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Real Estate-Backed Mortgages and Alternative Recovery Techniques: Evidence from Selected Banks in Tanzania

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Abstract

Inefficiencies accompanying foreclosures in recovering outstanding debts of real estate-backed mortgages have necessitated banks and other mortgage lenders to opt for alternative recovery techniques. Extant studies have focused much on the application of workouts mainly in developed economies (which are characterized by well-established real estate and financial markets) with less attention from emerging economies. This study aimed at exploring how banks in Tanzania apply alternative recovery techniques in real estate-backed mortgages. A qualitative approach was used to collect the data from multiple commercial banks in Tanzania. Interviews, annual reports, and government documents were used to triangulate the information. Findings revealed that different forms of workouts are preferred. The most preferred technique was mortgage modification, followed by mortgage refinancing. Other workout techniques such as forbearance, transfer of debt to a new borrower and short sale are minimally applied. Likewise, the banks were found applying the scare-tactics to enforce the customers do all they can to clear their debts before considering the use of the workouts. The study recommends that to facilitate optimal workouts, all stakeholders including the government, the bank systems, borrowers, and real property professionals must jointly cooperate for mutual benefits. The study proposed that further research could explore the fraudulent practice of borrowers that limit operationalization of workouts. Moreover, an investigation on whether borrowers' benefit by changing terms of their repayment could be made. Finally, further studies are needed to investigate whether there is heterogeneity in the application of workouts between commercial and residential mortgage with a view to establishing whether borrowers' default intentionally or not.

Keywords: Real estate-backed mortgages, mortgage modifications, mortgage refinancing, forbearance, short sale

1.0 INTRODUCTION

Over the past ten years, Tanzania has experienced dynamic escalation in its mortgage credit market ever since the establishment and the adoption of market-oriented housing finance approach (Gardner et al., 2020). The booming in mortgage market in the country has been attributed to increasing housing demand associated with population growth and rapid urbanization (Bah et al., 2018). Despite such prospect, Tanzanian mortgage credit market still suffers the non-performing mortgages, where the volume has increased over 400% in real terms (Mushi, 2020). The ultimate objective of mortgage lenders is always to have extended outstanding balances fully cleared by borrowers (Ambrose et al., 2016). However, full recovery of mortgages is not always accomplished. As a result, banks opt for different alternative recovery techniques (workouts) to ensure the outstanding balances are recovered efficiently (Chen & Deng, 2013). The introduction and adoption of mortgage workouts can be a solution to deficiencies of the traditional technique (the foreclosure) (Foote et al., 2009). In Tanzania for example, the government in partnership with Tanzania Mortgage Refinancing Company (TMRC) support commercial banks not only in mortgage lending but also in designing of different alternative arrangements to ensure maximum mortgage recovery.

Foreclosures are always accompanied with economic effects to both lenders and borrowers. The forced sales are not always successful given that sometimes it is difficult to get a customer to buy the property at the desired price within a short period of time (Navaretti et al., 2017). Moreover, it also reduces the ability of the lender to extend mortgages (McCoy, 2013). The more time foreclosure takes, the more the cost to lenders (Parr, 2017). This has led to the application of different mortgage recovery alternatives as the remedial for challenges accompanying the use of foreclosures (Levitin, 2009). The alternative recovery techniques are flexible instruments that may yield the maximum or entire payment of outstanding balance compared to foreclosure (Chen & Deng, 2013).

However, the alternative recovery techniques, are not always successful (Andritzky, 2014). Some techniques can help the continuation of payment, but default might reoccur which necessitate the trial of another workout (Quercia et al., 2005). Recurrences of delinquency might be due to failure of one recovery technique which leads to a bank to adopt another recovery technique. For instance, in

Tanzania, the government allows up to three times loan modifications. Extant studies (Ambrose et al., 2016; Navaretti et al., 2017; Seiler, 2014) show that, although banks adopt mortgage workouts there is still an increase in nonperforming mortgages. Thus, foreclosures become ineluctable when alternative recovery techniques do not produce desirable results.

There exist a number of studies in Tanzania (e.g. Komu, 2015; Kusiluka, 2008; 2012; Kusiluka et al., 2011; Mushi, 2020; Mwasumbi & Tarimo, 2019; Rothacher, 2011) that have addressed different aspects of real estate. To the best of our knowledge, the application of alternative workout techniques in Tanzanian mortgage market remained unexplored. It is therefore against that background that this study explored the adoption and application of workouts on real estate-backed mortgages in five selected mortgage banks in Tanzania.

■2.0 MORTGAGE MARKET IN TANZANIA

The number of banks offering mortgage loan in Tanzania rose from only three in 2010 to 32 in 2020. This steady increase has been ascribed to increased awareness of banks and housing demand (Gardner et al., 2020). However, the high interest rates charge by banks and lack of affordable housing due to high cost of construction have remained the major negative factors hindering the market growth (Mushi, 2020). As of December 2019, 32 mortgage lenders in the banking sector registered total lending of US$190.74 million whereas 5 banks accounted for approximately 70 percent of the market share. Most of these lenders offer mortgage loan for house purchase while a few offers for self-construction with the interest rates ranging between 15-19 percent which is still high for most average Tanzanian (Mirondo, 2020).

