

La Hipotecaria Holding Inc.

COMPANY BACKGROUND

Headquartered in Panama, La Hipotecaria Holding Inc. (LH Holding) is a full-service housing finance company specializing in originating, servicing and securitizing residential mortgages for low- and lower middle-income borrowers. LH Holding was established in 2000 to manage the operations of three subsidiaries: Banco La Hipotecaria S.A. in Panama; La Hipotecaria S.A. de C.V. in El Salvador; and La Hipotecaria de Colombia, S.A.. The latter two currently operate as non-deposit-taking specialized

Country: Latin America

Sector: Housing Finance

IFC's Investment: \$60 million in long-term debt financing and \$3.5 million in equity

commercial institutions. LH Holding employs 161 people in its eight offices in Panama, El Salvador, and Colombia.

DRIVERS FOR LH HOLDING'S INCLUSIVE BUSINESS MODEL

- Increased demand for mortgages among low- and lower middle-income borrowers as affordable housing development takes off
- Market opportunity for a specialized, private sector mortgage finance institution
- Government policies that enhance affordability for borrowers and reduce risk for the company

The affordable housing construction sector has become more competitive in all three countries in which LH operates—generating increased demand for home mortgages. Today, there is a diversified, experienced and reputable group of affordable housing homebuilders offering a variety of homes in different price ranges. These homebuilders seek to reduce the housing deficit across the three countries.

Yet the supply of mortgages has not kept up with demand, particularly among low- and lower middle-income segments. In Panama, LH Holding's main competitors are the government-owned banks, Banco Nacional de Panama and Caja de Ahorros, and private banks such as Banco General. Typically, banks target upper- middle- and high-income borrowers. Similarly, in El Salvador, government programs such as Fondo Social para la Vivienda target very low-income borrowers, while private banks mainly focus on upper-middle-income borrowers, leaving a large

underserved swath in between. There is ample opportunity to target this in-between segment in Colombia, too, as the five largest private banks—controlling 85% of the mortgage market—are also focused on middle- and high-income borrowers.

LH Holding believes the market opportunity is particularly strong for a specialized mortgage finance institution, as opposed to one that offers a range of financial products. Specialization enables the company to operate more efficiently, resulting in lower cost and better customer service.

Finally, government policy has played a role in enabling LH Holding's successful model. In Panama, the government compensates mortgage lenders that offer subsidized interest rates. In both Panama and El Salvador, legal frameworks facilitate loan collection via payroll deduction, thus reducing lenders' repayment risk.

LH HOLDING'S INCLUSIVE BUSINESS MODEL

LH Holding's inclusive business model is built on a niche product: mortgages for owner-occupied homes targeting formally employed borrowers whose average family incomes range from \$400 to \$800 per month.

The majority are first-time homebuyers seeking homes generally priced between \$15,000 and \$50,000. Loans range from \$5,000 to \$80,000 with an average of \$24,700.

LH Holding offers mortgages at variable interest rates with maturities of a maximum of 30 years. In Panama, a preferential interest rate law enables the company to offer interest rate subsidies in which the government compensates mortgage lenders through a tax credit equal to the difference between the Panamanian reference rate and the subsidized rates. As of June 2012, the Panamanian reference rate was 6.25%. Borrowers pay zero interest for homes up to \$30,000, 2.25% for homes between \$30,001 and \$65,000, and 4.25% for homes between \$65,001 and \$80,000. Correspondingly, mortgage lenders receive tax credits of 6.5%, 4%, and 2%, respectively, for mortgages in these three home price categories. Loans issued prior to July 2001 are eligible for subsidized interest rates for 10 years and subsequent loans for 15 years. Mortgages for used homes and refinancings, however, are not eligible. In El Salvador, where no such law exists, LH Holding offers loans at market rates. It does the same in Colombia.

