



# Brokerage Firms

## Sector Study

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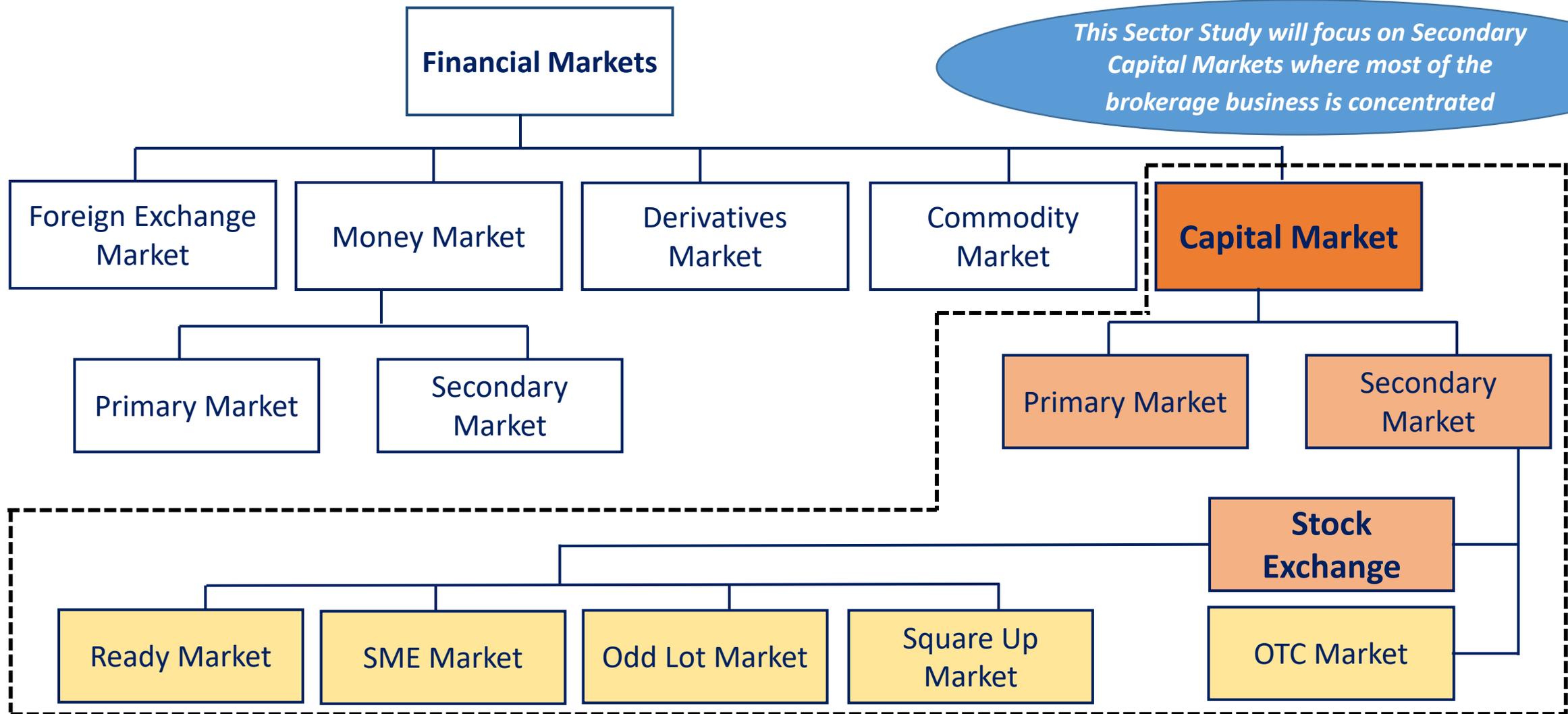


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# Brokerage Firms | Introduction

## Types of Financial Markets





## Capital Markets: An Overview

- Capital markets are a broad category of markets facilitating the buying and selling of financial instruments. In particular, there are two categories of financial instruments in which markets are involved. These are equity securities, which are often known as stocks/shares, and debt securities, which are often known as bonds. Capital markets involve the issuing of stocks and bonds for medium-term and long-term durations, generally terms of one year or more.
- Other than the distinction between equity and debt, capital markets are also generally divided into two categories of markets, the first of which being primary markets. In primary markets, stocks and bonds are issued directly from companies to investors, businesses and other institutions, often through underwriting.
- The capital market structure in Pakistan consists of an apex regulator of the markets, the Securities and Exchange Commission Pakistan (SECP), Pakistan Stock Exchange (emerged as a result of merging three stock exchanges), Mercantile Exchanges, Central Depository Company (CDC) and a Clearing and Settlement Company. The structure further includes intermediaries or market participants such as **brokers** which handle the transaction of shares in the capital markets on behalf of investors.
- The level of capital market development is an important determinant of level of savings, efficiency of investment and ultimately rate of economic growth.
- This Sector Study shall be focused on the Secondary Capital Markets, and KSE-100 shall be used as the benchmark Index for analysis purpose.

- **Equity**

- **Ready Market**: In this market segment, stocks of all companies listed are traded. Transactions are settled in two days (T+2).
- **Small & Medium Enterprise Market**: Shares of companies with post-issue paid-up capital between PKR25mIn and PKR200mIn are traded. Target investors for this segment include Qualified Institutional Buyers (QIBs) and High Net Worth Individuals (HNWI).
- **Odd lot Market**: In this market segment, investors can trade in securities in lots which are less than normal/regular lots (500 shares). The minimum number of shares that can be traded is 1. Settlement takes place in T+2 days.
- **Square Up Market**: In this market segment, if a Clearing Member (CM) fails to deliver sold securities, then the failed deliveries are squared up in the Square-up Market.
- **Real Estate Investment Trust (REIT)**: REIT is a fund based trust that owns income-producing real estate, buys real estate, develops, manage/ operates and sells real estate assets. REITs are modelled after mutual funds where all taxable income is paid out as dividends to shareholders.
- **Negotiated Deals**: Here negotiated deals are conducted outside the Exchange Trading Systems and are reported through the interface provided by the Exchange. These transactions are conducted between brokers.

- **Fixed Income**

- **Corporate Debt Instruments**: These include Term Finance Certificates (TFCs), SUKUK Certificates, Registered Bonds, Corporate Bonds etc., and all kinds of debt instruments issued by any Pakistani company or corporation registered in Pakistan.
- **Government Debt Instruments**: These are debt instruments issued by the Government of Pakistan. These include PIBs, Treasury Bills, National Savings Bonds, and Islamic Ijarah Sukuks.

