«APPROVED»
by the decision of the annual general meeting
shareholders of JSC «Mortgage Refinancing
Company Uzbekistan»
from June 29,2023

STRATEGY

JSC "Mortgage Refinancing Company of Uzbekistan" for 2022-24

CONTENTS

BASIC TERMS

ADB	Asian Development Bank
SAMA	State Assets Management Agency
HLA	High Liquidity Assets
MRA	Master Refinancing Agreement
Bookmark	A document that confirms that the apartment is pledged to the bank after the mortgage has been arranged. It guarantees the bank a refund if the borrower fails to pay the mortgage.
MBS	Mortgage-backed security
LTV	Loan-to-value ratio is the ratio of the loan to the value of the property pledged by the borrower
IDI	International development institutions
IFI	International Finance Corporation
DTI	Debt to income
MMSDP	ADB's mortgage market sector development programs
SMES	Social Management and Environmental Standards
UzMRC	Mortgage Refinancing Company of Uzbekistan (also Company)
PFI	Participating Financial Institution - shareholder banks that have signed the MRA with the Company
CBU	Central Bank of Uzbekistan

INTRODUCTION

UzMRC was created on November 4, 2019, by the Ministry of Finance through a resolution of the Cabinet of Ministers.

It would be fair to say that the recent major reform of the housing sector began in 2019 with the signing of the Presidential Decree on Additional Measures for the Growth and Development of the Mortgage Market. The decree outlined key objectives and a detailed action plan to be fully implemented. Among other things, this included the creation of a market-oriented mortgage refinancing company and the gradual consolidation of housing subsidy programs.

In a relatively short period of time, the mortgage loan portfolio increased from about 2.8% of GDP in January 2019 to more than 5.3% of GDP in January 2022, exceeding the prevailing levels in all Central Asian countries.

The financial services market saw significant inflows in the form of pre-financing from the government and refinancing from the UCRI. A noteworthy point worth mentioning is that, for the first time, banks can benefit from monetization of the created mortgage portfolio, thus making use of the secondary mortgage market. Although the start of the refinancing project was a bit slow, banks appreciated the benefits of the generation-distribution model.

Much has been done since the decree was enacted, but there is still much work to be done to fully achieve the objectives.

As in any area, reforms are not easy and many barriers remain to ensure the smooth and full operation of the secondary mortgage market.

Although the Company entered the active operational phase in October 2020, the mortgage refinancing mortgage foreclosure has had to be done purely on a formal (contractual) basis, without the use of a mortgage instrument as planned. Similarly, although the Company planned to issue its first mortgage bond in 2022, this could not be achieved due to the lack of a legal framework. This plan has now been postponed until 2023 pending approval of the Capital Markets Act and the related Mortgage Bond Act.

Meanwhile, the provision and financing of affordable housing continues to become increasingly important as households grow and capital markets develop.

We are optimistic about the prospects for housing finance, given the government's strong willingness and commitment to coordinate housing policy and provide the necessary resources. Banks are also ready to further promote mortgage products, which already account for more than 52% of the banking sector's retail portfolio. The growth of the mortgage market is expected to support the development of capital markets, thereby creating a financial ecosystem for market participants to obtain much needed liquidity.

Achieving the goals will depend largely on the commitment and continued efforts of the government, regulators and financial services market participants.

I. MISSION AND OBJECTIVES

2.1 Mission

Promote the growth and development of a mortgage market that offers affordable mortgage products to all income groups in society.

2.2 Objectives

- Provide liquidity to the banking sector for the sustainable development of mortgage lending;
- Development of local capital markets through the issuance of mortgage-backed securities;
- Promoting international mortgage lending standards and practices;
- Promoting a legislative framework that supports the operation of the secondary mortgage market.

2.3 Values

- Professionalism
- Innovation
- Efficiency
- Integrity
- Teamwork

II. OVERVIEW

2.1 Overview of the current activities

UzMRC became active in October 2020, one year after its establishment. Although the Company initially operated on a pre-financing basis, the Company has now fully transitioned to a model of refinancing eligible commercial bank mortgage portfolios. For this purpose, the Company has attracted long-term resources through signing an agreement with the Ministry of Finance of the Republic of Uzbekistan on refinancing the Asian Development Bank's loan for the equivalent of USD 150 million. The Company has obtained USD 150 million under the Mortgage Market Sector Development Project under Loan Agreement No. 3870-UZB dated 12.12.2019 between the Republic of Uzbekistan and the Asian Development Bank.

The Company has an approved organisational structure and qualified staff with extensive experience in the banking sector.

The Company is regulated by the Central Bank of Uzbekistan as a mortgage refinancing organisation based on the regulation of the Central Bank of Uzbekistan "On Coordination and Regulation of Activities of Mortgage Refinancing Organisations".

The Company's capital is UZS 100 billion, formed from the founding contributions of 13 shareholders.

Systematic work has been undertaken to increase and diversify funding sources through the issuance of corporate bonds and their sale by private subscription to a limited number of persons, including international financial institutions, as well as through a new long-term credit line with ADB.

2.2 Implementing the previous strategy

Over the initial two-year period since the start of active operations in 2019-21, the Company has set the following three strategic objectives, which the Company has been able to successfully achieve:

Objective 1: Establish internal policies and systems appropriate to refinancing companies and ensure compliance with local and international standards on an ongoing basis.

2020 was the year of the Company's formation and establishment of its regulatory, structural, logistical, resource and human resource framework and was marked by the following key developments:

The Executive Management of the Company has done a considerable amount of work on the formation of (a) internal regulations governing accounting policy, human resources policy, information technology policy, internal control, etc., (b) the regulations of the three committees under the Supervisory Board and their work plans, (c) the Business Plan and strategy of the Company subsequently reviewed and approved by the Supervisory Board.

Regulation and supervision

As one of the first steps in conducting its business, the Company registered with the Central Bank of Uzbekistan as a non-banking financial institution authorised to conduct mortgage loan refinancing operations.

In the absence of a relevant regulation, the CBU, in turn, approved a special regulation for the supervision of the Company's operations, approved by the Ministry of Justice of the Republic of Uzbekistan under No. 3219 dated 10.02.2020.

The Company, as a mortgage refinancing institution, is required to comply with prudential requirements for capital adequacy, liquidity ratios and exposure per borrower.

The basis for the calculation of prudential requirements is the Recommendations for the Preparation and Submission of Financial Statements of Mortgage Refinancing Entities to the Central Bank of Uzbekistan. These Recommendations entered into force on 15 September 2020.

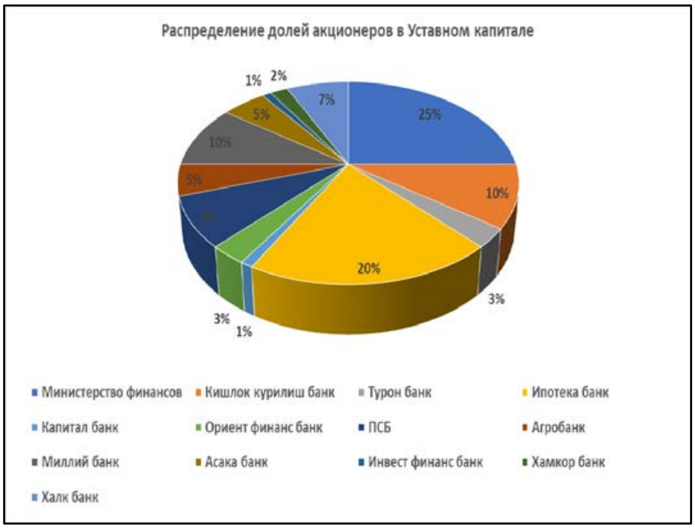
Capital formation

Based on the Presidential Decree No. 5715, which set out the prerequisites and conditions for the establishment of the Company, the Ministry of Finance provided start-up capital of UZS 25 billion. Shortly after the formation of the 7-

member Supervisory Board and in line with the intended use of the cooperative operating model, the Company issued additional shares and placed them among the most active mortgage banks. This increased the Company's capital base from UZS 25 billion to UZS 100 billion and the shareholders from one to thirteen.

