKING GIVEN PROBLEMS CURRENTLY FACING THE HOUSING SECTOR, A NEW GOVERNMENT, OTHER DONOR ACTIVITIES IN THIS SECTOR AND THE INHERENT POLITICAL AND BUREAUCRATIC SENSITIVITIES OF THE REFORMS NECESSARY TO MEET YOUR PROJECT OBJECTIVES.

DURING THE REVIEW PROCESS A NUMBER OF QUESTIONS WERE

RAISED WITH REGARD TO THE POLICY OBJECTIVES OF THE HG. THE POLICY AGENDA PRESENTED IN THE PID CONCENTRATES ON THE ANALYSES AND RECOMMENDATIONS WHICH ARE EXPECTED TO LEAD TO POLICY CHANGE. THE PRC EXPRESSED THE CONCERN THAT THE POLICY AGENDA NEEDS TO BE MORE EXPLICIT WITH RESPECT TO THE ACTUAL GOP POLICY AND INSTITUTIONAL REFORMS, WHICH ARE EXPECTED AS A RESULT OF THE PROGRAM. THE PP SHOULD BETTER DEFINE AND CLARIFY THE PROGRAM'S INTENT TO PRODUCE REAL POLICY CHANGE SUPPORTIVE OF ITS PURPOSE STATEMENT. THE GOP WILLINGNESS TO IMPLEMENT NECESSARY POLICY AND INSTITUTIONAL CHANGE WAS ALSO DISCUSSED AT SOME LENGTH. BEFORE PROCEEDING WITH THE AUTHORIZATION, THE GOP WILL HAVE TO AGREE TO THE OBJECTIVES OF THE PROGRAM. TO THE EXTENT SPECIFIC POLICY ACTIONS ARE IDENTIFIED, THE GOP SHOULD ALSO AGREE (AT LEAST IN PRINCIPLE) TO THEIR MODIFICATION/CHANGE,

STATE 409241 8234 084552 A

I.E., THE POLICY AGENDA. TO THIS END, MISSION SHOULD USE THE GOP'S QUOTE CONCEPT CLEARANCE UNQUOTE PROCESS TO OBTAIN THIS BROAD AGREEMENT.

WE CONCUR IN YOUR PROPOSAL TO ESTABLISH END OF PROGRAM OBJECTIVES AND THEN TO PHASE POLICY REFORM IMPLEMENTATION TOGETHER WITH CASH DISBURSEMENTS. ANNUAL NEGOTIATIONS WILL RESULT IN ANNUAL TARGETS WHICH ARE FAIRLY SPECIFIC AND WHERE POSSIBLE INCLUDE DATES FOR ACTIONS LIKE PHASING HBFC OUT OF MIDDLE INCOME HOUSING FINANCING OR CREATION/IMPLEMENTATION OF THE LEGAL/REGULATORY BASIS FOR ESTABLISHMENT OF PRIVATE HOUSING FINANCE INSTITUTIONS. THERE MUST, OF COURSE, BE FLEXIBILITY IN THE AGENDA AND SPECIFIC REFORM MAY ONLY BE AGREED TO ON AN ANNUAL BASIS. HOWEVER, THE PP SHOULD AT MINIMUM PRESENT A DESIRED END OF PROJECT STATUS (OBJECTIVES) WITH REGARD TO THE POLICY AND ADMINISTRATIVE ENVIRONMENT FOR HOUSING FINANCE AND THE SPECIFIC REFORM TARGETS FOR THE FIRST YEAR. THE BUREAU RECOGNIZES THE DIFFICULTIES AND SENSITIVITIES IN PREPARING A PROGRAM FOR THE PAKISTAN HOUSING SECTOR, THUS WE WOULD LIKE TO MAINTAIN OPEN COMMUNICATIONS WITH THE MISSION DURING THE DESIGN OF THE PROGRAM AND TO PROVIDE SUPPORT WHERE REQUESTED. TO THAT END, WE WOULD APPRECIATE YOUR SHARING THE MORE COMPLETE POLICY/INSTITUTIONAL AGENDA ON INFO BASIS AT APPROPRIATE POINT IN PROGRAM DESIGN PROCESS.

3. FUNDING LEVEL: THERE WAS DISCUSSION OF THE APPROPRIATE FUNDING LEVEL FOR THE PROGRAM. WILL DOLS 100.0 MILLION PROVIDE THE NECESSARY INCENTIVE TO MAKE THESE MAJOR REFORMS? WOULD LESS THAN DOLS 100.0 MILLION BE SUFFICIENT? THIS IS, OF COURSE, A JUDGMENT CALL BUT THE PP SHOULD EXPLAIN WHY YOU BELIEVE THE PROPOSED FUNDING LEVEL IS THE AMOUNT NEEDED TO ACHIEVE THE PROGRAM'S POLICY OBJECTIVES. SUPPORT FOR THIS LEVEL MAY INVOLVE INTER ALIA, ANALYSIS OF BUDGET EXPENDITURES IN THE HOUSING SECTOR, FUNDING FROM OTHER DONORS, IMPLICIT COST OF OVERCOMING ADMINISTRATIVE CONSTRAINTS, AND LENGTH OF TIME REQUIRED TO ACHIEVE MEANINGFUL AND IRREVERSIBLE SECTOR POLICY CHANGE.

4. PROGRAM (POLICY/SECTOR LEVEL) EVALUATION AND MONITORING: THE MISSION IS ENCOURAGED TO DEVELOP A PROGRAM INFORMATION BASE THAT WOULD UNDERPIN THE ANNUAL PROGRAM REVIEW AND NEGOTIATIONS LEADING TO DISBURSEMENT DECISIONS. THE ILLUSTRATIVE BENCHMARKS CITED IN THE PID CONSTITUTE ONE PART OF THIS BASE, ALTHOUGH SIMPLY STATING QUOTE PROCESS UNQUOTE STEPS IS PROBABLY NOT SUFFICIENT. A LIMITED NUMBER (EIGHT TO 12 MEASURES) OF KEY INDICATORS THAT WOULD DEMONSTRATE PROGRESS TOWARD PROGRAM OR SECTOR ASSISTANCE OBJECTIVES OVER TIME SHOULD BE DEVELOPED. FOR EXAMPLE, KEY INDICATORS MIGHT INCLUDE THE AMOUNT OF PRIVATE SECTOR LENDING FOR HOUSING CONSTRUCTION, THE TOTAL LEVEL OF GOP SUBSIDIES FOR SHELTER AND THE PERCENTAGE TARGETED FOR LOWER INCOME FAMILIES, AND MORTGAGE REPAYMENT RATES. THESE MEASURES MIGHT ALSO SERVE AS PROGRAM PERFORMANCE INDICATORS FOR THE MISSION'S ACTION PLANS. SPECIAL STUDIES IDENTIFIED IN THE PP WILL HELP GUIDE FORMULATION OF THE POLICY AGENDA AND EXAMINE OTHER CONSTRAINTS. THE PP SHOULD DISCUSS HOW THIS INFORMATION WILL BE USED IN THE ANNUAL REVIEWS WITH THE GOP. FINALLY, THE MISSION SHOULD CONDUCT AN EXTERNAL EVALUATION OF THE PROGRAM BEFORE THE THIRD AUTHORIZATION TO DETERMINE THAT THE OBJECTIVES CONTINUE TO BE REASONABLE AND ACHIEVABLE AND THAT THE PROGRAM SHOULD CONTINUE. BUREAU WOULD LIKE TO REVIEW OUTCOME OF EVALUATION AND YOUR CONCLUSION RESULTING FROM IT.

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OUTGOING TELEGRAM

Department of State



5. LOCAL CURRENCY BUDGET LEVELS: ONE OF THE PROGRAM'S INTENTIONS IS TO SUPPORT, THROUGH LOCAL CURRENCY EQUIVALENT AMOUNTS, THE GOVERNMENT OF PAKISTAN'S LOW INCOME SHELTER PROGRAMS. SOME DISCUSSION SHOULD BE PRESENTED IN THE PP ON HOW THE MISSION WILL ENSURE THAT THE GOP BUDGETARY LEVELS REMAIN ADEQUATE TO SUPPORT LOW INCOME HOUSING PROGRAM ACTIVITIES AND THAT BUDGET LEVELS DEMONSTRATE A SIGNIFICANT FINANCIAL COMMITMENT ON BEHALF OF THE GOP IN AREAS WHERE THE PRIVATE SECTOR WILL NOT BE ABLE OR ARE UNWILLING TO HELP MEET THE NEED. THIS IS

NOT MEANT TO IMPLY AN ADDITIONALITY REQUIREMENT. MAINTENANCE OR INCREASES OF BUDGETS FOR LOW INCOME HOUSING WHERE GOVERNMENT HAS A LEGITIMATE ROLE TO SUPPORT LOW INCOME HOUSING COULD BE INCLUDED AS PART OF YOUR POLICY AGENDA.

6. MONITORING BENEFICIARY IMPACTS: THE HG LEGISLATION REQUIRES THAT WE ESTABLISH THE RELATIONSHIP BETWEEN THE PROGRAM AND LOW INCOME BENEFICIARIES. CONCERNS HAVE BEEN RAISED ON HOW THE MISSION WILL DETERMINE THAT LOW-INCOME FAMILIES WILL BE REACHED BY THESE GOP PROGRAMS. THE PP MUST DEMONSTRATE HOW THESE GROUPS WILL BE ASSISTED BY THE HG. THE MONITORING SYSTEM FOR LOCAL CURRENCY USES SHOULD BE ABLE TO SHOW THAT WE ARE MEETING THESE REQUIREMENTS.

7. ENVIRONMENT: DURING THE PRC DISCUSSION, AN ISSUE WAS RAISED CONCERNING COMPLIANCE WITH 22 CFR 216 (REGULATION 16), AID'S ENVIRONMENTAL PROCEDURES. WHILE HG GENERATED LOCAL CURRENCIES ARE NOT REPEAT NOT INCLUDED UNDER AGENCY LOCAL CURRENCY POLICY GUIDANCE, PER SE, SUFFICIENT CONCERN EXISTS THAT AID ACTIVITIES SHOULD MEET HIGH ENVIRONMENTAL STANDARDS. IN THIS REGARD, MISSION'S ATTENTION IS DIRECTED TO AID/W QUOTE SUPPLEMENTAL GUIDANCE ON PROGRAMMING LOCAL CURRENCY UNQUOTE (HB 1, PART IV, TH 1:41, STATE 327494, OCTOBER 21, 1987), WHICH STATES IN PART QUOTE RESPONSIBLE SAFEGUARDS ENSURING THAT ENVIRONMENTAL CONCERNS WILL BE TAKEN INTO ACCOUNT IN THE DESIGN AND IMPLEMENTATION OF PROJECTS AND PROGRAMS SUPPORTED BY JOINTLY PROGRAMMED LOCAL CURRENCY AND TRUST FUNDS ARE APPROPRIATE. ACCORDINGLY, SPECIFIC POLICY GUIDANCE ON THIS SUBJECT IS BEING PREPARED .... UNQUOTE. THE MISSION IS URGED TO PAY PARTICULAR ATTENTION TO HOST COUNTRY ENVIRONMENTAL PROTECTION PROCEDURES TO ENSURE THAT ENVIRONMENTAL CONSIDERATIONS ARE BEING ADEQUATELY ADDRESSED IN THE IMPLEMENTATION OF HOUSING SECTOR PROGRAMS. IN PARTICULAR, THIS COULD INCLUDE SUPPORTING INSTITUTIONAL CAPABILITY OF RELEVANT HOST COUNTRY INSTITUTIONS TO CONDUCT APPROPRIATE ENVIRONMENTAL REVIEWS OF PROPOSED LOW-INCOME SHELTER PROGRAMS, INCLUDING ASSOCIATED BASIC INFRASTRUCTURE. THIS SHOULD BE DISCUSSED WITH THE ENVIRONMENT AND URBAN AFFAIRS DIVISION OF THE MINISTRY OF HOUSING AND WORKS, WHICH HAS THE LEAD ENVIRONMENTAL RESPONSIBILITY WITHIN THE GOP. THE PP SHOULD REFLECT THE OUTCOME OF THESE AND OTHER DISCUSSIONS RELATED TO ENVIRONMENTAL PROTECTION CONSIDERATIONS WITHIN THE PAKISTAN HOUSING SECTOR.

8. DONOR COORDINATION: THE PROPOSED PROGRAM IS PART OF A MULTI-DONOR EFFORT TO ASSIST THE PAKISTAN HOUSING SECTOR. THE DIVISION OF RESPONSIBILITY AS PRESENTED IN THE PID SHOWS THAT BOTH AID AND THE ASIAN DEVELOPMENT BANK (ADB) WILL HAVE SOME FOCUS ON THE ROLE OF THE HOUSE BUILDING FINANCE CORPORATION (HBFC), WITH THE ADB FOCUSING ON LAND RESOURCE ISSUES. AID'S PROGRAM IS SEEKING TO REDUCE THE ROLE OF THE HBFC IN THE HOUSING FINANCE SYSTEM, WHILE THE ADB PROGRAM IS SEEKING TO



STRENGTHEN THIS INSTITUTION'S CAPABILITIES. SPECIFIC DISCUSSIONS SHOULD BE PRESENTED IN THE PP ON HOW DONOR ACTIVITIES CAN BE COORDINATED AND OUR RESPECTIVE PROJECTS CAN SERVE TO STRENGTHEN THE HOUSING SECTOR AND OVERALL PROGRAM GOALS. SHULTZ

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بسم الله الرحمن الرحيم

OFFICIAL FILE

Annex 2

No. 2(2)US-I/88.
Government of Pakistan
MINISTRY OF FINANCE AND
ECONOMIC AFFAIRS
(ECONOMIC AFFAIRS DIVISION)

Telegram: ECONOMIC
Telex: ECDIV No. 05-834

*Islamabad, the* January 25, 1989

JARJEES ALI KIANI,
PHONE:- 820769.

Subject:- USAID SUPPORT IN THE HOUSING SECTOR.

Dear Mr. Tate,

Please refer to Director USAID's letter dated November 2, 1988 on the above subject.

2. I am pleased to inform you that the concept of USAID Support in the Housing Sector, is acceptable to the Government of Pakistan. USAID are requested to kindly make arrangements for detailed programme design at the earliest convenience.

With best regards,

Yours sincerely,

(JARJEES ALI KIANI)

RECEIVED JAN 29 1989

Mr. F. Wayne Tate,
Deputy Chief Programme Office,
USAID,
Islamabad.

ACTION

بسم الله الرحمن الرحيم

ANNEX 2-A

Telegram : ECONOMIC
Telex : ECDIV No: 05-634
SECRETARY
PHONE: 820629

No. 2(2)US-1/89.
Government of Pakistan
MINISTRY OF FINANCE AND
ECONOMIC AFFAIRS
(ECONOMIC AFFAIRS DIVISION)

Islamabad, the 1st June 1989

SHELTER RESOURCE MOBILIZATION PROGRAMME
(391-0507 AND 391-HG-001)

Dear Mr.Norris,

As a priority objective, Government of Pakistan intends to create a policy environment which will promote establishment of market-oriented shelter finance institutions and shelter programs for low income families. The program will benefit a broad spectrum of beneficiaries especially families earning below median income. To this end, the Government of Pakistan formally requests United States assistance in the amount of one hundred million dollars ($100,000,000) in housing guarantee loans and five [illegible] dollars ($5,000,000) grant, subject to the availability of funds, to finance the Shelter Resource Mobilization Program.

With best regards,

Yours sincerely,

( IZHARUL HAQUE )

Mr.James A.Norris,
Director,
USAID Mission,
ISLAMABAD.