On the other hand, the population increase, and urbanization have been linked to the increase of mortgage loan demand (Rothacher, 2011). Currently (in 2020), Tanzania has a population of approximately 60 million people with a growth rate of 3 percent annual, the population is expected to exceed 129 million people by 2050. Moreover, urbanization reduces the household size in rural areas and increase demand of houses mostly in major cities. As a result, construction cost in major cities is high. For instance, the cost of building a standard mortgage house in Dodoma-Tanzania is 51 percent more in Pretoria-South Africa, while it costs 7.5 percent more in Nairobi-Kenya compared to Dodoma-Tanzania (Gardner et al., 2020). Nevertheless, the impact of housing construction economic in Tanzania is higher than in South Africa. As reported by the Centre for Affordable Housing Finance in Africa (CAHF) in June 2020, residential rental services contribute up to 3.5 percent to GDP.

Due to the high capital investment needed for mortgage lending, banks are reluctant to issue mortgage loan to borrowers. The mortgage loans are always long-term and thus tied up bank's capital, which increases opportunity costs. Recognizing this, few banks and non-bank institutions have united to create a company called Tanzania Mortgage Refinance Company (TMRC) which operates as a mortgage financial resource providing long-term loans to mortgage lenders. The availability of capital to financial institutions has contributed to the increase of mortgage lenders to 32 banks to date (Mirondo, 2020). However, recovering of mortgage loan presents a challenge to many mortgage lenders since construction of houses take relatively longer time and is characterized by many unforeseen uncertainties. In a response to the challenge, Banks tend to work closely with borrowers to ensure total recovery of mortgage outstanding. Different techniques are applied to help both the bank and borrowers. In this regard, the study aims at investigating different techniques used by banks to collect mortgage repayment, and the challenges associated with these techniques.

■3.0 LITERATURE REVIEW

3.1 The Concepts of Real Estate-Backed Mortgages, Defaults and Foreclosure

To begin with, the aspect of real estate-backed mortgage refers to a loan issued in which the borrower pledges a property as collateral to the lender for an obligation owed to the borrower (Brueggeman & Fisher, 2016). Under this arrangement, the lenders issue funds to the borrowers where the borrowers accept to release their rights to the property for security of the funds offered to them. Ambrose et al. (2016) pointed out the increasing use of real estate properties as the most preferable securities for accessing mortgages worldwide and still considered as the most important form of collateral. Many problems associated with other non-property collateral have made an increased preference of property pledging as collateral, hence facilitated issuing of real estate mortgages (Seiler, 2014). The issues surrounding uncertainties, difficulties in perfecting security interest, costs and flaws associated with development of security interest have proven non-property securities to be insufficient collateral (Brueggeman & Fisher, 2016).

Even though real properties have been considered as most reliable form of collaterals, still lenders suffer the non-performing real estate mortgages due to defaults (Chen & Deng, 2013). Secondly, the term "default" has been perceived differently by different scholars in real estate literature. Giliberto and Houston (1989) described default as a sense of a point or situation in which the property changes ownership from the borrower to the lender in execution of foreclosure proceedings or in the case of deed in lieu of foreclosure (friendly foreclosure). Based on this perspective, default occurs only when the lender has failed to use all other means of reviving payments of the outstanding debts such that foreclosure has to take place. Building on that argument, Seiler (2014) further considered nonpayment of a scheduled mortgage payment as technical default, while the physical change of ownership of the property is the actual form of default. Brueggeman and Fisher (2016) have extended the meaning of the concept of default, suggesting that it occurs when a borrower fails to make full or partial instalments of the scheduled payments as per the agreements of the loan contract. Contrary to Giliberto and Houston (1989), Brueggeman and Fisher (2016) define technical default as failure to upkeep the collateral property to the standards agreed in the terms. In real estate-backed mortgages, contracts usually allow the borrower to use and possess the property that has been placed as collateral but with ultimate obligation and responsibility of maintaining the property to acceptable standards. Failure to fulfil this objective, results into technical default (McCoy, 2013).

However, the most common form of default discussed by many extant literatures is that in which the borrower fails to make installment payment of outstanding balance as agreed on the loan contract (Navaretti et al., 2017; Parr, 2017). In most cases, default is not considered problematic when a borrower misses one-month payment (Capone, 1996). This can alert the lenders but not to the extent of considering the default scenario worth of foreclosure proceedings (Johnston-Ross & Shibut, 2015). The decision on counts of default until foreclosure is executed varies between different lenders. In most cases, default is considered after the borrower has failed to make three consecutive payment instalments.