Table 1: Shareholder structure of the company

№	Shareholders	Share
1.	Ministry of Finance of the Republic of Uzbekistan	*25%*
2.	Ipoteka Bank	20%
3.	National bank of Uzbekistan	10%
4.	Qishloq Qurilish Bank	10%
5.	UzSQB	8%
6.	Xalq Bank	7%
7.	Asaka Bank	5%
8.	AgroBank	5%
9.	TuroBank	3%
10.	Orient Finans Bank	3%
11.	Hamkor Bank	2%
12.	Kapital Bank	1%
13.	Infin Bank	1%



Source: Company data

Organisational structure and corporate governance

Full and high-quality work was organised for all management bodies of the Company - the General Meeting of Shareholders, the Supervisory Board and the Executive Management - and appropriate internal regulations governing corporate governance and the Company's financial and business operations were developed.

The Company established a Supervisory Board and adopted a relevant policy according to which the Board consists of 7 members, at least 2 of whom must be independent. The Supervisory Board consists of three committees: 1) Audit Committee; 2) Risk Management Committee and 3) Nomination and Remuneration Committee.

Together with ADB and their housing finance experts, an optimal organizational structure was developed, considering the functions performed by the Company.

ADB consultants from the Frankfurt School of Business and Management were engaged to develop a strategy for information technology development and environmental and social management.

Objective 2: Identify and establish relationships with PFIs

Prior to launching the refinancing operation, the Company conducted extensive research and analysis of the banking sector to identify the most appropriate mortgage banks that could effectively contribute to the overall growth and development of the mortgage market.

As a result of the analysis, 12 public and private banks, together representing 94% of the market, were identified as leading mortgage lenders and invited to form a cooperative partnership.

Table No. 2 Key Indicators of Shareholder Banks as at 1 January 2022 (bln. UZS)

№	Банк	Актив		Кредиты		Ипотечный портфель		Капитал		Доля в УзКРИ	
		сумма	*%*	*сумма*	*%*	*сумма*	*%*	*сумма*	*%*	*сумма*	*%*
	Всего (по банковскому сектору)	444,922.48	100.0%	326,385.58	100.0%	35,825.80	100.0%	70,917.60	100.0%	75.00	75.0%
1	**НБУ**	89,919.41	20.2%	74,033.49	22.7%	4,537.50	12.7%	14,768.71	20.8%	10.00	10.0%
2	**УзПСБ**	56,511.32	12.7%	43,147.81	13.2%	3,271.60	9.1%	7,700.91	10.9%	8.00	8.0%
3	**Асакабанк**	50,804.36	11.4%	37,685.43	11.5%	3,244.30	9.1%	6,504.84	9.2%	5.00	5.0%
4	**Ипотека банк**	40,011.93	9.0%	29,046.32	8.9%	10,959.30	30.6%	5,087.15	7.2%	20.00	20.0%
5	**Агробанк**	39,971.15	9.0%	32,258.24	9.9%	462.20	1.3%	9,346.14	13.2%	5.00	5.0%
6	**Народный банк**	26,921.30	6.1%	19,595.96	6.0%	1,633.20	4.6%	5,479.51	7.7%	7.00	7.0%
7	**ККБ**	20,708.10	4.7%	17,496.15	5.4%	8,448.90	23.6%	2,696.44	3.8%	10.00	10.0%
8	**Капитал банк**	15,635.56	3.5%	8,030.16	2.5%	405.80	1.1%	1,488.74	2.1%	1.00	1.0%
9	**Хамкор банк**	12,422.20	2.8%	9,333.63	2.9%	521.20	1.5%	1,927.57	2.7%	2.00	2.0%
10	**Турон банк**	11,009.62	2.5%	8,129.47	2.5%	431.00	1.2%	1,915.19	2.7%	3.00	3.0%
11	**Ориент Финанс банк**	5,870.97	1.3%	3,627.04	1.1%	554.70	1.5%	1,343.48	1.9%	3.00	3.0%
12	**Инвест Финанс банк**	5,768.99	1.3%	3,774.44	1.2%	86.50	0.2%	765.14	1.1%	1.00	1.0%
	Остальные банки	69,367.55	15.6%	40,227.44	12.3%	1,269.60	3.5%	11,893.78	16.8%	-	-

Source: CBU

The inclusion of the candidate banks as shareholders was the first step in the transition to a cooperative operating model. In the second stage, the Company conducted a comprehensive assessment of the banks' financial management in accordance with international standards. As a result, credit lines were gradually established with 9 of the 12 shareholder banks, which subsequently signed a Master Refinancing Agreement with the Company.

The key terms of all the lines of credit are that the Company only considers refinancing eligible mortgages originated by the PFI. This includes underwriting the mortgages in accordance with a set of eligibility criteria, which were developed and later revised (see below) with ADB. In addition, PFIs were required to comply with the Company's Standards on Social and Environmental Management and the gender covenant developed with ADB consultants.

Table 3: Eligibility criteria for mortgage loans

Loan Standart	Requirement
Objective	1. To purchase an existing residential property that will be owner-occupied; 2. For the purchase of a fully completed owner-occupied dwelling; or 3. For the renovation of an owner-occupied residential property that does not involve structural changes or extensions.
Type of eligible property	A detached house or flat in a block of flats. The property to be financed must be owner-occupied, i.e. by the borrower and/or co-borrower.
Lending to secondary properties	Не разрешено: - Второй ипотечный кредит на ту же жилую недвижимость - Ипотечный кредит на вторую жилую недвижимость - Ипотечный кредит на инвестиционную недвижимость
Borrowers who meet the eligibility criteria	Must have a stable source of income. Only individuals are allowed to take out loans. Borrowers can be civil servants, self-employed people or employees.
Age of borrowers	Minimum age is the age of legal capacity (18 years).
Maximum monthly income of the borrower (household)	UZS 15 mln.

Loan Standart	Requirement
Mortgage loan term	For the purpose of acquiring residential property: Minimum 10 years, maximum 20 years For the renovation of residential properties: Maximum term of 10 years. Banks must disclose to clients/applicants the total amount of interest payable (according to the repayment schedule for different repayment terms (e.g., 10, 15, 20 years) as well as the monthly payments in these cases).
Mortgage limit	UZS 400 million for the purchase of real estate, and UZS 80 million for renovation.
Interest rate structure	The interest rate on the mortgage loan must be fixed. PFIs will lend these funds to final borrowers with a maximum spread of 5% for mortgage loans and 4% for renovation loans.
Currency	Uzbek soums only.
Initial payment	- Minimum 25% of the appraised value or purchase price of the residential property, whichever is lower - A down payment is not required for property renovation loans. But collateral of at least 125% of the loan amount is required to finance such a loan.
Loan-to-value (LTV) ratio	A maximum of 75% of the appraised value or purchase price of the residential property (the lower of the two is taken into account).
Debt to monthly income (DTI)	<50% of the net monthly income of the borrower (household).
Valuation of real estate	Conducted by an independent licensed appraiser.
Collateral	Real estate purchased on credit.
Geographical location	Within the country.
Overdue payments	All loans granted must be current, with no outstanding balance.
Ownership of the property	Legal title, no encumbrances.
Property insurance	100% replacement value required.
Borrowers' credit history	*No past due loan payments of more than 30 days within the last 12 months*
Mortgage amortisation	Monthly payments, full repayment, no grace period

Source: Company data

Objective 3: Expand the refinancing portfolio conservatively and in close cooperation with ADB and PFI