ANNEX 3-A

THE HOUSING GUARANTY PROGRAM

STATUTORY CHECKLIST
PAKISTAN

PROJECT NO. 391-HG-001 and 391-0507

| | ANSWER YES/NO OR PUT PP PAGE REFERENCES AND/OR EXPLANATIONS WHERE APPROPRIATE |
|---|---|
| A. General Criteria Under HG Statutory Authority. | |
| Section 221(a)<br>Will the proposed project meet the following criteria: | |
| (1) is intended to increase the availability of domestic financing by demonstrating to local entrepreneurs and institutions that providing low-cost housing is financially viable; | Yes (See Sec. 3.2) |
| (2) is intended to assist in marshalling resources for low-cost housing; | Yes (See Sec. 3.2) |
| (3) supports a pilot project for low-cost shelter, or is intended to have a maximum demonstration impact on local institutions and national; and | Yes (See Sec. 3.2) |
| (4) is intended to have a long run goal to develop domestic construction capabilities and stimulate local credit institutions to make available domestic capital and other management and technological resources required for low-cost shelter programs and policies | Yes (See Sec. 3.2) |
| Section 222(a)<br>Will the issuance of this guaranty cause the total face amount of guaranties issued and outstanding at this time to be in excess of $2,158,000? | No |

| | ANSWER YES/NO OR PUT PP PAGE REFERENCES AND/OR EXPLANATIONS WHERE APPROPRIATE |
|---|---|
| Will the guaranty be issued prior to September 30, 1989? | Yes |
| Section 222(b)<br>Will the proposed guaranty result in activities which emphasize: | |
| (1) projects providing improved home sites to poor families on which to build shelter and related services | Yes (See Sec. 2.4 |
| (2) projects comprised of expendable core shelter units on serviced sites | No |
| (3) slum upgrading projects designed to conserve and improve existing shelter | Yes (See Sec. 2.4 |
| (4) shelter projects for low-income people designed for demonstration or institution building | Yes (See Sec. 2.4 |
| (5) community facilities and services in support of projects authorized under this section to improve the shelter occupied by the poor? | Yes (See Sec. 2.4) |
| Section 222(c)<br>If the project requires the use or conservation of energy, was consideration given to the use of solar energy technologies, where economically or technically feasible? | N/A |
| Section 223(a)<br>Will the A.I.D. guaranty fee be in an amount authorized by A.I.D. in accordance with its delegated powers? | Yes |
| Section 223(f)<br>Is the maximum rate of interest allowable to the eligible U.S. Investor as prescribed by the Administrator not more than one percent (1%) above the current rate of interest applicable to housing mortgages insured by the Department of Housing and Urban Development? | N/A |

| | ANSWER YES/NO OR PUT PP PAGE REFERENCES AND/OR EXPLANATIONS WHERE APPROPRIATE |
|---|---|
| **Section 223(j)** | |
| (1) Will the proposed Housing Guaranty be coordinated with and complementary to other development assistance in the host country? | Yes (See Sec. 2.2.6) |
| (2) Will the proposed Housing Guaranty demonstrate the feasibility of particular kinds of housing and other institutional arrangements? | Yes (See Sec. 3.1) |
| (3) Is the project designed and planned by A.I.D. so that at least ninety percent (90%) of the face value of the proposed guaranty will be for housing suitable for families below the median income or below the median urban income for housing in urban areas, in the host country? | Yes (See Sec. 2.4) |
| (4) Will the issuance of this guaranty cause the face value of guaranties issued with respect to the host country to exceed $25 million in any fiscal year? | No |
| (5) Will the issuance of this guaranty cause the average face value of all housing guaranties issued in this fiscal year to exceed $15 million? | No |
| **Section 238(c)** | |
| Will the guaranty agreement provide that it will cover only lenders who are "eligible investors" within the meaning of this section of the statute at the time the guaranty is issued? | Yes |

ANSWER YES/NO OR PUT PP PAGE REFERENCES AND/OR EXPLANATIONS WHERE APPROPRIATE

B. Criteria Under General Foreign Assistance Act Authority

Section 620/620A

| | |
|---|---|
| 1. Does the host country meet the general criteria for country eligible under the Foreign Assistance Act as set forth in the country eligibility checklist prepared at the beginning of each year? | Yes |
| 2. Is there any reason to believe that circumstances have changed in the host country so that it would now be ineligible under the country statutory checklist? | No |

ANNEX 3-B

PROJECT 391-0507 CHECKLIST
TECHNICAL ASSISTANCE AND TRAINING GRANT IN SUPPORT OF HG-001

Listed below are statutory criteria applicable to projects. This section is divided into two parts. Part A includes criteria applicable to all projects. Part B applies to projects funded from specific sources only: B(1) applies to all projects funded with Development Assistance; B(2) applies to projects funded from Development Assistance loans (N/A); and B(3) applies to projects funded from ESF.

CROSS REFERENCES: IS COUNTRY CHECKLIST UP TO DATE? HAS STANDARD ITEM CHECKLIST BEEN REVIEWED FOR THIS PROJECT? YES

A. GENERAL CRITERIA FOR PROJECT

1. FY 1989 Continuing Resolution Sec. 523; FAA Sec. 634A. Describe how authorization and appropriations committees of Senate and House have been or will be notified concerning the project.

A CN has been prepared. Obligation will occur following expiration of the Congressional notification period without objection.

2. FAA Sec. 611(a)(1). Prior to obligation in excess of $500,000, will there be (a) engineering, financial or other plans necessary to carry out the assistance and (b) a reasonably firm estimate of the cost to the U.S. of the assistance?

(a) YES

(b) YES

3. FAA Sec. 611(a)(2). If legislative action is required within recipient country, what is basis for reasonable expectation that such action will be completed in time to permit orderly accomplishment of purpose of the assistance?

No further legislative action is required.

| | | |
|---|---|---|
| 4. | FAA Sec. 611(b); FY 1989 Continuing Resolution Sec.501. If project is for water or water-related land resource construction, have benefits and costs been computed to the extent practicable in accordance with the principles, standards, and procedures established pursuant to the Water Resources Planning Act (42 U.S.C. 1961, ex seq.)? (See AID Handbook 3 for guidelines.) | N/A |
| 5. | FAA Sec. 611(e). If project is capital assistance (e.g., construction), and total U.S. assistance for it will exceed $1 million, has Mission Director certified and Regional Assistant Administrator taken into consideration the country's capability to maintain and utilize the project effectively? | N/A |
| 6. | FAA Sec. 209. Is project susceptible to execution as part of regional or multilateral project? If so, why is project not so executed? Information and conclusion whether assistance will encourage regional development programs. | NO<br>N/A<br><br>N/A |
| 7. | FAA Sec. 601 (a). Information and conclusions on whether projects will encourage efforts of the country to: (a) increase the flow of international trade; (b) foster private initiative and competition; and (c) encourage development and use of cooperatives, and credit unions, and savings and loan associations; (d) discourage monopolistic practices; (e) improve technical efficiency of industry, agriculture and commerce; and (f) strengthen free labor unions. | The development of Pakistan's housing finance system will foster private initiative and competition as the private sector becomes more involved in the financing of shelter services. Private financing of housing and shelter services should also have a positive impact on (a), (c), (d) and (e).<br><br>(f) N/A. |

| | | |
|---|---|---|
| 8. | FAA Sec. 601(b). Information and conclusions on how project will encourage U.S. private trade and investment abroad and encourage private U.S. participation in foreign assistance programs (including use of private trade channels and the services of U.S. private enterprise). | The project will finance long - and short-term technical assistance and training from the United States. |
| 9. | FAA Sec. 612(b), 636(h); FY 1989 Continuing Resolution Sec. 509. Describe steps taken to assure that, to the maximum extent possible, the country is contributing local currencies to meet the cost of contractual and other services, and foreign currencies owned by the U.S. are utilized in lieu of dollars. | The GOP will provide the equivalent of $100,000,000 for the project for shelter services benefiting the urban poor. |
| 10. | FAA Sec. 612(d). Does the U.S. own excess foreign currency of the country and, if so, what arrangements have been made for its release? | NO |
| 11. | FY 1989 Continuing Resolution Sec. 522. If assistance is for the production of any commodity for export, is the commodity likely to be in surplus on world markets at the time the resulting productive capacity becomes operative, and is such assistance likely to cause substantial injury to U.S. producers of the same, similar or competing commodity? | N/A |
| 12. | FY 1989 Continuing Resolution Sec. 552. (as interpreted by conference report). If assistance is for agricultural development activities (specifically, any testing or breeding feasibility study, variety improvement or introduction, consultancy, publication, conference, or | |

training), are such activities (a) specifically and principally designed to increase agricultural exports by the host country to a country other than the United States, where the export would lead to direct competition in that third country with exports of a similar commodity grown or produced in the United States, and can the activities reasonably be expected to cause substantial injury to U.S. exporters of a similar agricultural commodity; or (b) in support of research that is intended primarily to benefit U.S. producers? N/A

13. FY 1989 Continuing Resolution Sec. 553.

Will the assistance (except for programs in Caribbean Basin Initiative countries under U.S Tariff Schedule: Section 807," which allows reduced tariffs on articles assembled abroad from U.S.-made components) be used directly to procure feasibility studies, prefeasibility studies, or project profiles of potential investment in, or to assist the establishment of facilities specifically designed for, the manufacture for export to the United States or to third country markets in direct competition with U.S. exports, of textiles, apparel, footwear, handbags, flat goods (such as wallets of coin purses worn on the person), work gloves or leather wearing apparel? NO

14. FAA 118(c). Does the Assistance comply with the environmental procedures set forth in A.I.D. Regulation 16? Does the assistance place a high priority on conservation and sustainable management of tropical forests? Specifically, does the assistance to the YES. See Annexes 12, and 16, and Sec. 3.3

fullest extent feasible:
(a) stress the importance of conserving and sustainably managing forest resources; (a) N/A
(b) support activities which offer employment and income alternatives to those who otherwise would cause destruction and loss of forests, and help countries identify and implement alternatives to colonizing forested areas; (b) N/A
(c) support training programs, educational efforts, and the establishment or strengthening of institutions to improve forest mangement; (c) N/A
(d) help end destructive slash-and-burn agriculture by supporting stable and productive farming practices; (d) N/A
(e) help conserve forests which have not yet been degraded, by helping to increase production on lands already cleared or degraded; (e) N/A
(f) conserve forested watersheds and rehabilitate those which have been deforested; (f) N/A
(g) support training, research, and other actions which lead to sustainable and more environmentally sound practices for timber harvesting, removal, and processing; (g) N/A
(h) support research to expand knowledge of tropical forests and identify alternatives which will prevent forest destruction, loss, or degradation; (h) N/A
(i) conserve biological diversity in forest areas by supporting efforts to identify, establish, and maintain a representative network of protected tropical forest ecosystems on a worldwide basis, by making the establishment (i) N/A

of protected areas a condition of support for activities involving forest clearance or degradation, and by helping to identify tropical forest ecosystems and species in need of protection and establish and maintain appropriate protected areas; (j) seek to increase the awareness of U.S. government agencies and other donors of the immediate and long-term value of tropical forests; and (k) utilize the resources and abilities of all relevant U.S. government agencies?

(j) N/A

(k) N/A

16. FAA Sec. 119(g)(4)-(6). Will the assistance (a) support training and education efforts which improve the capacity of recipient countries to prevent loss of biological diversity; (b) be provided under long-term agreement in which the recipient country agrees to protect ecosystems or other wildlife habitats; (c) support efforts to identify and survey ecosystems in recipient countraies worthy of protection; or (d) by any direct or indirect means significantly degrade national parks or similar protected areas or introduce exotic plants or animals into such areas?

(a) N/A

(b) N/A

(c) N/A

(d) N/A

17. FAA 121(d). If a Sahel project, has a determination been made that the host government has an adequate system for accounting for and controlling receipt and expenditure of project funds (either dollars or local currency generated therefrom)?

N/A

B. FUNDING CRITERIA FOR PROJECT

1. Development Assistance Project Criteria — This project is not DA-funded

2. Economic Support Fund Project Criteria

a. FAA Sec. 531(a). will this assistance promote economic and political stability? To the maximum extent feasible, is this assistance consistent with the policy directions, purposes, and programs of Part I of the FAA? — Yes, the project supports a HG program which addresses domestic resources mobilization as a means to promote sustained economic growth.

b. FAA Sec. 531(e). Will this assistance be used for military or paramilitary purposes? — NO

c. ISDCA of 1985 Sec. 207. Will ESF funds be used to finance the construction, operation or maintenance of, or the supplying of fuel for, a nuclear facility? If so, has the President certified that such country is a party to the Treaty on the Non-Proliferation of Nuclear Weapons or the Treaty for the Prohibition of Nuclear Weapons in Latin America (the "Treaty of Tlatelolco"), cooperates fully with the IAEA, and pursues non-proliferation policies consistent with those of the United States? — NO

d. FAA Sec. 609. If commodities are to be granted so that sale proceeds will accrue to the recipient country, have Special Account (counterpart) arrangements been made? — N/A

## ANNEX 3-C

## STANDARD ITEM CHECKLIST

Listed below are the statutory items which normally will be covered routinely in those provisions of an assistance agreement dealing with its implementation, or covered in the agreement by imposing limits on certain uses of funds.

These items are arranged under the general hearings of (A) Procurement, (B) Construction, and (C) Other Restrictions.

### A. PROCUREMENT

1. FAA Sec. 602(a). Are there arrangements to permit U.S. small business to participate equitably in the furnishing of commodities and services financed? — YES

2. FAA Sec. 604(a). Will all procurement be from the U.S. except as otherwise determined by the President or under delegation from him? — YES

3. FAA Sec. 604(d). If the cooperating country discriminates against marine insurance companies authorized to do business in the U.S., will commodities be insured in the United States against marine risk with such a company? — Pakistan does not so discriminate against U.S. marine insurers.

4. FAA Sec. 604(e); ISDCA of 1980 Sec. 705(a). If non-U.S. procurement of agricultural commodity or product thereof is to be financed, is there provision against such procurement when the domestic price of such commodity is less than parity (Exception where commodity financed could not reasonably be procured in U.S.). — N/A

| | | |
|---|---|---|
| 5. | FAA Sec. 604(g). Will construction or engineering services be procured from firms of advanced developing countries which are otherwise eligible under Code 941 and which have attained a competitive capability in international markets in one of these areas? (Exception for those countries which receive direct economic assistance under the FAA and permit United States firms to compete for construction or engineering services financed from assistance programs of these countries.) | N/A |
| 6. | FAA Sec. 603. Is the shipping excluded from compliance with the requirement in Section 901(b) of the Merchant Marine Act of 1936, as amended, that at least 50 percent of the gross tonnage of commodities (computed separately for dry bulk carriers, dry cargo liners, and tankers) financed shall be transported on priately owned U.S. flag commercial vessels to the extent such vessels are available at fair and reasonable rates? | NO. Section 901(b) applies. |
| 7. | FAA Sec. 621(a). If technical assistance is financed, will such assistance be furnished by private enterprise on a contract basis to the fullest extent practicable? Will the facilities and resources of other Federal agencies be utilized, when they are particularly suitable, not competitive with private enterprise, and made available without undue interference with domestic programs? | YES |

| | | |
|---|---|---|
| 8. | International Air Transportation Fair Competitive Practices Act, 1974. If air transportatio of persons or property is financed on grant basis, will U.S. carriers be used to the extent such service is available? | YES |
| 9. | FY 1989 Continuing Resolution Sec. 504. If the U.S. Government is a party to a contract for procurement, does the contract contain a provision authorizing termination of such contract for the convenience of the United States? | All A.I.D. direct contracts will so provide. |
| 10. | FY 1989 Continuing Resolution Sec. 524. If assistance is for consulting service through procurement contract pursuant to 5 U.S.C. 3109, are contract expenditures a matter of public record and available for public inspection (unless otherwise provided by law or Executive order)? | YES. Any such expenditures will be so available. |

B. CONSTRUCTION

1. FAA Sec. 601(d). If capital (e.g., construction) project, will U.S. engineering and professional services be used?

2. FAA Sec. 611(c). If contracts for construction are to be financed, will they be let on a competitive basis to maximum extent practicable?

3. FAA Sec. 620(k). If for construction of productive enterprise, will aggregate value of assistance to be furnished by the U.S. not exceed $100 million (except for productive enterprises in Egypt that were described in the CP), or does assistance have the express approval of Congre — N/A

OTHER RESTRICTIONS

1. FAA Sec. 122(b). If development loan repayable in dollars, is interest rate at least 2 percent per annum during a grace period which is not to exceed ten years, and at least 3 percent per annum thereafter? — N/A

2. FAA Sec. 301(d). If fund is established solely by U.S. contributions and administered by an international organization, does Comptroller General have audit rights? — N/A

3. FAA Sec. 620(h). Do arrangements exists to insure that United States foreign aid is not used in a manner which, contrary to the best interests of the United States, promotes o assists the foreign aid projects or activities of the communist-bloc countries? — N/A

4. Will arrangements preclude use of financing:

a. FAA Sec. 104(f); FY 1989 Continuing Resolution Secs. 525, 538. (1) To pay for performance of abortions as a method of family planning or to motivate or coerce persons to — (1) YES

| | | |
|---|---|---|
| | practice abortions; (2) to pay for performance of involuntary sterilization as method of family planning, or to coerce or provide financial incentive to any person to undergo sterilization; (3) to pay for any biomedical research which relates, in whole or part, to methods or the performance of abortions or involuntary sterilzations as a means of family planning; or (4) to lobby for abortion? | (2) YES<br>(3) YES<br>(4) YES |
| b. | FAA Sec. 483. To make reimbursements, in the form of cash payments, to persons whose illicit drug crops are eradicated? | YES |
| c. | FAA Sec. 620(q). To compensate owners for expropriated or nationalized property, except to compensate foreign nationals in accordance with a land reform program certified by the President? | YES |
| d. | FAA Sec. 660. To provide training advice, or any financial support for police, prisons, or other law enforcement forces, except for narcotics programs? | YES |
| e. | FAA Sec. 662. For CIA activities? | YES |
| f. | FAA Sec. 636(i). For purchase, sale, long-term lease, exchange or guaranty of the sale of motor vehicles manufactured outside U.S., unless a waiver is obtained? | YES |
| g. | FY 1989 Continuing Resolution Sec. 503. To pay pensions, annuities, retirement pay, or adjusted service compensation for military personnel? | YES |

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| h. | FY 1989 Continuing Resolution Sec. 505. To pay U.N. assessments, arrearages or dues? | YES |
| i. | FY 1989 Continuing Resolution Sec. 506. To carry out provisions of FAA section 209(d) (transfer of FAA funds to multilateral organizations for lending)? | YES |
| j. | FY 1989 Continuing Resolution Sec. 510. To finance the export of nuclear equipment, fuel, or technology? | YES |
| k. | FY 1989 Continuing Resolution Sec. 511. For the purpose of aiding the efforts of the government of such country to repress the legitimate rights of the population of such country contrary to the Universal Declaration of Human Rights? | YES |
| l. | FY 1989 Continuing Resolution Sec. 516. To be used for publicity or Propaganda purposes within U.S. not authorized by Congress? | YES |

PAKISTAN: SHELTER RESOURCE MOBILIZATION PROGRAM
LOGICAL FRAMEWORK
Life of Program: 5 years; Inputs: HG $100 Million; Grant: $5 Million

| NARRATIVE SUMMARY | OBJECTIVELY VERIFIABLE INDICATORS | MEANS OF VERIFICATION | ASSUMPTIONS |
|---|---|---|---|
| Program Goal:<br>o To develop the role of housing finance in Pakistan's financial sector through the mobilization and application of domestic sources to the shelter needs of Pakistan | Indicators of Goal Achievement:<br>o An increase in the level of investment in shelter utilizing institutions linked to the overall financial sector. | Goal Verification:<br>o MOF data indicating increase in domestic savings mobilization and housing finance loan approvals benefitting a wide range of households including those of low income. | Important Assumptions for Achieving Goal:<br>o The GOP will continue its concern for rationalizing the financial sector and shifting the burden of providing shelter credit from the national budget to the financial markets. |
| Project Purpose:<br>o To create the policy environment which will promote the market establishment of market oriented shelter finance institutions.<br>o To initially support through local currency equivalent amounts, GOP shelter programs that are affordable to low income families. | End of Project Status:<br>o The existence of a self-sustaining national system of market-oriented housing finance institutions.<br>o The existence of $100M in affordable shelter components including serviced land and upgraded slums. | o MOF and SBP data indicating lending at market rates, and a high level of loan repayments.<br>o GOP records indicating that the local currency equivalent of $100 M has been expended on qualified projects benefitting low-income households. | o The GOP will support and encourage development of a market-oriented shelter finance system and is therefore open to policy discussion.<br>o That removal of constraints associated with many GOP shelter programs will allow the latent market demand for housing finance to become manifest. |
| Outputs<br>o More efficient financial markets through the establishment of a market oriented shelter finance system.<br>o Strengthened, stable economic growth.<br>o Shelter services valued at $100M which benefit below-median-income urban households. | o More appropriate use and targeting of subsidies; establishment of a housing finance regulatory and supervisory capability; development of a revised role for HBFC consistent with a market-oriented system of housing finance.<br>o Increased investment in capital assets, e.g., housing and infrastructure.<br>o The development of infrastructure required to service land for shelter purposes benefitting low income households. | o GOP actions as reflected in MOF, SBP, and HBFC records, and program monitoring and evaluation.<br>o GOP and shelter finance institution records (using IBRD and ADB sector data as baseline)<br>o GOP annual national budget figures supported by AID monitoring, including field verification of beneficiaries. | o A market-oriented shelter finance system will be more efficient and equitable than the current GOP approach which is dependent on subsidized loans from HBFC.<br>o That the ability to invest in shelter under the system envisioned in this program will be attractive to many households, and therefore engender their participation in the formal financial systems. |

ANNEX 4

ANNEX 5

PRESS ARTICLES

# Housing sector in Pakistan present situation & future options

PAKISTAN at present is faced with one of the most difficult periods in the economic history of the country. Never before the country has been faced with such a formidable combination of challenges and strains, unprecedented urbanization, an un-favourable international climate, stagnating per capita GNP, runway inflation, a rapid population increase, spiralling unemployment, severe financial constraints and exceptionally high level of external debits. The government during the past dacade, with unsound and callous policies has aggravated the situation to alarming levels.

