Powered by پیسہ Upaisa

The Bulletin

Issue: 01

051-111-282-265
www.ubank.com.pk
/UMicrofinanceBankLimited

Introducing The Bulletin, our quarterly newsletter covering U Bank's innovation and research work.

With this newsletter we not only seek to highlight our own work but also deep-dive into global and local financial sector trends and developments. It is meant to be an exploration of the various sectors and topics that intersect with banking, microfinance, financial inclusion and sustainable development in an effort to encourage dialogue on the key challenges and opportunities while working on pushing forward the frontier when it comes to ensuring financial access & coverage. In this first issue, we talk about our recently concluded impact assessment baseline study as we get ready to launch the full report, a few of the projects we have been working on and supporting under our innovation related programming and we delve into the dynamics of the affordable housing space and the role financing, particularly by microfinance institutions, plays in helping address the national housing deficit (estimated at 10 million units according to the World Bank).

We welcome thoughts and feedback, as well as suggestions on topics to cover in future issues. Our hope with this newsletter is to build a community of engaged readers interested in sincere discourse about the challenges and opportunities we face as a sector, the disruptions (technological or otherwise) required to serve our customers better and building a Pakistan that is more inclusive.

Yours sincerely,

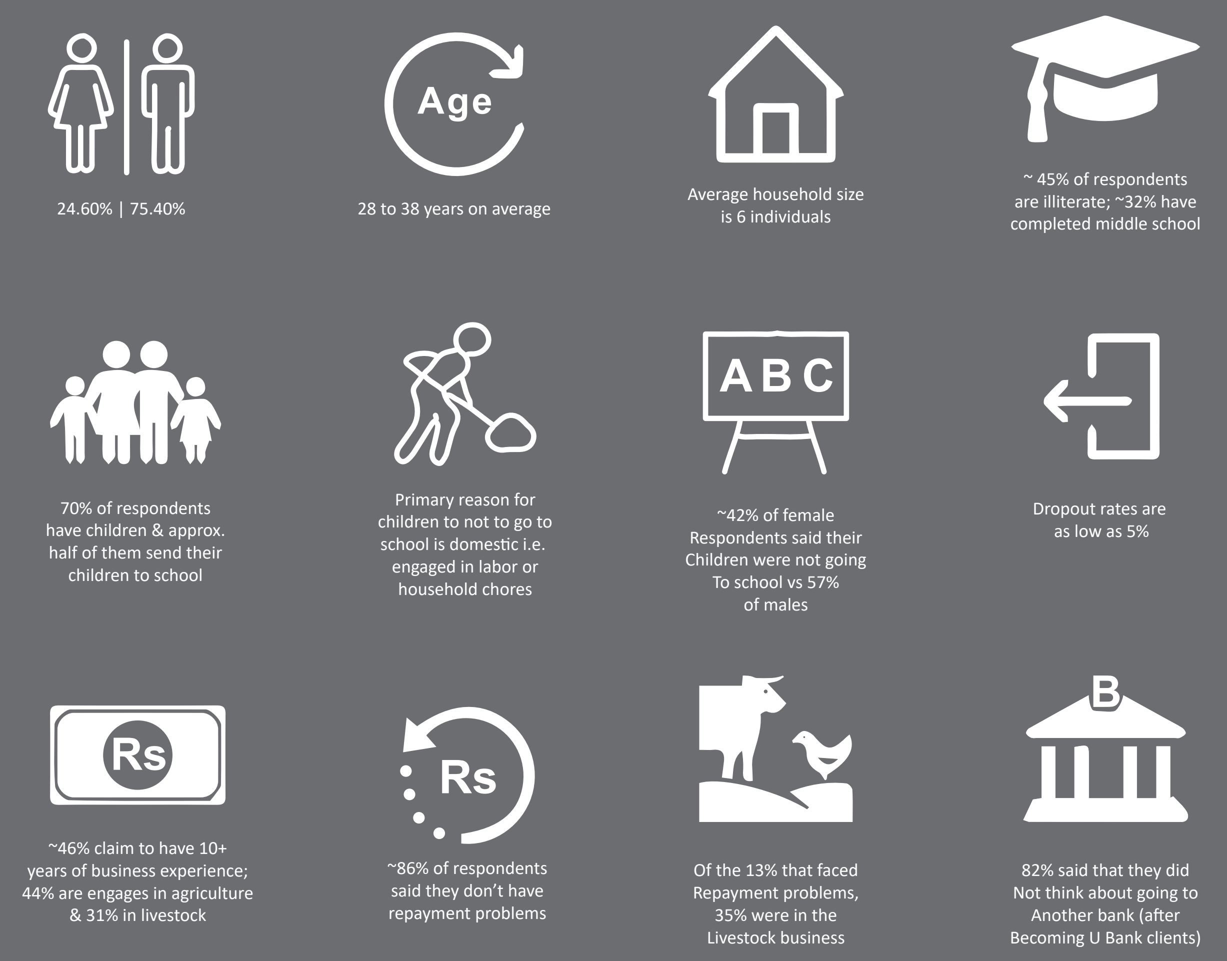
Anusheh Naveed Ashraf
Head of Research & Strategy
anusheh.naveed@ubank.com.pk