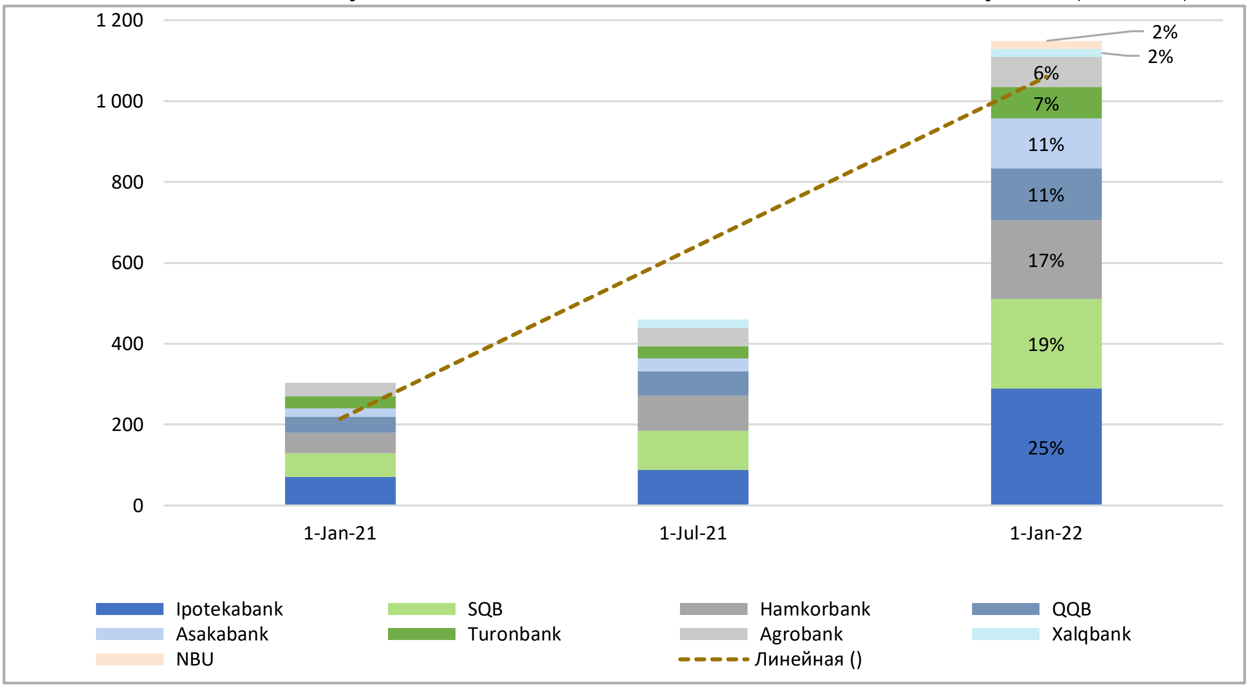
In May 2020, the Company received a loan of $150 million in UZS equivalent from the Ministry of Finance under ADB's Mortgage Market Sector Development Programme.

The loan was aimed at promoting mortgage lending with a defined set of underwriting standards and eligibility criteria. Given the concessional nature of the loan, the product has been extremely successful and at the time of preparation of this strategy paper, the facility is more than 90% utilised.

All loans provided by UzMRC were secured by a mortgage portfolio and alternative collateral, in cases where an acceptable portfolio was temporarily unavailable.

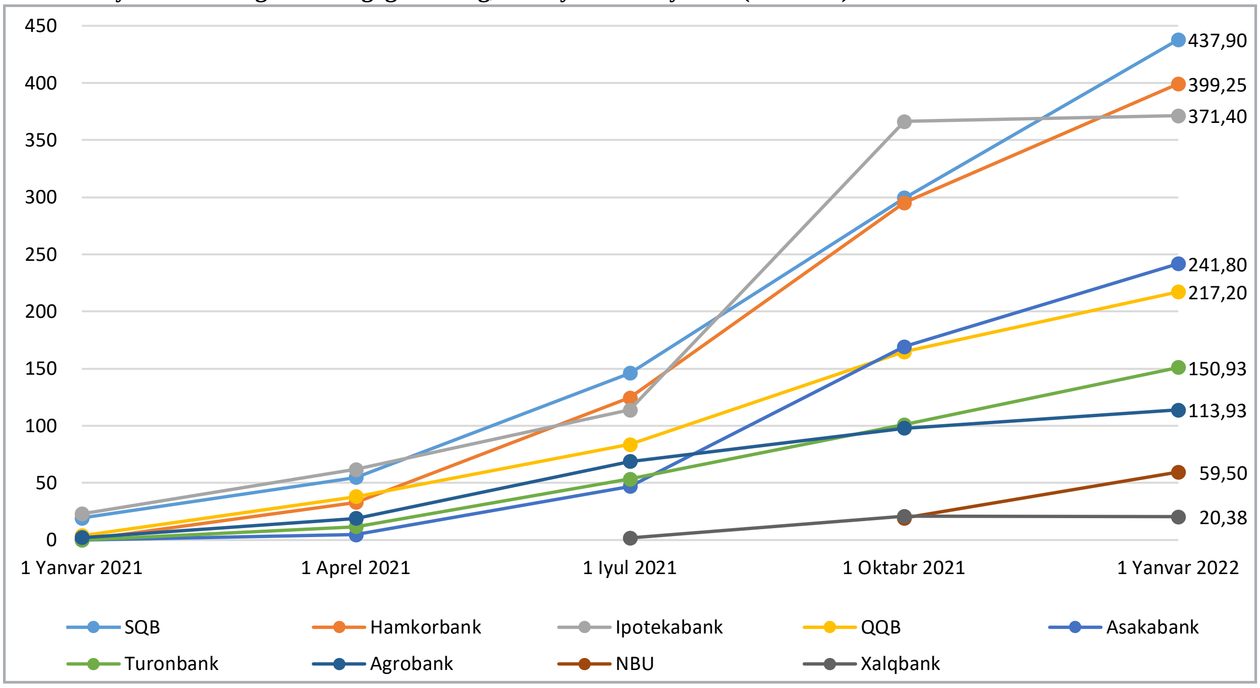
As at the beginning of 2022, 10,324 mortgage loans worth UZS 2,013 billion were originated under the Company's requirements, of which UZS 1,408 billion (69.5%) were refinanced by the Company.

Chart 1: Structure and Dynamics of the Loan Portfolio of UzMRC as at 1 January 2022. (bln. UZS)



Source: Company data

Chart 2: Dynamics of eligible mortgage lending, PFI by 1 January 2022 (bln. UZS)



Source: Company data

As a result of the execution of the Mortgage Market Development Project, the Company's assets amounted to UZS 1,280.6 billion at the end of 2021.

2.3 Key Lessons

As a company initiated by the government to promote the development of the mortgage market, UzMRC is directly involved in shaping the legal and regulatory framework for the mortgage industry. Accordingly, the following lessons learned from the previous strategy cover issues relevant to both the Company and the industry.

Lessons related to housing finance

a. Housing finance policy should be developed based on careful research and a clear set of priorities, taking into account a comprehensive analysis of the impact of the proposed policy.

Housing finance policy in Uzbekistan is mainly led by the Ministry of Finance and UzMRC. While the economic difficulties caused by the outbreak of COVID in 2019 necessitated changes to the housing finance policy, the results of this policy showed that any national review of the strategy should be critically assessed before its implementation. Some of the undesirable outcomes of the housing finance policy included:

- Competition of the housing finance programme, under DP-6186 run directly by the government, with another government initiative run by the Company, which compromised the Company's efforts and caused temporary confusion among mortgage lenders and borrowers.
- Preferential rates for mortgages provided by banks participating in the state programme distorted the formation of commercial rates and consequently led to inorganic increases and heated prices in the housing market.
- Displacement of private sector banks which cannot compete with the mortgage rates offered by the state banks participating in the programme.
- Increased dependence of mortgage lenders on state resources to finance their mortgage lending activities.

б. Coordination of the housing finance policy and its coordination with the key players in the market should be a priority and an important step in the formulation of the strategy.

Cooperation between market players will help calibrate the strategy, achieve common goals more effectively and avoid undesirable consequences for the sector.

Lessons related to regulation and legislation

a. Develop regulatory requirements related to the activities of mortgage refinancing companies.

Prudential requirements are not appropriate for a mortgage refinancing institution. A company borrows from the market to refinance a ready mortgage portfolio, which is also used as collateral. Prudential requirements, such as for PFI and risk concentrations and misidentification of problem loans, force the company to restrict its lending activities and make unnecessary provisions for theoretical losses that are unlikely to occur.

б. Timely and proper implementation of the government-approved action plan is critical.

The Company's business model is built with the necessary regulatory infrastructure in place to achieve the Company's objectives. The changing capital markets regulatory environment has significantly delayed the implementation of the envisaged legal and regulatory reforms. While delays in the implementation of new reforms are normal and expected, it is important to have a backup mechanism at the government level to ensure that action plans are implemented, as the fate of the industry is directly dependent on these actions.

в. The involvement of UzMRC as well as mortgage lenders in the drafting stage of all regulations and legislation related to housing finance remains critical.