Foreclosure for a long period has been used as the conventional method to recover non-performing real estate-backed mortgaged due to default (Quercia et al., 2005). This is a legal process in which the property is sold for the purpose of recouping the outstanding debt. It involves termination of rights of ownership of the borrower such that the property is sold, and the rights are transferred while sale proceedings are used to cover the outstanding debt that the borrower owed the bank (Davis et al., 2009). When a borrower defaults, banks tend to be patient and consider proposals that are brought forward by the borrowers on options that can be used to revive delinquency and default situation rather than proceeding to foreclosure (Shiller et al., 2019). The sale of the property is not an ultimate objective of the banks as they do not engage in real estate business, and for this reason the banks usually consider alternative means to recoup their funds other than foreclosure (Navaretti et al., 2017). However, patience has limit and on worst case scenario banks are obligated to settle and process foreclosure proceedings (Brueggeman & Fisher, 2016).

3.2 Alternative Mortgage Recovery Techniques: Adoption and Challenges

Alternative methods to mortgage recovery (workouts) is a subject that has recently captured the attention of researchers and practitioners in real estate financing (Chen & Deng, 2013; Parr, 2017). Despite their effectiveness in yielding what is expected of them, workouts are still accompanied by several limitations that arise from their application (Shiller et al., 2013; Tutag & Singh, 2011).

Quite regularly, implementation of foreclosure decisions is associated with side effects to either one party or both parties (lender or/and borrower) (Butler & Steiner, 2001). By anticipating an increase in value of the property in future, the borrower may intentionally decide to default by declaring inability to continue servicing the debt (Tutag & Singh, 2011). However, if in future, the value drops, which serves an implication that the borrower will lose the value of property. In these cases, the borrower will prefer to undertake workouts rather than releasing the property to the lender (Shiller et al., 2019). On the other side, if the lenders anticipate that there is going to be a future fall in price of the property, in some cases, they tend to delay and withhold the workouts arrangements in order to avoid the risk of future delinquency and consequently the fall of the property value (Quercia et al., 2005).

Extant literature reveals different alternative recovery techniques used in different countries. In most cases, the aspects of mortgage recovery are considered in terms of loss mitigation tools on the side of the lender or foreclosure prevention methods when considering the borrower's side (Ellen & Dastrup, 2012). Both ways are effective depending on the primary interests of the workout originator or the party that has presented an intention to initiate the workouts arrangement (Chen & Deng, 2013). Execution of workouts in both modules is far most similar since both parties prefer to avoid foreclosure by any chance while executing their primary objectives and obligations of the loan contract (Foote et al., 2009). Thus, discussions on alternative methods in most studies base on either loss mitigation programs or foreclosure prevention initiatives (Capone, 1996; Davis et al., 2009).

Some studies point out that the most preferred form of alternative methods is loan modification or loan contract restructuring (Gerardi & Li, 2010: Parr, 2017). Another study by Ambrose et al. (2016) made a cost-benefit analysis of the lenders` decision on loss mitigation tools or foreclosure. They argued that the lender might have at least four alternatives to adopt in case of serious default. These methods include restructuring of the loan, short sale (pre foreclosure sale), deed in lieu of foreclosure and forbearance, or if all these possible methods fail or other that makes foreclosure a better option than either of these techniques, then the lender can opt for foreclosure especially when dealing with a borrower who has been seriously re-defaulting (delinquent borrower). The study discussed the idea of self-cure in loan recovery processes where the workouts should concentrate on resolving the issue or problem that had caused defaulting and delinquency against the idea of the borrower releasing the property to the lender which is a loss rather than cure to the borrower (Chen & Deng, 2013). Ambrose et al. (2016) concluded that mortgage modification should be the first technique to be considered before other workouts.

Another commonly adopted method of the alternative techniques to recovery discussed by some studies is forbearance (Foote et al., 2009). Forbearance is the method in which the lender allows the borrower a grace period to temporarily stall payment instalments of the outstanding balance in order to allow the borrower to seek for relief or re organize themselves financially and continue servicing the loan. Literature indicate that forbearance is another effective alternative technique available in real estate-backed loan lending institutions. McCoy (2013) proposed that forbearance is the best way that can save homeowners from losing their homes and that in such situations, proposes arrangements in which financially stressed borrowers can receive subsidized loans from the government with less stringent terms and conditions or financial grants in order to help them partially cover their outstanding balance in such a way that the payment burden does not become an overload to the borrower.

Another widely accepted alternative technique of loan recovery is short sale or commonly termed as pre-foreclosure sale (Davis et al., 2009). This has been an option that is mostly used for seriously incurable delinquencies since it involves the sale of the property and consequently the loss of the property to the borrower. The lenders adopt this method when other 'friendly' methods have proven failure to revive delinquency (Seiler, 2014). The option of short sale cannot be costless to the lender either, in fact it is sometimes initiated by the lender when the value of the property has dropped beyond the amount of the loan owed. Lenders can approve the sale after a careful consideration of the financial effects it has and if it is the best way possible to revive the outstanding balance (Capone, 1996).