ARE RANDOMIZED CONTROLLED TRAILS (RCTS) THE ONLY WAY TO MEASURE IMPACT?

And what we've found out about our customers this past year.

Globally, the microfinance space is attempting to answer the big questions around its ability to deliver on its dual promise of social and economic performance. The tool which was long believed to be the silver bullet solution to "lifting people out of poverty", became shrouded in doubt when the results of a multi-year random control trials (RCTs) based impact evaluation spanning six countries was released in 2015. According to this study, conducted by the non-profit Innovations for Poverty Action (IPA) and the Abdul Lateef Jameel Poverty Action Lab (J-PAL) at MIT, microcredit improved the ability of clients to sustain financial shocks resulting from wedding expenses, crop-failures, natural disasters, illness and other similar tragedies but did not make them less poor. It also concluded that there were no increases in customers' consumption or average income and only one case established that microfinance led to gains in women's decision-making power. While small business owners were found to make more business investment due to micro-credit, this did not translate into higher profits. Part of the problem lies within the apparent conflict between being able to alleviate poverty while also becoming profitable as an institution. Fittingly so then the Microfinance Barometer 2018, an annual review of the global microfinance market, was titled Microfinance and Profitabilities and explored questions like "should microfinance be profitable? If so, can it be socially responsible? Where does the balance lie between reasonable interest rates and sustainable profitability?" The report concludes that financial profitability can in fact be reconciled with positive social impact. It also makes the case for a mindset shift when it comes to the traditional conceptions and definitions of profitability among MFPs and investors alike and argues that profitability cannot be reduced only to its financial dimension and calculations must incorporate positive social impact on both borrowers and communities.

Despite the results of the J-PAL study and these important questions, all evidence indicates that microfinance does remain an important part of the equation (within the Graduation Model*) and small tweaks to the product design and delivery mechanisms can go a long way in making it a more effective tool to help clients improve livelihood and quality of life standards. Currently, there is an RCT based evaluation being conducted by LUMS and PMN which seeks to contextualize the research design and find out the impact of micro-financing activity on women's empowerment, durable consumption, schooling and employment generation in Pakistan. While we wait for the results of the study to be published, an important question to ask is whether cost and time intensive RCTs are the only way to measure and assess impact?



We believe that there are more innovative approaches to be able to assess impact, extract actionable insights and measure how microfinance is changing things in the lives of our clients. Therefore, this past year we conducted a study based on a blended research design approach which combined elements of experimental, mixed methods (an approach that integrates both qualitative and quantitative data) and Acumen's lean data (an approach that applies lean experimentation principles to measure business performance as well as the social benefits people experience) research designs to dive deeper into what's happening on the ground. We are aware of the limitations that come with this approach. For starters, it cannot establish causality but in developing country contexts even RCTs struggle to establish true causality thanks to the multiple social development programs being run in the community at the same time. However, once repeated on a regular schedule it can glean important insights from customers on what's working and what's not and we can reasonably conclude that our products and services are playing a part in changing the lives of the end customer. Another limitation is that this survey was only conducted with U Bank customers at this point in time. Important follow-ups will include speaking to non-customers and more importantly the customers that have "dropped out" i.e. did not return to U Bank after their first loan and/or defaulted on their loans.