The legal and regulatory framework is created for the benefit of all shareholders and participants. It is important that the provisions of the law are built from the bottom up at the practitioner level to the level of the regulator. Lack of discussion can lead to undesirable consequences. With the creation of the UzMRC, the development of an effective and practical legal mechanism for the transfer of claims on mortgages has become particularly important. The existing provisions in the current law and the new draft law, however, did not address the root cause of the problem, as practitioners in the mortgage sector were not consulted during the drafting phase. This meant that the bill had to be redrafted, which significantly delayed the implementation of the legal project.

III. OPERATING ENVIRONMENT

3.1 Economic overview

Despite the continuation of the coronavirus pandemic in the world, the emergence of new strains, and the unwinding of new waves of disease in the first half of the year, Uzbekistan's economy has reached a record growth rate for the previous year. Gross Domestic Product (GDP) for 2021 was 7.4% (the WB's 6.2% and the EBRD's 6.9%), according to the State Statistics Committee. By comparison, during the same period last year, the economy grew by only 1.9% due to the pandemic and lockdowns. At the same time, it should be noted that the situation in the economies of Uzbekistan's main trading partners is stabilising at the end of 2021 and aims to return to a growth trajectory.

Inflation in Uzbekistan continues to slow in the consumer sector. At year-end 2021, prices will have risen by 10.0% overall, compared to 11.1% in 2020, according to the Central Bank.

At the end of 2021, investments in fixed assets from all sources of funding amounted to UZS 244,962.6 billion, and the growth rate to the corresponding period in 2020 was 105.2%. At the same time, the share of investments financed at the expense of enterprises in total amount of investments into a fixed capital has made 29,1 %, foreign credits under the guarantee of the Republic of Uzbekistan - 7,1 %, credits of commercial banks and other borrowed funds 8,0 %, direct foreign investments and credits 42,7 %, including direct foreign investments - 12,3 %, funds of population - 9,0 %, the Republican budget - 8,8 %, Development and reconstruction Fund - 1,3 %, Development Fund of water supply and sewerage systems - 1,1 %.

Positive production dynamics is observed in all sectors of the economy. The main drivers are industry and services.

In 2021, enterprises in the country produced industrial products worth UZS 451.6 trillion, the index of industrial production to the same period last year amounted to 108.7% against 100.9% in 2020. Compared to the same period of the previous year, the growth rate of consumer goods amounted to 113.5% with their share in total industrial output reaching 33.7 %.

The service sector, despite continuing difficulties due to the pandemic for individual sub-sectors such as tourism, catering and accommodation, is performing impressively, growing by 19.2 % in 2021 compared to 3.0 % in 2020. The transport sector is recovering strongly from the downturn in 2020, with freight traffic growing by 10.0% and passenger traffic by 9.5%. Retail trade increased by 12.0% over the period under review (5.7% in 2020).

An acceleration of the dynamics against the previous year was recorded in the agriculture sector, up to 4.0% vs. 2.9%. It is worth noting that the growth rate of the construction sector slowed down to 6.8%, compared to 9.5% in 2020.

Foreign trade also managed to overcome the recession. In the past year, trade grew by 16.0% to $42.07 billion, compared to a major decline of 13.2% in the same period the previous year. In the period under review, exports rose by 10% to $16.6 billion and imports increased by 20.4% to $25.5 billion. Over the past year, Uzbekistan actively sold gold abroad amid a positive price environment in the global market.

The structure of exports in terms of raw materials showed a decline in ferrous metals (articles thereof) by 41.3% and cotton fibre by 7.0% compared to the same period last year.

In the structure of imports, the main share falls on machinery and equipment (including parts and components) - 37.1% (increase 6.2%), chemical products (and articles thereof) - 16.7% (increase 24.0%), foodstuffs - 11.5% (increase 35.5%) and ferrous metals (and articles thereof) - 7.8% (increase 34.8%). Thus, at the end of the year, Uzbekistan's economy is actively overcoming the consequences of the crisis and is on track to outperform pre-crisis indicators

3.2 Overview of the mortgage market

In the second half of the 2010s, the government set out to transform the mortgage sector and make it move towards the market. Before this transformation, the mortgage sector had too many very inefficient and corruption-prone mortgage programmes. To transform the mortgage sector, the government has done a lot of research and preparatory work with the help of the ADB. According to ADB studies conducted in 2015-2018, in order to meet the existing housing demand (deficit) as well as future projected demand, about 145,000 residential units needed to be built in Uzbekistan annually (according to preliminary IFC studies conducted in 2021, about 240,000 units need to be commissioned each year to meet demand)

As part of this work, the Ministry of Finance of the Republic of Uzbekistan together with the ADB developed the concept of "The Programme of Development of the Mortgage Market Sector in Uzbekistan for 2019-2021", which provides for termination of all previously existing preferential mortgage programmes and consolidation of these programmes into a single programme under a "new order" based on market principles (Decree No 5886 of the President of Uzbekistan of 2019 - On Additional Measures to Improve Mortgage Lending Mechanisms)

The essence of the new programme, unlike the old ones, was to give pricing and underwriting independence of mortgage products to commercial banks. The limited access of commercial banks to long-term financing was the main factor which hindered the development of the mortgage market in Uzbekistan. In order to solve the problem of "long money" for commercial banks to issue mortgages, the state has been providing long-term (up to 20 years) local currency loans at a fixed rate (CBU base rate minus 1 per cent). The distinctive feature is that the rate on previously issued mortgages under the programme will be reduced if the CBU base rate decreases and will remain at the same level if the CBU base rate increases. The Ministry of Finance of Uzbekistan started to place the first "long" money to finance mortgage loans according to market principles in commercial banks from the beginning of 2020 - from the funds budgeted to finance housing construction programmes. The new procedure allowed banks to extend mortgage loans for the purchase of flats in houses built by private contractors with their own funds and loans from commercial banks in the primary housing market. In comparison, under the old mortgage programmes, citizens could only buy housing in strictly defined houses, which were usually standard developments with finishing in remote areas.

The concept also envisaged a $200 million ADB loan "for the establishment of a sustainable long-term mortgage financing system based on market principles". The first tranche of $50 million was allocated to reform the government housing subsidy system. The ADB provided the remaining $150 million in financing to the mortgage sector through the Company.

The government's aggressive reforms in the mortgage market did not pay off, with the share of mortgage loans in the country's GDP rising from 3% in 2018-19 to 5.4% by the end of 2021. This high rate, judging by all indications, will grow further at a rapid pace for the foreseeable future. Given the reforms in the mortgage sector, the increasing interest from MIRs and private foreign investors, the strong growth of the population with its low housing stock, and the resulting priority of affordability for the government, mortgage lending is expected to grow strongly. Given the growth rate, one can confidently expect the mortgage loan portfolio to increase to 8% of GDP by 2024-25.

As of the beginning of 2022, the mortgage portfolio of the banks stood at UZS 35.8 trillion (US$3.31 billion) with 279,800 mortgages (approximately 0.8% of the country's population).

By comparison, the mortgage portfolio of Kazakhstani banks as of September 1, 2021 was more than 3.02 trillion KZT (US $7.09 billion). The number of loans for the purchase or repair of housing or purchase of land was more than 270,000, (approximately 1.4% of the population of the republic) reported the First Credit Bureau of Kazakhstan.