## PSX Products

- **Derivatives**
  - **Deliverable Futures Contract (DFC)**: DFCs are forward contracts to buy or sell a certain underlying instrument with actual delivery of the said instrument occurring. The minimum lot for purchasing these shares is 500 shares. Settlement takes place 30 days after the contract is purchased.
  - **Single Stock Cash Settled Futures (CSF)**: Single Cash Settled Futures are standardized contracts to buy/sell single stock futures to be settled in cash, where the result of the trade is the cash difference between the buying and selling price. Settlement occurs purely on cash basis. Settlement can occur 30, 60, & 90 days after the contract is purchased.
  - **Stock Index Futures Contract (SIFC)**: SIFC is an agreement to buy or sell a standardized value of a stock index (basket of shares) on a future date at a specified price. SIFC gives opportunity to investors to trade in entire stock market by buying index futures instead of buying individual securities with the efficiency of mutual funds. Currently 90 days SIFCs are available at PSX.
- **Exchange Traded Funds (ETFs)**: ETF is a pooled investment vehicle with units that can be bought or sold on the Stock Exchange at a market-determined price. Similar to mutual funds units, ETF owns the underlying assets (stocks or bonds) and offers investors a proportionate share in a pool of stocks, bonds, and other assets. ETFs are new to Pakistan and were first introduced in March 2020. There are currently four ETFs available to investors on the PSX.
- **Margin Trading System (MTS)**: In MTS (Margin Trading System), an investor can buy MTS eligible securities having a part percentage of funds available of the total value of MTS eligible securities bought. An investor may buy a number of MTS eligible securities while having only a fixed percentage of funds available. The remaining amount is financed or leveraged by the Brokerage firm.

# Brokerage Firms | Global Stock Exchanges

## Overview

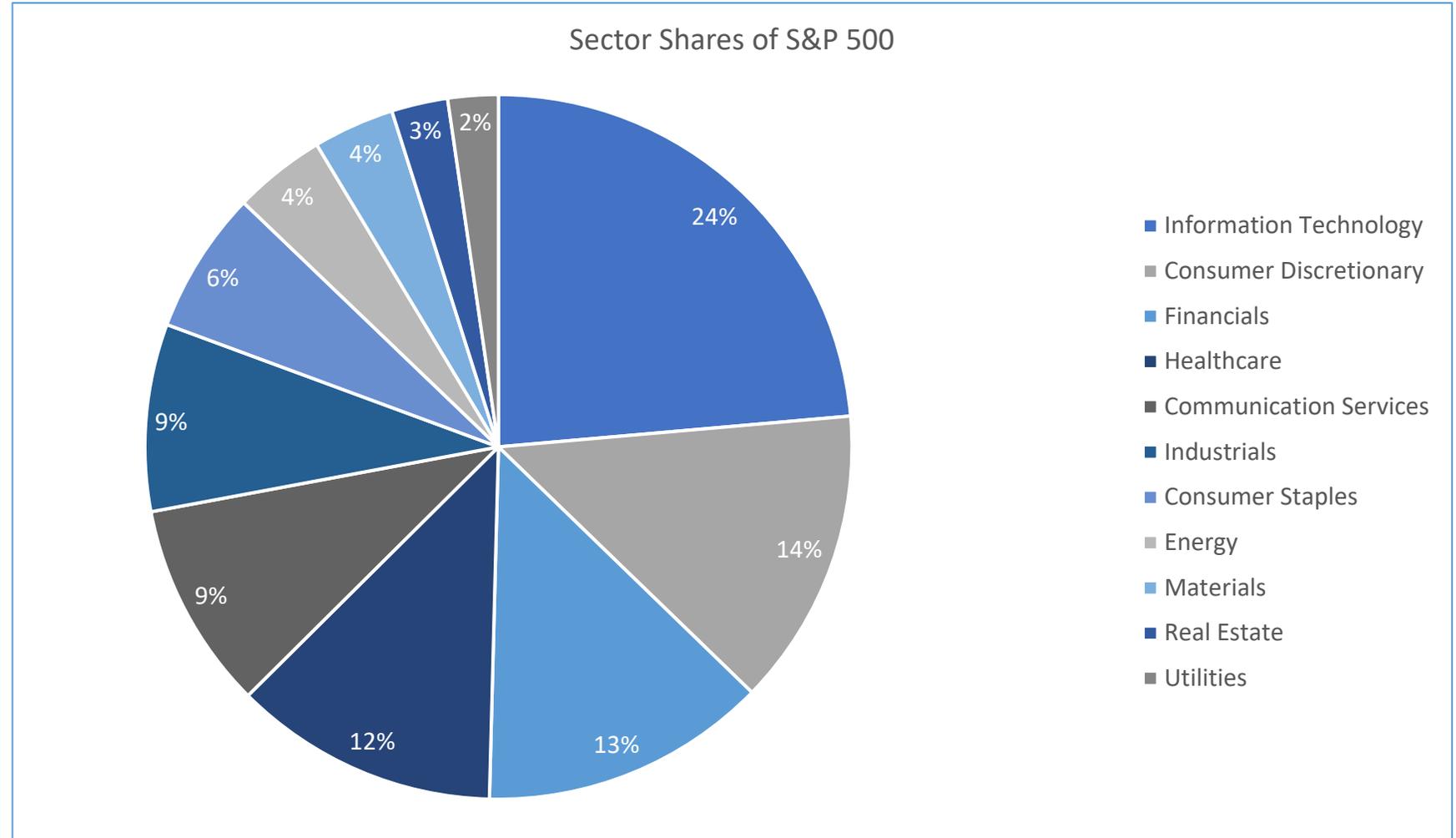
- The table shows some of the largest stock exchanges in the world in terms of market capitalization along with their recent performance. The top 10 exchanges combined represent approximately ~80.0% of total global market capitalization.
- During Dec-21, most of the major indices experienced positive returns. The highest return was earned by the Euro Stoxx 50 Index of ~5.8%
- Moreover, CY21 was also a period of positive return for most indices as major economies recovered from the COVID-19 pandemic. The highest return during CY21 was earned by the Tadawul All Share Index of the Saudi Stock Exchange, ~28.8%.

Stock Exchange	Market Capitalization	Index	1 Month Performance (Dec-21)	12 Month Performance (Jan-21 to Dec-21)
	(USD Trn) [Oct-21]			
New York Stock Exchange	28.2	S&P 500	4.4%	26.9%
Nasdaq	24.1	Nasdaq	0.7%	21.5%
Shanghai Stock Exchange	7.8	Shanghai Composite	2.1%	5.9%
Euronext	7.4	Euro Stoxx 50	5.8%	21.0%
Tokyo Stock Exchange	6.7	Nikkei 225	3.5%	4.9%
Hong Kong Exchange	5.8	Hang Seng	-0.3%	-14.1%
Shenzhen Stock Exchange	5.8	SZSE Component	0.4%	2.7%
London Stock Exchange	3.8	FTSE 100	4.6%	14.3%
Bombay Stock Exchange	3.5	SENSEX	2.1%	22.0%
National Stock Exchange of India	3.4	NIFTY 50	2.2%	24.1%
Saudi Stock Exchange	2.8	Tadawul All Share	4.8%	28.8%
Pakistan Stock Exchange	0.1	KSE 100	-1.1%	1.9%

# Brokerage Firms | Global Stock Exchanges

## S&P 500 | Sectoral Composition

- The S&P 500 index is dominated by the information technology sector which occupies ~24% of the total market.
- This is due to the presence of companies such as Apple, Microsoft and Amazon, whose individual market capitalizations have crossed the trillion dollar mark.