Housing is one of man's fundamental requirements. The provision of accommodation, therefore, forms part of the responsibilities of the Public Administration everywhere. The provision of accommodation is not only a social task performed by the governments, but it also contributes significantly to the important economic and employment activities. The important role of this sector as a stimulus for domestic economic activity and national development can be identified from three points of view:-

i) Investment in this field is labour intensive.

ii) It can stimulate the production of local building materials

iii) It can act as incentive to mobilize house hold savings by offering an attractive investment opportunity

The Housing Sector, inspite of its importance and unprecedental recognization on the part of administrators, has not been able to attract even modest allocation of Public sector resources. Rapid urbanization is creating additional unprecedented pressure for shelter and related community services. The cities have been growing at enormous rate and the trend is to continue in the coming years, putting further strain on the existing infrastructure and services. Such a growth will have profound implications for the country. The efficiency of the urban areas, or lack thereof, will be a major determinant of the overall quality of life and economic strength of the country. The Government is already confronting enormous needs across all sectors of the economy with limited financial resources and has its limitations to cope with the housing problems. The problems have been further compounded by the inordinate and careless policies persued during the past few years

The housing conditions in Pakistan are among the worst even in Asia in 1980 there was an average of 6.7 persons per housing unit and 3.5 persons per room. Only 31% of housing had access to electricity and 38% had inside access to piped water. 48% of the units had outer walls comprised of unbaked bricks and mud.

The Government is doing its best, wherever possible, to improve the conditions. It will not be too far when all the villages would also have been provided electricity and the rural housing units, which comprise 80% of the housing stock in the country, would have access to electricity. Similarly great emphasis is being given to the improvement of infrastructure. However, very little has been possible in the area of providing new accommodation, mainly because of scarcity of resources. Further the publicly aided building of private housing does not entirely fulfil its socio-economic aim since publicly subsidised housing construction is too expensive. It has also been seen in various countries that construction of housing by public sector actually results in the negative contribution to the housing stock because the private contribution towards house construction decreases. The formal sector of the economy in Pakistan has been

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# Housing sector in Pakistan present situation

From Page 1

building 40,000 to 50,000 dwelling units per year compared to the annual growth of households of 120,000 per year. Unless special efforts are made towards this provision of additional housing units than the present level of annual production, the situation will assume alarming dimensions.

The Governments make policies to ensure the development of decent housing programmes. These policies are followed by the respective Governments because they are concerned with squatter settlements and poor quality of living conditions in such settlements and overcrowded urban slums and have the desire to improve these conditions. However, sofar the government in Pakistan, have unfortunately played a vital role in worsening the situation. The "famous Katchi Abadis" slogan might have paid dividends to the political leaders in political terms but this has contributed towards the creation of inhuman living conditions in and around all urban centres of the country. These have also deprived the nation of the valuable parcells of urban land which otherwise could have been used to generate economic activity to its fullest potential. Further large sums of money have been thrown at the electorate, few month before the election, like a balloonist jetissoning ballast in an attempt to keep afloat. However, while we must take stock of the intentional mistakes of the past so that their repetition can be avoided, we must look forward and move ahead to direct our steps in the right direction in the future. We must learn from our mistakes in the past. We have to realize that in many countries of the world, the efforts on the part of the government to construct housing in the public sector have met with failures because sufficient finance for such programmes is usually not available, costs are normally higher and consequently problem get multiplied instead of being solved. Hence the policy should be "Minimum intervention maximum support" to the people's own efforts. Unrealistic and unstable subsidies in the form of free land must be stopped or restricted to benefit only a few at the lowest level of income. Financial assistance must be given but not without making provision for recovery of the money.

Many intenational agencies are of the view that individual and private initiatives are the real solutions to the housing problems. It is true that the governments have an indispensable role in providing infrastructure, secure land tenure and in creating the climate and policies that will facilitate the production of housing by individual and private action. Very rarely is Government an efficient producer or owner of housing.

The Government at best can encourage development or reform of housing financing institutions in the Private Sector. In Pakistan such a policy can assume overriding importance in view of the fact that personal savings are at the lowest level. The desire to own a home can be pleasantly expected to encourage increased personal savings. It should also be noticed that in almost all countries of the world, the housing finance institutions in the private sector have played the vital role of mobilising personal savings. The importance of such institutions, such as building societies, in respect of economic and employment activities also has been of significant importance to the economics of even the developed world. These private institutions have mobilized personal savings and have contributed to housing development to a great extent, and have provided housing finance to the tune of over 80% of the total investment.

The activities of these private sector organizations have thus contributed significantly to the national economics on the one hand and provided the much needed shelter to the majority of the popultion on the other hand.

So far, in Pakistan, the House Building Finance Corporation, HBFC, has been the main provider of housing finance loans. The HBFC has obtained its funds from the Public Sector. Banks remain the major financial institutions which lend mostly to industry. There is no housing finance institution in the Private Sector. Such an organization can play vital role in mobilizing additional personal savings, which would be ploughed back into the national economy.

This will prove highly successful in Pakistan because the hidden income, which is over 30% total currency in the country, which now remains inactive in the hands of the individuals, will be channeled towards savings to be used for the purchase of a home. It is very well known that presently large number of personal sector income earners do not participate in the national economy.

The housing in all urban centres of Pakistan has become very expansive. The funds used in the purchase of housing would amount to billions of rupees but all this wealth remains latent. It is not in circulation and hence does not play any active role in the national economy. The Banks in Pakistan do not loan against real estate. In 1980-81 the banks lent 251 million rupees on the security of real estate out of total lending of 6,286 million rupees. Hence lending against real estate security is only 4% of the total lending. In the developed countries the private sector housing finance organizations have market share of personal savings of over one half and their share in the total loans to the housing sector is over 78%. Hence when the private housing finance organizations lend to the personal sector, financial institutions increase the funds available to them and these can be used for reinvestment with the financial institutions.

Almost all countries of the world, including India, having Private Sector Housing Development and Finance Organizations which have mobilized enormous personal sector resources and are contributing significantly to the national economy. In the developed world such organizations are already playing this major role in the economic and employment sectors by demonstrating that over 75% of the housing sector loans are arranged and managed by these organizations. The performance of a Private Sector Housing Development Finance Corporation in India is being referred to as a success story in the Third World. The housing sector requirements and the subjective conditions in Pakistan clearly establish that there is a dire need for such organizations to supplement the present efforts of the Government.

The peoples government has already placed high priority in the housing sector. The judicial use of the government resources in a planned manner, combined with private efforts can go in a long way in meeting the needs of the nation in this vital sector. The question of existing government contribution and subsidies should be critically reviewed with the goals of increasing their effectiveness, avoiding unintended side effects, minimising costs to the public and private sectors and distributing benefits fairly in relation to need. The government contributions must be carefully targetted to groups that have a specific demonstrable need.

The government resources should be allocated towards the improvement of sites and services and slum upgrading, provision of infrastructure, the development of land information system, the reform of the land tenure system and the development to financial markets and institutions. The task of building new homes as well as providing loans to home owners should be diverted to the private sector.

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## Private investment companies

By TARIQ BUTT

# Efforts to refund money to depositors blocked

ISLAMABAD, March 21: Efforts to refund money to investors of the now-disbanded private finance companies, undertaken by an official committee, now appear to have come to a halt. The reason is: An OSD (on Sind Affairs) to the Prime Minister has formed a parallel body, which has effectively made the previous one redundant.

The original committee has suspended its operation, and Maulana Abdus Sattar Edhi, a relentless social worker, who was appointed its trustee, has decided to dissociate from it in frustration.

The original committee comprises one representative each of a finance company whose depositors are refunded their money, FIA, and Ministry of Interior and Begum Ansari, a social worker. It was formed with the approval and consent of the Interior Minister, Aitzaz Ahsan.

To begin with, the trustee advanced Rs.20 million from Edhi Foundation Funds to the committee on behalf of three companies — Chawla Food Industries, Ali International and Raza Enterprises — in return for pledge of their immovable properties

Nearly 1,000 cheques were prepared for account holders having deposits upto Rs 50,000. The understanding was that the money advanced by the trustee would be recovered when assets of these companies were liquidated.

Before the disbursement of these cheques to the hapless investors began, the OSD, Shafi Mohammadi suddenly entered the scene. He hurled what critics describe as "unfair and disparaging" remarks on the FIA regarding its performance in the matter.

This created apprehensions in the mind of Maulana Edhi about the return of his Foundation's Rs.20 million and accordingly, he decided to suspend all the work. He also ordered his banks to stop payment of cheques issued to the investors.

Shafi Mohammadi is said to have further announced that his committee, which has not been approved by the Federal Government, will take over the sale of assets of the finance companies and refund money to account holders from their proceeds. His sudden intervention in the affair perturbed members of the original committee who nonetheless decided to keep mum.

The committee was to start delivery of cheques to depositors of some three companies in the last week of February. It was to operate throughout the country. The Federal Government extended complete cooperation and assistance to the committee to undertake a really assiduous task.

Begum Ansari who is Chairman of the Committee laments over the intervention of Shafi Mohammadi in an affair which needed no help from him. "We were doing an excellent job. Our months' long efforts were about to bear fruit, but these were scuttled", she told "The Muslim".

She was all praise for the Interior Minister who she said readily agreed to the formation of the committee proposed by her. "Although I did'nt want to be included in it, the Minister persuaded me to help in the realisation of the noble cause", she said.

Similarly, Begum Ansari appreciated the cooperation and interest shown by Mir Fawad of the FIA, a member of the committee, in making arrangements for refund of the deposits. "Allegations levelled against him by Shafi Mohammadi have no basis", she emphasised.

Beguin Ansari stressed that the committee would not involve itself in money transactions. It would be Maulana Edhi's Foundation whose integrity is above board to receive sale proceeds of the assets of the companies, she said.

The committee, she said, discussed the format for refund of money and other related matters with the government in detail and introduced a fool-proof arrangement to implement the task.

She pointed out that had there been no intervention from any quarter in the working of the committee, it would have made concrete progress so far. She said the frustration among the investors would continue to mount unless they received their hard-earned money back.

The committee had planned to expand its operation to refund big deposits after it had done so in the case of small account holders. It had intended first to pay them their original deposits after deducting whatever amounts they had already got back in the form of monthly profits. But if the sale proceeds of assets of a company in question increased these refunds, the remainder was proportionately again to be paid to the depositors.

Begum Ansari has appealed to Prime Minister Bhutto to prevent her OSD from "subverting the progress" so far made by the FIA and Maulana Edhi towards the return of money to the poor investors. She feels that Maulana Edhi would again be ready to assume his old role provided a Prime Minister assurance was forthcoming.

The private finance companies which illegally mushroomed were disbanded abruptly last year. Their operators who had pocketed billions of rupees disappeared from the scene leaving the investors high and dry. The account holders made concerted efforts through different means to get their money back, but made little progress.

The FIA which has been entrusted the job of netting the proprietors of the disbanded companies and forcing them to refund deposits, had made some progress. The formation of the Edhi committee was also a positive step in this direction.

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# Competitive banking

COMMERCIAL banks in Pakistan were nationalised in January 1974 to enable them to better serve the interests of the national economy. But the change while curbing the earlier ills spawned a series of new ones. And before these could be corrected 11 long years of Martial Law and quasi Martial Law followed when commercial banking functioned without any accountability. It suffered from all the vices of bad banking and only absence of competition from the private sector kept it above water. The sector now presents a picture of an overstaffed body with undertrained hands offering a poor standard of service. It became, among other things, a provider of jobs for favoured individuals from its key posts down. The Martial Law regime also used the banks to meet its enormous budgetary deficits. It borrowed at low rate of interest, fuelling inflation. Advances of billions of rupees were made to influential persons in contravention of banking principles and practices, which were then written off without any banking qualms. This resulted in severe distortions in the money market.

The sad state of affairs has led to demands for reinduction of private banking in the economy. Now even the President of National Bank of Pakistan has made a plea for it. He considers this important for cutting down reliance on deficit finance, since private sector could promote self-financing through greater resort to money market. Private banking will also no doubt offer competition to the nationalised commercial banks and force the latter to improve their performance. At the same time, however, it will be important to ensure that the pre-nationalisation ills do not come barging back. Concentration of credit in a few hands, for instance, should be guarded against. Small entrepreneurs now face great difficulty in obtaining finance from the money market. Private banks can make up that deficiency by fixing a quota of advances for such entrepreneurs.

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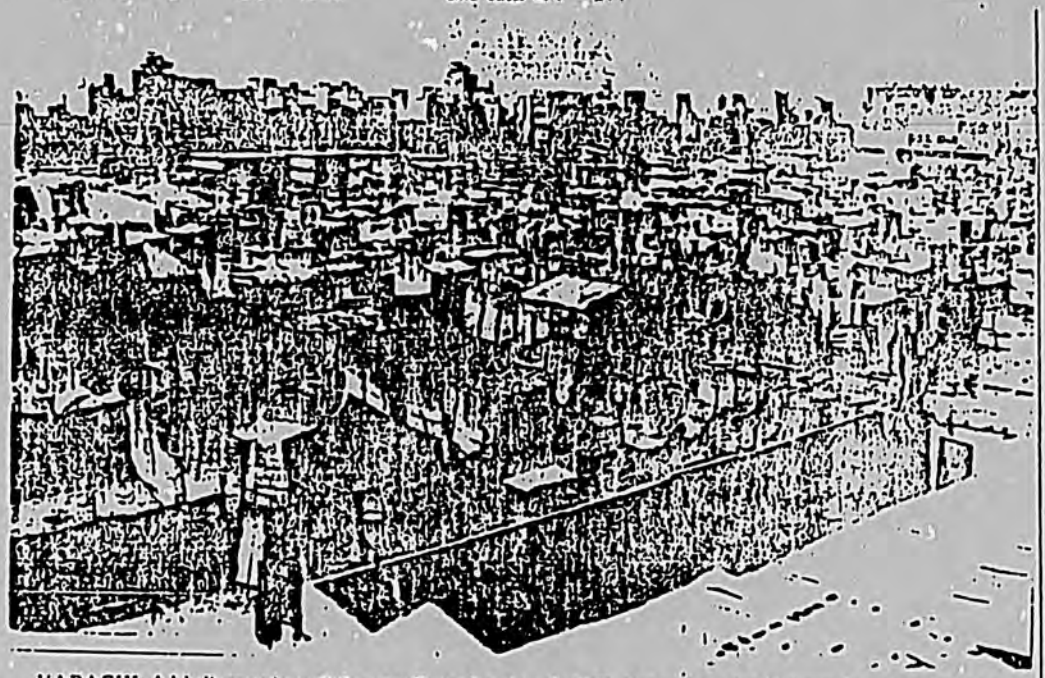

KARACHI: A bird's eyeview of the new jhuggis set up in F.C.. Area opposite Al-Azam Square—DAWN photo

# Emergence of over 100 jhuggis overnight

By Our Staff Reporter

KARACHI, March 11: More than a hundered jhuggies have been put up overnight on the 10-acre plot in F.C. Area, opposite Al-Azam Square, in Liaquatabad.

Land-grabbers demarcated the plots, made lanes and narrow passages during the night and immediately thereafter put up bamboo huts to determine occupancy, residents said. They have not yet moved into the new hutment colony, however.

Residents reported the matter to several concerned agencies but none has taken note of it. These include the PPWD which owns bulk of the property in F.C. Area, the police, KDA and the ZMC Central.

According to inquiries there is a dispute about the ownership of this land between Hamdard Trust and several others. The matter is now before the Supreme Court of Pakistan.