Table No. 4 Share of the mortgage portfolio in the country's GDP

№	Countires	Share of mortgage portfolio in GDP, (%)	For
1	Kazakhstan	3,8	08/2021
2	Russia	10,5	07/2021
3	Belarus	6,7	08/2021
4	Armenia	6,7	08/2021
5	Kyrgyzstan	2,9	09/2021
6	Uzbekistan	5,4	01/2022

Source: CBU, www.kapital.kz

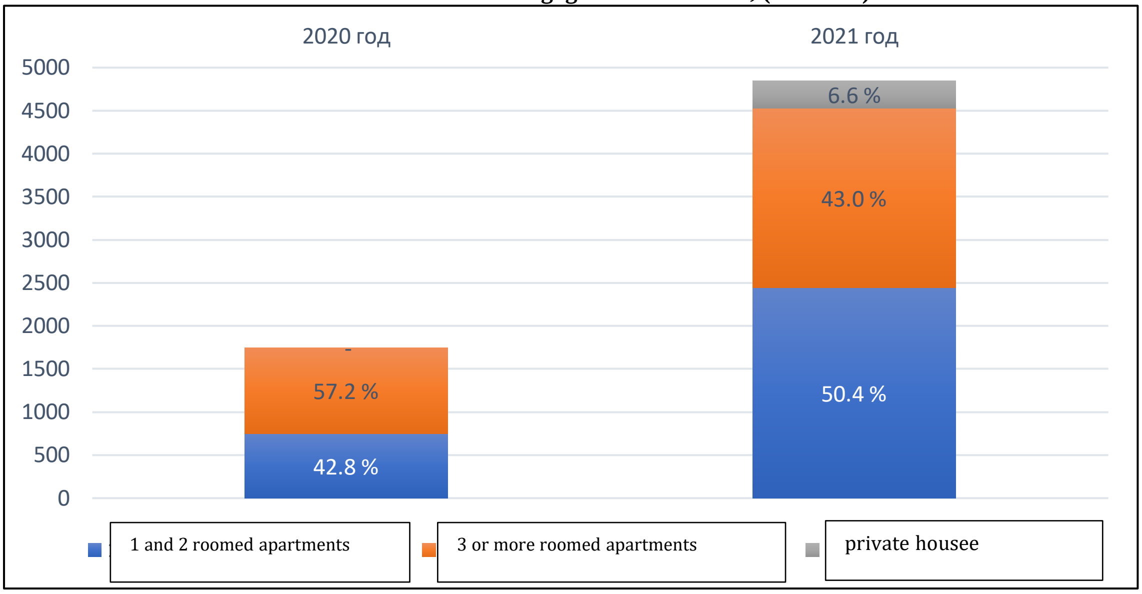
Currently, there are mainly two state programmes operating in the mortgage market:

1. Presidential Decree No. 5886 of 28 November 2019 (amended by PD-6186 of 11 March 2021 and PD-33 of 10 December 2021) established a "New Order" for granting mortgage loans to the population. Mortgage housing loans are financed for the purchase of flats in new buildings or for the construction and reconstruction of individual housing.

2. In accordance with Presidential Decree No. 1902 on the Programme for individual housing construction on standardized projects in rural areas for 2013 and No. 2639 on the Programme for affordable housing construction on new standardized projects in rural areas for 2017-2021. This programme completes its mission in 2022.

In 2020-2021, in accordance with the terms of the "new order", 14 out of 33 banks operating in the country issued housing mortgages, and the government, represented by the Ministry of Finance, placed more than UZS 6.6 trillion (2020 - UZS 1.7 trillion; 2021 - UZS 4.9 trillion) in them. Three commercial banks - Ipoteka Bank, JSCB Kishlok Kurilish Bank and NBU, which is owned by the state, received more than half of all funds.

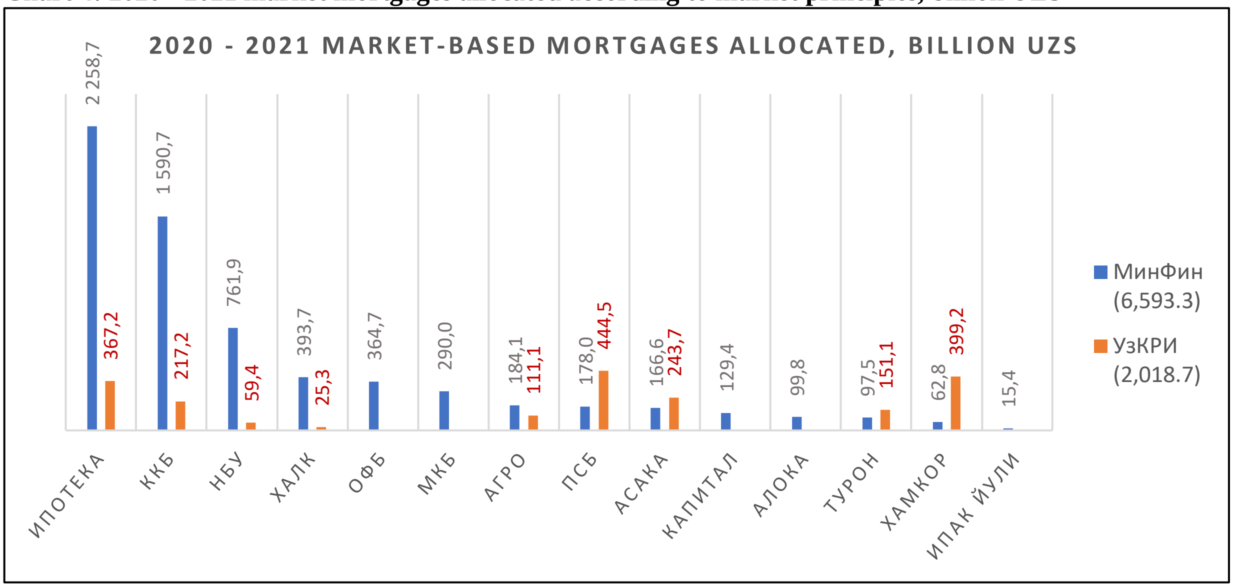
Chart 3: New Order Mortgage Loans PD-6186, (bln. UZS)



Source: CBU

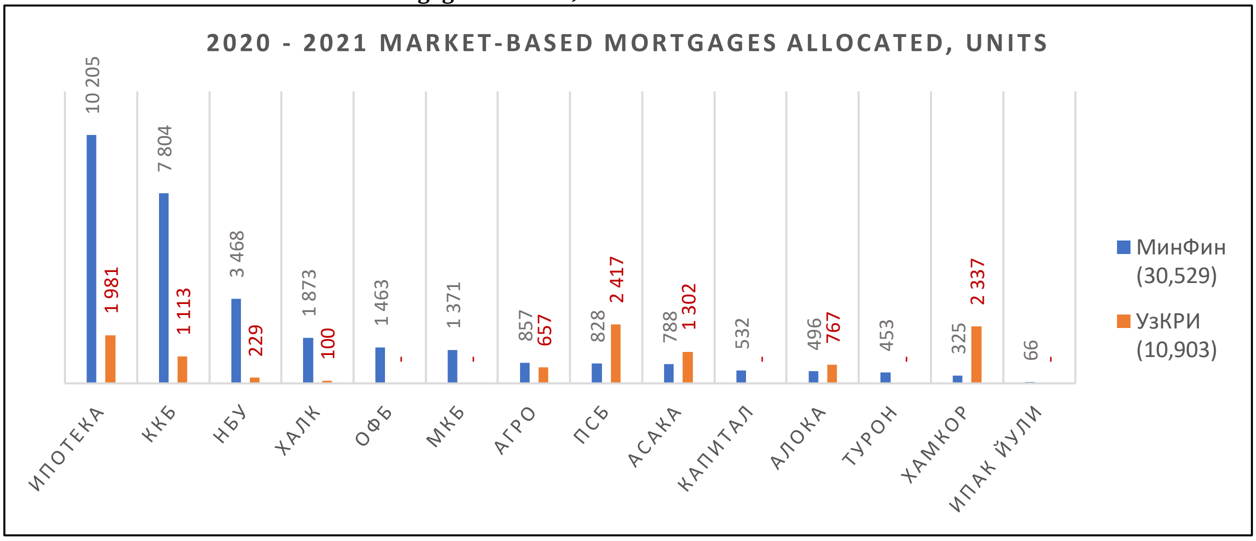
Without state support, "cheap" market mortgages will not yet be able to exist in Uzbekistan.

Chart 4: 2020 - 2021 market mortgages allocated according to market principles, billion UZS



Source: CBU

Chart 5: 2020 - 2021 market-based mortgages allocated, units



Source: CBU

In 2021, more than 59,57 thousand mortgages worth UZS 9.8 trillion were issued in Uzbekistan. The share of "market order" mortgages in monetary terms in the total mass of loans was 49.5%.