## Regional Comparison | INDIA

- The Securities and Exchange Board of India (SEBI) is the regulatory body which oversees brokerages in the country. The Securities and Exchange Board of India (Stock Brokers and Sub-Brokers) Regulations, 1992 is the legislation which regulates the brokerage industry.
- The regulation defines 3 categories of brokers, trading members, self-clearing members and clearing members. These correspond with the categories introduced in Pakistan through the new broker regime.
- The regulation also defines a sub-broker as ‘any person not being a member of stock exchange who acts on behalf of a stock broker as an agent or otherwise for assisting the investors in buying, selling or dealing in securities through such stock brokers’.
- The base minimum capital requirement for stock brokers is INR 1mln, while for self-clearing members is INR 10mln and for trading plus clearing members the minimum capital requirement is INR 25mln.

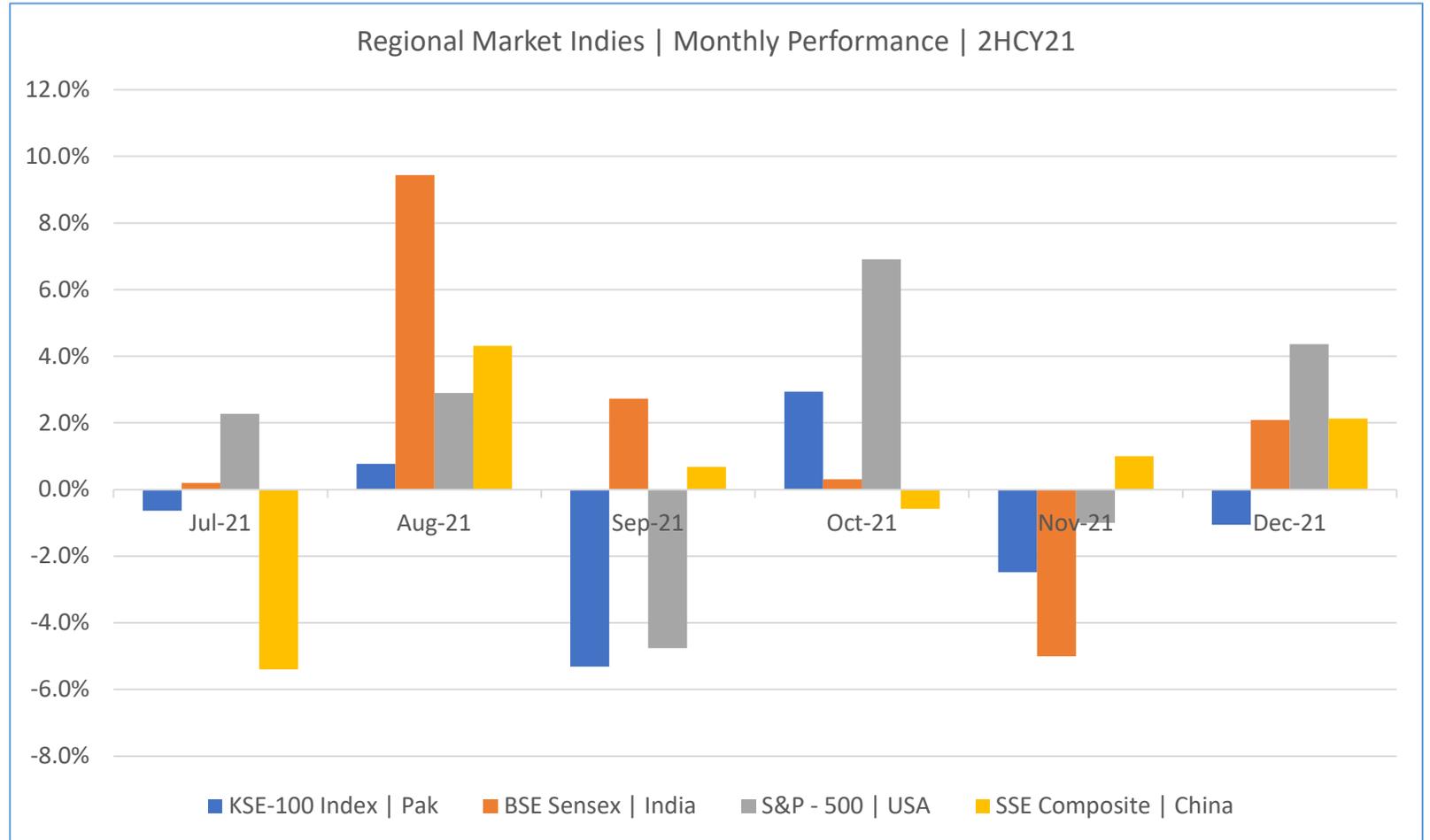




# Brokerage Firms | Global Indices

## Index Performance Comparison

- The performance of Global Stock Indices has remained volatile during CY21, with overall economic recovery witnessed in most economies. However, multiple waves of the pandemic along with COVID-19 variants continued to create uncertainty.
- During CY21, the S&P 500 Index had the highest overall return of ~26.9% with average monthly return of ~2.2%. The BSE Sensex Index observed a total return of ~22.0% during the same period.
- Meanwhile, the KSE-100 had an overall return of ~1.9% in CY21 and the SSE Composite had overall returns of ~5.9% during the period.



# Brokerage Firms | Global Equity Markets

## MSCI Classifications

- The adjacent table shows the MSCI categorization of various international equity markets into developed, emerging and frontier markets.
- Pakistan was recently downgraded from the Emerging Markets Index, where it occupied a weight of 0.02%, to the Frontier Markets Index.
- Three Pakistani securities have been added to the Frontier Markets Index with a total weight of 1.25%
- The MSCI statement regarding downgrading said “Although the Pakistani equity market meets the requirements for market accessibility under the classification framework for emerging markets, it no longer meets the standards for size and liquidity.”