Hakim Mohammad Said, Chairman of Hamdard Foundation, told "*Dawn*" he had informally told government functionaries that he would transfer his claim to any agency, including the ZMC Central, KDA, PPWD or the KMC, if the plot was converted into a park-cum-playground to meet the recreational needs of the huge population.

Repeating the offer he said Liaquatabad and adjoining localities were virtually starved of open spaces and recreational facilities. Former Sind Governor, Lt-Gen (retd) Abbasi had also recognised this deficiency and it was at that time that he informally made the offer.

Residents said the first effort reported that professional land-grabbers had hatched a similar plan to occupy the huge plot opposite Civic Centre where at one time the KMC proposed to build the new Municipal Hall.

This plot is also the subject matter of litigation and the case is awaiting adjudication of the Supreme Court, inquiries show.

According to official sources the land-grabbers have dismantled the boundary wall of this plot from many sides and a couple of hutments had already come up.

The encroachers have, in the meantime, grabbed land in and around the Milk Plant area and are closing in fast. The encroachment had started from Issa Nagri but now stretches from the graveyard to the Civic Centre roundabout.

Another group of land grabbers have occupied land on both flanks of the new Circular Road Bridge next to the graveyard. Shops have come up and a second hand furniture market is flourishing here.

In spite of being its full view, the Anti-Encroachment Cell of the KDA remains indifferent as ever.

Until some time back, the KDA attributed its failure to tackle the menace to lack of cooperation of the police.

Considering the seriousness of the situation, the Provincial Government sanctioned last year a full-fledged police station of the KDA with a regular force of more than 150 officers and men. The police station has been working for several months. However, it has not done anything substantial to check the menace of land grab and encroachment in the city.

**LAST STRAW:** The emergence of more than hundred jhuggis overnight was the last straw on the camel's back and posed a very serious threat to the general law and order situation besides worsening of the municipal problems particularly water supply, sewerage and sanitation, etc.

Meanwhile, KDA's Anti-Encroachment Cell has received

# Shelter for the homeless

THE CHALLENGE CANNOT BE MET WITHOUT THE EXTENSIVE PARTICIPATION OF THE PRIVATE SECTOR IN HOUSING DEVELOPMENT.

Prime Minister Mohammad Khan Junejo, addressing a large gathering of Pakistan Ordnance Factories workers the other day, assured that one million housing units would be built during the next five years to provide residential facilities to the shelterless people in the country. This commitment is already reflected in the P.M.'s Five-Point Programme which is now under implemention. It is gratifying that preliminary work has been completed for the construction of 75,000 one room houses in the country on seven-marla rural and three-marla urban plots. These houses, to be given away free to the poor, will cost a total amount of two billion rupees and are being built with Zakat funds. There is another scheme for the construction of 55,000 low-cost houses, each costing Rs 25,000. These houses will be provided to shelterless people on easy instalments, to be repaid over twenty years. At the same time, the House Building Finance Corporation has started implementing a loan scheme for the construction of 20,000 houses under the Five-Point Programme. The Corporation will extend a loan of Rs.10,000 to each owner of a plot of two or three marlas with a monthly income of less than Rs.1150 per month, repayable in monthly instalments of Rs.100 over a period of 15 years. All these housing schemes providing for the construction of 150,000 units are meant to be completed by the end of 1988. It has been realised that a mere increase in the supply of houses will not yield the desired results. The Government has, therefore, decided to provide civic amenities such as drainage, water supply, pavement of streets, etc. to the occupants of the new houses. "Apni Basti" scheme started this year is being implemented in accordance with the requirements of proper planning. The regularisation and development of *Kachchi Abadis* (slums) have already been undertaken.

It is noteworthy that the construction of one million houses during the next five years will not overcome the shortage of about three million housing units estimated in 1985-86 (1.4 million in urban areas and 1.6 million in rural areas). The shortage is increasing with a substantial rise in the country's population at the rate of over 3 per cent. It is estimated that the demand is going up at the rate of 600,000 housing units per annum. Moreover, there is a continuous rise in the migration of people from the rural to the urban areas in search of employment, aggravating the housing problem in big cities and towns in the country. Evidently, the shortage of houses will persist even after all the Government schemes for the provision of shelter to the masses are implemented in letter and spirit. The Government does not have the resources required to launch a crash housing programme to provide residential facilities to all the people who cannot afford to build or purchase houses. The challenge cannot be met without the extensive participation of the private sector in housing development. The latter should be allowed to establish savings and loan associations and mortgage banks for financing construction and purchase of housing units. These institutions will also provide a new effective channel for mobilising savings which have remained largely untapped. The industrialists and businessmen should also launch housing schemes for their workers and employees. The House Building Finance Corporation can also contribute to the solution of the housing problem by switching from mere providing finance to actually building houses for the low-income groups. The cost of houses can be recovered in easy monthly instalments extending over a period of 20 years or so. There is also an urgent need to reduce the cost of house construction by using cheaper but solid building material through the application of appropriate technology.

# HBFC gets go-ahead for commercial operations

By M. Sabihuddin Ghausi

KARACHI, March 7: The Federal Government has finally given the go-ahead signal to the House Building Finance Corporation (HBFC) for commercialisation of its operations.

Detailed working plans in this regard are expected to be finalised before the end of current fiscal year.

Simultaneously, preparations are almost in the final stages to launch a purely market oriented housing loans organisation, which is being sponsored by the Pakistan Industrial Credit and Investment Corporation (PICIC) in collaboration with some international agencies and local entrepreneurs.

According to informed sources, the HBFC has already started exercises for preparing manuals and procedures for extending loans to the house builders on commercial rates and also for mobilisation of funds from the open market, various deposit schemes, and international agencies.

Sources revealed that HBFC has convened from Wednesday (March 8) a three-day conference of its top executives and heads of all the regional offices to formulate procedures and methods for the new loaning operations, recoveries and all related matters.

The conference will also discuss proposals to make HBFC an autonomous organisation which should have its own independent board of directors to formulate the policies. The idea is to make HBFC function on lines of an autonomous financial institution.

These proposals the sources said, would then be discussed with an Asian Development Bank team from next Monday (March 13). The final draft of the working plan is likely emerge within this month, which would be submitted to the Federal Government for approval.

Sources said that even after commercialisation, the HBFC would continue to offer loans on subsidised rates to the low income group people, for which the Government is expected to provide finances.

According to the experts, the HBFC at present offers loans on 16 different rates of return to its clients. The lowest rate of return is 7.5 per cent on loans upto Rs 60,000 and the highest rate is 15 per cent for loans between Rs 1,50,000 to 200,000.

But since most of the HBFC loans go to low income group people in the form of small loans, the yearly average rate of return on total portfolio hardly comes to 8 to 9 per cent.

Even this rate of return, the experts say, becomes effective after a year of the grant of loan, which the international agencies have particularly disapproved.

The summarised income statements of the HBFC reveal that it earned an almost insignificant profit of Rs 340 thousand in 1987 after suffering a loss of Rs 4.74 million in 1986 and Rs 14.68 million in 1985.

In view of the precarious financial condition, the HBFC is also seeking a major restructuring and has asked the Government to write off loans of about Rs one billion given in the past to the flood affected persons, repatriated

(Continued on EBR IV)

## HBFC

(Continued from EBR I)

Biharis from Bangladesh and for Mela Mandi loans.

Simultaneously, sources said, the HBFC has also asked the Government to convert Rs 800 million loan of the State Bank of Pakistan into equity. At present the debt-equity ratio of the HBFC is 98:2 which the experts feel is unsafe for any financial institution. The desirable level would be 90:10.

Sources said that the PICIC has already prepared the feasibility report for the setting up of a housing finance institution which should function purely on commercial lines. Working details are also reported to have been finalised for the joint venture company, which, sources hoped, would be completed before the end of June.

In another major development, the draft for the National Housing Policy is also reported to have been given the final shape and would be discussed at a high level meeting in Islamabad on March 22. The draft has been prepared in the light of the promises made by the Pakistan People's Party in its election manifesto.

# New housing policy to incorporate PPP's programme

F.P. Bureau Report

ISLAMABAD — A meeting of development experts of the ministry of housing and works is scheduled to be held here on March 22, in which the proposed "national housing policy" will be hammered out.

The meeting is expected to finalise recommendations and submit them to the federal minister for housing and works for final approval.

Sources said that in line with the PPP election's manifesto, the government is attempting to formulate a comprehensive housing policy in which 500,000 new houses will be constructed each year. The magnitude of the problem is gigantic, according to a report. It estimates that if serious action is not taken soon, 50 per cent of the population will be living in *Katchi Abadis* by the year 2000.

The new policy proposals are essentially aimed at bringing relief to the low income groups. A senior official reaffirmed that 'plots are not available to middle income groups'. He said that the cost of land had risen so greatly in the past decade that it was beyond the means of the low income earners. He added that the main problem facing the government was the availability of land at the present market prices.

The plan envisages distributing the 500,000 housing amongst the provinces under two possible scenarios. The first is based on the accepted population formula i.e. 56 per cent to Punjab, 20 per cent to Sind, 15 per cent to NWFP and 9 per cent to Baluchistan. The other scenario is more general, according to which distribution is made on an ad hoc basis of 50 per cent to Punjab, 30 per cent to Sind, 15 per cent to NWFP and 5 per cent to Baluchistan. However, inspite of what option is chosen 60 per cent of the new stock will be seven marlas (200 square yards) in rural areas and three marlas (about 75 square yards) in the urban areas.

Rather than building complete houses, the intentions to procure as much land as possible and then provide a basic infrastructural support such as water, sewerage facilities and roads connections. It would then be left to individuals to construct the houses.

In order to provide incentives to initiate construction it is putting forward a comprehensive financial policy proposals include the exemption of property tax for low income groups, the provision of soft loans from the House and Building Finance Corporation (HBFC) and other financial institutions. In order to expedite development, tripartite arrangements between the allottees of the plots, the financial institutions and developers will be made.

# Widow's plea

Unfortunately my husband, Abdul Hafeez Rajput, expired at Nishtar Hospital, Multan, on September 16, 1988, after protracted illness, leaving behind six minor children with no source of livelihood.

My late husband had received a loan of Rs. one lakh from the House Building Finance Corporation for the construction of a shelter against which he had regularly paid seven instalments under Account No. 2260001043-XE. The deceased has also left behind an aged mother and a widow with no other resource except the house. I cannot make both ends meet. Under the circumstances, it is impossible for me to clear the balance of the HBFC loan which is soaring with the passage of time.

I, therefore, humbly appeal to Prime Minister Mohtarama Benazir Bhutto, Federal Finance Minister and other concerned authorities to help a destitute widow by remitting the balance and earn her and her six children's gratitude. — MANZUR BEGUM, Widow of Haji Abdul Hafeez Rajput, Zargar Islamia/Halim Colony, Circular Road, D.I. Khan.

4 March 89

# The housing challenge

A NATIONAL housing policy is promised to be announced shortly. The stress will be on provisions for low-income groups and salaried persons. A large number of r...s are to be developed in the new satellite towns, and the House Building Finance Corporation will advance soft-term loans to the allottees for constructing houses.

That much is easily decided. Ambitious policies were drawn up in the past too. Yet the gap between planning and actual achievement remained as yawning as ever. The previous regime had said it would construct one million housing units in five years as part of its Five-Point Programme and launched the 7-marla and 3-marla schemes for rural and urban areas. But it was able to make no more than a dent in the problem of providing shelter to the shelterless. The planning and mismanagement was lopsided. The MNAs and MPAs manoeuvred the allotment of houses and plots to their partymen, friends and relatives and thus tried to make political capital out of it. The really needy ones remained out in the cold.

The present shortage runs to three million housing units, and an additional 600,000 are needed annually to cater to the growth in population. In the last few years, the ratio of people per unit of housing is estimated to have risen from 5.4 to 6.7 persons. In the urban areas, a quarter of the population is living in slums and the ratio is rising in consequence of the continuing flow of migrants from villages. Obviously, a colossal effort is needed to tackle it. Compact low-cost housing will have to be planned on a massive scale. Institutions like Housing and Physical Planning, HBFC and PCSIR will need to evolve the right technology, design and indigenous building material. There should be a long-term and comprehensive policy for ensuring unhindered availability on easy terms of the three basic inputs in house construction, i.e. land, building material and finance.

Land may even be allocated to private companies on the same conditions as are applicable to individuals. Improvement in local production of building materials could provide the substitute for present imports. A system of material budgeting based on forward planning and forecasting of future requirements can be evolved. And review and adjustment of duty and tax components on the local production and imports can be made a continuous process. All this will help lower construction costs for middle-income groups. To create additional sources of finance savings and loans institutions should be set up. There is wide scope for mobilising the savings of middle classes.

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# Two levels of life in Capital

By ZEBA TUFAIL

The cluster of mud huts with narrow passage-ways located right in the midst of Islamabad's elitist residential area of F-7/4 mirrors the two levels of the life in the Capital. The tumble-down dewllings of the wretched of the city stand in sharp contrast to the modern style homes of the rich.

Euphemistically called French Colony, it was actually so named because of its closeness to the French Embassy.

This kachi abadi, is inhabited by about 400 families. In all about 3,000 people are living in extremely difficult conditions.

In such colonies life poses tremendous difficulties for the residents since they lack even basic amenities.

On entering the French Colony, one is greeted by punget smells and polluted air pours into one's system. The poor residents, however, have become quite accustomed to this style of living.

What amazed this correspondent most was the non-availability of toilets for the residents. Heaps of garbage dotted the narrow streets, dirty water draining out of the houses formed puddles in the streets. Young children play in these lanes wallowing in the dirt and mud.

George who works in a government department told The Pakistan Times that normally children get sick becomes of the unhygienic conditions prevailing in the Colony.

He said that the Colony because a mess when it rains. One can hardly walk to one's house in the rainy season. Not infrequently, the mud houses crumble, damaging property and hurting people.

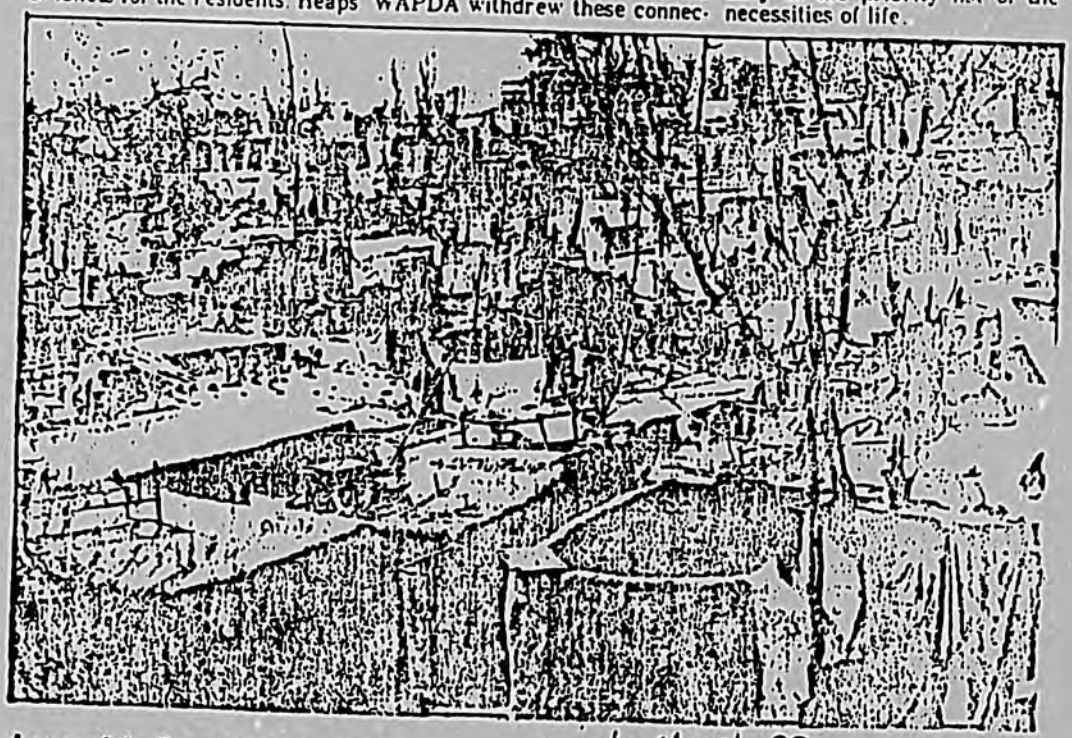
The residents were also not satisfied with the medical attention and the attitude of the doctors towards them. A resident said that they were always ignored by the doctors when sick patients were taken to the hospital.

Another major problem facing the residents was the non-availability of electricity in the Colony. A year ago, the WAPDA had provided electricity connections but two months after, the WAPDA withdrew these connections. Geroge said that despite the continued efforts of the residents no progress had been made to restore electricity to the Colony.

Since most of the children are school-goers, is is very difficult for them to study after the school hours because of non-availability. Hence the children study under lamps and candle light, eye sight of most of the children thus becomes weak. They suffer from other eye ailments as well, said George.

Women, residing in the colony, are generally house wives, however, a few of them have to work to supplement the family's income especially since the average number of people in a family were six to seven.

Forgetting that even certain basic amenities were lacking for them the women went as far as demanding for Sui gas. Children of the sweepers, equally energetic and enthusiastic, complained that they had no place to play forgetting that such things were secondary in the priority list of the necessities of life.



*A view of the French Colony — P.T.*

6 March 89

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4 March 89

## Small plots for homeless

# Benazir's directive to utilise Federal land

RAWALPINDI March 3: According top priority to housing for the homeless, Prime Minister Benazir Bhutto has directed that Federal land in possession of certain Ministries and Divisions be utilised for developing small plots for allotment to the homeless.

According to knowledgeable sources, the Prime Minister is reported to have expressed concern and even displeasure during a recent Cabinet meeting over the fact that thousands of acres of such valuable Federal land was lying unutilised in many cities and towns for lack of initiative and planning.