This baseline study consisted of a sample size of 2023 U Bank customers and used a proportional sampling methodology based on the geographic spread and density of our customers. While this sampling approach limits the statistical analysis possible, it helps build a snapshot of the various subgroups within our portfolio to understand better who our clients are. This approach also meant that a bulk of our sample was concentrated in Punjab, followed by Sindh**. While the full report shall be launched soon, with a detailed breakdown of the descriptive indicators, insights from the focus groups as well as results from the regressions we ran on the data, listed below are some of the interesting trends that came up:

90%

of our respondents indicated that they save a portion of their income but only 3% of them save formally with a bank or microfinance institution (MFI). The most popular ways of saving informally were in the form of committees (peer-to-peer savings groups) or collecting cash at home. 75% of male respondents reported that they engaged in saving behavior, while only 25% of female respondents indicated they save. This is an interesting finding particularly when we put it in the context of previous research which indicates that women borrowers are much more likely to save. An important questions to answer is why the number of women saving in our portfolio remains low? Is this due to women having lower earnings/income and hence not enough left over to save? Or is it because the lack financial decision making power? Or is this a lack of awareness and financial literacy issue?

37%

of respondents agreed that the loan was essential for their business to survive and continue and about 32% strongly agreed with this statement. When asked directly "what was the impact of the loan on your business?" 77% of the customers stated that their income had increased whereas 11% said that it had decreased. A common perception for the later was that repayment of loan installments equated to less disposable income in the minds of these customers. This may indicate a gap in customers' financial understanding and planning.

To understand spending patterns of our clients we asked them to list down the assets they owned before and after receiving the loan.

41% of them indicated that they had increased livestock assets and

26% of the respondents indicated that they'd been able to invest in electronics. This is an interesting insight because it may indicate that customers are using their loans for consumption purposes, despite claiming to have taken and spent the loans on business activities. The high response rate for the livestock option, also does not match-up with current portfolio trends. This indicates a need for deeper inquiry to understand our customers spending patterns.

Only **549** respondents chose to respond to the question that asked whether getting access to the loan helped them save more and 74% of them answered that it helped them increase their savings.

While macro-level data points on the microfinance sector have been collected and reported regularly, there has been a dearth of micro-level, customer side data in Pakistan. The current reporting on social indicators happens on very surface level indicators and on a self-reporting basis by MFPs. Our research is the first of its kind but we hope that it starts a process of greater, publically available, customer side research and reporting. There is a lot of room for other players to learn and iterate from our research design and to work with us to build a survey tool and/or scorecard that measures social performance. A key point that we want to see more discussion around is whether we need to re-evaluate the metrics that are measured when we talk about social impact as it relates to the microfinance industry. Microfinance alone cannot fulfill the promise of graduating people out of poverty, but if it facilitates them in sending their children to school and keeping them in school, smoothing consumption so that their standard and quality of life improves - then why are these metrics not considered equally worthy? After all, something as simple as having access to a fridge that keeps food items for longer, allows them to freeze ice to tide over the extremely hot summer months can make a huge impact on the lives of those that we are seeking to help.

Our Impact Assessment Baseline Study launches soon and we look forward to engaging with many of you on these questions and more in the coming months.

* Simply put, the graduation programs model establishes that any interventions to lift people out of poverty need to incorporate six key components: (1) providing assets like livestock or goods that can be used to make a living; (2) offering training on how to manage those assets; (3) offering food and cash support to help navigate emergencies; (4) making frequent visits to reinforce skills; (5) giving health education and access to health care; and (6) providing a savings account for future investment. None of these approaches are groundbreaking, and interventions designed around each of these have been implemented globally for many years. However, what is innovative is that under the graduation model all of these approaches need to be integrated simultaneously.
** The geographical spread of U Bank clients has changed since the implementation of this survey.

THINK PIECE

Tackling Affordable Housing and what role Microfinance Banks (MFBs) can play in financing such initiatives?