Despite their suitability, the adoption and application of workouts is still constrained by challenges (Adelino et al., 2009). The limitations differ in one way or another due to social (cultural) and economic contextual diversities from one country to another (Chen & Deng, 2013). The differences in legal and banking institutional frameworks also complicate these limitations.

White (2009) found out that servicers' compensation and reliance on outdated cash flow models are the sources of failure of loan modification programmes in the United States during the financial crisis. He further argued that compensation to servicers is based on the case of paying the interest advances to the investors of the bank even when the loan is modified. Nevertheless, Navaretti et al. (2017) concluded that these compensations are expensive such that lenders can decide to foreclose, thereby advancing enough funds to cover the debt and service different forms of compensation fees.

Reliance of outdated cash flow models has been a major problem that limit performance of loan modification programmes. Outdated cash flow statements do not represent true current financial situation of the borrower, thus modifying based on this cash flow can result in re-default cases (White, 2009). Other limitations to effective adoption and application of workouts have been pointed to be the costly nature of loan workouts, lack of enough knowledge on the accounting standards junior liens, tax consequences and threat of lawsuits by servicers (Johnston-Ross & Shibut, 2015; McCoy, 2013).

In brief, the foregoing discussion has pointed that the available studies on the application of workouts are those depicting in the situation of developed countries that might have different institutional and economic settings of real estate and financial markets. Based on the formulation, studies exploring the aspect in Tanzania were terribly lacking. Thus, the current study sought to investigate how banks in emerging economies apply these alternative recovery techniques in real estate-backed mortgages, drawing on the case of Tanzania.

■4.0 METHODOLOGY

4.1 Research Design and Approach

The study employed a case study design in answering the principle research question, namely: *how banks in Tanzania apply alternative recovery techniques in real estate-backed mortgages?* The case study was chosen on the ground that it provides an in-depth analysis of few selected cases (Eisenhardt, 1989; Mohajan, 2018). Furthermore, the multiple case study approach was employed since it allows cross-case comparison and analytical generalization, hence increase external validity (Yin, 2014). The study was basically qualitative in terms of the approach. As rightly argued by Yin (1989) and Phelan (2011), the use of qualitative method can be justified by the fact that the topic is unexplored. Applying the view to the study, it appeared logical to use the qualitative approach since the mortgage market in Tanzania remained largely unexplored.

4.2 Research Setting

Five banks that offer mortgage in Tanzania were purposively selected. Of the selected banks, four dominate the mortgage market shares in Tanzania. Due to the lack of knowledge about the application of alternative techniques recovery, one bank with lower market shares in terms of mortgage provisions was included in the study with a view to enhancing diversity and deeper understanding of the inquiry. The rationale and procedures for choosing the banks are further elucidated below.

Firstly, all the banks that offer mortgage in Tanzania market were identified from the database of Tanzania Mortgage Refinance Company Limited (TMRC). Data was collected from five banks (herein referred to as bank A, B, C, D and E) out of 32 Tanzania's mortgage lenders. Reports by TMRC and Bank of Tanzania show that only five banks dominate 72 percent of mortgage market in Tanzania as of June 2019. We conducted interviews with four leading mortgage banks and one bank from low market share category to allow variation in the sample (Khan, 2014). Selection of 4-10 cases was considered adequate that could yield results allowing a reasonable level of theoretical saturation (Howitt & Cramer, 2011; Eisenhardt, 1989).

Worth noting, Tanzania was among the five countries selected in 2018 by the Centre for Affordable Housing Finance in Africa (CAHF) to explore the mortgage market. In effect of this, the country recently amended its Land Act to ensure proper regulations, monitoring and supervision of mortgages. These amendments include a directive that the money obtained from mortgage has to be invested in Tanzania. Additionally, mortgagors must first submit evaluation reports from a registered valuer and thereafter submit another report showing how the money obtained from the mortgage has been utilized to develop the mortgaged land or property in addition to photographs showing the current status of the development (refer The Land Act 1999). Since the improvements of the legal framework, there has been a rapid increase of mortgage issuers in the market. Currently, the mortgage market comprises 32 lenders (Mirondo, 2020) as compared to decades ago where four banks were the only providers.

The selected five banks had different experiences in mortgage market in Tanzania. They also had different ownership structures allowing variations in the sample. The prevalence of high correlation of answers from these branches increased reliability of our data. Table 1 summarizes the main characteristics of each of the banks studied.