Developed Markets			Emerging Markets			Frontier Markets		
Americas	Europe & Middle East	Pacific	Americas	Europe, Middle East & Africa	Asia	Europe & CIS	Middle East & Africa	Asia
Canada United States	Austria Belgium Denmark Finland France Germany Ireland Israel Italy Netherlands Norway Portugal Spain Sweden Switzerland United Kingdom	Australia Hong Kong Japan New Zealand Singapore	Argentina Brazil Chile Colombia Mexico Peru	Czech Republic Egypt Greece Hungary Kuwait Poland Qatar Russia Saudi Arabia South Africa Turkey United Arab Emirates	China India Indonesia Korea Malaysia Philippines Taiwan Thailand	Croatia Estonia Iceland Lithuania Kazakhstan Romania Serbia Slovenia	Kenya Mauritius Morocco Nigeria Tunisia WAEMU* Bahrain Jordan Oman	Bangladesh Sri Lanka Vietnam Pakistan

# Brokerage Firms | Local Industry

## Overview

- A broker or brokerage firm acts as an intermediary by matching a customer’s buy order with a third party’s sell order or vice versa.
- Brokerage firms receive compensation through a commission or fees that is charged once the transaction has been successfully completed. This amount may be paid by the customer or the exchange.
- It is common for brokerage firms to offer a variety of other services to their customers which include money management, tax advice and financial consultation. They also provide up-to-date stock quotes, research regarding economic environment and market analysis.
- There are currently ~200 brokerage firms licensed by the Securities and Exchange Commission of Pakistan (SECP). Out of these ~23 brokerage firms have Entity Ratings while ~37 have Broker Management Ratings and ~17 have Broker Fiduciary Ratings.

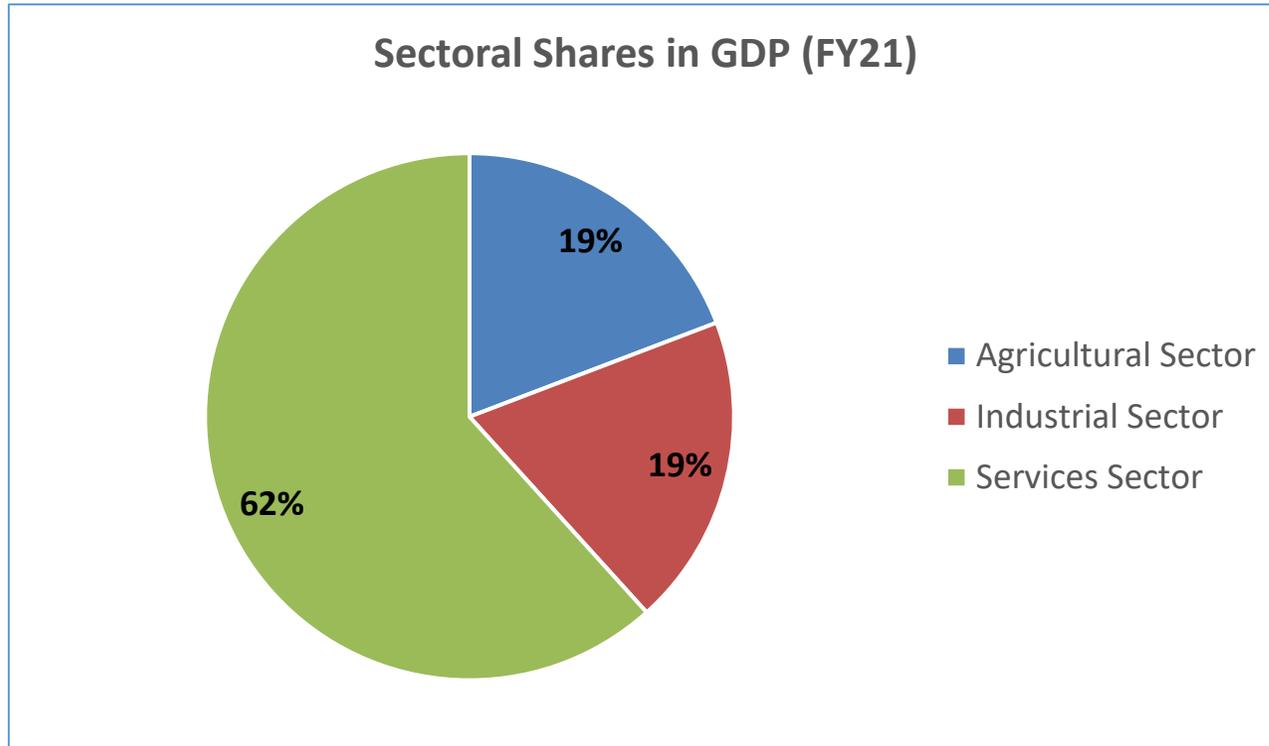
Sector Overview	FY19	FY20	FY21	6MFY22
KSE-100 Index (period end)	33,902	34,422	47,356	44,596
KSE-100 Return	-19.1%	1.5%	37.6%	-5.8%
KSE-100 Average Volumes (in millions)	96.8	135.9	246.9	127.7
No. of Brokerage Firms	~200 Brokerage Firms			



# Brokerage Firms | Local Industry

## GDP Break Up

- Pakistan’s real GDP grew by ~3.9% in FY21 and stood at PKR~13,036bln as compared to PKR~12,532bln in FY20.
- The top 5 sectors in terms of contribution to GDP are (i) Wholesale & Retail Trade, (ii) Transport, Storage & Communication, (iii) Other Private Services, (iv) Livestock, and (v) Large Scale Manufacturing.



FY21 Sector Wise GDP Break-Up (%)	
Crops	6.9
Livestock	11.5
Forestry	0.4
Fishing	0.4
<b>Total Agricultural Sector</b>	<b>19.2</b>
Mining and Quarrying	2.4
Large Scale Manufacturing	9.7
Small Scale Manufacturing	2.1
Slaughtering	0.9
Electricity Generation + Distribution & Gas Distribution	1.4
Construction	2.6
<b>Total Industrial Sector</b>	<b>19.1</b>
Wholesale & Retail Trade	18.8
Transport, Storage & Communication	12.2
Finance & Insurance	3.7
Housing Services	7.0
General Government Services	8.2
Other Private Services	11.8
<b>Total Services Sector</b>	<b>61.7</b>

