HOUSE BUILDING FINANCE COMPANY LIMITED

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PAKISTAN'S REAL ESTATE TAXES AND TRENDS

RESEARCH REPORT

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TABLE OF CONTENTS

ABSTRACT

Pakistan's house building sector has experienced significant shifts in consumer financing. In FY19, the sector accounted for 17% of total consumer financing, totaling PKR92.5 bn. This share decreased to 15% in FY20, but rebounded in FY21 with financing rising to PKR103.6 bn while maintaining its 15% share. The sector saw substantial growth in FY22, with financing nearly doubling to PKR200 bn (22% of total consumer financing), and continued to peak at PKR 212 bn (25% of the market) in FY23. Although FY24 saw a slight decline in financing to PKR 204 bn, the sector maintained its 25% market share, indicating potential market stabilization after rapid growth. This growth is likely driven by favorable government policies, low-interest rates, and increased housing demand for small and large property segments.

The Pakistan government's FY25 fiscal budget introduces significant reforms to real estate taxation, aimed at increasing revenue, curbing speculation, and enhancing transparency. Notable changes include the elimination of the holding period for properties acquired after July 1, 2024, and a flat 15% capital gains tax for Active Taxpayers List (ATL) filers. Additionally, the budget introduces tax incentives for sustainable development and affordable housing, such as rebates for green building projects and tax credits for affordable housing developers. Real Estate Investment Trusts (REITs) also benefit from favorable tax treatment. These fiscal measures align with observed trends in Pakistan's real estate market from 2012 to 2024, particularly in the growth of small and medium property segments, driven by urbanization and middle-class demand. The combination of new tax incentives and ongoing market trends suggests strong potential for investment returns, especially in these segments.

Pakistan's property taxation system presents a mixed picture when compared to other countries in the region. While its property tax rates (0.15% to 0.75% of property value) are relatively low, making it competitive with nations like India and Singapore, other aspects of its tax structure are less favorable. Pakistan's 15% Capital Gains Tax (CGT) for filers is lower than China's 20% but comparable to Bangladesh's rate. It's higher than India's in some cases and less favorable than Singapore's 0% for properties held for over three years. Stamp duty rates in Pakistan, ranging from 2% to 5%, are comparable to other countries, but the addition of a unique Capital Value Tax (CVT) at 2% of property value sets Pakistan apart and potentially increases the overall tax burden on property transactions.

When considering the cumulative effect of various taxes and fees, including registration fees and the CVT, Pakistan's overall taxation on property transactions may be less attractive compared to some other countries in the region. Countries like Singapore, Hong Kong, and the UAE offer certain tax advantages, such as no capital gains tax for individuals in Singapore (for properties held for at least 3 years) or the absence of federal capital gains tax in the UAE. However, it's important to note that each country's tax structure is unique, and the impact on property owners and investors can vary based on factors such as property values, holding periods, and individual circumstances.

PAKISTAN'S FISCAL BUDGET 2024-25: A PARADIGM SHIFT IN REAL ESTATE TAXATION

The 2024-25 fiscal budget, as introduced through the Finance Act of 2024, represents a major shift in Pakistan's real estate taxation framework. These reforms are aimed at increasing revenue, curbing market speculation, and promoting transparency.

Key changes include the elimination of the holding period concept for properties acquired on or after July 1, 2024. A flat 15% capital gains tax (CGT) now applies to ATL (Active Taxpayers List) filers, while non-ATL filers face higher progressive rates . For properties sold within a year, a 15% CGT is imposed, with lower rates for longer holding periods depending on property type. Rental income tax has also been standardized across all taxpayer categories, with calculations based on net income after allowable deductions.

Additional reforms include a 50% reduction in stamp duty for affordable housing transactions and property tax exemptions, with full exemption for units valued up to PKR 2.5 million and a 50% reduction for properties valued between PKR 2.5-5 million. Withholding tax has been adjusted, reducing it from 2% to 1% for properties held over three years, and eliminating it entirely for those held more than 10 years.

To encourage sustainable building practices, the budget offers up to a 10% tax rebate for green projects meeting LEED certification standards and developer tax credits up to 15% of project costs for affordable housing developments. Real Estate Investment Trusts (REITs) benefit from tax-exempt dividend income and a reduced corporate tax rate of 15%. Additionally, land transfer tax has been reduced by 25% for properties transferred within family members.

These reforms aim to stimulate growth in the real estate sector, encourage long-term investment, and support sustainable development. However, the full impact of these changes on market dynamics remains to be seen.