Table 1 Characteristics of banks in the sample

Characteristics	**Banks**				
	A	B	C	D	E
Origin	Foreign	Local	Foreign	Local	Local
Amount of outstanding debt (in USD million)	26.15	12.07	10.31	3.69	3.34
Number of outstanding debt accounts	182	554	161	814	62
Number of branches in Tanzania	9	16	6	8	224
Year of commencement of issuing real estate-backed loan	2010	2010	2010	2009	2015
Number of employees	191	244	181	207	3,316
Founded	1992	1995	1962	2001	1997

4.3 Sources of Data and Collection Procedures

The data were collected from the local headquarters located in the city of Dar es Salaam. The main sources of data were semi-structured interviews with managers from mortgage and risk assessment departments, company documents including annual and financial reports, and secondary data from external organization like Tanzania Mortgage Refinance Company Limited (TMRC), Bank of Tanzania and magazine articles. These data were triangulated (the use of multiple data sources) to ensure their validity (Yin, 2014; Gibbert & Ruigrok, 2010).

The data collection procedure started by sending an official letter to the sampled banks' headquarters requesting for permission to conduct the interviews. The face-to-face interviews were conducted with key informants in the banks at their headquarters. In some cases, the initially interviewed managers linked the researcher with other managers from related department for more information. In additional, bank E provided the researchers the access to interview another branch for more comprehensive information. Initially, the interviews were conducted by one researcher but later the second researcher conducted the second round of interviews with different participants within selected banks to clarify concerns raised during data analysis as well as to reduce biases.

The interviews started with general questions about the benefit of mortgage regulations and recovery rate. As it progressed, the interview questions focused more on the recovery techniques used by the banks visited and the challenges experienced during the application of the raised alternative techniques. The length of the interviews ranged from 45 to 135 minutes. The number of interviews were limited to 14. As aptly suggested, addition of more participants could not yield any new information (Astalin, 2013; Green & Thorogood, 2004).

Table 2 Interview overview and data sources

Bank	Participants' department			Interview length	Other data sources
	Mortgage Recovery Dept.	Credit/Mortgage Underwriting Dept.	Insurance Dept.		
A	SM HoD			60 min 45 min	*Newspaper articles, Bank of Tanzania reports, Centre for Affordable Housing Finance in Africa (CAHF) reports, Bank's websites, Annual reports, The Land Act regulations.*
B	PO	SM	SM	40 min 60 min 90 min	
C	HoD LO		SM	65min 135 min 90 min	
D	HoD		SM	75 min 90 min	
E	SM LO	SO		30 min 120 min 45 min	

4.4 Data Analysis

All interviews were audio recorded and transcribed in NVivo software. The content of the interviews was analyzed focusing on the emerged themes and subthemes (Corbin & Strauss, 2015). We refined the coding process by constantly comparing the coded data and theoretical codes from the existing literature (Glaser & Strauss, 2009; Ragin, 1997). We summarized our findings in figures to reduce the amount of data (Miles et al., 2019).

■5.0 FINDINGS AND DISCUSSION

This section addresses the two research questions articulated in sections 4.1 and 4.2 of this paper. The questions investigated the alternative recovery techniques applied by mortgage banks in Tanzania and applications of these techniques by lenders. Consistent with the questions, the findings are hereunder presented and discussed.

5.1 Alternative Recovery Techniques

The study revealed five real estate-backed mortgages recovery techniques mostly used by banks in Tanzania. The techniques were: mortgage terms restructuring (mortgage modification), mortgage refinancing, mortgage transfer, forbearance, and short sale of property. Moreover, the study identified different considerations put forward by banks as justifications for the application of these techniques. The recovery techniques below are presented from most preferred to the least preferred.

5.1.1 Mortgage Terms Restructuring

All the banks` officials reported that restructuring of the mortgage contractual agreement is the most applied alternative recovery technique. All parties to mortgage loan do not incur total loss under mortgage modification. Banks in our sample reported more than 50 percent of their mortgages are subjected primarily to modification arrangements; with two banks (A and C) of the sample reporting more than 70 percent. One respondent said:

> *Most frequently, we use mortgage modification because it least allows for delinquency. In this case, the lenders do not lose the entire amount of outstanding debt and the customer does not lose property upon foreclosure proceedings.* (Respondent Bank A)

Mortgage modification safeguards the lender from losses, ensuring that servicing of the outstanding debt is revived without disposing the collateral property, which in turn favors the borrower (Chen & Deng, 2013). Another reason attributed to mortgage modification preference by lenders is maintenance of customer relationship, as reported:

> *Even though the process has financial costs to both parties, it is the best as it also helps to maintain the bank-customer relationship. The aim of any bank is to extend mortgages and also retain customers who may have experienced challenges in making payments. (*Respondent Bank C)

This finding support prior researches by Ambrose et al. (2016) and Gerardi and Li (2010) who established that mortgage modification is the most prioritized technique. Mortgage modification provides a room for assessing the current financial capabilities of the borrower (Parr, 2017). Since the banks in Tanzania have no money that is invested in the long-term loans, the mortgage in the country is financed by the Bank of Tanzania (BOT). This is done through Tanzania Mortgage Refinancing Company Limited (TMRC). In this case, the BOT allows up to three loan modifications. The borrower applies for modifications and the bank makes decisions based on the prevailing terms and conditions. The banks can allow early repayments, step up arrangement, reduction of installment amount or write-off.