## Macro Economic Indicators

	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	6MFY22
<b>Average Inflation Rate (CPI)</b>	11.9%	11.0%	7.4%	8.6%	4.5%	2.9%	4.2%	3.9%	7.3%	10.7%	8.9%	9.8%
<b>Average KIBOR</b>	13.5%	12.3%	9.8%	9.9%	8.9%	6.5%	6.1%	6.4%	10.4%	12.0%	7.4%	8.7%
<b>Monetary Policy Rate (MPR)</b>	13.7%	12.4%	9.9%	9.8%	8.8%	6.0%	5.8%	6.0%	9.7%	11.8%	7.0%	7.6%
<b>PKRV</b>	13.0%	11.9%	9.6%	9.8%	8.7%	6.3%	6.0%	6.3%	10.2%	11.8%	7.3%	8.6%
<b>Average Exchange Rate (PKR/USD)</b>	86.3	89.2	96.8	102.8	101.5	104.4	104.8	110.1	136.5	158.4	160.5	169.3
<b>(USD mln)</b>	<b>FY11</b>	<b>FY12</b>	<b>FY13</b>	<b>FY14</b>	<b>FY15</b>	<b>FY16</b>	<b>FY17</b>	<b>FY18</b>	<b>FY19</b>	<b>FY20</b>	<b>FY21</b>	<b>6MFY22</b>
<b>Current Account Balance</b>	214	-4,658	-2,496	-3,130	-2,815	-4,961	-12,270	-19,195	-13,434	-2,970	-1,852	-7,089*
<b>Exports</b>	25,369	24,718	24,802	25,078	24,090	21,972	22,003	24,768	24,257	22,536	25,630	15,070
<b>Imports</b>	35,796	40,370	40,157	41,668	41,357	41,118	48,001	55,671	51,869	43,645	53,785	37,498
<b>Trade Balance</b>	-10,427	-15,652	-15,355	-16,590	-17,267	-19,146	-25,998	-30,903	-27,612	-21,109	-28,155	-22,428
<b>Foreign Exchange Reserve</b>	18,244	15,289	11,020	14,141	18,699	23,099	21,403	16,384	14,482	18,886	24,398	24,019

\*

\* Current Account Balance is for 5MFY22

Source: SBP, MUFAP

# Brokerage Firms | Local Industry

## Macro Economic Indicators | Monthly

	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21	Jul-21	Aug-21	Sep-21	Oct-21	Nov-21	Dec-21
<b>Average Inflation Rate (CPI)</b>	5.7%	8.7%	9.1%	11.1%	10.9%	9.7%	8.4%	8.4%	9.0%	9.2%	11.5%	12.3%
<b>Average KIBOR</b>	7.4%	7.6%	7.8%	7.8%	7.7%	7.7%	7.6%	7.6%	7.8%	8.5%	9.4%	11.3%
<b>Monetary Policy Rate (MPR)</b>	7.0%	7.0%	7.0%	7.0%	7.0%	7.0%	7.0%	7.0%	7.3%	7.3%	7.8%	9.4%
<b>PKRV</b>	7.2%	7.4%	7.7%	7.6%	7.6%	7.5%	7.5%	7.4%	7.7%	8.4%	9.3%	11.1%
<b>Average Exchange Rate (PKR/USD)</b>	160.4	159.3	156.1	153.3	153.6	156.5	159.9	164.5	168.5	172.0	173.6	177.5
<b>(USD mln)</b>	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21	Jul-21	Aug-21	Sep-21	Oct-21	Nov-21	Dec-21
<b>Current Account Balance</b>	-210	-31	-33	-200	-650	-1,644	-814	-1,473	-1,134	-1,760	-1,908	
<b>Exports</b>	2,097	2,176	2,610	2,295	2,129	2,497	2,251	2,348	2,634	2,381	2,716	2,740
<b>Imports</b>	4,433	4,501	5,205	4,969	4,959	6,322	5,399	5,998	6,053	6,028	6,423	7,597
<b>Trade Balance</b>	-2,336	-2,325	-2,595	-2,674	-2,830	-3,825	-3,148	-3,650	-3,419	-3,647	-3,707	-4,857
<b>Foreign Exchange Reserve</b>	20,149	20,105	20,604	22,690	23,273	24,398	24,777	27,068	25,983	23,829	22,329	24,019