QUANTITATIVE TAXATION MEASURES ON REAL-ESTATE

TAX CATEGORY	DETAILS
1.Capital Gains Tax	**General Rule:** *15%* tax if sold within 1 year of purchase for all property types (open plots, constructed properties, flats).
	Open Plots: • 12.5% (1-2 years) • 10% (2-3 years) • 7.5% (3-4 years) • 5% (4-5 years) • 2.5% (5-6 years) • 0% (over 6 years)
	Constructed Properties: • 10% (1-2 years) • 7.5% (2-3 years) • 5% (3-4 years) • 0% (over 4 years)
	Flats: • 7.5% (1-2 years) • 0% (over 2 years)
2. Rental Income Tax	**Uniform Taxation:** Same tax rates for all taxpayers (individuals and AOPs).
	Net Income Basis: Tax calculated on income after allowable deductions (up to 4% of gross receipts).
	Withholding Tax (WHT) Rates: • 0% (income up to PKR 300,000) • 5% (PKR 300,001 - 600,000) • 10% (PKR 600,001 - 2,000,000) • 25% (over PKR 2,000,000). • Rates double if the recipient is not an active taxpayer.

QUANTITATIVE TAXATION MEASURES ON REAL-ESTATE

TAX CATEGORY	DETAILS
	Sub-leases: WHT rules apply to all rental payments, including sub-leases.
	Loss Offset: Losses from property income can be offset against other income under this heading.
3. Stamp Duty	**Affordable Housing:** 50% reduction for transactions involving affordable housing units (valued up to PKR 2.5 million). **Other Property Transactions:** No changes.
4. Property Tax	**Affordable Housing Projects:** Full exemption on property tax for units valued up to PKR 2.5 million. **Mid-Range Housing Projects:** 50% reduction in property tax for units valued between PKR 2.5 million and PKR 5 million. **Luxury Properties:** No change in property tax rates for properties valued above PKR 5 million.
5. Withholding Tax on Property	**Revisions for Property Transactions:** • Reduced from 2% to 1% for properties held for more than 3 years. • No withholding tax for properties held for more than 10 years.
6. Tax Incentives for Green Buildings	**Incentives for Sustainable Development:** • Up to 10% tax rebates for projects meeting LEED certification standards or equivalent. • Additional deductions for expenses related to sustainable technologies, such as solar panels and rainwater harvesting systems.
7. Tax Credits for Developers	**Affordable Housing Development:** • Tax credits of up to 15% of the project cost for developers engaged in affordable housing projects. • Additional credits for developers incorporating green building practices.

QUANTITATIVE TAXATION MEASURES ON REAL-ESTATE

TAX CATEGORY	DETAILS
8. Tax Treatment for REITs	**Favorable Tax Treatment:** • Dividend income from REITs exempt from tax to encourage investment in real estate through this vehicle. • Reduced corporate tax rate for REITs set at 15%, compared to the standard corporate tax rate.
9. Land Transfer Tax	**Adjustments for Family Transfers:** • 25% reduction in land transfer tax for properties transferred within family members. • No change for other property transfers.

REAL ESTATE TAXATION ACROSS BORDERS

To understand Pakistan's new tax structure in a global context, we've conducted a comparative analysis with seven other countries: India, China, Singapore, Hong Kong, Bangladesh, UAE, and Malaysia. This comparison reveals significant variations in real estate tax structures across these markets.

Property Tax: Pakistan's property tax rates of 0.15% to 0.75% of property value are generally more competitive compared to other countries in the region. These rates are lower than India's 5% to 20% of annual rental value and Singapore's 4% to 32% of annual value. They're also comparable to or lower than China's 0.4% to 1.2% for residential properties and Bangladesh's varying rates of 0.3% to 4%. Pakistan's straightforward system based on property value, rather than rental income, potentially makes it more attractive for property ownership from a tax perspective, though overall property costs involve other factors beyond just property tax.

Capital Gains Tax: Pakistan's capital gains tax on property, set at 15% for filers and 45% for non-filers, presents a mixed picture when compared to other countries in the region. This rate is higher than Singapore's 0% for properties held for at least 3 years and Hong Kong's non-applicable status for individuals. It's also more complex than China's flat 20% rate. However, it's potentially more favorable than India's system, which uses income tax slab rates for short-term gains and 20% or 12.5% for long-term gains. The UAE's lack of federal capital gains tax for individuals makes it more attractive in this aspect. Malaysia's recent introduction of a 10% rate for residents is lower than Pakistan's rate for filers. Overall, Pakistan's capital gains tax structure, particularly for non-filers, could be seen as less competitive compared to some regional counterparts, potentially impacting its attractiveness for property investment.