She directed the concerned Ministries and Divisions holding such land to examine the development of 80 to 120 square yards plots either in combined lots of 1000 plots or by breaking it down in appropriate chunks for allotment to homeless and helpless people.

Mohtarma Benazir Bhutto has also directed that possibilities be examined to sell away high priced unutilised Federal land to generate funds for buying cheaper land for development of housing colonies for the poor.

All Federal agencies in possession of such land are understood to have already received necessary directives in this regard and full evaluation is now underway. The Federal Ministries of Railways, Defence and Water and Power are the major holders of such lands in major, urben and even rural areas —APP.

6 March 89

## HBFC loans

A few days back it appeared in the Press that the House Building Finance Corporation has increased the percentage of interest on the loans given to people for building houses. This is really a very sad news particularly for those who have been paying the instalments regularly for the last many years. This step, certainly, would not be in favour of the people of this country. The present government has declared to provide shelter to the homeless but the decision of the Corporation is against that policy. Through an undesirable action it is trying to create problems for those who have drawn loans as it will prolong the period of instalments being paid by them already, and that too with a greater percentage of interest despite their poor income and unchecked dearness.

The Prime Minister is requested to intervene in the matter and instruct the Corporation not to increase the percentage of interest which in fact should have been decreased under the existing state of affairs to provide relief to the people of Pakistan —ZAHOOR AHMED, Rawalpindi.

Friday, March 3, 1989

## Housing policy

# Bhutto orders allocation of more funds

F.P. Bureau Report

LAHORE — The prime minister, Ms. Benazir Bhutto, has directed the federal finance ministry to allocate sufficient funds to federal housing ministry to implement the new housing policy being formulated by it.

The federal ministry for housing is expected to announce a new housing policy within this month to solve the problems of homeless people, especially the low-paid government servants.

The prime minister has also ordered the housing ministry to conduct field research in this connection. Under the new scheme plots in satellite towns would be allocated to the deserving people and the ministry would order House Building Finance Corporation to provide loans on easy terms. In the allotment of plots, and in providing the house building loans, priority would be given to the low-paid government servants.

Mr. Jehangir Badar, federal minister for housing and physical planning, said the other day that the government was committed to fulfilling its promise of providing basic necessities to the people. He said the federal government had ordered the housing ministry to provide shelter to all the people who needed it and that his ministry would prepare a feasibility report, formulate a policy and implement it very soon, as the government did not believe in cliches but in genuine service to the people.

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DAWN
Monday, February, 27, 1989

Tel: 516761-65; 516751-55; Cable Dawn, Karachi, Telex 23623 PIIPL PK and 24167 PIIPL PK

# Housing for the urban poor

LACK of proper shelter for hundreds of thousands who trek to the overcrowded cities from the rural areas every year has become a major cause of the degeneration of the urban environment in Pakistan. Crowded cities like Karachi and Lahore provide an example of how the mushroom growth of 'kachchi abadis' can lead to civic and social disruptions. Because of their electoral strength and the potential for launching agitations, the squatters have begun to attract a lot of political attention. Plans for low-cost housing for the urban poor remain high on the agenda of every administration and political party vying for power. Aid giving agencies and the World Bank have also been putting more emphasis recently on the urban crisis and, consequently, on housing for the poor. The World Bank is providing assistance to Pakistan for low cost housing and its delegation has met the Federal Minister for Housing and Works in Islamabad to discuss specific project. According to a report, the delegation has asked the Minister to submit to the Bank a final plan embracing low-cost housing schemes.

Such a plan should have been formulated a long time ago but the National Housing Policy of which the low cost housing schemes would be a part has been in the works for about a decade and is yet to be released. It is not clear if the Pakistan People's Party has done the required home work in this field and whether it is ready with a workable blueprint. In any case, it stands committed to providing shelter to the shelterless. In its manifesto, the party has made the ambitious promise of "half a million houses every year". This is to be achieved through provision of incentives to the private sector in the form of loans and tax relief. The manifesto also refers to special incentives for low cost housing and promises that the public sector would engage in crash programmes and endeavour to provide indigenous raw material and appropriate technology. These are bold designs and should lead to a gradual change in the housing situation if they are supported by planned action. It may however, be noted by way of aspects

pective that during the Sixth Plan, only 400,000 houses were constructed against the target of 670,000 houses. The needed effort to arrest the gradual deterioration in our housing conditions has yet to be made.

The present Government will be expected to make a major effort directed towards meeting the needs of the low-income families. Assistance from the World Bank and other aid giving agencies now increasingly mindful of the social sector should provide an additional incentive for coming up with the right strategy. The problem, without any exaggeration, is awesome. We share, with the rest of the Third World countries, a chronic shortage of shelter in our cities. The cycle of the creation of unauthorised slums and the compulsions to regularise them has vastly complicated the problem of providing shelter to the poor. This is a familiar pattern in developing countries where the unplanned, unregulated and often unserviced informal sector is responsible for 60 per cent of all new housing. It has also given rise to speculation and land-grabbing. We have seen how land, building materials and credit facilities are for the most part monopolised by the rich and the middle-class. Karachi underlines the irony of having so many flats, the cost of which is beyond low-income families, lying vacant and the 'kachchi abadis' overflowing with residents. This situation demands some new approaches to overcome the shortage of housing. These approaches may be formulated by experts who can begin by initiating a debate about ends, means, techniques and resources. Political, governmental and financial decision-making would play a crucial part in pursuing the right strategy. Planners who have been studying this issue have contrasted the sterility of multi storeyed blocks with the 'organic' qualities of slums. This is important because houses should be conceived as homes. This and other aspects of the urgency of providing shelter to the poor demand a long term plan and an innovative approach. But the imperative need of finding a solution in a relatively short period of time cannot be ignored.

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# LIST OF PERSONS MET

## Government of Pakistan

### Ministry of Finance

1. Mr. Zafar Iqbal, Joint Secretary, Internal Finance
2. Mr. Javed A. Noel, Joint Secretary, Investment
3. Mr. Athar M. Khan, Deputy Secretary

### Ministry of Planning & Development

1. Mr. A. G. N. Kazi, Deputy Chairman, Planning Commission
2. Mr. Zhaukat Kazmi, Joint Chief Economist
3. Mr. K. N. Soofi, Chief, Fiscal & Monetary Section
4. Mr. Fasihuddin, Chief, Private Investment Section
5. Mr. Naveed Ahmed, Deputy Chief, Programming Section
6. Mr. Riaz Ahmed, Research officer
7. Mr. Ijaz Akhtar, Chief, Housing & Physical Planning

### Ministry of Housing and Works

1. Mr. Humayun Faiz Rasul, Director General, National Housing Authority
2. Mr. Shamsul Haq, Joint Secretary, Urban Development and Environment
3. Mr. Bashid Ahmed, Joint Secretary, Katchi Abadis
4. Mr. Hasan Mahmood, Director, National Housing Authority

### Pakistan Industrial and Credit Investment Corporation

1. Mr. Aftab Ahmed, Deputy Managing Director

## Punjab (Lahore)

1. Mr. Shahzad Jamil, Director (Tech), National Housing Authority
2. Mr. Mohammad Naseeb, Director (Ad & Coord), National Housing Authority
3. Mr. A. U. Saleem, Director General, Katchi Abadis

## Sind (Karachi)

1. Mr. Salahuddin Qureshi, Additional Chief Secretary
2. Mr. T. A. Jafri, Director General, Sind Katchi Abadis Authority
3. Mr. Shahid Saleem, Director, Karachi Special Development Project
4. Mr. A. Baqi Siddiqui, Chief Engineer, Karachi Water & Sewerage Board
5. Mr. M. Yusuf Siddiqi, Project Director, Karachi Development Authority
6. Mr. S. Naeem Ahmed, Director General, Karachi Development Authority

## State Bank of Pakistan

1. Mr. Sibghutallah, Executive Director
2. Mr. R. A. Chughtai, Senior Deputy Director

Pakistan Banking Council

1. Mr. A. A. Sakrani, Member

Habib Bank Limited

1. Mr. Anwar Samad, Executive Vice President

House Building Finance Corporation

1. Dr. F. A. Rabbani, Managing Director
2. Mr. K. M. Talpur, Executive Director

Rawalpindi Municipal Corporation

1. Mr. Muhammmad Iqbal Saddozai, Chief Corporation Officer
2. Mr. S. Irshad H. Bokhari, Chief Engineer
3. Mr. Agha A. Rashid Tilani, Mayor

N.W.F.P. (Islamabad)

1. Mr. A. Majid Mohmand, Secretary, Physical Planning & Housing

World Bank

1. Mr. Geoffrey Read
2. Mr. Michel Chretien, Urban Finance Specialist (Washington)
3. Mr. A. H. Qureshi, Industries & Communications Adviser
4. Mr. Shahid Kardar, (Consultant) Systems Limited, Lahore

Asian Development Bank

1. Mr. Jeffrey Stubbs

Citibank

1. Mr. Sagheer Mufti, Resident Vice President

UNCHS Habitat

1. Mr. Bob Hardy, Architect, Senior Technical Adviser

Development et de L'aide Humanitaire (Switzerland)

1. Mr. Benoit Giradin, Secteur Urbain
2. Mr. Peter Schubeler, Planning & Architecture

U.S. Embassy

1. Mr. Lawrence N. Benedict, Economic Counselor
2. Ms. Carol E. Thompson, Finance & Development Officer

## COUNTRY RISK ANALYSIS

Summary: Since 1977, Pakistan has been averaging a robust growth rate of over 6 percent per annum in real terms. With the population growing at a rate of slightly over 3 percent per annum, per capita income growth has been about 3 percent per year. Officially recorded inflation had been moderate until recently. Of late however, the inflation rate has been rising and is currently estimated to be around 7 percent. Generally, open unemployment has not been a major problem to date. According to the latest World Bank country economic memorandum on Pakistan dated March 21, 1988, Pakistan's balance of payments performance over the same period has been "acceptable", though the external account suffers from inherent structural weaknesses. As of end-December 1986, the total level of disbursed and outstanding external debt was $14.6 billion, of which 89 percent consisted of medium and long-term (mlt) debt. Concessional assistance accounted for some 72 percent of total public debt. The average maturity of public mlt debt is estimated at about 26 years with an average interest rate of 5 percent. Pakistan's current credit worthiness allows it to borrow on short-term basis around $150 M (if it so desired) annually from international commercial banks. In recent years, the interest rate on these short term commercial loans has ranged from 75-100 basis points above LIBOR. Part of this credit worthiness stems from the fact that Pakistan has never defaulted on any commercial, bilateral or international development assistance including loans extended by such institutions as the World Bank, IFC, Asian Development Bank, etc. These institutions have been very active in extending development assistance to Pakistan. The current annual World Bank program is in excess of $500 million whereas the Asian Development Bank's is also over $500 million. The aid to Pakistan consortium countries at their recent meeting pledged $2.5 billion assistance for PFY 1988/89 beginning July 1, 1988.

Budget Deficit: Large budget deficits in recent years are a cause for serious concern. Between PFY 83 and PFY 87 the budget deficit more than doubled. It was 9 percent of GDP in PFY 87, and though projected to decrease to 8.1 percent of GDP for the current fiscal year, it is nonetheless unsustainable, and poses a strong threat to external and domestic financial stability of the economy. The large deficits have resulted in a rapid accumulation of debt service obligations both on domestic and external debt. Large budget deficits affect the balance of payments as well, and with external debt servicing ratio defined in terms of exports of goods and services now at 28 percent, lower current account deficits will be required to maintain international credit worthiness.

Monetary and Exchange Rate Policy: The Central Bank has for past 7-8 years been pursuing a relatively "tight money policy". The aggregate amount of credit in the economy is decided by the central bank whereby commercial banks have to adhere to a strict overall credit ceiling as well as sectoral credit limits. Monetary expansion has been prudent with

the money supply growth rate exceeding on average the nominal GDP growth rate by 2 to 3 percentage points at most. The exchange rate policy is that of "managed float" whereby the central bank regularly adjusts the value of the local currency against major international currencies. Since 1981, the rupee has depreciated by 40 percent in real terms against the U.S. dollar. Real depreciation in FY87 over FY86 was 14.3 percent. In recent years, Pakistan has relied almost exclusively on monetary policy for its economic management.

Current Balance of Payments Performance: With an almost 2:1 ratio of imports and exports, Pakistan's trade balance has been persistently negative. However, the trend in recent years has been that of a declining trade imbalance. In FY87, export cover had risen to 60 percent of imports. Compared to the rest of the 1980s, Pakistan's current account deficit was exceptionally low in PFY87 declining from about $1.7 billion (5 percent of GNP) in PFY85 to $.720 billion (2 percent of GNP). This was largely because of continuing strong export performance coupled with low international prices of Pakistan's major imports. Information to date on PFY87/88 suggest a 24 percent increase (in dollar terms) in export performance over PFY86/87 primarily due to higher international prices of cotton--Pakistan's principal export item. However, import growth for the same period has been 16 percent. As a consequence, compared with budget estimates, the current account deficit is expected to shrink by only $92 million to $964 million (or 2.4 percent of GNP). Worker's remittances, which at their peak level were $3 billion, have been steadily declining, thereby decreasing the cushioning impact provided for the current account deficit. These remittances are expected to stabilize at around the $2 billion level.

The capital account performance is expected to be affected by the lower-than-anticipated level of gross aid disbursements for the current fiscal year. Actual gross disbursements are expected to be $1.5 billion against the projected level of $1.6 billion. Despite this downward revision, however, gross disbursements would still be 7 percent higher than the previous year. Debt service obligations for the year (including $300 million repayments to the IMF) are expected to be around $1.2 billion. Though the overall balance of payments is expected to be positive, debt service obligations are likely to result in a draw-down of $300 million in gross foreign exchange reserves. Year-end FX reserves are not expected to be higher than four weeks work of imports of goods and services or around $500 million. The trend during the last year has been that of a declining absolute level of reserves (excluding gold holdings).

Future Prospects: Pakistan's balance of payments prospects depend on developments in the world economy as well as on domestic policies. Economic growth of industrial countries has been well below 3 percent per annum since 1985, although according to the World Bank, there are signs of improvement. Also of relevance to Pakistan is the projected modest growth of the oil exporting countries as a result of the stagnation of

oil prices. These are expected to remain at $18 per barrel up to 1990, and then rise gradually to $25 per barrel by 1995. The positive impact of the lower import bill for petroleum and petroleum products is, however, offset by declining remittances from migrant workers.

The World Bank's latest assessment of the Pakistan economy is contained in the March 21, 1988 country economic memorandum: growth through adjustment, along with a policy reform agenda to which the GOP has agreed. This document suggests that even with modest world trade growth, currently projected at 4 percent per annum, further progress on trade liberalization and domestic deregulation with continuation of an active exchange rate policy would have salutary effects on Pakistan's future economic performance. Undertaking such a policy reform agenda would result in improved competitiveness of Pakistan's exports whereby real export growth of 6.7 percent per annum can be envisaged and the share of exports in GDP would increase. Following this policy reform agenda, import growth can be restricted to 4.1 percent per annum.

According to the World Bank, these projections would result in a falling current account deficit, as a share of GDP, through PFY 1991, with a slight increase thereafter as permitted by the continued improvement in the debt servicing ration. This improvement in the balance of payments would enhance Pakistan's credit worthiness, by enabling it to finance its borrowing needs from traditional sources and rebuilt its gross reserves. The projections envisage a gradual buildup of reserves for about three weeks of imports to ten weeks over the period, and a reduction in the debt service ratio from the FY 1988 level of 28 percent to 21 percent.

Conclusion: The Mission endorses the spirit of the agreed upon policy reform agenda, and intends to support these trade and tariff liberalization measures through its continuing policy dialogue with the Government of Pakistan. Considering Pakistan's economic track record, its continued strong economic performance in recent years coupled with its ability and potential to further successfully undertake economic reform measures designed to control the twin deficits of the budget and the current account, Pakistan should have the ability to adequately service a long term loan such as the envisaged $100 million, 30 year maturity housing guarantee loan. This assessment is further bolstered by the fact that to date Pakistan has never rescheduled any foreign commercial debt or defaulted on any of its contractual liabilities involving foreign capital inflows. Moreover, as noted earlier, other major donors such as the World Bank and the ADB, despite some reservations, continue to support their respective multi-million dollar development assistance programs. Finally, there is also a strong possibility of the World Bank and the IMF extending a new structural adjustment facility along with a standby credit agreement to Pakistan so it can undertake the needed policy reforms.

# REVIEW OF THE PICIC PROPOSAL FOR THE HOUSING FINANCE CORPORATION OF PAKISTAN LTD.

The proposal has been prepared by Syed Aftab Ahmed, Deputy Managing Director, PICIC.

The Housing Finance Corporation will be registered as a joint stock company. Total subscribed capital will be Rs 125 million. The ownership will be as follows:

| | percent |
|---|---|
| IFC | 15 |
| PICIC | 15 |
| HBFC | 10 |
| SLIC | 10 |
| NIT | 10 |
| NDFC | 10 |
| General Public | 30 |

The Corporation will operate on commercial lines without any subsidy from the Government. The Chairman would be the Governor of the SBP.

The Corporation would aim to lend Rs 300 to 1,000 million to finance housing units for 5,000 to 10,000 households annually in its first five years. These households will have incomes in the range of Rs 1,000 to 5,000 per month.

Four different schemes are proposed:

1. Integrated developments- A typical 25 acre development would include 1,300 low income, 500 lower middle, and 200 middle income units. There would also be about 15,000 sq. ft. of commercial activity. Four such projects per year would require financing of about Rs 380 million.

2. Cooperatives- Such developments would tend to be at higher densities. Cooperatives have the advantage of having preferential tax status in the registration of mortgages. Joint liability would simplify the collection task.

3. Employee Groups- The Corporation would try to supplement existing programs, moving down the income distribution. Projects would range from 50 to 200 units and cost about Rs 10 million. The Corporation would hope to obtain guarantees from the sponsoring companies.