Chart 6: Mortgage loans by source of finance (bln UZS)

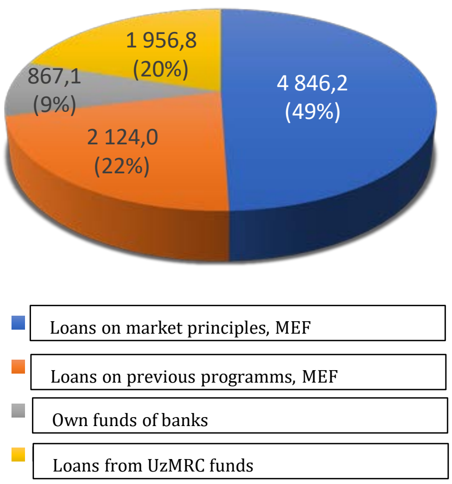
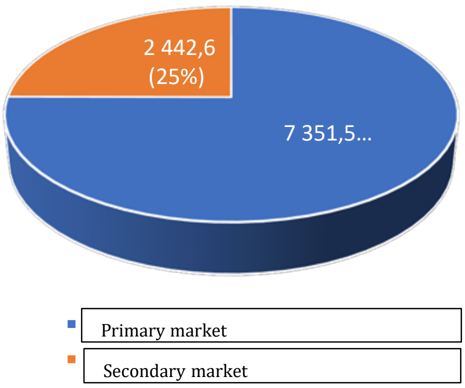


Chart 7: Structure of mortgage loans by property market (bln UZS)

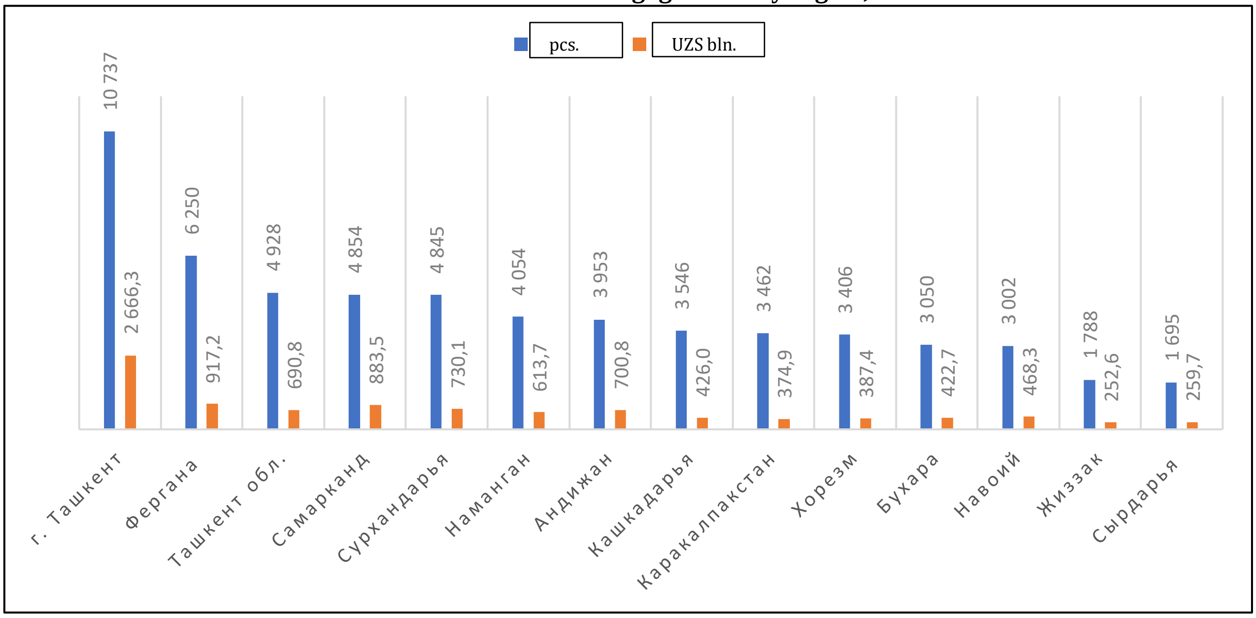


Source: CBU

The structure of mortgage loans by real estate market is as follows:

Among the regions, Tashkent and Tashkent region were the leaders in terms of the volume of market mortgage loans, with their residents receiving 2,666.3 bln UZS and 917.2 bln UZS respectively.

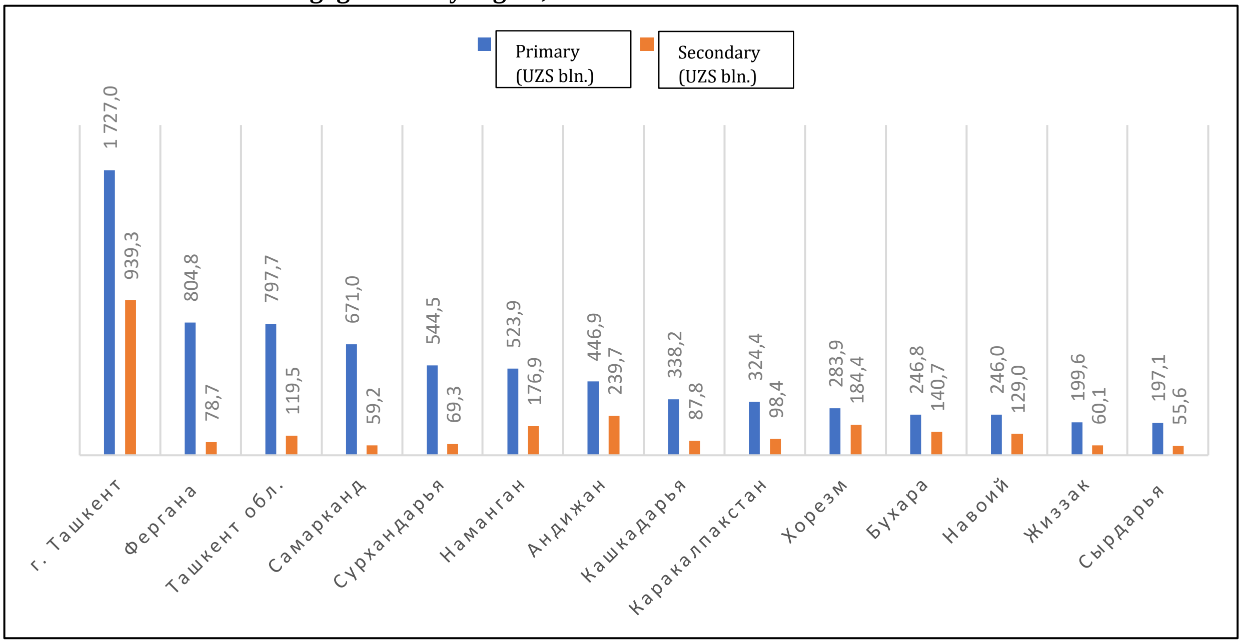
Chart 8: Structure of mortgage loans by region, 2021



Source: CBU

Of these, the distribution by property market was as follows:

Chart 9: Structure of mortgage loans by region, 2021



Source: CBU

For low-income citizens in need of housing improvements, the government pays subsidies from the budget (as a co-borrower on a mortgage loan) to compensate for part of the down payment, or interest on a mortgage loan, or both.

For the year 2020-2021, 10,787 citizens received subsidies for market mortgages, according to the Ministry of Finance, who were paid UZS 2.420.8 billion. Most of the money went to subsidising the down payment, while the rest went to repaying the interest on the loans.

The Government of Uzbekistan plans to gradually reduce its direct role in providing long-term financing for residential mortgage lending in favour of market-based funding mechanisms and eliminate other distortions in the financial sector.

3.3 Key challenges

The unprecedented reforms of the mortgage sector and the introduction of the mortgage refinancing mechanism have entailed several legislative, regulatory and market challenges, primarily for the Company, which is expected to reform the sector and pave the way for a vibrant secondary mortgage market.

Legislation

а. The transfer of mortgage claims is not fully operational, mainly due to impractical requirements such as the physical presence of the parties at the notary for the execution of mortgages on individual mortgage transactions. This was already highlighted in ADB's 2017 mortgage law studies and recommendations. However, implementation has been significantly delayed mainly due to structural changes in the capital market area. Once the intended changes and adjustments are implemented, it is expected that transactions in the secondary mortgage market will be greatly facilitated and thereby create a legal basis for the distribution of the accumulated mortgage portfolio on banks' balance sheets. Until then, market participants will find it difficult to attract foreign investors into the debt and local capital markets, thereby limiting the ability of the banking sector to optimise its accounts.