Stamp Duty: Pakistan's stamp duty on property transactions, ranging from 2% to 5% of property value or circle rate (whichever is higher), is generally competitive within the region. This rate is lower than India's 3% to 8% and comparable to Singapore's tiered system of 3% to 4%. It's significantly higher than China's 0.05% for residential properties, but lower than Bangladesh's rates of 4.5% for larger apartments and 5% for land. The UAE's rates of 2% to 4% are similar to Pakistan's. Hong Kong's system, which varies based on property value and buyer status, can be higher for non-residents and corporate buyers. Malaysia's 1% to 4% range is comparable to Pakistan's. Overall, Pakistan's stamp duty rates fall within the mid-range for the region, making them neither a strong deterrent nor a significant advantage for property transactions compared to most neighboring countries.

Registration Fee: Pakistan's registration fee for property transactions, ranging from 0.25% to 1% of property value depending on the province, presents a mixed picture when compared to other countries in the region. This fee structure puts Pakistan at a disadvantage compared to China and Singapore, where no registration fees are applicable. However, it remains competitive with India's 1% of the total value of the Sale Deed plus a small fixed charge, and Bangladesh's flat 1% of property value. Pakistan's rates are generally higher than Hong Kong's 0.03% to 0.06%, but potentially lower than Malaysia's 1% of property value or RM 100, whichever is greater. The absence of registration fees in China and Singapore could make these markets more attractive for property transactions from this specific cost perspective, potentially putting Pakistan at a slight disadvantage in regional property investment competitiveness.

Capital Value Tax (CVT): Pakistan's Capital Value Tax (CVT) of 2% on property value is unique in the region, as other major South and Southeast Asian economies do not impose a similar tax. This additional cost on property transactions could put Pakistan at a competitive disadvantage in attracting real estate investment. The CVT, combined with other property-related taxes and fees, increases the overall expense of property dealings in Pakistan. This distinctive tax burden may make Pakistan's real estate market less attractive compared to neighboring countries, potentially impacting its position in the regional property investment market.

Pakistan's property taxation system presents a mixed picture compared to its regional counterparts. While it offers competitive property tax rates, its capital gains tax structure is less favorable, especially for non-filers. Stamp duty and registration fees are generally mid-range, but the unique Capital Value Tax adds an extra burden. Overall, Pakistan's multi-layered property taxation may reduce its attractiveness for real estate investment compared to some neighboring countries, despite having advantages in certain individual tax categories.

GLOBAL ANALYSIS ON REAL ESTATE TAXES

Tax Type	Pakistan	India	China	Singapore	Hong Kong	Bangladesh	UAE	Malaysia
Property Tax	0.15% to 0.75% of property value (depending on province and property type)	5% to 20% of annual rental value	0.4% to 1.2% of original value for residential properties	4% to 32% of annual value (based on estimated rental income)	15% (flat rate for individuals, subject to certain exemptions)	Varies by city corporation (0.5% to 4% of assessed value for city corporations, 0.3% for municipalities)	5% of annual rental value for residential, 10% for commercial (paid by tenant)	Varies by local authority, typically 4% of annual rental value, assessment tax on strata properties
Capital Gains Tax	15% for filer and 45% for non-filer.	Income tax slab rate (short-term), 20% with indexation or 12.5% without (long-term)	20% (flat rate)	0% for individuals (for properties held for at least 3 years)	Not applicable (rates apply to rental income instead)	15% (flat rate, but can be lower depending on the holding period and the individual's tax bracket)	No federal capital gains tax for individuals	10% on chargeable income for residents (effective from 1 January 2024)
Stamp Duty	2% to 5% of property value or circle rate (whichever is higher), depending on the province	3% to 8% of transaction value or circle rate (whichever is higher), varies by state	0.05% (for residential properties)	3% on the first S$180,000, 4% on the next S$180,000, and 4% on the remaining amount	Varies depending on property value and buyer's residency status (15% for non-permanent residents and corporate buyers, lower rates for first-time buyers and permanent residents)	4.5% (apartments over 1600 sq ft), 2% (apartments under 1600 sq ft), 5% (land)	4% of property value (Dubai), 2% (Abu Dhabi)	1% to 4% of property value (depending on value), 0.5% on loan agreement
Registration Fee	0.25% to 1% of property value, depending on the province	1% of the total value of Sale Deed + Rs. 100/- pasting charge.	NA	NA	0.03% for property transactions with value of $750,000 and 0.06% for those over $750,000.	1% of the property value.	Varies depending on the Emirate and property value	1% of property value or RM 100, whichever is greater
Capital Value Tax (CVT)	2% of property value	Not applicable	Not applicable	Not applicable	Not applicable	Not applicable	Not applicable	Not applicable

REAL ESTATE PRICES: A DEEP DIVE INTO EACH PROPERTY SEGMENT (2012-2024)