4. Individuals- This would be for higher income clients.

Most of the Corporation's loans would be for less than Rs 50,000 per unit. Loans would cover 60 per cent of the cost of the unit, and be for 10 to 15 years at market rates, and would aim for a 2 to 3 per cent spread. The security would be a first mortgage on the property.

The Corporation plans to have 5 regional offices, each with three people initially. Total staff will grow from 50 in the first year to 78 in the fifth. The high initial staff is needed to build up a sufficient volume of business to cover costs (presumably of financial resources).

The Corporation would obtain its financial resources from individual deposits linked to an eventual loan, and from TFCs and other long term marketable securities. It is suggested that about 8 per cent be paid on the deposits, which is comparable to one year time deposits at commercial banks. It is anticipated that depositors might be eligible for loans after three years. Most of the funding will come approximately in equal proportions from term debt and share capital and reserves: this will amount to about Rs 1.1 million out of a total of Rs 1.6 million in the first five years. The Corporation will market its obligations to institutional savers. However the proposal admits that this will be difficult in the early years, as the Corporation builds up its reputation. A Rs 300 million line of credit from IFC is suggested to reassure institutional lenders. After several years he Corporation would issue mortgage backed instruments.

The proposal admits to the risks inherent in the proposed financial structure. There is high operating leverage once the initial staff and systems are in place; the incremental cost of generating new mortgage loans is small. There is also high financial leverage; minimal reserves are needed since borrowing is backed by secured, stable home loans. However the Corporation has to be able to originate a high volume of secure loans fairly quickly. HFC will also have a large burden of borrowings. The intention is to control this risk by having a debt/equity limit of 15:1 as part of the its credit line conditions. Interest coverage criteria would also have to be set up before additional debt is incurred. Finally the Corporation may not be able to raise sufficient long term resources to fund its operations. A SBP standby line of credit of Rs 500 million is suggested to reduce this risk.

The key requirements for success are that there is substantial latent demand for housing finance and that the necessary long term financial resources can be raised.

The exceptionally low level of housing investment in recent years, compared with other developing countries, may mean that there will be considerable demand for housing finance (see Annex 10). The household survey carried out as part of the ADB studies of the housing sector indicate not only that many households are prepared to pay for better housing conditions, but that they are prepared to make savings deposits in institutions such as the Corporation to achieve better housing.

Conditions are now being created that will make it easier for the Corporation to raise long term funds.If market rates are offered institutional investors should be prepared to take up much of the debt. Also, mortgage backed bonds should be appealing if their price is sensitive to market conditions. The recent sale of WAPDA bearer bonds may have been less successful than expected partly because they were incorrectly priced to attract "black" money. The next issue of WAPDA bonds will also be more liquid. Their issue may also have been handicapped by the fact the financial system is not integrated and much of it depends upon directed and subsidized credit and is characterized by distorted prices. As the financial system is integrated and becomes market based, proposals such as PICIC's will become more viable.

# THE ROLE OF HOUSING FINANCE IN THE DEVELOPMENT OF PAKISTAN'S FINANCIAL SECTOR

Housing finance is one of the safest ways to initiate the process of financial liberalization. Financial liberalization can be defined as paying greater attention to proper interest rates and the measurement of risks while giving less attention to the volume of credit going to specific sectors.

Pakistan has accepted the need to liberalize its financial sector, including housing finance. Pakistan has a system of directed credit and interest rates that do not reflect the real risks and public or joint sector financial institutions that are not financially viable. Public sector interventions in the housing sector are characterized by directed credit and substantial subsidies. The financial sector policy changes agreed between the World Bank and the Government are referred to in the main text.

Housing is one of the safest assets in the economy. Financial systems will become more stable if financial institutions are allowed to diversify their asset portfolios into housing.

Housing finance systems can encourage the accumulation of financial savings. The accumulation of financial savings in the form of deposits rather than physical assets adds to financial deepening and will promote a more efficient allocation of savings in the economy as a whole. There is also a complementarity between the accumulations of savings in the form of deposits in housing finance institutions and future investment in housing, which is the main asset of most households.

Better access to housing finance also helps in the achievement of shelter policy objectives. A good housing finance system will improve the efficiency and stability of housing and urban infrastructure investment.

Housing finance also brings social benefits. Market based systems for those who can pay frees up resources for those who cannot. Also, indirectly, a stable and abundant supply of housing will benefit the poor by stabilizing housing rents.

A market-based housing finance system can bring fiscal benefits by eliminating the need for directing credit to the sector. Resource transfers through directed credit are an implicit tax on the financial system. They are an inefficient means to allocate resources.

HBFC, the commercial banks and other Pakistani financial institutions provide only a very small proportion of the credit required for housing. According to the ADB Survey, 59 per cent of the funding required for land and 42 per cent of the funds for housing come from personal savings; 26 per cent and 15 per cent respectively come from the liquidation of assets. The bottom quartile of the income distribution obtain all the finance for land and housing from these two sources. HBFC provides 17 per cent of the housing requirement and nothing for land.

This means that most of the real housing finance system is not integrated into the formal finance system for the economy as a whole.

This lack of integration is a serious problem because housing is such a large component of economic activity. As countries develop, housing forms a larger proportion of investment and GDP. Housing investment typically contributes 3 to 10 per cent to GDP; Pakistan is at the low end of that range according to official statistics. Housing as a proportion of gross capital formation typically ranges from 18 to 25 per cent; the proportion for Pakistan is an exceptionally low 9 per cent, according to official statistics. Housing is typically a large proportion of the fixed capital stock. In India, for example, housing is the largest single form of reproducible household wealth. In the U.S., housing represents 50 per cent of the fixed capital stock. When the housing sector (or any other important sector) is not integrated in the financial sector, the economy as a whole suffers efficiency losses since the financial system does not provide the information about relative prices and investments that it could.

Housing has a very important role to play in the mobilization of savings, a critical objective of this program as well as the financial sector adjustment as a whole. Official statistics indicate that Pakistan's domestic savings rate is now a very low 10 per cent of national income, less than half the average for low income countries. Where housing finance is available, housing provides the dominant savings instrument for most families. Savings for housing take place in three forms: prior savings for down payments; savings through the amortization of loans; and capital gains.

There are a number of reasons why savings for housing is particularly appealing to households in developing countries. The return on housing is not reduced by the interest rate ceilings that affect other forms of financial savings. House values keep pace with inflation and tend not to fluctuate. Housing is a widespread and familiar investment. Little financial sophistication is required to save through ownership of a house. In a rapidly urbanizing country such as Pakistan, housing has a very high and stable rate of return.

Market-oriented housing finance institutions have to perform two forms of intermediation that are not likely to be forthcoming elsewhere in an underdeveloped financial sector: denomination and maturity intermediation. Under the former, the problem is that households are prepared to save small sums but need to borrow large amounts of money to buy a house. Savers may be prepared to deposit one quarter of their annual income; borrowers may require mortgages that amount to two to three times annual incomes. Maturation intermediation is important because savers have on average shorter time horizons than borrowers.

In a financially repressed economy such as Pakistan, housing finance policy raises some issues that are quite distinct from the financial policy as a whole. There are two reasons for these unique policy concerns. The first is that housing finance represents the single most important liability for almost all low income households. Improving the efficiency of this form of finance will have the broadest distributive effects of all improvements in financial efficiency. The second reason is that the demand for housing as an asset is income elastic: demand should expand as the economy grows and urbanizes. However, supply has not expanded to meet demand partly

because of Pakistan's repressed finance system. Housing finance policy has been designed to discourage rather than encourage investment, despite the ambitious housing policy goals, as the statistics on low housing investment as a proportion of GDP and on overcrowding show. The highly subsidized public programs are not a viable alternative to a market-oriented housing finance system.

It is important to make a very clear operational distinction between social housing programs and the housing finance system. Pakistan has confused the two, resulting in neither working well. There is a conflict between the federal or provincial government concern with the affordability problems of their low income constituents and the necessity to price realistically and share financial risks under mortgage lending. HBFC has had social as well as financial objectives; the outcome has been that it has failed to provide finance for any but middle and upper income households and that it has at the same time incurred large financial losses.

The housing finance system in Pakistan could probably best assist in the achievement of shelter goals, while at the same time making a substantial contribution to the integration of the financial sector, if the housing finance institutions concentrated on the low-to-middle income groups and above and the Government applied its limited resources to the lowest income groups. The housing finance system will eventually evolve into a market-oriented one that also serves low income households, but that will probably take many years.

Housing finance can contribute to long term financial development, particularly in terms of resource mobilization. Housing finance institutions can familiarize small savers with the banking system by exploiting the reciprocity between deposit and lending needs and encouraging the creation of mutual housing finance institutions. At the moment this tends to occur only in the informal sector in Pakistan.

Housing finance can also play a positive role in meeting the demand for high quality long term financial assets. Provident, pension, and insurance funds often find long term bonds backed by well written mortgages an appealing way to provide such securities at positive yields.

To maximize the impact of housing finance on the development of the financial sector, a regulatory system is required that will encourage new lenders to enter the market. The objectives of such a system are as follows:

- -- protect the public from the consequences of fraudulent bankruptcies
- -- foster growth and diversification
- -- insure the financial integrity of the housing finance institutions
- -- establish net worth requirements for the safety of depositors
- -- restrict conflict of interest
- -- insure the proper management of risks.

Given the need for greater financial integration, it is desirable that the supervisory body be located with the overseers of other financial institutions; this would seem to be the SBP. However, housing finance is sufficiently distinct from other forms of finance for there to need to be a separate department within SBP.

Two related examples of current GOP policy 'reforms' are underway. First is the issue of user fees to help finance costs associated with water and sanitation infrastructure provision. The GOP has asked the Provinces to support the concept, and it is at the municipal level (due to pressure on elected officials) that reform is stymied. The second policy is to lower "environmental standards", eg., the requirement for water-bourne waste disposal. The GOP clearly recognizes that katchi abadis are the result of standards which preclude a large segment of the population from formal housing.

## THE HOUSING MARKET IN PAKISTAN

The result of imperfections in the shelter provision market are known in Pakistan as Katchi Abadis. These are settlements in urban areas consisting of housing without legal land tenure, little or no public services, and in most cases poorly constructed dwellings.

GOP estimates state that approximately 25 per cent of the urban population is in Katchi Abadis, and up to 35 per cent in some cities like Karachi. Even the master planned capital of Islamabad has a Katchi Abadi population estimated at over 15,000.

Most Katchi Abadis were developed as an encroachment on state or federally owned land, and in direct response to a lack of available housing sites. While the paucity of serviced land was the most significant factor behind their creation, the lack of housing finance also contributed by reducing the affordability of what plots were available.

In many cases, the residents of Katchi Abadis have occupied their homes for some time. A survey in Karachi found that 29 per cent had been there since birth, and another 32 per cent since 1955. Not surprisingly, a very high percentage (84%) of households surveyed consider themselves owners of the dwellings they occupy, in spite of the fact that virtually none of the residents have legal tenure rights to their plots. The response is due no doubt to both their longevity on the site and the previous administration's decree of forthcoming proprietary rights.

In spite of the length of their residence, the occupants of the surveyed Katchi Abadis still had low incomes. The median household income of the sample was Rs. 1,700 per month, and the average income Rs. 2470. The survey also ascertained that personal savings was by far the largest source of financing for both housing construction, and purchasing of existing homes.

The following table indicates the breakdown of sources of housing finance for Katchi Abadi properties.

| | | Percent of** Households Using Source | Average financing Per Property by Source (Rs) | Percent of Finance |
|---|---|---|---|---|
| A. | If Property Constructed | | | |
| | Savings | 81 | 16,781 | 62 |
| | Loans | 40 | 5,800 | 21 |
| | Remittances | 3 | 1,655 | 5 |
| | Others* | 10 | 2,781 | 11 |
| | | | 27,017 | 100 |
| B. | If Property Purchased | | | |
| | Savings | 76 | 13,167 | 56 |
| | Loans | 34 | 5,226 | 22 |
| | Remittances | 2 | 1,413 | 6 |
| | Others* | 17 | 3,702 | 16 |
| | | | 23,508 | 100 |

(See next page for notes and source)

* Other sources include sale of jewellery and other assets, gifts from relatives, etc.

**The column total for the four sources may exceed 100% because of the use of multiple sources of finance for a property.

Source: IBRD Shelter Sector Review

What is unfortunately not known is the source of loans, although given the lack of secure title they are most likely from informal sources, i.e. not HBFC or commercial banks.

A recent analysis of the housing sector by consultants for the ADB found that construction costs account for 60 per cent of the total cost of shelter, with serviced land accounting for the remainder. Referring to the table above, if land cost were included at the proportion just noted along with cost of non construction noted in item "A", the total cost of the house and plot would be approximately Rs. 45,000.

Interestingly, Rs. 45,000 is the cost of the least expensive low housing unit and land available in Karachi, as identified by the ADB. The unit was developed in the North Karachi township of Surjani, in a turn-key process in which the KDA serviced the land and private house builders completed the dwelling. In this project land costs ran only 23% of the total; but the land was priced at a below-market price, based on its original cost. If the land was priced at current market value, the cost of a cross-subsidized 70 square meter plot would increase by Rs. 2,200.

Assuming that the least expensive, non-subsidized unit possible is in the Rs. 47,200 range, what is the potential housing finance market to both households in general, and the Katchi Abadi households represented in the survey?

Based on the assumption that households are willing and able to pay 20% of their income in housing, can assemble a 30% down payment, and repay a 15% rate of return to the lender over 20 years, just over half the households (52%) in Sind would be unable to afford the least expensive unit noted above. The required income is estimated to be Rs.2,197 per month. This figure is some Rs. 500 higher than the median, but Rs. 300 lower than the average in the surveyed Katchi Abadi.

If the cost of this representative least-cost unit was reduced by 25% to Rs. 36,000, the number of households unable to afford formal housing drops to 35% - even at a commercial rate of return on credit of 15 percent. The new required monthly income is Rs. 1,536 which is nearly Rs. 150 lower than even the <u>median</u> income in the surveyed Katchi Abadis.

Such a 25% reduction in costs may not be difficult to achieve, recalling that 77% of the total cost was accounted for by construction. Of this amount, 40% is accounted for by labor costs. Permitting the owner to engage in "self-help" finish work and reducing the standard of the water supply/sanitaryware (which accounts for 12% of the entire construction cost) could quite possibly accomplish the reduction.

Thus, assume that formal housing can be developed that is affordable to nearly two-thirds of the urban population, with the assistance of a market-oriented housing finance system. Assume also that the HBFC and NHA will administer GOP programs that assist the remaining 35 percent of the urban population. What does this say about the possible country-wide demand for market-oriented housing finance?

A report prepared by a consultant to the ADB estimates the total financing need at Rs. 9.1 billion in 1988/89, and that it will rise to Rs. 14.6 billion in 1993/94 (in constant prices). The report further breaks down the actual market for housing finance as follows:

| | | Rs: Billion |
|---|---|---|
| A. | Upper Income Sector (Rs.6000 per month and above) | 2.7 |
| B. | Moderate to Middle Income Sector (Rs.1,500-Rs.6,000 per month) | 4.8 |
| C. | Low Income Sector (Less than Rs.1,500 per month) | 1.6 |
| TOTAL | | 9.1 |

Of this total amount, Rs. 7.5 billion/year (US$395M) could be lent by market-oriented housing finance institutions for housing costing down to and including the representative Rs. 36,000 house and plot in North Karachi. Significantly, between 1979 and 1987, only 12% of HBFC's total disbursements were at the level of Rs. 40,000 or less, and these were highly subsidized.

The ADB report also indicates that in 1988-89, Rs. 9.9 billion (RS$521M) could be made available for housing finance by non-commercial sources, e.g., personal remittances from abroad, savings, and informal borrowings. Although this figure may seem high, an estimated Rs. 10 billion was made available last year, from largely these same sources, to invest in what turned-out to be fraudelent investment schemes. "Black money" is another potential source of capital. A recent newspaper article (see Annex 5) stated that 30 percent of all the currency in circulation was in this category.

Given the proper financial incentives and regulatory protections, a good portion of all of these funds could capitalize the proposed market-oriented housing finance system.

## BACKGROUND INFORMATION ON ENVIRONMENTAL CONDITIONS

Eighty per cent of the urban population in Pakistan is said to have access to a "safe" water supply. However, the water distribution system servicing that population is suspect: inadequate pumping facilities combined with old decaying waterlines allow seepage that introduces both chemical and biological pollutants into the domestic water system. (Of that percentage, only 35 per cent have connections at their homes, with the remainder using public taps or standpipes.) Residents in the 20 per cent that do not have access to safe water are of course exposed to even greater risks.

Contaminated drinking water can result in gastrointestinal disorders as well as other serious infectious diseases such as polio, hepatitis, cholera, typhoid, and tuberculosis. While a similar figure is not available for Pakistan, a recent study in India estimated that just under $350 million is spent every year in terms of medical treatment and lost production due to illness and disease caused by unsafe drinking water in urban areas.

Water quality is affected by contaminants from industrial, agricultural, and domestic sources. Only the latter will be discussed here, as it is the most closely linked to shelter. Domestic water supplies are primarily affected by biological contamination caused by improper disposal and treatment of human wastes. It is currently estimated that 52 per cent of the urban population has access to sewage facilities. However, only a very small proportion of the waste represented by that number is treated in any way. For example, in Karachi (one of the few cities that has a treatment capability at all) nearly 200 million gallons of sewage is generated each day, while only some 30 MGD is treated.

The GOP's goals in the areas of water supply and sanitation are articulated in the current Seventh Five-Year Plan. The water supply target is to bring safe water to 100 per cent of the urban population in large municipalities, and 70 per cent in smaller cities. The sewerage target is for 95 and 50 per cent coverage. The Plan estimates that 13.6M people will be affected by the water provision, and 12.4M by the sewerage. No total cost is given for this work over the Plan period, but Rs. 3.45 billion has been allocated in the SDP budget. Additional funding will come from the PSDP account and budgets of local councils.