б. There is no legislation defining the rights of investors and borrowers in bank-backed debt capital market transactions. This is a serious barrier for any investor and hinders the conclusion of relevant transactions. In the absence of relevant legislation, even UzMRC, which is tasked with providing liquidity to the banking sector through a mortgage-backed bond market, will not be able to fully and sustainably perform its task

Regulation and supervision

а. There is no concept or clarification as to how the mortgage portfolio "sold" by banks will be classified on their balance sheet in terms of asset classification and loss reserve accrual.
Current banking sector regulation focuses mainly on the primary mortgage market due to the lack of banking activity in the secondary mortgage market. However, once the secondary mortgage market is fully operational, banks are expected to increasingly "offload" the active part of their balance sheet in terms of mortgage portfolios, thereby helping to create a financial ecosystem. This, in turn, will help the banking system optimize its balance sheet structure. This will be difficult to achieve in the absence of recognition and approval by the CBU of banks' request for easing to the capital adequacy ratio calculation regarding the refinanced part of their loan portfolio.

б. UzMRC is regulated as a risk-taking banking institution to maximize profitability, ignoring the peculiarities of its operating model.
In particular, these requirements relate to leverage, concentration and classifications of its problem loans. Under the above requirements, the Company must raise additional capital to continue refinancing activities once the refinancing portfolio reaches UZS 3.3 trillion.

в. As the Company is 25% state-owned, in addition to regulation by the Central Bank, the Company is also regulated by the SAMA. The reporting provided by SAMA is for companies engaged in manufacturing rather than financial services. This continues to place an administrative burden on the Company's limited resources and supports inefficient regulation.

Market

а. **The benefits of the "generation for distribution" model are not fully understood by banks and are therefore not widely applied**.

Banks operate on the classical model whereby they raise funds and lend against them, with a certain level of margin not necessarily commensurate with the perceived risk. International experience shows that this is not the best way for banks to operate, as banks are not in a position to borrow and lend on a continuous basis. At some point, banks' balance sheets will come under pressure in terms of regulatory requirements, financial performance and many other factors. Asset allocation in the form of refinancing will allow banks to remove the margin on their existing loans and further expand their loan portfolios. One simple transaction like this improves almost all a bank's financial indicators, including profitability, capitalisation and leverage.

The more such transactions take place, the more liquid the market will become and the more competitive mortgage rates will become for final borrowers.

Without creativity and efforts to optimise the balance sheet of banks, the banking sector will not be as efficient as it could be and capital markets are in their infancy.

б. Mortgage underwriting standards remain weak. For example, the prevailing notion in the market is that a DTI for a mortgage loan of 70% is acceptable. Although according to international practices a value in the region of 50% is a healthy common standard. Local market practice leads to a situation where the quality of the available mortgage portfolio in the economy is lower than the quality of mortgage portfolios in other countries. The situation is similar with the LTV ratio. This in turn makes it difficult to securitise the mortgage portfolio of the economy, thereby leading to a shortage of resources to provide new mortgages.

в. Limited capital market, especially debt market in the country. The size and capacity of the capital market is relatively small at present.

As of the date of writing, there are only 10 bonds in circulation, all in the form of unsecured corporate bonds with a total market value of UZS 733 billion, 41 per cent of which are issued by banks. Due to the lack of domestic capital, most corporations issue on the international market, including the government. Past experience has shown that wholesale borrowing on international markets carries certain risks. In times of economic downturn or geopolitical tension, debt issuers have been 'starved' of the resources needed to develop their businesses. In the same context, UzMRC faces the challenge of securing a sustainable source of liquidity for refinancing operations. In the absence primarily of a legislative and regulatory infrastructure, the Company will struggle to allocate its portfolio and create a self-sustaining environment in the capital markets.

г. Limited mortgage portfolio in the system possible for securitisation (monetisation). To date, the majority of the mortgage portfolio generated in the economy has been under resources provided by the Ministry of Finance in accordance with TO 6186 (New Procedure for Providing Housing through Market-Based Mortgage Loans). In accordance with the requirements of the new procedure, mortgages are issued with conditions which are not attractive from the investors' point of view. For example, the maximum LTV requirement is up to 85%, the maximum DTI requirement is 70%, and the age until which mortgages may be issued to borrowers is set at 60. Accordingly, mortgages (equal to the portfolio) with these parameters have a high potential credit risk compared with similar mortgages originated according to international practice standards.

IV. STRATEGIC PRIORITIES

4.1 Establish a sustainable and automated refinancing mechanism for mortgage loans

The establishment of a sustainable refinancing facility is critical to the Company's operations as a new business that has not existed before in the economic and economic life of the country.

Accordingly, the establishment of a sustainable refinancing mechanism involves a set of measures both within the Company's operations and coordinated systemic measures and activities, involving various government agencies, aimed at:

- Establishment of a legal framework in terms of creating a mechanism to secure the obligations of PFIs with the portfolio of mortgage loans provided while refinancing operations.
- Establish an IT system to effectively monitor the quality of collateral pledged in the form of the refinanced mortgage loan portfolio and determine its current value.
- Establish a legal framework for raising finance through the issuance of secured bonds and securitisation of the mortgage loan portfolio.
- Establishing appropriate regulation for both the Company and the PFI to ensure that the financial and regulatory benefits of refinancing are realised without compromising the effectiveness of supervision.
- Establishing a sustainable pricing mechanism so that the Company can adequately cover its operating costs while maintaining competitive pricing and compliance with market conditions.
- Synchronisation and standardisation of refinancing operations between the company and its partners, both in terms of timing and frequency.
- Raising public awareness, in particular among mortgage lenders and borrowers, of the refinancing mechanism and the Company's role and tasks in the development of the mortgage market.

To date, there is no legal and regulatory framework for the operation of a mechanism to secure PFI's obligations under refinancing operations, with property in the form of a portfolio of mortgage loans. For this purpose, to date, active and ongoing work has been undertaken under the Company's initiative: a working group of representatives of various interested government agencies and ADB has been set up. Draft amendments to the legislation have already been prepared and submitted for approval and application to the current legislation. The Company plans to ensure the completion of legislative amendments to ensure the creation of an effective tool for the control and supervision of collateral provided in the form of mortgages with the direct involvement of the Cadastral Agency and the Central Securities Depository.

One of the Company's main priorities is to establish an information system as an essential part of the technical infrastructure of the Company's mortgage refinancing operations. In order to control the refinanced mortgage loan portfolio, the Company plans to establish an information system synchronised in real time with the PFI's information system for full and complete monitoring and control over pledged mortgage collateral. To achieve this, the banks will have to work together to integrate the information systems of each of the PFIs and the Company's information system..

With regard to the Company's fundraising, the ADB's "Mortgage Market Sector Development of Uzbekistan" programme has been working extensively to introduce changes and adapt current legislation to allow for the issuance of secured bonds and pledging as collateral for the mortgage loan portfolio by banks. To date, there are no particular barriers to the issuance and purchase of corporate bonds by banks, insurance companies and pension funds, but the mechanism for the issuance of the Company's secured bonds has not been elaborated.

In order to ensure broader coverage of the mortgage market, involve more private banks in refinancing operations and create flexibility for the Company's day-to-day operations, the Company plans to expand the range of partners of the PFI, both by expanding the Company's shareholder base and by establishing partnerships (counterparties). During the current strategy document, the Company plans to expand the range of shareholders by 3-5 PFIs.

In terms of synchronisation, standardisation and frequency of refinancing operations, the Company will announce (through publication on the corporate website) the schedule and number of refinancing rounds for the coming years.

In terms of education and outreach to raise awareness among the general public about sustainable mortgage lending practices, ongoing work is planned both at the level of personal work with banks and public coverage of the company's activities in the media, as well as on the corporate website and social media pages.

New initiatives to promote mortgage lending

a. Mortgage guarantee programme

The purpose of this programme is to support PFIs in providing mortgage loans to borrowers who cannot afford a down payment of 25% but are solvent on their monthly loan payments, taking into account all their other obligations.