The Fact Sheet

National housing deficit	~ 10 million units
Urban population growth is growing faster than the total population	2.7% as compared to 2.4% per year
Urban households living in informal settlements (katchi abadis)	47%
Urban working population employed in the informal sector of the economy without verifiable or steady income	~ 68%
At prevailing prices of grey construction, cost of an 80 square yard unfinished single story house	PKR 3.3 million (not including financing cost and developers profits)
Pakistan's mortgage-to-finance ratio	0.23% (lowest in South Asia)
Housing loans outstanding as of 2018	~ 68,000 with outstanding loan balance of PKR 83 billion over a tenor of 13 years
New mortgage loans extended per year since 2016	1500 with average loan size of PKR 6.1 million
SBP projections for increasing the number of mortgage borrowers and total mortgage finance by June 2021	68,000→200,000 and PKR 83 billion→PKR 250 billion

Source: All data points extracted from the Optimizing the Naya Pakistan Housing Policy Opportunity Working Paper by TabadLab.

Affordable housing is a tough nut to crack. The rising land and construction costs, population growth and rising urbanization, nuclearization of the urban Pakistani family (i.e. more young Pakistanis are choosing to exit joint family living arrangements), absence of eviction and foreclosure laws, lack of forward thinking policy mandating affordable housing obligations (AHO), poor or inadequate urban planning and a financing sector that is almost non-existent have all helped exacerbate the country's housing crisis. While a few projects have been undertaken over the years without much success, the issue of housing has started receiving renewed interest since the current government made it a key priority area.

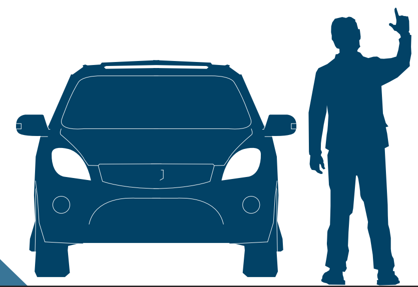
While the recent SBP "Policy for Promotion of Low-Cost Housing Finance" and the "Naya Pakistan Housing Programme (NPHP) " have been great steps forward, and have made affordable housing become a part of national discourse and a key priority area, there remain substantial gaps when it comes to ensuring that these policies are implemented in a way that is sustainable in the long-term. One of these concerns is that low-income housing schemes lead to ghettoization. This is due to multiple factors such as limited disposable incomes to contribute towards maintenance and development of the community. The lack of mixed income households in a community also limit the employment opportunities for low-income individuals and other safety nets and supports that come with living in such a neighborhood. Another limitation is that unlike the SBP policy the NPHP will not facilitate in acquiring housing financing. Due to the low margins to be found in building affordable housing, the incentives for builders/developers to get into the space will remain low especially due to no incentives on the financing side of things. A few projects that were undertaken to alleviate the housing crisis suffered through another problem in the way of ghost towns i.e. communities built in urban peripheries which would bring costs down but pose major development problems due to them being too far away from urban centers. Employment opportunities due to a lack of proper infrastructure and public transportation also made these schemes unlivable.

The way forward might be to take a page out of Turkish, Singaporean and Malaysian government's playbooks and focusing efforts on AHOs on a policy level. This obligation would mean that builders need to allot a minimum percentage of residential units in all new high-rise constructions or sellable area as low-cost units/housing by law. This has been an extremely successful way of combatting poverty concentration in particular areas and building mixed-income housing communities that thrive. In our Pakistani context, a crude example of this working well across the country would be to look at military cantonments .

What is the barrier to progress then, especially given the vast evidence from the success of these projects working internationally? A major hurdle is the lack of financing options available. While the lack of foreclosure laws has often been cited as the most critical factor that makes housing finance provision especially risky for banks, there might also be a limitation to how innovatively banks want to engage with the challenge. For microfinance banks especially, the riskiness involved should not be as major a concern considering that they're in the business of lending to those deemed the most risky and un-creditworthy by commercial banks. Hence, ideally speaking getting into affordable housing finance (especially given the recent change in regulation that will allow them higher loan limits) should represent an opportunity given their dual purpose of creating social and economic purpose. According to a report called Enhancing Builder Financing in Pakistan published by Karandaaz, housing development has substantial implications on economic growth and social inclusion. The report states that increasing the housing units in Karachi alone by 100,000 in a year stands to contribute 2.2% to the GDP output and drive growth in about 50 connected industries.

[1] While the NPHP doesn't specifically identify its target audience to be low income, the upper cap limit for monthly installments of PKR 20,000 corresponds with the SBP definition of low-income households earning PKR 60,000 per month as outlined in the Optimizing the Naya Pakistan Housing Policy Opportunity working paper.