\* Current Account Balance for Dec-21 was not available

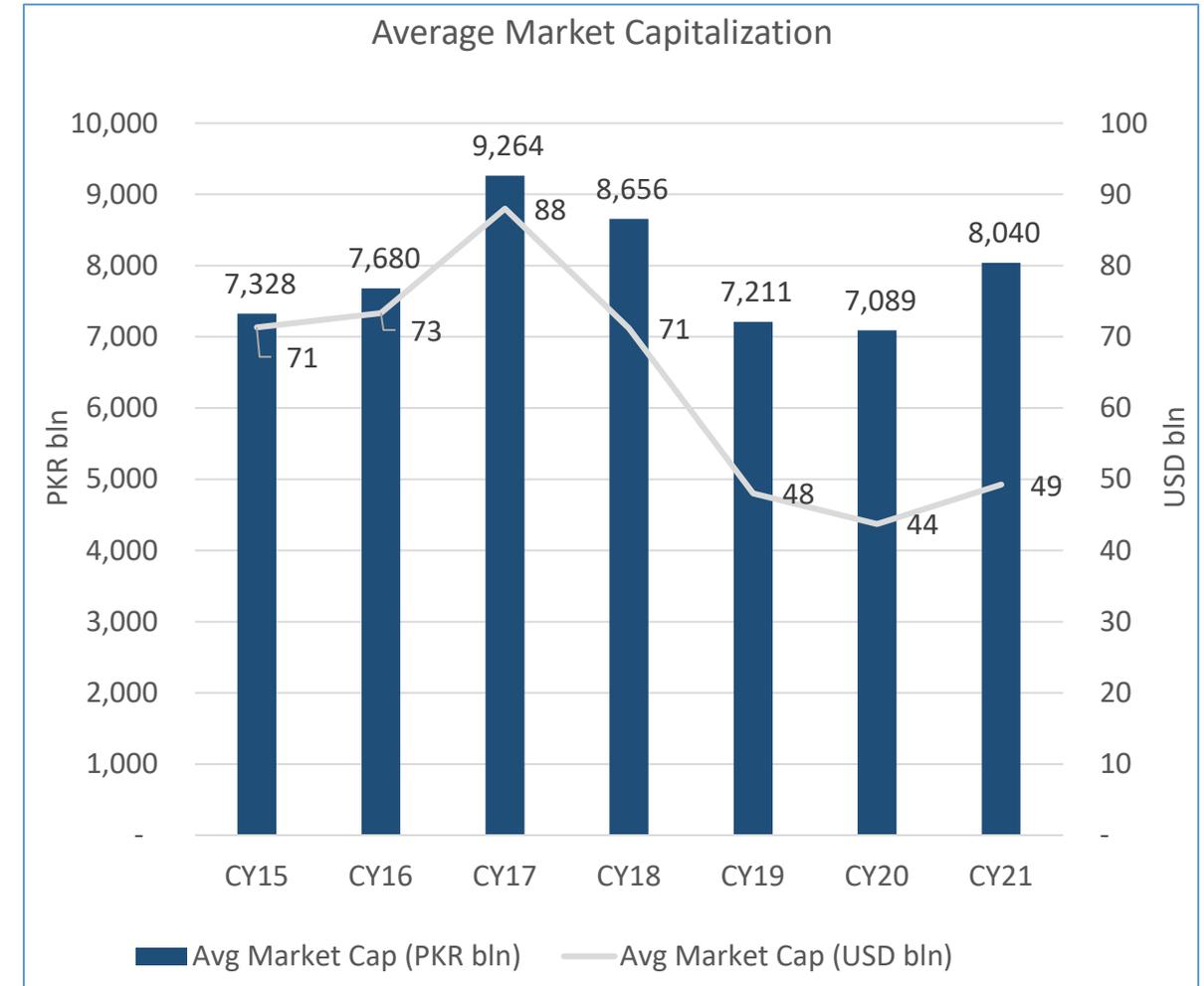
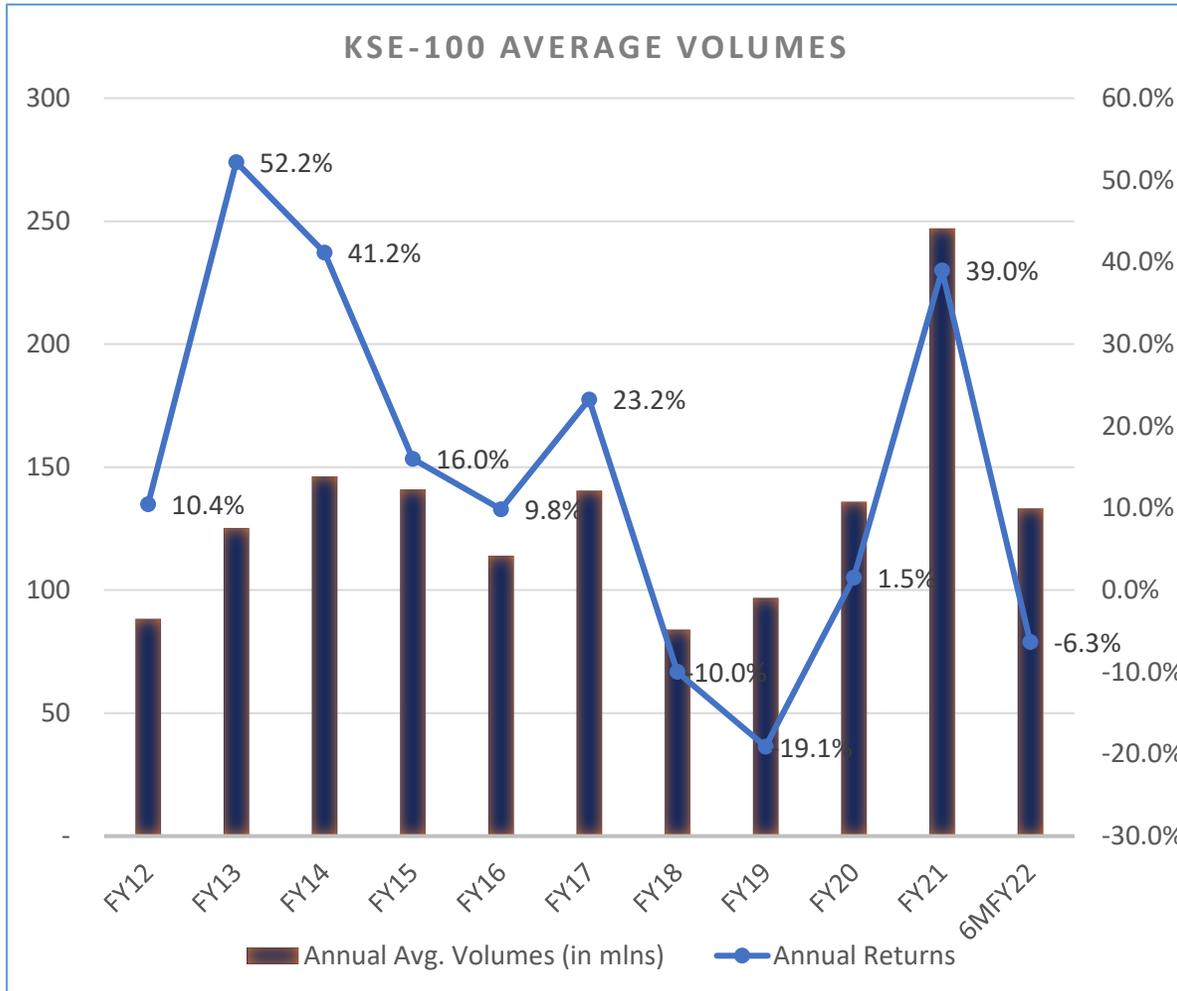
## KSE-100 Returns | Monthly & Annual

KSE 100 Index	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	6MFY22
Index Value	12,496	13,801	21,006	29,653	34,399	37,784	46,565	41,911	33,902	34,422	47,356	44,596
Returns (%)	29.0%	10.4%	52.2%	41.2%	16.0%	9.8%	23.2%	-10.0%	-19.1%	1.5%	37.6%	-5.8%

KSE 100 Index	CY11	CY12	CY13	CY14	CY15	CY16	CY17	CY18	CY19	CY20	CY21
Index Value	11,348	16,905	25,261	32,131	32,816	47,807	40,471	37,067	40,735	43,755	44,596
Returns (%)	-4.0%	49.0%	49.4%	27.2%	2.1%	45.7%	-15.3%	-8.4%	9.9%	7.4%	1.9%