Rather than a bricks-and-mortar model of extensive branch offices, LH Holding reaches new home buyers through an on-the-ground sales force. Each sales representative is assigned to 8-10 housing developers in target regions and educates applicants about loan products and the application process. Housing developers, in turn, promote LH Holding's products and refer clients to the company. Housing developers also allow sales representatives to be based at their construction sites to meet potential clients. There, they can expedite a sale by initiating the loan application process on the spot. LH Holding employs this marketing method to originate new home mortgages and

uses its branch offices to serve clients seeking used home loans or refinancing.

Prudent, consistent underwriting criteria and a standard approval process for all types of mortgages are essential to LH Holding's success in serving its target borrowers. Its underwriting criteria include, but are not limited to, a good credit history, a minimum of two years of formal employment, a mortgage payment of 35% or less of gross family income at the time of loan approval, and a total debt payment (including consumer loans) of 55% of gross income. LH Holding also uses a four-stage loan approval process. First, sales representatives or applicants submit loan applications to branch offices. Second, staff at branch offices screen loan applications before sending them to the credit department in the country where the loan is originated. Third, the credit department conducts further credit analysis. And fourth, the credit department presents loan applications to the loan committee based at LH Holding's headquarters for final credit analysis and approval.



Monthly payments are collected in three ways: payroll deduction, bank account deduction, and voluntary payment. Legal frameworks enabling payroll deduction in Panama, utilized by 85% of clients, have minimized late payments and delinquencies. In El Salvador, payroll deduction is negotiated with individual employers, and used by 75% of clients. Borrowers making voluntary payments in Panama have three options intended to maximize customer convenience, and therefore the likelihood of on-time payment: first, to deposit payments into La Hipotecaria bank accounts at two banks with over 100 branches; second, to pay authorized collectors located in a major supermarket chain offering extended hours seven days a week; and third, through an authorized money transfer company that

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also operates seven days a week nationwide. LH Holding's servicing systems automatically signal a missed payment, regardless of the payment method.

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RESULTS OF LH HOLDING'S INCLUSIVE BUSINESS MODEL

- Efficient mortgage origination, with approximately 45% of all applications approved in Panama and 50% in El Salvador
- 20,750 total mortgages issued, approximately 65% of these to first-time homebuyers
- Net income of \$4 million in 2011, up 10.12% from the previous year
- Multiple successful mortgage-backed securities issuances in Central America and the United States

LH Holding prides itself on being an efficient originator of mortgages in both Panama and El Salvador, and expects to reach and maintain this efficiency in Colombia. It approves approximately 360 loans per month in Panama and 90 loans per month in El Salvador—approximately 45% and 50% respectively of all applications received in those countries. To date, 20,750 loans have been issued in total: 15,368 in Panama and 5,382 in El Salvador. Approximately 65% of these were to first-time homebuyers.

At the end of 2011, LH Holding's residential mortgage portfolio under administration consisted of 16,146 loans for a total of \$399.6 million. Its non-performing loan ratio

for loans on its books and securitized stood at 1.04%, well below the averages for the banking sector in Panama and El Salvador. Its net income reached \$4 million, up 10.12% from the previous year.

In 1999, La Hipotecaria S.A. in Panama became the first company in Central America to successfully issue a \$15 million mortgage-backed securities transaction. In 2007, it was the first non-bank company to issue a \$90 million cross-border securitization in the United States, and in 2008 the first to securitize mortgages originated and serviced in El Salvador through a \$12.5 million issuance in Panama.

IFC'S ROLE AND VALUE-ADD

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Investment Year: 2005 to 2010

- Increased access to long-term finance for low-and middle-income borrowers in Panama and El Salvador through credit lines of up to \$15 million and \$20 million respectively in 2004
- Assisted LH Holding in developing the sale of mortgage-backed securities for the Salvadorian capital market, and provided a true revolving feature for the El Salvador loan which enabled the company to issue a volume of mortgages many times larger than the size of the facility
- Further strengthened existing mortgage lending operations in Panama and El Salvador and facilitated ramp-up of operations in Colombia through a credit line of up to \$25 million and a \$3.5 million equity investment in 2009

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