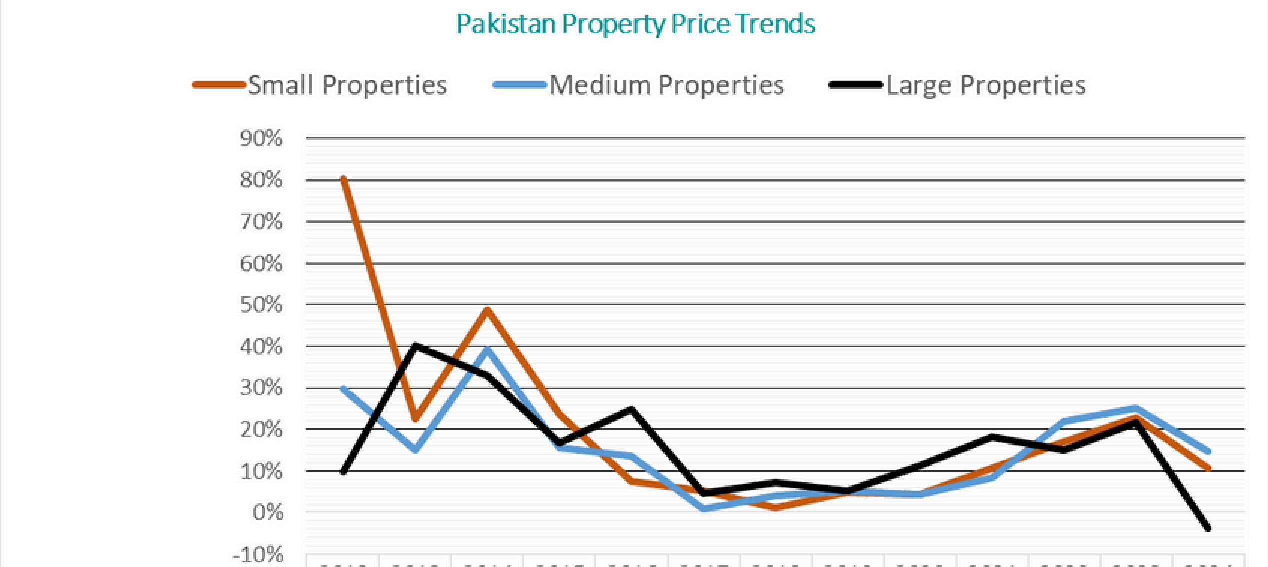
To understand the impact of these tax reforms, it's crucial to analyze the historical trends in Pakistan's real estate market across different property segments.

Small Properties (3 Marla - 5 Marla & 7 Marla): A dramatic 80% surge in 2012 was followed by significant fluctuations, with notable peaks in 2014 and 2023 at 49% and 23%, respectively. However, the market also experienced periods of minimal growth, including a dip to just 1% in 2017. Despite this volatility, the trend points to a resilient market for small properties, with consistent price increases in recent years, culminating in a projected 11% rise for 2024. The overall compound annual growth rate (CAGR) for the period from 2012 to 2024 is 17.79%, reflecting substantial average annual growth. A closer look reveals distinct phases: a high-growth period from 2012 to 2017 with a CAGR of 27.05%, followed by a more moderate growth phase from 2017 to 2024, with a CAGR of 9.05%. This analysis highlights the dynamic nature of Pakistan's small property market, marked by periods of rapid expansion and phases of consolidation.

Medium Properties (10 Marla - 15 Marla): The analysis for medium properties reveals a similar pattern of volatility, but with a notably lower overall CAGR of 11.55% compared to small properties. The period from 2012 to 2017 saw a CAGR of 17.38%, indicating robust growth, while the subsequent period from 2017 to 2024 experienced a significant slowdown with a CAGR of only 5.91%. This suggests that while the market for medium properties has also seen appreciation, it has been less dynamic and more susceptible to market fluctuations compared to the small property segment.

Large Properties (1 Kanal - 2 Kanal): The market for large properties has displayed significant volatility over the past decade. After experiencing robust growth from 2012 to 2016, with rates peaking at 40% in 2013, the market saw a sharp decline in 2017-2019, with growth rates dropping to single digits. A recovery phase began in 2020, with growth steadily increasing to 22% by 2023, indicating renewed demand for luxury properties. However, 2024 marked a sudden reversal, with the market contracting by 4%. This pattern reflects the influence of affluent buyers and overseas investors, while also highlighting the segment's susceptibility to economic fluctuations and market corrections.