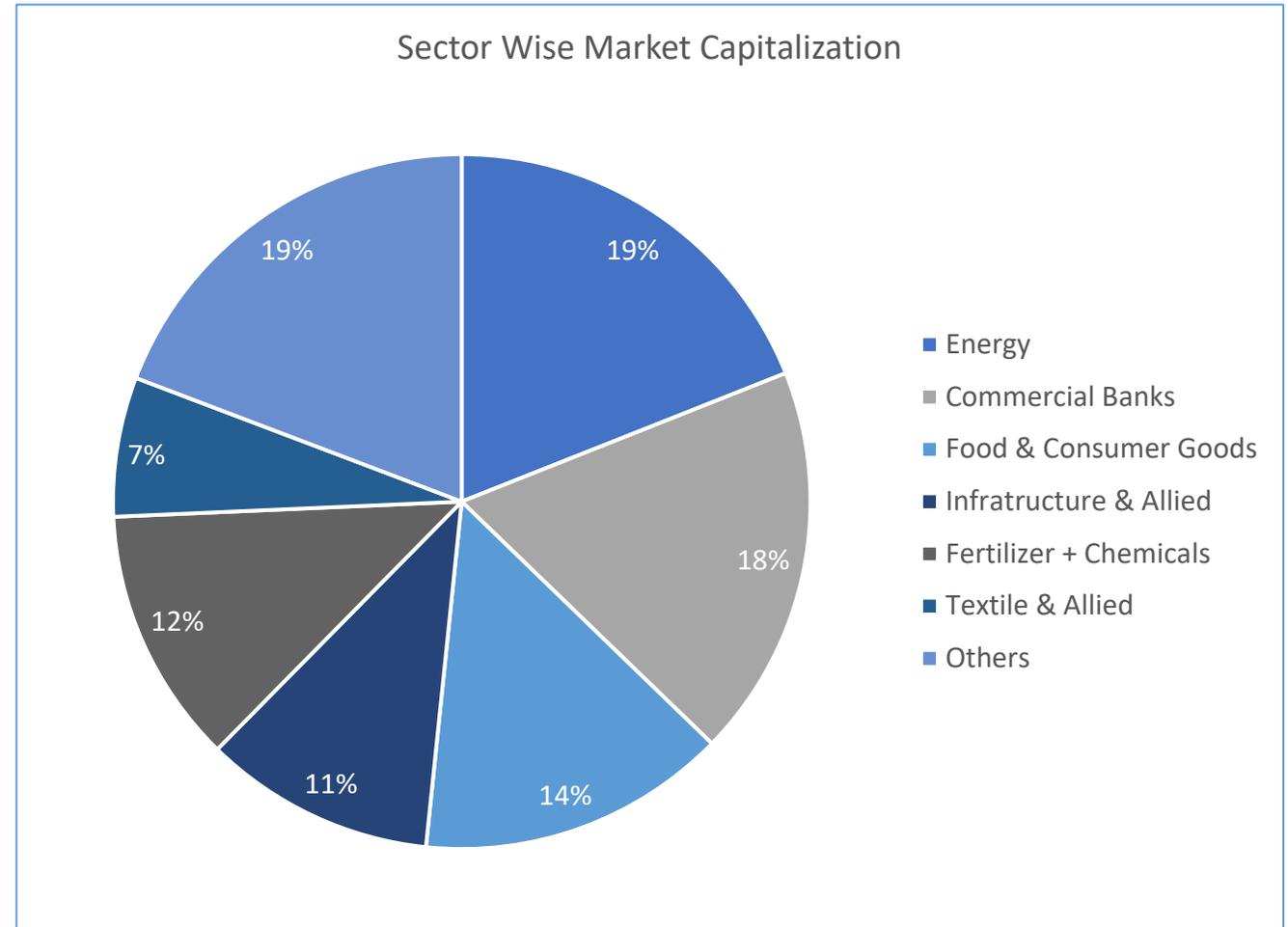
KSE 100 Index	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21	Jul-21	Aug-21	Sep-21	Oct-21	Nov-21	Dec-21
Index Value	46,386	45,865	44,588	44,262	47,896	47,356	47,055	47,420	44,900	46,219	45,072	44,596
Returns (%)	6.0%	-1.1%	-2.8%	-0.7%	8.2%	-1.1%	-0.6%	0.8%	-5.3%	2.9%	-2.5%	-1.1%

## MARKET VOLUMES & CAPITALIZATION



## Market Capitalization | Sectoral Composition

- This data is based on market capitalization of PKR~7.6trn as on 3<sup>rd</sup> Jan, 2022.
- Energy is the largest sector with a market capitalization of PKR~1,449bln amounting to ~19.0% of the total market capitalization. The energy sector comprises of Oil & Gas Exploration & Production, Oil & Gas Marketing, Power Generation & Distribution and Refineries.
- The second largest sector is Commercial Banks with a market capitalization of PKR~1,397bln which amounts to ~18.3% of the total market capitalization.



## Fee Income

- With effect from 14<sup>th</sup> Oct, 2019, PSX vide Notice No. PSX/N-1258 dated 9<sup>th</sup> October, 2019 issued a notification regarding implementation of standard range/scale of brokerage commission.
- According to the notice, the commission range of 3 paisa per share or 0.15% of the transaction value (whichever is higher) up to 2.5% of the transaction value is prescribed.
- The decision was taken in light of the fact that some brokerage houses were charging nominal or zero commission rates, which was adversely affecting market competitiveness and creating a disadvantage for market participants in the form of disparity in service standards.
- As the decision has ensured a minimum commission fee for the brokerage sector, many firms have gone into profits in the past year. The decision, however, faced some resistance from the market participants as they believed that it should be a free market based on the level of services provided and client comfort.
- In addition, during FY21 the higher volume of shares traded also boosted the firms' revenues. Average daily volumes of the KSE-100 index stood at ~247mln shares in FY21. However, this figure has fallen to ~126mln shares in 6MFY22.

Fee Income		
Month	Total Volumes (KSE-100)	Minimum Fee (3 paisa per share)
Jan-21	6,868,916,780	206,067,503
Feb-21	5,036,039,923	151,081,198
Mar-21	5,153,979,959	154,619,399
Apr-21	3,411,414,185	102,342,426
May-21	3,411,467,923	102,344,038
Jun-21	7,077,956,194	212,338,686
Jul-21	2,793,671,422	83,810,143
Aug-21	2,572,783,708	77,183,511
Sep-21	3,210,087,831	96,302,635
Oct-21	2,382,201,375	71,466,041
Nov-21	2,741,866,010	82,255,980
Dec-21	2,394,858,248	71,845,747

## NET BUY/SELL

Net Buy/Sell (PKR mln)						
Participants	FY17	FY18	FY19	FY20	FY21	6MFY22
Individuals	-5,526	580	20,796	34,001	53,276	12,164
Companies	13,354	10,853	14,553	4,245	22,142	10,421
Banks / DFIs	-19,648	-1,139	9,009	-8,516	-15,412	4,743
NBFC	-631	-907	-172	707	27	788
Mutual Funds	60,460	-3,550	-20,080	-7,792	1,761	-1,846
Other Organizations	2,043	8,547	3,423	4,973	6,889	7,200
Broker Proprietary Trading	-626	-4,852	-1,801	-2,105	-5,270	-1,987
Insurance Companies	23,142	22,817	17,887	20,179	-1,357	11,336
<b>LIPI NET</b>	<b>68,483</b>	<b>32,349</b>	<b>43,615</b>	<b>45,691</b>	<b>62,055</b>	<b>42,819</b>
Foreign Individuals	-513	256	61	-134	12	697
Foreign Corporates	-70,198	34,936	-44,540	-49,033	-60,141	-52,119
Overseas Pakistanis	2,241	2,351	865	3,477	-1,926	8,603
<b>FIPI NET</b>	<b>-68,483</b>	<b>32,349</b>	<b>-43,615</b>	<b>-45,691</b>	<b>-62,055</b>	<b>-42,819</b>