One important note is that the Plan states that, "Full recovery of capital and operation & maintenance costs will be made through levy of user charges, in order to eliminate subsidies and enable the project(s) to pay for (themselves)". The Plan goes on to say that in order to keep the capital costs (and user fees) of the projects low, external loans will be passed on to the executing agencies by the federal government at the same rate as actually charged by the foreign donor agencies.

# POLICY ACTION PLAN

Objective No. 1: Develop policies for market-oriented housing finance within the context of both structural reform in financial and capital markets and overall shelter policies.

## Actions

1. Establish a Working Group on Housing Finance to address the housing finance policy objectives, the promotion of the concept and purpose of market-oriented housing finance institutions, the necessary legal and regulatory framework, the role of the GOP in housing finance, and the elimination of barriers to the flow of funds to mortgage lending.

   Implementing Steps

   a. AID requests the GOP appoint the Joint Secretary for Internal Finance, head of a Working Group for Housing Finance.

   b. The Joint Secretary, with AID support, will establish a Program that addresses key housing finance policy objectives, technical assistance that may be required to prepare specific studies, promotion strategies and work schedules among other.

   Benchmarks

   a. The AID Letter of Request is sent to the Minister of Finance.

   b. The Working Group Promotion, Technical Assistance and Training Plans are prepared.

   Estimated Timing

   a. The Working Group constituted by June 1989.

   b. The Working Group Promotion, Technical Assistance and Training Plans prepared by January 1990.

2. Within the framework of shelter policy, formalize responsibility for formulation of market-oriented housing finance policies in the Ministry of Finance, and specifically with the Secretary for Internal Finance.

   Implementing Steps

   a. AID requests that the GOP formalize responsibilities for formulation and promotion of market-oriented housing finance in the Joint Secretary for Internal Finance of the MOF.

Benchmarks

a. USAID/Pakistan Director sends letter to Minister of Finance with request.

b. MOF Minister appoints Joint Secretary for Internal Finance Chair of the Working Group on Housing Finance and responsible for the development of housing finance policies and the market-oriented housing finance system.

Estimated Timing

a. Letter sent by June 1989.

b. Joint Secretary appointed by June 1989.

Coordinate housing finance policy development with shelter policy as directed by the Ministry of Housing and Works, and reform of the financial sector as determined by the GOP in conjunction with the financial sector adjustment loan.

Implementing Steps

a. Assign responsibility to the Working Group to coordinate with and monitor progress on financial and shelter sector policy development.

b. Coordinate with World Bank (IBRD) and Asian Development Bank (ADB) staff and technical assistance teams assisting the GOP develop financial and shelter policies.

c. Formulate recommendations to promote and integrate housing finance into policy development.

d. Convene meetings with GOP financial and shelter sector policy development committees.

Benchmarks

a. The Working Group formally made responsible for coordination.

b. Recommendations prepared by the Working Group.

c. Meetings convened by both the Working Group and AID with financial sector and shelter sector policy committees and the ADB and IBRD.

Estimated Timing

a. Working Group coordination responsibilities established by September 1989.

b. A round of coordinating meeting was held with other donors during March 1989 the next round would be held during May 1989.

c. Coordinating meetings with GOP policy committees will be carried out on an on-going basis.

Objective No. 2: Rationalize the GOP role in financing shelter

Actions

1. Focus GOP subsidies to low income families through programs implemented by the NHA. Eliminate GOP subsidization of interest rates in segments of the market where the private sector can finance shelter needs at market interest rates.

Implementing Steps

a. Formulate recommendations as necessary to assure compatibility of future HBFC mandate and market-oriented housing finance system.

b. Recommend guidelines to establish and target manageable levels of GOP subsidies for shelter to benefit low-income families.

c. Review the experience of other developing countries in targetting subsidies.

d. Analyze public and private sector shares of the housing market.

e. Review NHA experience in implementing GOP shelter projects and the feasibility of NHA becoming the sole entity responsible for GOP subsidized shelter programs.

Benchmarks

a. Recommendations on compatibility between HBFC and a housing finance system prepared and presented to GOP for review and implementation.

b. Study completed that reviews experience in targetting subsidies, developing subsidy guidelines and the role of NHA in subsidized programs.

c. Report completed that analyzes public and private sector shares of the housing market.

Estimated Timing

a. Compatibility recommendations prepared by January 1990.

b. Subsidy guidelines prepared by March 1990, including targetting and role of NHA.

c. Housing market analysis completed by June 1990.

2. Establish roles for the NCBs, DFIs and HBFC consistant with the formulation of market-oriented private and joint sector institutions.

Implementing Steps

a. Prepare study that analyze the conditions and requirements that may be required that support the NCBs and HBFC participation in a market-oriented housing finance system.

b. Present conclusions and recommendations of study to MOF, Pakistan Banking Council, HBFC, NCBs and donors.

c. Develop TA and Training Program to support new role implementation by NCBs and HBFC.

Benchmarks

a. The Study on NCBs and HBFC participation in the system completed.

b. TA and Training plan developed for NCBs.

Estimated Timing

a. Scope of Work for study by January 1990. Final draft by June 1990.

b. Worskshop convened to present results by July 1990.

c. TA and Training Program developed and first activities initiated by September 1990.

Coordinate efforts to recapitalize HBFC and restructure the institution and its housing finance policies.

Implementing Steps

a. Coordinate closely with HBFC/ADB technical assistance teams to advance alternative role for HBFC.

b. Monitor actions proposed by HBFC to write off defaulted portfolio and restructure its lending operations.

c. Develop report on effects of HBFC interest rate policy on the housing finance system for the shelter policy development committee.

d. Include HBFC in TA and Training designed to support the development of HFCs.

Benchmarks

a. Meetings held with HBFC and ADB technical advisors.

b. Participate in reviews of policy and program development proposals.

c. Study prepared for discussion with GOP coordinating committees.

d. TA and Training modules developed and events held.

Estimated Timing

a. Coordination and monitoring has already begun with donors and HBFC and will continue throughout the life off the project.

b. Scope of Work for HBFC interest rate policy analysis by September 1989. Final report by May 1990.

c. TA and Training for HFCs with HBFC participation initiated by January 1990.

4. Monitor the returns to deposits in savings schemes to ensure their consistency with market competition.

Implementation Steps

a. Prepare analysis of National Savings Schemes to determine the volume of deposits generated, participants in the schemes, deposit end use, interest rate structure and effect on market competition for deposits, especially for housing finance.

b. Propose recommendations for alternative National Savings Schemes deposit rates and the impact new regulations will have on the national budget, as well as other depository institutions.

c. Promote the adoption of recommended regulations.

Benchmarks

a. Scope of Work for analysis of National Savings Scheme prepared. Final report completed.

b. Proposed regulations for National Savings Schemes prepared by.

c. Recommended regulations adopted.

Estimated Timing

a. National Savings Scheme completed by January 1991.

b. Proposed regulation prepared by March 1991.

c. Recommended regulation adopted by July 1992.

Objective No. 3: Develop a legal framework appropriate to the creation of private and joint sector housing finance companies.

Actions

1. Confirm an interim process for review and licensing of housing finance institutions within the context of current procedures of the MOF and State Bank of Pakistan and the proposed reforms and consolidation efforts.

Implementing Steps

a. Analyze current procedures of the MOF to review and license new finance institutions and any special considerations that need be made for housing finance institutions.

b. Verify within the MOF the office or department responsible to which applications would be presented.

c. Inform the public of the process to facilitate participation.

Benchmarks

a. Scope of Work for study of procedures prepared and study completed that presents responsibilities and procedures.

b. MOF manual for review and licensing of housing finance companies prepared.

c. Newspaper announcements present MOF intent and process.

d. Private and joint sector HFC's are formed and licensed.

Estimated Timing

a. MOF current procedures analysis completed by June 1989.

b. Newspaper announcements published by June 1989.

2. Monitor the status of the newly drafted law that would consolidate the regulatory and supervisory functions of banking and non-bank finance institutions.

Implementing Steps

a. Working Group reviews draft law for references to housing finance and makes recommendations to advance the housing finance theme.

b. Coordinate with SBP staff responsible for draft legislation of Working Group recommendations.

Benchmarks

a. Working Group review of draft law completed.

b. SBP informed of conclusions in working session with Working Group.

Estimated Timing

a. Review completed by July 1989.

b. SBP informed by August 1989.

3. Review the merits of establishing special provisions for housing finance within the proposed framework of legislation and regulations for establishing banking and non-bank finance institutions.

Implementing Steps

a. Prepare a study that identifies special provisions for housing finance that may be required in legislation and the regulatory framework, and propose recommendations to draft legislation and current regulatory and supervisory practice.

b. Present recommendations to responsible institutions.

c. Enact modifications to proposed language and procedures.

Benchmarks

a. Scope of Work prepared for study of the need for special provisions for housing finance.

b. Study completed and recommendations disseminated

c. Work sessions called to debate recommendations.

d. Modified laws approved by responsible entity.

Estimated Timing

a. Scope of Work prepared by January 1990.

b. Study completed by June 1990.

c. Working sessions held and recommendations adopted by August 1990.

d. Modified laws and regulations approved by January 1991.

Objective No. 4: Establish regulatory and supervisory provisions appropriate to market-based housing finance institutions.

Actions

1. Confirm the interim process for supervision and closure of housing finance companies with in the current procedures of the MOF and SBP.

Implementing Steps

a. Review current regulatory and supervisory framework's ability to accommodate housing finance companies.

b. Prepared modifications, if necessary, to current procedures.

Benchmarks

a. Report prepared on review of process.

b. Modifications presented and enacted, if necessary, to accomodate housing finance companies.

Estimated Timing

a. Review Report prepared by September 1989.

b. Modifications recommended and enacted by November 1989.

2. Coordinate development of the housing finance regulatory framework with GOP efforts to consolidate regulatory functions for banking and non-bank financial institutions within the State Bank of Pakistan.

Implementating Steps

a. Inform entities responsible for consolidating regulatory functions within the State Bank of Pakistan of special provisions for housing finance.

Benchmarks

a. Report that identifies the needs for special provisions for housing finance prepared and presented to SBP.

b. Regulatory framework reflects housing finance requirements.

Estimated Timing

a. Special Provisions report prepared and presented to SBP by March 1990.

b. Regulatory framework modified by March 1990.

3. Evaluate current review and audit procedures and information systems employed by the current regulatory system and make recommendations to strengthen them.

Implementing Steps

a. Prepare analysis of review and audit procedures.

b. Develop recommendations for strengthening procedures.

c. Provide TA to implement recommendations.

d. Prepare analysis of information systems.

e. Develop recommendations for strengthening information management.

f. Provide TA to implement recommendations.

Benchmarks

a. Scope of Work prepared for analysis of review and audit procedures.

b. Report presented and recommendations discussed.

c. TA contracted.

d. Scope of Work prepared for information systems analysis.

e. Report presented and recommendations discussed.

f. TA contracted.

Estimated Timing

a. Scope of Work prepared by September 1989.

b. Reports presented by January 1990.

c. TA contracted by April 1990.

Objective No. 5: Develop instruments and procedures to facilitate the growth of housing finance and to remove barriers and disincentives to market growth.

Actions

1. Review the legal and administrative steps of the current foreclosure laws and make recommendations to reduce the bottlenecks and delays in the present foreclosure process.

Implementing Steps

a. Prepare review of current foreclosure laws and practice.

b. Develop recommendations to facilitate the present foreclosure process and to modify existing legislation.

c. Convene workshop to discuss foreclosure issues and enact recommendations.

Benchmarks

a. Scope of Work developed for review of foreclosure laws and process.

b. Report prepared and disseminated.

c. Recommendations for modified legislation and administrative procedures prepared.

d. Modified legislation enacted and administrative procedures instrumented.

Estimated Timing

a. Scope of Work prepared by September 1989.

b. Report prepared by January 1991.

c. Recommendations prepared by June 1991.

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d. Modified legislation enacted by June 1992.

e. Administrative procedures instrumented by January 1991.

2. Coordinate review of foreclosure and arrears with GOP measures to improve debt recovery in all sectors.

Implementing Steps

a. Review other GOP activities related to debt recovery in other sectors.

b. Inform indicated entities of foreclosure activities.

Benchmarks

a. Scope of Work prepared for review.

b. Review prepared.

c. Workshop held with pertinent GOP and TA groups on debt recovery.

Estimated Timing

a. Scope of Work prepared by September 1989.

b. Review prepared by March 1990.

c. Workshop held by August 1990.

3. Review the desirability of mortgage and deposit insurance as an interim procedure designed to enable risk reduction and mobilization of private capital.

Implementing Steps

a. Prepare analysis of utility of mortgage and deposit insurance to the development of a housing finance system.

b. Hold workshop with private sector and GOP entities to discuss results of analysis.

c. Make recommendations to GOP.

Benchmarks

a. Scope of Work prepared for analysis.

b. Workshop held.

c. GOP responds to recommendation made.

Estimated Timing

a. Scope of Work prepared by July 1990.

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b. Workshop held by December 1990.

c. GOP responds by March 1991.

4. Investigate the applicability of adjustable mortgage instruments designed to assist in long-term lending in an environment of uncertainty and inflation.

Implementing Steps

a. Prepare an analysis of the applicability of adjustable mortgage instruments in Pakistan and their effect on resources mobilized for housing and on the potential borrowers.

b. Hold workshop for public and private financial, housing and banking entities to discuss results of analysis.

c. Develop recommendations to build adjustable mortgage instruments into the housing finance system.

Benchmarks

a. Scope of Work prepared for analysis.

b. Workshop held.

c. Recommendations prepared and disseminated.

Estimated Timing

a. Scope of Work prepared by July 1990.

b. Workshop held by January 1991.

c. Recommendations prepared and disseminated by March 1991.

5. Review the adequacy and applicability of the State Bank's line of credit to finance institutions for short-term liquidity requirements.

Implementing Steps

a. Prepare review of adequacy and applicability of SBPs line of credit for short-term liquidity requirements.

b. Convene meeting with SBP to discuss findings and develop recommendations.

c. Confirm and/or modify the SBP line of credit.

Benchmarks

a. Scope of Work for review prepared.

b. Presentation of findings made to SBP.

c. SBP line of credit confirmed and/or modified.

Estimated Timing

a. Scope of Work developed by January 1990.

b. Presentation to SBP held by September 1990.

c. SBP line of credit acted upon by November 1990.

6. Assess the utilization in housing finance of long-term funds such as those available in life insurance or pension schemes.

Implementing Steps

a. Prepare a report on the utilization a long-term funds in housing finance such as these available in life insurance or pension schemes.

b. Convene meeting with MOF and life insurance and pension schemes representatives to present findings and prepare recommendations.

Benchmarks

a. Scope of Work for report prepared.

b. Report prepared.

c. Meeting convened to discuss findings.

d. Recommendations prepared and presented to MOF.

Estimated Timing

a. Scope of Work prepared by March 1990.

b. Report completed and meeting held by September 1990.

7. Review rent control, land titling, standards, and the revenues such as the stamp tax that may adversely affect the development of the housing market.

Implementing Steps

a. Prepare analysis of other potential barriers to the development of the housing market.

b. Hold a workshop to present the results of the analysis and to recommend follow up actions.

Implementing Steps

a. Prepare Analysis of special requirements lending for construction finance may imply.

b. Present findings to MOF.

Benchmarks

a. Scope of Work prepared for analysis.

b. Report of findings completed.

c. Meeting convened to present findings to MOF.

Estimated Timing

a. Scope of Work prepared by September 1989.

b. Report completed by January 1990.

c. Meeting convened by February 1990

d. Actions taken by April 1990.