[2] This is not to say that there may not be inherent problems in those housing schemes and neither is meant to be taken as a judgment for or against the existence of said cantonments. It merely draws from the author's experience having lived in Military Cantts where a wide-range of mixed-income housing units were available. The service staff was also able to engage in gainful employment by providing services such as laundry, milk delivery, running small corner retail shops and cooking and cleaning services to the more affluent residents. These residents in-turn provide safety-nets such as access to healthcare and medical treatments and even financial support. The result is a mixed-income community that thrives.



We spoke to Jawad Aslam, Founder & CEO of Ansaar Management Company (AMC – the only local affordable housing builders in Pakistan) about the problem and he believes that the lack of foreclosure laws being an impediment is perhaps over-exaggerated as the key roadblock especially when it comes to talking about the customer segments that MFBs cater to. He points to the research on the subject that indicates that the low-income segments are generally proven to be better when it comes to repayment of loans. He further identified the lack of innovation and higher interest rates charged on housing finance as the main reasons that make such development programs unaffordable for the end-customers . The operating model of AMC works such that it considerably brings down the risks associated with such loans thanks to them providing a large number of clients in one place and offering collection services as well (which brings down the administrative costs associated with a loan). In addition, the underlying asset is secured and centralized. Despite this his conversations with banks have historically revolved working downwards from the prevalent interest rates rather than upwards from the cost of funds, which he believes is the critical mindset shift necessary to make finance for affordable housing work.

From the banking side of things, these numbers should work. Talking with professionals in the microfinance sector, it seems that banks are in a position to absorb these costs and provide lower interest rates (closer to their cost of funds than current rates). A bank would have to extend significantly less loans in housing to breakeven on administrative costs of lending compared to their current models/portfolio. However, this would require sacrificing short-term, immediate income and profits in favor of long-term gains and that requires buy-in from various internal and external stakeholders. In the past, simply put there hasn't been a need to change the way MFBs have been operating, thanks to the lucrativeness of the current model. However, as the sector fast reaches its saturation point and the current portfolio becomes increasingly vulnerable to risks such as climate change and water scarcity, MFBs are now beginning to see value in diversifying their portfolios. An important incentive at this point that can push microfinance banks in this direction is if they are able to get funding at discounted rates so that their cost of funds can be lowered.

The government making affordable housing a key priority, the recent SBP and NPHP policies, the increasing need of MFBs to diversify their portfolios are all proving to be important catalyzing elements when it comes to starting the conversation on how to bridge the gap that exists in financing such projects. While urban planning reforms and stronger foreclosure laws remain significant problems, changing them will take considerable time despite things moving in the right direction. In such an environment, it becomes critical for the microfinance sector to start asking the important questions about what it will take for the sector to push its innovative boundaries and do its part. By no means do we intend to imply that the problem is simple one and we realize that a lot more nuances exist within the housing ecosystem but asking these questions is the need of the hour. Without changing the way business as usual is done, the sector will not be able to live up to its promise of economic and social upliftment.

Note: This piece draws on the work done by TabadLab's working paper on Optimizing the Naya Pakistan Housing Policy Opportunities, authored by Ibrahim Khalil and Umar Nadeem, which does an excellent job of unpacking the current situation, the policy gaps and challenges as well as the opportunities and recommendations. This piece only covers a few aspects covered in the paper and you can find the complete paper here for more details. We'd also like to thank Jawad Aslam, Founder and CEO Ansaar Management Company and Riasat Zaman, Head of Product at U Bank and microfinance professional whose experience spans more than a decade in the industry.

[3] Typically longer loan tenures ease the repayment pressure faced by borrowers by lowering the EMI amount due. However, this is not the case with housing loans. The rates at which housing loans are affordable are much lower than prevailing rates for other loan types. This is due to a combination of factors like the low average loan size available which forces borrowers to finance a significant portion of total finance needed for housing via their savings. Another factor is that higher interest rates translate into the loan installment amount due as a proportion of total monthly income being too high. Furthermore, these loans do not stand to have any monetary benefits of increased income for our clients.

[4] These gains include stable earnings spread out over longer terms, no costs associated with renewing loans every year (which is the case with the current loan cycles) and lower administrative costs.