Early payment is allowed in Tanzania to reduce risk. Lenders allow a borrower to settle in advance all or part of the loan from the money obtained from other sources. The step-up arrangement does not change the installment time but can allow the borrower to change the installment amount depending on the sources of income. For example, a borrower can double installment for a certain period and pay less in the subsequent period. On the other hand, reduction of installment amount requires the bank to extend the mortgage time to allow a borrower pay less than the installment initially agreed upon. Lastly, if it turns out that all these modifications have failed and the borrower has no means of paying the mortgage installment, the bank is forced to sell the property and write off the outstanding balance. Figure 1 summarizes the process of mortgage modification practiced by banks in Tanzania.

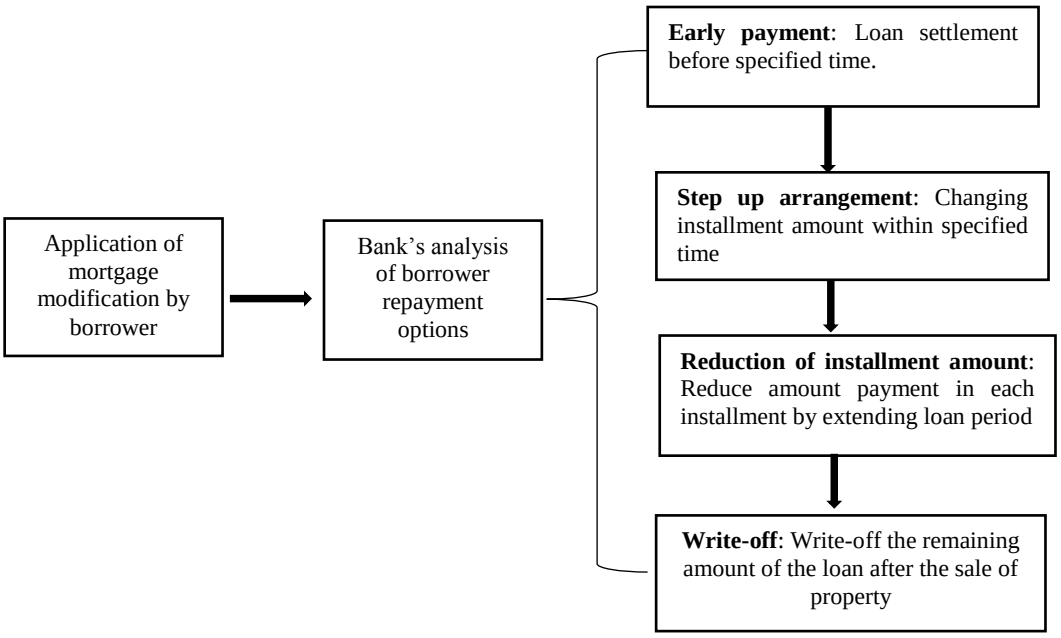

Figure 1 The process of mortgage modification

5.1.2 Mortgage Refinancing

The respondents suggested that the notable increase in the trend of mortgage refinancing through buying back methods. In this scenario, other banks take over the mortgage by servicing off the outstanding balance on lump sum arrangements and issue such finance as another

mortgage to borrowers with different terms. The banks reported that refinancing through buying back has recently become very common. The popularity has currently risen in Tanzania due to increasing competition in the mortgage market, for banks are trying to attract borrowers (Tutag & Singh, 2011). However, its application is less compared to modification. In view of a respondent from Bank A, it accounts for less than 20 percent of real estate-backed mortgages in banks. Another respondent further argued,

> *Refinancing arrangements are mostly common in servicing outstanding debts amounting less than 9,000 USD*. (Respondent Bank D)

5.1.3 Mortgage Debt Transfer

As evidenced by the banks in our sample, mortgage debt transfer is the least used recovery techniques in the country. The borrower in this arrangement does not necessarily own property to which the mortgage has been applied for. In addition, the arrangement requires a borrower to have a guarantor/third party who is also obliged to surrender property when the borrower does not have enough properties to accomplish the financing requirement. In case the borrower has defaulted, the guarantor is notified. If the guarantor accepts to service the mortgage, then mortgage obligations are transferred to the guarantor who now becomes the new borrower. One respondent was quoted reporting that most banks have stopped using mortgage transfer due to the challenges of third-party property in their credit policies.

> *The use of third-party property has been a long-time challenge in most banks in our country. Usually, borrowers start well but later they lose responsibility of their contractual obligations because if one defaults foreclosure proceedings, that cannot lead to any direct effects since he/she is not the property owner*. (Respondent Bank E)

The arrangements to ensure that the pledged property is not sold in foreclosure usually ends up with the guarantor accepting paying the outstanding debt in order to keep the property (Johnston-Ross & Shibut, 2015). However, the data indicated that owing to the prevalence of financial constraints in the economy, the use of mortgage transfer debt to new borrowers has declined over time. Moreover, lack of informatics technology for data storage and legal system have contributed to less people agreeing with mortgage transfer arrangements.