## Qualified Projects for Local Currency Attribution

The GOP projects that have been identified in the 1988-89 SDP as qualifiable for local currency attribution are identified below by Province.

| Province/Project | Total Cost In Millions | Past Exps. | Total Allocation 1988-89 |
|---|---|---|---|
| **PUNJAB** | | | |
| 1. Trunk and lateral sewer of WASA in SW Lahore | 39.5 | 0 | 8.005 |
| 2. Trunk and lateral sewer of WASA in SE Lahore | 48.0 | 0 | 8.004 |
| 3. Greater Faisalabad water supply, sewerage and drainage | 49.0 | 0 | 32.018 |
| 4. Water supply scheme part IV Faisalabad | 49.9 | 0 | 16.009 |
| 5. Sewerage scheme part IV Faisalabad | 49.5 | 0 | 16.009 |
| 6. Improvement and extension of water supply, sewerage and drainage facilities in med. sized cities | 11.6 | 0 | 9.284 |
| 7. Water supply scheme for Rawalpindi | 9652.5 | 0 | 4.006 |
| 8. Punjab urban development | 3360.0 | 0 | 96.045 |
| **SIND** | | | |
| 1. Greater Karachi bulk water supply phase IV | 446.0 | 0 | 130.0 |
| 2. Katchi Abadi | Unavailable | 0 | 212.0 |
| **NWFP** | | | |
| 1. Peshawar slum improvements* | Unavailable | 0 | 0 |
| **BALUCHISTAN** | | | |
| 1. Quetta sewerage and sanitation | 140.0 | 30.0 | 20.8 |
| 2. Quetta water supply | 188.0 | 110.0 | 47.5 |

The total costs associated with the SDP projects listed above are:

1988-1989: Rs. 599.675 (US$31.5 million)
Total over the Plan Period: Rs. 13.894 billion (US$731.26 million)

*Likely future expenditure in the SDP yearly budget

# PAKISTAN

## Financial Sector Adjustment Loan

## Overview Matrix

| Key Reform Areas | First Phase (By Board Presentation) | Second Phase (By Second Tranche Release) | Medium Term (Potential Future Loans) |
|---|---|---|---|
| i) Government Debt Management. | Draft operational program for introducing market based borrowing program and pilot auction for government securities. | Rationalisation of rate structure on all government securities and full auction program for short and long term securities. Establishment of revised rediscount facilities. | Full development of secondary markets. Refinement of monetary control mechanisms. |
| ii) Interest Rate Policy and Directed Credit. | Increase of concessional interest rates, market determinated long term credit rates, limit on directed credit and monitoring of asset quality under directed credit schemes. | Further movement toward market rates of interest | Market determinated rates and abolition of credit targets. |
| iii) Bank Supervision, Restructuring, and Legal Reforms. | Tighter prudential regulation, improved supervisory framework, portfolio audit of major banks, improved credit policies and reform of legal system for debt recovery. | Restructuring/recapitalization of major banks, first steps to unify supervision of financial institutions under the State Bank. | Unified prudential regulation and supervision of all financial institutions under State Bank, further improvements in supervision and credit policies. |
| Autonomy, Accountability and Competition in the Banking System. | Improved Autonomy and Accountability for Nationalised Commercial Banks (NCBs), licensing of new private investment banks. | | Graduation of private investment banks into full fledged banks, disinvestment of NCBs. |

# INITIAL ENVIRONMENTAL EXAMINATION (IEE) FOR SHELTER RESOURCE MOBILIZATION PROGRAM

| | | | |
|---|---|---|---|
| 1. | Program Country | : | Islamic Republic of Pakistan |
| 2. | Program Title & Number | . | Shelter Resource Mobilization Program (391-0507; 391-HG-001) |
| 3. | Life of Program | : | FY 1989 - FY 1993 |
| 4. | Program Funding | : | $100 Million Housing Guaranty Loan<br>$5 Million Technical Assistance |
| 5. | Recommended Environmental Action | : | Negative Determination |
| 6. | Prepared by | : | Chaudhary Laiq Ali<br>Mission Environmental Engineer |
| 7. | Reviewed and Concurred by: | | Waldemar Albertin<br>Mission Environmental Advisor |
| 8. | Chief, Energy and Environment: Concurrence | | T. David Johnston<br>Date: May 25, 1989 |
| 9. | Bureau Environmental Coordinator for Asia and Near East | : | See State 163872 (Copy attached) |

E&E.CLAli
SRMIEE:5/25/89

# INITIAL ENVIRONMENTAL EXAMINATION (IEE) FOR SHELTER RESOURCE MOBILIZATION PROGRAM

1. Program Country: Islamic Republic of Pakistan

2. Program Title & Number. Shelter Resource Mobilization Program (391-0507; 391-HG-001)

3. Life of Program: FY 1989 - FY 1993

4. Program Funding: $100 Million Housing Guaranty Loan
$5 Million Technical Assistance

5. Goal and Purpose of Program

Goal: The goal of the Shelter Resource Mobilization Program is to encourage the mobilization and application of domestic resources to improve the shelter conditions of low income families.

Purpose: The purpose of the Program is to create the policy environment which will promote the establishment of private shelter finance institutions. A second purpose is to initially support, through local currency equivalent amounts, the Government of Pakistan (GOP) shelter programs. This includes land and infrastructure development to facilitate the expansion of the housing finance market and to promote a continuous supply of shelter for low-income people during the period of change. If it is successful, the program will permit the State Bank of Pakistan (SBP) to gradually reduce subsidized credit allocations to the House Building Finance Corporation (HBFC) for middle and upper income shelter loans. What shelter sector subsidies remain in the GOP's budget would be focussed on the poor and delivered outside of the private shelter finance system. The program will assist in setting up a shelter finance delivery system with clearly defined public and private sector roles, procedures and support mechanisms.

To achieve these program purposes, the GOP will need to adopt a number of reforms within the overall financial sector that will put mortgage and improvement lending on a market-oriented basis. The GOP will also have to actively encourage private participation in the shelter finance system both as equity investors in housing finance companies and as savings depositors. The creation of an appropriate regulatory and supervisory framework for housing finance will be a key step toward gaining private sector participation, as will the establishment of procedures, terms and conditions to which the public and the private sector would adhere to make the shelter finance system work.

6. Program Description

The Shelter Resource Mobilization Program will consist of two closely related components. The first component is the Housing Guaranty (HG) funded capital assistance. The second component is the grant funded technical assistance and training.

Under the HG, Pakistan will borrow up to $100 million from the U.S. capital market under an A.I.D. guaranty. This private U.S. capital can be used by the GOP as unrestricted foreign exchange. The A.I.D. guaranty assures the GOP of loan terms that are relatively attractive compared to normal commercial borrowing and that are roughly equivalent to IBRD terms.

In consideration for the A.I.D. loan guaranty, the GOP would develop and implement a package of policy reforms to be agreed with A.I.D. The intent of these reforms would be to create the policy and regulatory environment which would encourage the development of a market-oriented shelter finance system. Achievement of this goal would help to strengthen and deepen Pakistan's financial markets. The reforms would also permit the GOP to better focus its shelter sector expenditures to the benefit of low income families at reduced cost.

A.I.D. will pursue a jointly developed policy agenda with the GOP by negotiating a Policy Action Plan acceptable to both parties for the first tranche of HG funds. The A.I.D. guaranteed dollar loans would ultimately lead to an increase in available housing finance resulting from the policy changes. Progress against this Action Plan will be assessed on a yearly basis, and a new Action Plan negotiated before the next tranche of HG funds is authorized. This process will be repeated until $100 million in guaranties is authorized. In the event that the GOP policy actions do not meet agreed targets, the Mission retains the option to reduce, postpone, or cease further HG authorizations.

In view of the necessity to take the pressure off the sector and allow a climate conducive to the above policy changes, the rupee equivalent of the dollar loans will initially be used to support GOP low-income family shelter programs. As the Program develops and the shelter finance system gains experience rupees may be applied to a secondary market facility or liquidity fund in which the private sector housing finance institutions could participate to support the flow of resources through the system. These investments will be monitored through the review of GOP expenditures reports for HG eligible programs. A.I.D. will assign its rupee equivalents to existing budget expenditures for shelter development and seek improvement in the economic efficiency of such investment through policy reform.

A GOP stated objective in the shelter sector is to facilitate the provision of one million houses during the next five years. To achieve this end, the GOP has adopted a strategy involving several different types of programs. Each of these programs may be implemented individually; however, more typically, several types of programs are combined in a given project. The structure of government does not provide a single authority having responsibility for planning or implementing of all shelter programs. Nor is there an agency charged with technical or financial matters. Programs can be designed, financed, and implemented at federal, provincial, and municipal levels.

While the Environment and Urban Affairs Division of Ministry of Housing and Works has responsibility for coordinating and monitoring specific programs, such as the 3 and 7 Marla schemes, it is involved in administrative matters and monitors only physical progress. It has no regulatory or disciplinary powers. Nor does it monitor financial progress - even when the federal government provides funds for project implementation. Successful implementation of these programs will facilitate the development of the housing finance market. Technical assistance to these efforts, provided by the ADB and the World Bank, will support A.I.D.'s efforts to create a private housing finance system.

Based on discussions with GOP officials at various levels and in a number of agencies and the policies and programs broadly outlined in the Seventh Plan, it appears that the GOP will continue to pursue shelter programs and projects comprised of "katchi abadi" upgrading, sites and services, nucleus house construction, and home improvement loans. The expansion of water and sewerage services in shelter development areas is also an important component because of the impact it can make on expanding the housing finance market.

Shelter for the Shelterless Program under National Housing Authority, Provision of 300,000 Housing Units Program under National Housing Authority, Katchi Abadi Upgrading in Karachi under Karachi Municipal Corporation, Surjani Model Township program under Karachi Development Authority and 3-Marla programs under the Provincial Governments are the current and proposed GOP programs whose rupee expenditures might qualify as eligible under the Shelter Resource Mobilization Program. Portions of programs which are ineligible have been excluded. Final identification of programs and investment levels would be undertaken during program implementation.

Taken together, programs that are potentially eligible for HG-related investments represent some Rs. 8.7 billion, approximately $484 million, ($1.00 = Rs. 18) in expenditures over a 7 year period. The greatest financial requirements would occur during the first 2 to 3 years.

The HG component of the program will be supported by a technical assistance and training component (TA/training). $5 million of grant resources will be used to : (1) manage the policy dialogue process; (2) provide technical and policy analyses necessary to advance the policy reform agenda; (3) evaluate the policy dialogue process and the impact of policy changes on low income families; and (4) provide training for Pakistanis who will be critical to the development of a market-oriented shelter finance system.

The TA/training component would provide short term technical assistance to the Ministry of Planning and Development, the Ministry of Finance, and the State Bank of Pakistan (SBP) as the key partners in the policy dialogue process. A long term advisor placed in the Ministry of Finance or the Ministry of Planning and Development would manage the TA/training component. The advisor would be the person responsible for developing working relationships with high level counterparts in key ministries and institutions to pursue the policy agenda and projects policy dialogue. A Mission Shelter Finance Advisor (contractor or direct hire) would be placed in USAID/Pakistan. The advisor would identify short term policy development and technical assistance needs, monitor and support the policy dialogue, coordinate TA and training inputs with USAID and RHUDO, and develop eligible rupee expenditures guidelines and monitor their application. To the extent possible the short term TA and training activities will be carried out by Pakistani expertise through local contracts in conjunction with expatriate expertise as necessary.

7. Categorical Exclusion

The proposed program will provide a housing guarantee to the GOP for the purpose of stimulating policy reforms aimed at developing a housing finance system in Pakistan. Because the principal objective of the program is policy reform, AID will not prescribe use of the funds obtained by the GOP from private sector lenders under the guarantees and will have neither knowledge of nor control of the specific activities financed from this funding. Under the program, AID would require the GOP to maintain its own budget expenditures for low income housing at certain minimum levels but will not be involved in the review and approval of specific activities within the overall GOP budget.

Considering the above program approach, it is recommended that the proposed program receive a categorical exclusion from further environmental review. The recommendation is consistent with AID Regulation 16, Section 216.2(c)(2)(x) which provides for a categorical exclusion in situations where "support for intermediate credit institutions when the objective is to assist in the capitalization of the institution or part thereof and when such support does not involve reservation of the right to review and approve individual loans made by the institution."

The technical assistance component is also exempt from further environmental review under section 216.2(c)(2)(i).

8. Environmental Action Recommended: Negative Determination

9. Prepared by: Chaudhary Laiq Ali
(Based on the information provided by Thomas Johnson, RHUDO/Asia)
Mission Environmental Engineer

10. Reviewed and concurred by: Waldemar Albertin
Mission Enviromental Advisor

11. Concurred By: T David Johnston
Chief, Energy and Environment
USAID/Pakistan

12 Bureau Environmental: Coordinator for Asia and Near East
See STATE 163872
(Copy Attached)

Clearance: F. Wayne Tate, PRO: (in draft)

E&E:CLAli:aa
SKMIEE:4/27/89

ACTION AID INFO AMB DCM ECON AREP/5

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DIST: AID
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AIDAC FOR F.W.TATE AND D.JOHNSTON

E.O. 12356: N/A
TAGS:
SUBJECT: IEE FOR SHELTER RESOURCE MOBILIZATION PROGRAM (391-0507)

REF: A) ISLAMABAD 11581, B) ALBERTINE/KUX FAX 5/9/89

1. ANE/PD/ENV CONCURRS IN THE INITITAL ENVIRONMENTAL EXAMINATION (IEE) PREPARED BY USAID/ISLAMABAD (REF A) FOR SUBJECT PROJECT THAT THE PROGRAM IS EXEMPT FROM FURTHER ENVIRONMENTAL REVIEW AS AID WILL NOT RESERVE THE RIGHT TO REVIEW AND APPROVE THE SPECIFIC ACTIVITIES FINANCED UNDER THE HOUSING GUARANTEE (HG) COMPONENT OF THE PROJECT. THE SECTION OF THE AGENCY ENVIRONMENTAL PROCEDURES THAT SHOULD BE CITED IN THE IEE IS SEC. 216.2 (C) (2) (X).

2. THE TECHNICAL ASSISTANCE COMPONENT IS ALSO EXEMPT UNDER SEC. 216.2 (C) (2) (L).

3. HOWEVER, AS THE PROGRAM DESCRIPTION (NO. 6. IN THE IEE) INDICATES THAT THE EXPANSION OF WATER AND SEWERAGE SERVICES IN SHELTER DEVELOPMENT AREAS MAY BE A COMPONENT OF THE PROGRAM BEING SUPPORTED WE WOULD SUGGEST, AS A MATTER OF POLICY AND RESPONSIBLE OPERATIONAL STANDARDS, THAT THE MISSION CONSULT WITH THE ENVIRONMENT AND URBAN AFFAIRS DIVISION OF THE MINISTRY OF HOUSING AND WORKS, OR OTHER GOP AGENCIES, TO DETERMINE WHETHER THE CAPABILITY EXISTS TO ASSURE ENVIRONMENTAL SOUNDNESS OF THE SUB-ACTIVITIES. IF NEEDED, CONSIDERATION SHOULD BE GIVEN TO USING THE TECHNICAL ASSISTANCE RESOURCES TO BUILD THAT CAPABILITY. BAKER
BT
#3872

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EGE Action To: ALBERTINE
Due Date:
Action Taken:
Date:
Initials:



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OFFICIAL FILE

ANNEX 17

From: Athar Mahmood Khan,
Deputy Secretary(IF),
Phone: 823929.

Ministry of Finance
Government of Pakistan
(Internal Finance Wing)
Islamabad the 10th May, 1989.

No.F.10(5)IF.II/88-243

Subject: US AID SHELTER RESOURCE MOBILIZATION PROGRAMME:

My dear NORRIS

Please refer to your letter dated 27th March, 1989 on the subject noted above.

2. To assign responsibility for promotion and development of the subject scheme a Working Group on Housing Finance is constituted as under:-

| | |
|---|---|
| 1. Mr. M. Zafar Iqbal, Joint Secretary (IF), Finance Division, Islamabad. | Coordinator |
| 2. Mr. Javed A. Noel, Joint Secretary (Inv.) Finance Division Islamabad. | Member |
| 3. Mr. Shaukat Kazmi, Joint Chief Economist, Planning Commission, Islamabad. | -do- |
| 4. Mr. R.A. Chughtai, Senior Deputy Director, Banking Control Department, State Bank of Pakistan, Karachi. | -do- |
| 5. Mr. Kasim Parekh, Chairman, Pakistan banking Council, Karachi. | -do- |
| 6. Mr. A. Ghafoor Mirza, Joint Secretary, Economic Affairs Division, Islamabad. | -do- |
| 7. Mr. Humayun Faiz Rasul, Chairman, National Housing Authority, Islamabad. | |

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ACTION 3/27

Cont'd.....page/-2

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8. Corporate Law Authority, Islamabad. — Member

9. Any other representation from State Bank of Pakistan — -do-

2. Objectives of the programme Nos 1-6 are agreed, subject to the following modifications as per discussions with the representatives of USAID Mission:-

| | | |
|---|---|---|
| Objective No.2 | 2(2) | Establish roles for the NCBs, DFIs, PICIC and HBFC consistent with the formulation of market-oriented private and joint sector institutions. |
| | 2(3) | Coordinate efforts to recapitalize HBFC and restructure the institution and its housing finance policy. |
| | 2(4) | Monitor returns of deposits in savings scheme to ensure their consistency with market competition. |
| Objective No.3 | 3(4) | Deleted. |
| Objective No.5 | 5(7) | Review rent control land titling standards, and revenues such as the stamp tax that may adversely affect the development of the housing market. |
| Objective No.6 | 6(1) | Assess alternative arrangements for the development of construction finance by the housing finance companies, the NCBs, DFIs and HBFC. |

3. The working paper to be preapred by USAID may kindly be furnished to us at an early date.

Yours sincerely,

Athar Khan

(Athar Mahmood Khan)

Mr. James A. Norris,
Director,
US AID Mission,
ISLAMABAD.

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Annex 18

UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT
MISSION TO PAKISTAN

Cable: USAIDPAK

HEADQUARTERS OFFICE
ISLAMABAD

**SHELTER RESOURCE MOBILIZATION PROGRAM**
**(391-HG-001; 391-0507)**

**Certification for Compliance with Gray Amendment**

I, James A. Norris, the principal officer of the Agency for International Development in the Islamic Republic of Pakistan, do hereby certify that the acquisition plan in the Project Paper was developed with full consideration of maximally involving the Minority and Women-Owned Firms, or Gray Amendment Organizations, in the provision of required goods and services. Set-aside opportunities for such organizations to participate in this project have been assessed and deemed inappropriate at this stage. However, such organizations are encouraged to compete or contract awards, and prime contractors are expected to make an effort to sub-contract, as appropriate, with these entities. During the course of implementation, opportunities for such organizations to participate in the project will be further considered.

James A. Norris
James A. Norris

June 1, 1989
Date

Annex 19

UNITED STATES AGENCY FOR INTERNATIONAL DEVELOPMENT
MISSION TO PAKISTAN

Cable: USAIDPAK

HEADQUARTERS OFFICE
ISLAMABAD

**SHELTER RESOURCE MOBILIZATION PROGRAM**
**(391-HG-001; 391-0507)**

**FAA Section 611 (e) Certification**

I, James A. Norris, the principal officer of the Agency for International Development in the Islamic Republic of Pakistan, having taken into account, among other things, the maintenance and utilization of projects in the Islamic Republic of Pakistan, previously financed or assisted by the United States, do hereby certify, pursuant to Section 611(e) of the Foreign Assistance Act of 1961, as amended, that, in my judgement, the Islamic Republic of Pakistan has both the financial capability and the human resources capability effectively to implement, utilize and maintain the proposed Shelter Resource Mobilization Program.

This judgement is based upon the project analysis as detailed in the Shelter Resource Mobilization Program and is subject to the conditions imposed herein.

James A. Norris
James A. Norris

June 6, 1989
Date