According to mortgage lenders in Uzbekistan, some 75% of borrowers are potentially constrained by the lack of sufficient savings to meet deposit requirements, rather than the availability of sufficient income to cover mortgage payments. However, analysis in international mortgage markets shows that borrowers with adequate or high repayment capacity, expressed as a debt burden of 50% or less, do better on mortgage payments than those with a higher DTI (above 50%), but with sufficient or high down payment.

The guarantee programme will provide PFIs with the opportunity to purchase a guarantee for a portion of the mortgage loan on a portfolio basis. The programme will compensate PFIs for a portion of the net loss incurred following the realisation of the mortgaged property under the mortgage loan provided in the form of collateral.

Priority in this area will include setting the terms of the guarantee mechanism to ensure that the PFI adequately covers the additional risks and that the final products are adequately priced for mortgage borrowers.

Achievements in this area will depend on the sustainability of bank liquidity and the willingness to expand mortgage lending.

б. Promotion of Islamic mortgages

Considering that the overwhelming majority of the population of Uzbekistan professes the Islamic religion, Islamic mortgages are on the Company's agenda and the Company is interested in refinancing mortgage loans issued on Islamic principles. The Company is committed to introducing Islamic mortgage refinancing operations during the current term of the Company's strategy document, but the Company's activities in this direction are wholly dependent on systemic regulatory and legislative factors.

While the law and regulation on Islamic banking are in the pipeline, the Company's priority will be to ensure that the legislative and regulatory framework adequately reflects the activities of secondary market players. In parallel, the Company will work on Shariah-compliant refinancing terms and appropriate eligibility criteria for Islamic mortgages.

в. Promotion of Green Mortgages

The Company is guided by socially responsible and sustainable attitudes (approaches) in conducting its business and is firmly committed to becoming an initiator and campaigner of green mortgages in the country. It is worth noting that there are currently no energy efficiency standards for buildings to implement green mortgages.
Priority in this area will include initiating the standard setting process with the support of the Ministry of Finance, Ministry of Construction and technical assistance from MID.

At the same time, the company will prioritise green renovation, which involves creating a mechanism for borrowers to undertake renovations using energy efficient building materials and thus contribute to the energy efficiency of the house.

4.2 Optimize the Company's financing by raising direct resources in the loan and debt capital markets

One of the main objectives and goals of JSC "Mortgage Refinancing Company of Uzbekistan" in accordance with the Decree of the President of the Republic of Uzbekistan PD-5715 from 13.05.2019. "On additional measures to develop and expand the mortgage lending market" is to attract financial resources in the domestic and international capital markets, including funds of international financial institutions and foreign government financial institutions, as well as through the issue of debt securities, including mortgage bonds, and their placement among investors, with their subsequent channeling to the refinancing of mortgage loans.

Between 2022 and 24, the Company plans to raise resources from three sources:

1. Credit lines from international financial institutions, including from ADB under the IFC.

2. Credit lines of the Ministry of Finance of the Republic of Uzbekistan in accordance with the Decree of the President of the Republic of Uzbekistan PD-33 from December 9, 2021 "On additional measures to provide the population with housing through mortgage loans on the basis of market principles”.
3. By means of placement of corporate bonds. This source of raising funds will greatly depend on the investors' willingness to accept the new type of instrument, which will be secured bonds. First of all, the development of this source of raising funds depends on the improvement of the legal and regulatory framework. Currently, active work is under way on drafting laws on the capital market, mortgage instruments and securitisation, as well as on developing the infrastructure for the operation of new financial instruments directly related to the Company's operations.

To continue to carry out its activities and fulfil its assigned tasks, the Company has the prospect of raising funds in the domestic capital market through the issue and placement of secured bonds. The collateral will be the rights of claim on refinanced loans issued to commercial banks against mortgage loans.

The issuance of the Company's secured bonds will become possible once the relevant laws and regulations, which are currently being actively worked on by the regulatory authorities, come into force.

A significant role in determining the attractiveness of these bonds by investors, particularly local commercial banks, will be played by the fact that the Central Bank of Uzbekistan will classify the secured bonds issued by the Company as highly liquid assets and will also be weighted as zero risk assets.
The Company will also take the opportunity to issue unsecured corporate bonds up to the amount of its equity. In the first stage, such bonds are planned to be placed by private subscription. Investors will include local commercial banks, insurance companies, international financial institutions and others.

The company will also use the option of issuing unsecured corporate bonds up to the amount of equity capital. At the first stage, such bonds are planned to be placed by private subscription. Investors will include local commercial banks, insurance companies, international financial institutions and others.

The Ministry of Finance has made significant efforts as a capital market regulator to improve the attractiveness and liquidity of the market. One of the main initiatives has been the abolition of tax on income and capital gains from investments in bonds and equities until 2024.

These efforts are expected to start bearing fruit and improve the depth and breadth of capital markets, thereby creating an enabling environment for companies to operate in capital markets.

4.3 Promote the streamlining of relevant legislation and regulation in the secondary mortgage market

a. Introduce the use of electronic pledges

The current legislation of Uzbekistan provides for a complicated and impractical process of creating and circulating mortgages in paper form only. This circumstance prevents the use of a mortgage as a security that can be pledged to attract additional investment into the mortgage lending market.

Presidential Decree No. PD-5715 of 13 May 2019 on Additional Measures to Develop and Expand the Mortgage Lending Market, participation in the development of the methodological and regulatory framework for mortgage lending and refinancing, including by engaging foreign experts and specialists, is identified as the main tasks of the Company.

Paragraph 7 of the road map for the development of the mortgage lending system in Uzbekistan for 2019-2021 approved by the above presidential decree provides for the drafting and submission to the Cabinet of Ministers of a bill on amendments and additions to certain legislative acts to improve procedures for the registration and transfer of rights under pledge agreements and mortgages, as well as procedures for foreclosing on pledged property, considering international practice.

In order to meet the requirements of the Presidential Decree No. PD-5715 of 13 May 2019 "On additional measures to develop and expand the mortgage lending market", the working group established from among representatives of the Company, interested ministries and departments, with the involvement of an independent expert, is developing draft amendments and additions to the current legislation.

These amendments and additions provide for an electronic form of mortgage, which is a non-issue security capable of being pledged, sold or otherwise disposed of and which enables its holder to obtain the relevant profit with the least risk.

The amendments and additions to the current legislation of the Republic of Uzbekistan will facilitate the rapid development of the mortgage loan market, from raising funds for refinancing to issuing mortgage-backed securities.

б. ***Promote the establishment of a regulatory and supervisory framework for mortgage bonds, and subsequently for Mortgage-backed securities.***

The development and implementation of a law on secured (mortgage-backed) bonds, along with the regulation of the circulation of Mortgages, is one of the most important (at this stage) laws vital to the Company's operations. To date, there is no business practice in the country as a financing instrument for borrowing by means of issuing secured bonds. Accordingly, there is no legal and regulatory infrastructure to regulate and control the issuance and circulation of secured bonds. In particular, a comprehensive and comprehensive law on secured bonds should be developed and implemented, which should detail such aspects as the procedure and regulations for issuing secured bonds, the role and functions of collateral supervisors for the benefit of bondholders, the mechanism for monitoring and controlling collateral, the functions and powers of the regulator, and other aspects. Also, in line with global practice, the functions of the CBU should be expanded to regulate the issuance and circulation of covered bonds.

The issuance of Mortgage-Backed Securities is the culmination of any mortgage refinancing company's activities. Consequently, given the state of development of the stock market and capital market in the country, it can be stated that the introduction of the instrument of Mortgage-Backed Securities is a very long and painstaking process requiring the investment of great efforts and resources from various state authorities to create a regulatory and legal environment, and a process which simply requires a certain maturity of the stock market and capital market in the country.

Conclusion

To date, UzMRC is the only company operating in the secondary mortgage market.

Achievement of the strategic objectives will largely depend on the successful implementation of the mortgage sector reform action plan already approved by the government. This, in turn, requires a collective effort to build the necessary mortgage finance and legal infrastructure.

The increasingly uncertain geopolitical environment is expected to affect progress towards the goal. Where possible, this requires taking a flexible approach to interventions, but adhering firmly to the objectives.

The results of the strategic activities, highlighting key lessons learned, will be presented in the next reporting period.