5.1.4 Forbearance

This is a process in which the lender approves the grace period of several months so that the payment of the mortgage is postponed for the borrower to consolidate the source of income (Chen & Deng, 2013). This practice is common in Tanzania especially among the employees who use their salary in servicing the mortgage. Connected to that, a respondent was quoted saying:

> *Forbearance arrangements can only permit a grace period ranging between two to three months in accordance with the bank's policy. All banks have a policy stating that longer periods of forbearance are not allowed due to a number of reasons, but exceptions are sometimes considered especially when the borrower is expecting an inflow of an income in the future from trusted sources like government entities*. (Respondent Bank E)

Another respondent from Bank D added that banks rarely provide grace periods to a borrower's promise of finding and getting another job. This method is not normally an attractive option for borrowers due to the cost incurred for grace period extension. One officer said:

> *Usually our banks require the borrower to make payments of the accrued interest income that lost during the grace period offered to the borrower. Therefore, borrower signs commitment forms stating that after the grace period, they will pay the increased amount of the instalment that includes the principal amount plus the usual interest rate together with the accrued interest rate*. (Respondent Bank D)

Our findings on the period of forbearance contradict the previous findings which established that the period ranges between six to twelve months or slightly longer in some special cases (Brueggeman & Fisher, 2016). In Tanzania, the period ranges from two to three months as confirmed by this study. This is partly due to the financial risks faced by the lender as compared to other recovery techniques. The mortgage and banking industry in Tanzania are still growing, hence characterized by high demand of the working capital. Thus, lenders cannot afford to provide longer grace periods (Davis et al., 2009; Foote et al., 2009).

5.1.5 Short Sale of the Property

Short sale occurs when the value of the property has fallen short far less than the outstanding balance (Navaretti et al., 2017). The study respondents from banks A, B, C and D reported that short sales constitute only about 1 to 2 percent of all mortgages' recovery techniques. On the contrary, bank E reported a higher rate of 5 to 10 percent. The Central Bank of Tanzania allows banks to dispose property when the price is anticipated to reach at least 35 percent of the estimated price. When the real estate market is unstable and the property is

anticipated to perform well when released in foreclosure arrangements, lenders can propose and approve short sale in order to acquire the highest amount possible even if it will not cover the full debt.

> *It is not common at all. We do not practice it here. Most often, the real estate properties appreciate but currently we have been experiencing depreciation of the property value*. (Respondent Bank C)

Our findings indicate less use of short sale recovery technique in Tanzania mortgage market. This finding contradicts those reported by the previous research which indicated high frequency in the use of short sale technique (Ambrose & Capone, 1996; Cordell et al., 2009). This is partly because the borrowers have perceptions that short sale leads to loss of property. Thus, many borrowers would prefer to file for court injunctions as a delaying tactic until they can raise money to service their mortgage. Another salient reason is based on the instability of the real estate market in Tanzania. Banks are reluctant to take risks by writing off part of the debt for short sale proceedings which may not recover the entire outstanding balance. Decreasing property values have alerted banks to hesitate acceptance of short sales.

5.2 Application of Alternative Recovery Techniques

Banks have different considerations when it comes to application of workouts. Application in this case means how the bank chooses to take (approve) or disapprove an alternative recovery technique. Thus, application deals with the decision-making environment based on the policies or practices of approving or disapproving a workout (Shiller et al., 2019). Each bank has its own way of applying the workouts. While some of the workout techniques are regularly applied in all banks, others are rarely used and some are not applied at all, for different justifications, as the management teams of the banks see fit.

5.2.1 Initiation and Approval of Workouts

The interviews focused on the major two issues regarding the initiation of workouts. First, the study investigated who initiates the workout negotiations. Secondly, the study explored how the banks approve the applications of workouts while controlling the rate of the workouts approved.

Insofar as the first issue was concerned, most of the banks selected reported that initiation of workouts is regularly a step taken by the borrower. The borrower is primarily obliged to report the hardship or situations faced that implicate the ability to service mortgage during or prior to delinquency. The study participants said that in most cases, borrowers react early by applying for workout negotiations as early as they receive the first 'demand' notice from the bank. A demand notice saves as a reminder to the borrower of their contractual obligations regarding scheduled payments and an intention to foreclose. The bank officials explained further that sometimes the bank can initiate the workout strategies (especially to those borrowers undertaking business operations) as soon as the bank has noticed difficulties in the business in their regular follow ups. In this regard, the bank officials can convince the borrower to consider different options like mortgage modification or other alternative techniques that can relieve the borrower before delinquency has occurred or worsens. Bank A and Bank C particularly reported that doing so is a strategic movement of improving the bank-borrower relationship with the customer.