PAKISTAN'S PROPERTY PRICE TRENDS

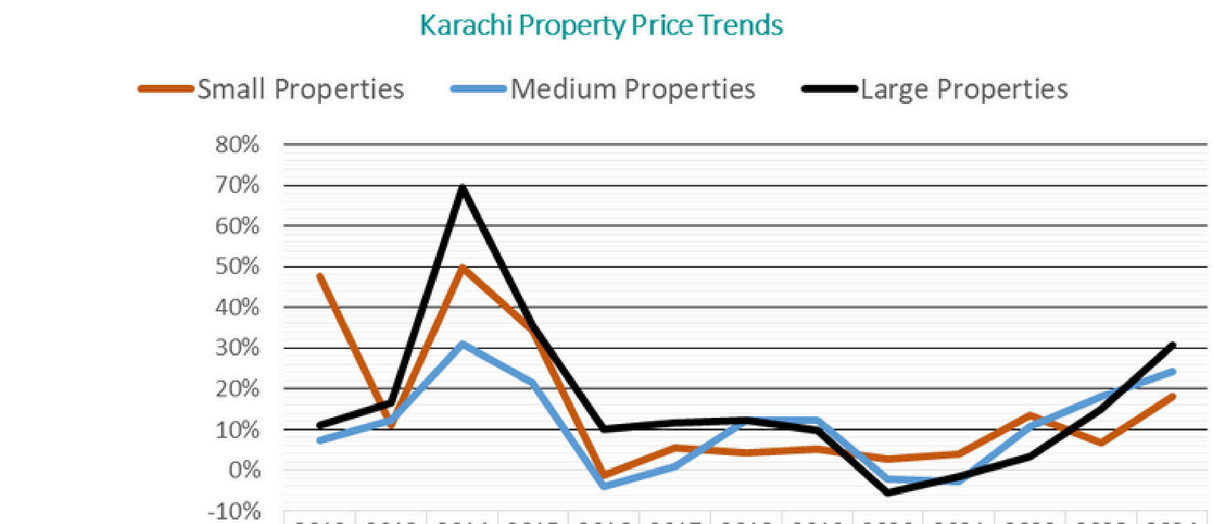


	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Small Properties	80%	23%	49%	24%	7%	5%	1%	5%	4%	11%	17%	23%	11%
Medium Properties	30%	15%	39%	16%	14%	1%	4%	5%	4%	8%	22%	25%	15%
Large Properties	10%	40%	33%	17%	25%	5%	7%	5%	11%	18%	15%	22%	-4%

Source: HBFC Research, Zameen.com

City-Specific Analyses: To provide a more granular view of the market, trends in four major cities—Karachi, Lahore, Islamabad, and Rawalpindi—were analyzed.

KARACHI REAL ESTATE TRENDS



	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Small Properties	48%	11%	50%	34%	-1%	5%	4%	5%	3%	4%	14%	7%	18%
Medium Properties	7%	12%	31%	22%	-4%	1%	12%	12%	-2%	-3%	11%	18%	24%
Large Properties	11%	17%	69%	36%	10%	12%	12%	10%	-6%	-2%	3%	15%	31%

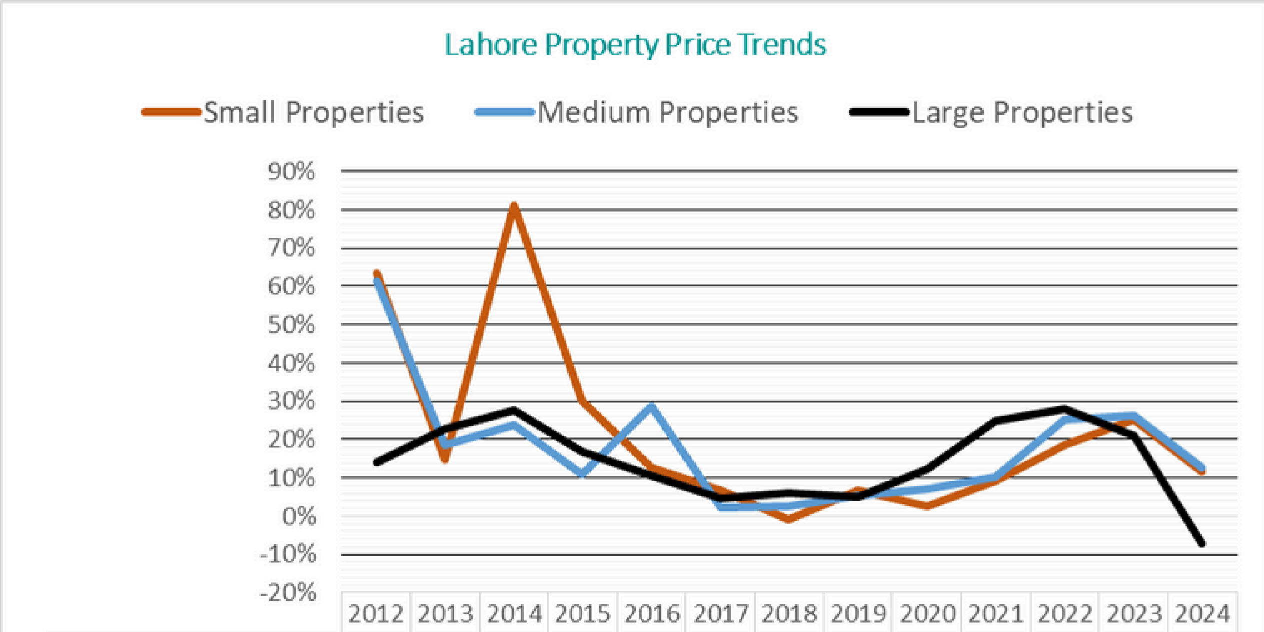
Source: HBFC Research, Zameen.com

Karachi Real Estate Market:

Small properties in Karachi experienced explosive growth from 2012 to 2014, peaking at 50% in 2014. After a brief decline in 2016, the market saw moderate but steady growth, with a resurgence in 2021-2022, showing growth rates of 4% and 14%, respectively, and accelerating to 18% growth in 2024. Medium properties have followed a more volatile trajectory, with contractions in 2016 and 2020, but recent recovery led to 24% growth in 2024.

Large properties in Karachi showed mixed performance with periods of high growth and contractions, peaking at 69% growth in 2014, with steady growth of 11% in 2012, 15% in 2023, and an acceleration to 31% in 2024.

LAHORE REAL ESTATE TRENDS



	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Small Properties	64%	15%	81%	30%	12%	7%	-1%	7%	3%	9%	19%	25%	12%
Medium Properties	61%	18%	24%	11%	28%	2%	3%	5%	7%	10%	25%	26%	13%
Large Properties	14%	23%	28%	17%	10%	5%	6%	5%	12%	25%	28%	21%	-7%

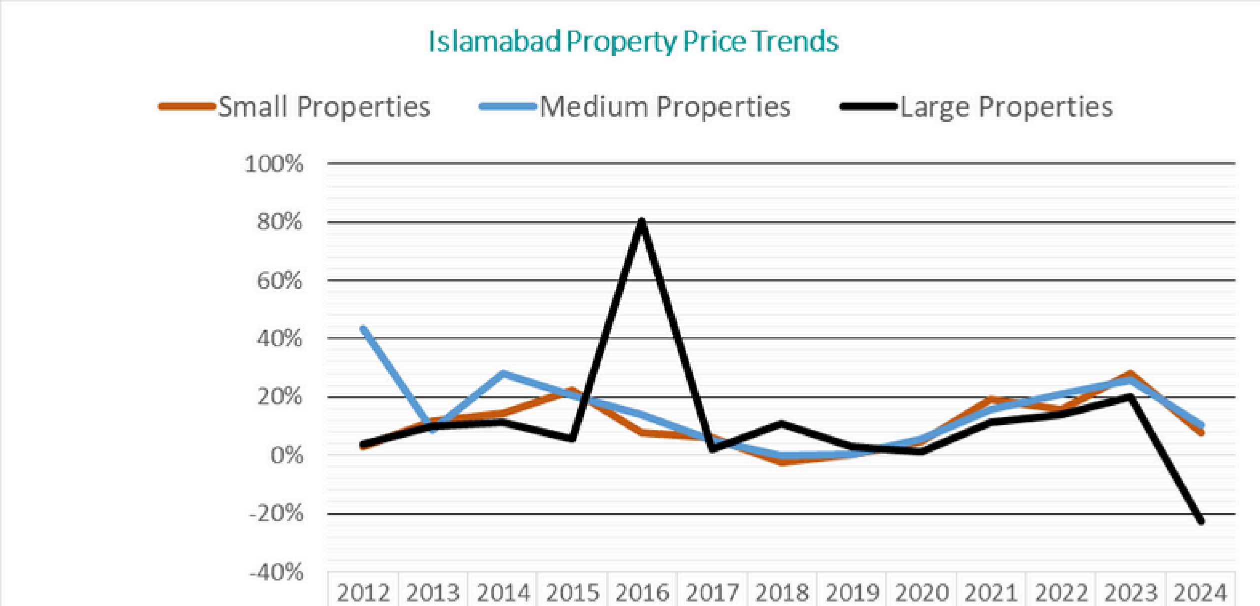
Source: HBFC Research, Zameen.com

Lahore Real Estate Market:

Lahore's property market showed varied performance across segments from 2012 to 2024. Small properties experienced high volatility, peaking at 81% growth in 2014 and maintaining double-digit growth in recent years, ending at 12% in 2024. Medium properties demonstrated more consistent growth, with notable peaks of 61% in 2012 and 28% in 2016, stabilizing at 13% in 2024.