On the second issue, that is, the banks' policy on control of workouts applied as a management strategy, interviewees reported that application of workouts is mostly a situational matter. They reported that workouts, in many successful occasions, save as the best options of resolving delinquency while at the same time maintaining good relationship with borrowers. Therefore, it is not in the interests of the banks to limit the frequency of workouts. However, it is certain that workouts have effects to the banks. As a result, banks impose certain limitations in their policy statements to control different aspects related to workouts. These limitations include imposing limits or parameters like duration, interest rates, principal amount and limit of the grace period that can be advanced in workout negotiations.

Adelino et al. (2009) found that during the global financial crisis, foreclosure and mortgage modification decisions highly depended on the future price movement of the secured properties. As a result of housing bubble, many of these decisions were concluded to foreclosure. Making such decisions based on future property values in Tanzania is challenging due to absence of property value database and property indices which can be used as reference to anticipation of future property values. The occurrence of valuation variations is another factor that hinders reliability of valuation reports on the anticipation of property values to decide on whether the bank should allow mortgage modifications or not.

5.2.2 Criteria Considered in the Approval of Alternative Recovery Techniques

Implementation of the workouts is a managerial decision especially when it affects the business operations of the banks. Our sampled banks reported the following criteria that influence the criteria for approval of the alternative recovery techniques.

The most crucial consideration was reported to be the amount of the outstanding debt owed at the time of delinquency. Three banks - B, D and E reported outstanding debt as the most significant consideration. The higher the amount, the more the bank prioritizes the workout consideration to enable the customer to reinstate the debt payment. Owing to prevalence of problems associated with foreclosures, banks prioritize approvals for workouts especially on modification for delinquent mortgages with large amounts of outstanding debt as written off costs to the bank than pardoning the terms agreed in workout arrangements.

An official respondent from Bank C explained that sometimes the amount owed was relatively smaller to an extent that it could not be sufficient to decide approval of a workout arrangement. Thus, the bank only uses scare-tactics to ensure that the customer use all the means possible to clear the debt instead of considering mortgage modification. The scare-tactic is done by disapproving application of the modification. The banks uphold that if such debt is not cleared as agreed contractually, foreclosure will be affected immediately. In this scenario then, the borrowers will do all they can to clear the debt to avoid foreclosure at the final minutes.

The second most considered criterion was the bank's relationship with the customer (borrower). Out of the five banks studied, two banks - A and C considered the relationship between the bank and the borrower a priority to the amount of outstanding balance recovery when it comes to considerations on approving a workout arrangement. When the credit and mortgage lending industry is still at the infancy stage, foreclosure is not a preference as during the worst scenarios when the borrowers tend to lose their properties. Thus, banks cooperate with the borrower so that the situation that resulted to delinquency is solved and payment of the mortgage is reinstated. By doing so, the banks improve their relationship and retain their customers while maintaining the bank's reputation.

■6.0 CONCLUSION, LIMITATIONS, AND AREA FOR FURTHER RESEARCH

6.1 Conclusion

The study has established that different forms of workouts are used in Tanzania. However, restructuring of the mortgage terms (mortgage modification) is the dominating technique followed by refinancing of the credit facility. Other techniques rarely applied include transfer of mortgage debt to a new borrower, forbearance, and short sale of the property. Application of workouts has generally been eclipsed by socio-economic factors that limit their fully application. Given the evidently increase in the nonperforming mortgages (most of which are backed by real estate) and failures of mortgage modifications programs, there is a seemingly inevitable urgency of establishing and improving other workout techniques that will enable banks to recover their funds. That could ultimately help avoiding foreclosure to borrowers. To affect this, all stakeholders including the government, the bank systems, borrowers, and real property professionals must work closely together.

6.2 Limitations and Area for Further Research

This research can be used as a reference material for studies probing on the alternative recovery techniques of real estate-backed mortgages and other types of mortgages. However, a caution must be made that there exist some limitations. First, though we believe that five banks might be a good representative sample of 32 banks that offer mortgage loan in Tanzania, the results obtained from the study cannot be generalized much as to reflect the situation of the whole country. Therefore, we suggest the findings could be replicated after conducting more studies especially using the quantitative approaches. Those studies could test if there are differences in the application of these workouts among banks and the factors linked to variations or similarities. Besides that, longitudinal studies using big data could help validating the causes of preference of the modification techniques and point to the best alternatives or models.

Second, our paper has provided the result from the side of the lender. Further studies could explore the fraudulent practice of borrowers that limit operationalization of workouts. Third, research could investigate whether the borrowers do benefit by changing terms of their repayment. This might uncover whether the borrowers do default intentionally or not. Fourth, the current study assumed that workout techniques are applied in both types of the mortgage loan. Future research could investigate whether there is heterogeneity in the applications of the workouts between commercial and residential mortgage.

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