Large properties saw significant fluctuations, reaching highs of 28% in 2014 and 2022, but unexpectedly declined by 7% in 2024. This contrasting performance in 2024, with continued growth in small and medium segments but a downturn in large properties, suggests a shift in Lahore's real estate dynamics, possibly reflecting changing investor preferences or economic factors affecting the luxury market.

ISLAMABAD REAL ESTATE TRENDS



	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Small Properties	3%	12%	14%	22%	8%	6%	-2%	0%	5%	19%	16%	28%	8%
Medium Properties	44%	9%	28%	21%	14%	5%	0%	0%	5%	16%	21%	26%	11%
Large Properties	4%	10%	11%	5%	81%	2%	11%	3%	1%	11%	14%	20%	-23%

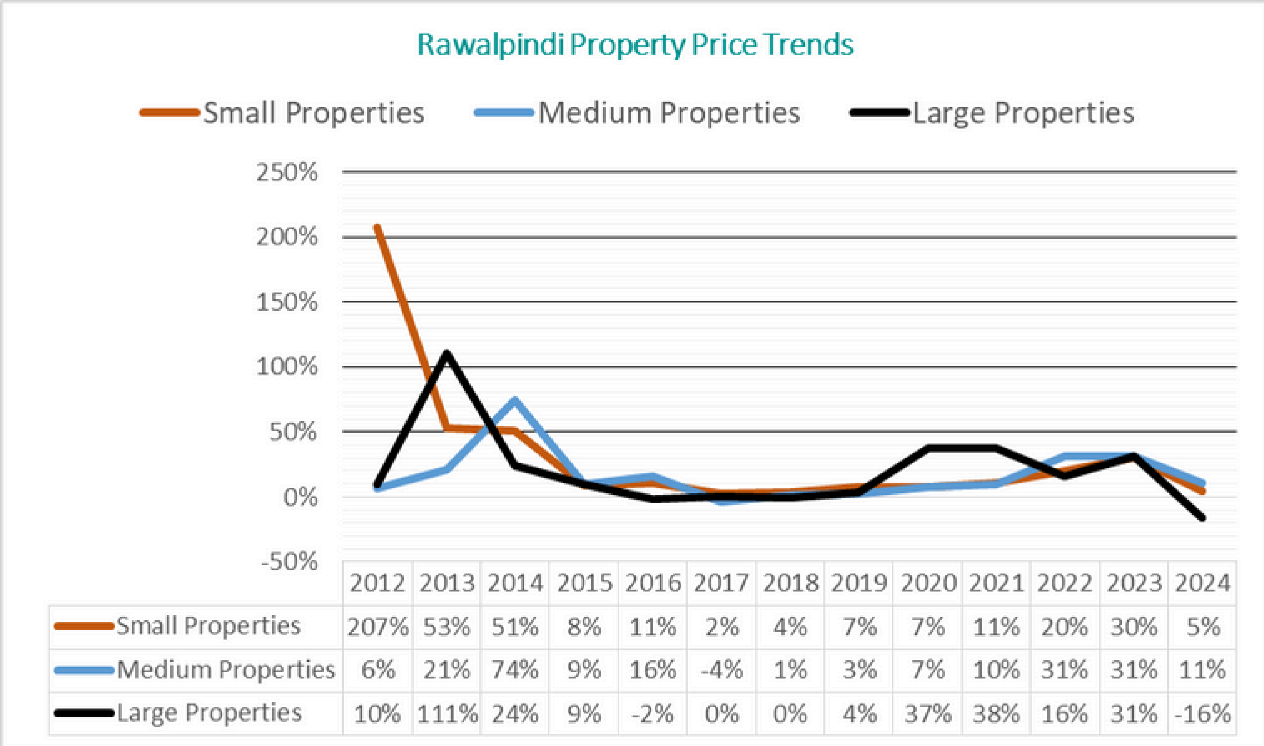
Source: HBFC Research, Zameen.com

Islamabad Real Estate Market:

The market for small properties in Islamabad has fluctuated from 2012 to 2016, with significant growth in 2013 (12%) and 2015 (22%). However, the market faced a notable dip in 2017 and 2018, followed by a strong rebound in 2021 with 19% growth, continuing to 28% in 2023, and moderating to 8% growth in 2024. Islamabad's medium property market fluctuated significantly from 2012 to 2024, starting with 44% growth, declining to 0% in 2018-2019, then recovering.

The market peaked again at 26% growth in 2023 before moderating to 11% in 2024, indicating cyclical trends. Large properties in Islamabad have had mixed results, with significant fluctuations, including an impressive 81% growth in 2016, followed by sharp declines and a negative growth of 23% in 2024, indicating significant market challenges.

RAWALPINDI REAL ESTATE TRENDS



	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024
Small Properties	207%	53%	51%	8%	11%	2%	4%	7%	7%	11%	20%	30%	5%
Medium Properties	6%	21%	74%	9%	16%	-4%	1%	3%	7%	10%	31%	31%	11%
Large Properties	10%	111%	24%	9%	-2%	0%	0%	4%	37%	38%	16%	31%	-16%

Source: HBFC Research, Zameen.com

Rawalpindi Real Estate Market:

Small properties in Rawalpindi experienced a remarkable surge of 207% in 2012, followed by 53% growth in 2013. This was followed by more moderate growth from 2014 to 2019, with fluctuations between 2% and 11% annually. In 2024, a modest 5% growth indicated stable demand. Medium properties in Rawalpindi have followed a gradual and steady growth trajectory, gaining momentum in 2014 with a 74% increase.

Consistent growth has been observed in recent years, with a 31% increase in both 2022 and 2023, and 11% growth in 2024, suggesting increasing demand for medium-sized homes. Rawalpindi's large property market experienced extreme volatility from 2012 to 2024. After a modest 10% growth in 2012, it surged dramatically to 111% in 2013, followed by 24% in 2014. The market then cooled, facing slight contraction and stagnation from 2016 to 2018.

A strong recovery began in 2020 with 37% growth, maintaining momentum through 2023. However, 2024 saw a sharp reversal with a 16% decline, highlighting the market's unpredictable nature.

DOMESTIC TRENDS, ECONOMIC SHIFTS, AND INVESTMENT ENVIRONMENT

The real estate market in Pakistan has also been heavily impacted by recent economic challenges. High inflation rates, which averaged around 24% in FY24, have eroded purchasing power, particularly affecting demand in the mid to high-end property segments. Historically, Currency devaluation, with the Pakistani Rupee depreciating against major currencies, has made real estate an increasingly attractive option for overseas Pakistanis and foreign investors, potentially driving up prices in specific segments. However, this year rupee remains largely unchanged against other currencies which also impacted real estate prices. Moreover, the State Bank of Pakistan's policy rate increase to 22% in 2023 amid higher inflation has made mortgages more expensive, potentially slowing down market activity. Economic uncertainty has also contributed to cautious investor sentiment, with many adopting a 'wait-and-see' approach before making significant investments.

Pakistan's real estate market stands at a crossroads, with recent tax reforms poised to significantly reshape the sector. While challenges exist, particularly in terms of short-term market adjustments and economic headwinds, there are also substantial opportunities. The focus on affordable housing, sustainable development, and increased transparency could drive long-term growth and attract both domestic and foreign investment.

The market shows varied dynamics across different property segments and cities, with small and medium properties generally demonstrating more resilience and consistent growth. The new tax structure, while introducing some higher rates, also offers unique advantages that could stimulate certain market segments.

As the market adapts to these changes, stakeholders must stay informed and agile. Policymakers should remain responsive to market feedback, potentially fine-tuning policies to achieve the right balance between revenue generation and market stimulation. Investors and developers, meanwhile, should closely monitor market trends and align their strategies with the evolving regulatory environment.

Looking ahead, Pakistan's real estate sector has the potential to play a pivotal role in the country's economic development. By addressing challenges and capitalizing on emerging opportunities, the sector can contribute significantly to urban development, housing accessibility, and overall economic growth. Moving ahead, monetary easing across globe including Pakistan and persistent decline in the inflation rates may boost real estate activities in coming years.

DATA SOURCES & METHODOLOGY

- Zameen.com, State Bank of Pakistan, Reuters, gov.hk, iras.gov, revenue.delhi.gov, taxsummaries.pwc.com, Housing.com, bdo.global, bankbazaar, creationbc.

Methodology

- Property price data, sourced from zameen.com, was analyzed for various cities across Pakistan. Due to the differing frequencies of data availability per city, return calculations for small, medium, and large properties were based on the segments where data existed for all three categories. To better understand real estate segmentation and demand in Pakistan, properties are divided into three categories:

1. **Small Properties:** These typically range from 3 to 7 marla in size and cater to individuals or small families with budget constraints or those seeking starter homes.
2. **Medium Properties:** Ranging from 10 to 15 marla, these properties are suitable for growing families or those seeking more space and amenities than smaller properties offer.
3. **Large Properties:** Spanning from 1 to 2 kanal, these properties cater to affluent individuals or large families who desire spacious homes with luxurious amenities and ample outdoor space.

This segmentation provides insights into the diverse needs and preferences of property buyers in Pakistan, enabling a more targeted analysis of market trends and demands across different property segments.

GLOSSARY OF TERMS

- ***Circle Rate:*** The minimum value at which a property is registered, usually set by the government.
- ***LEED Certification:*** Leadership in Energy and Environmental Design, a widely used green building rating system.
- ***Real Estate Investment Trust (REIT):*** A company that owns, operates, or finances income-generating real estate.

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