Net Buy/Sell (USD mln)						
Participants	FY17	FY18	FY19	FY20	FY21	6MFY22
Individuals	-53	5	166	213	332	72
Companies	127	100	111	27	138	60
Banks / DFIs	-187	-10	63	-55	-95	28
NBFC	-6	-8	-2	5	0	5
Mutual Funds	576	-35	-146	-50	10	-11
Other Organizations	-19	78	28	32	45	43
Broker Proprietary Trading	-6	-44	-15	-13	-32	-12
Insurance Companies	220	204	150	128	-10	66
<b>LIPI NET</b>	<b>652</b>	<b>289</b>	<b>356</b>	<b>285</b>	<b>387</b>	<b>250</b>
Foreign Individuals	-5	2	0	-1	0	4
Foreign Corporates	-669	-312	-362	-306	-375	-305
Overseas Pakistanis	21	21	6	22	-13	50
<b>FIPI NET</b>	<b>-652</b>	<b>-289</b>	<b>-356</b>	<b>-285</b>	<b>-387</b>	<b>-250</b>

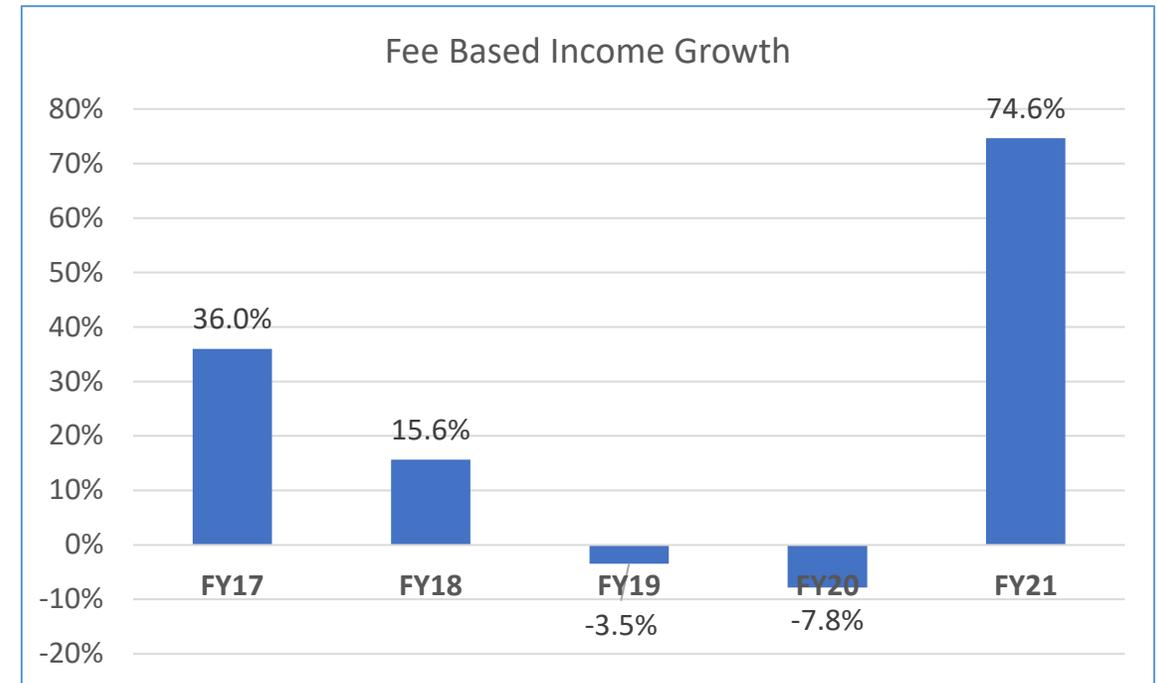


# Brokerage Firms | Local Industry

## Business Risk

- Business risk for brokerage firms arises from the possibility that a broker may experience lower than expected profits or may incur a loss. This would prevent the broker from providing investors and stakeholders with adequate returns.
- The stability and sustainability of income from core operations is key to minimizing this risk.
- The industry’s fee based income growth stood at ~74.6% in FY21 as compared to -7.8% in FY20. The growth in fee based income came on the back of recovery of the stock markets in the aftermath of the COVID-19 pandemic and relatively higher volumes traded during the period.
- Another positive indicator has been the fixation of minimum commission rate for brokerage services effective from 14<sup>th</sup> Oct, 2019. The industry’s profitability remained positive during previous two fiscal years after a period of loss incurred during FY19.

Industry Average	FY17	FY18	FY19	FY20	FY21
Fee Based Income Growth	36.0%	15.6%	-3.5%	-7.8%	74.6%



*Note: Industry Averages are based on 15 Listed/Rated firms*



# Brokerage Firms | Local Industry

## Financial Risk

- **Credit Risk:** It emanates from the inability of clients to pay for the securities purchased on their behalf. This can be minimized through appropriate procedures and controls regarding client acceptance and assessment of client credit worthiness.
- **Market Risk:** It arises primarily from adverse movements in investment values such as the change in stock price of an equity instrument. Investors can have different appetites for the level of market risk that they are willing to take on. Moreover, different instruments have different levels of risk associated with them.
- The industry's exposure to market risk can be evaluated through the equity instruments to total investments ratio. The greater share of equity indicates greater level of market risk. The industry's average ratio stood at ~53.4% in FY21 (FY20: ~56.1%).
- **Liquidity Risk:** It occurs due to insufficient funds to meet financial obligations when they become due. This can be minimized by maintaining sufficient liquid investments and having the ability to raise funds in a timely and cost-effective manner from external sources.
- The liquidity risk can be evaluated through liquid assets to trade related liabilities ratio. The industry has an average ratio of 188.0% in FY21 (FY20: 246.8%). A ratio above 100% indicates that the firm has enough liquidity to pay off liabilities that may arise in the short term.
- The final ratio is the capital adequacy ratio i.e., equity to total assets. The industry's average for this ratio clocked in at ~62.2% during FY21 (FY20: ~54.6%).

Industry Average	FY18	FY19	FY20	FY21
Equity Instrument/Investments	54.6%	50.6%	56.1%	53.4%
Liquid Assets/Trade Related Liabilities	249.7%	344.9%	246.8%	188.0%
Equity/Total Assets	60.5%	61.7%	54.6%	62.2%

## Regulatory Framework

- The primary regulatory body for brokers is the Securities and Exchange Commission of Pakistan. There are a comprehensive set of regulations that govern the activities of brokers. These include the Securities Brokers (Licensing and Operations) Regulations 2016, the SECP Act 1997, the Anti-Money Laundering Act 2010 as well as regulations of the Pakistan Stock Exchange (PSX), Central Depository Company (CDC) and National Clearing Company of Pakistan (NCCPL)
- The PSX prescribes a standard commission range of 3 paise per share or 0.15% of the transaction value (whichever is higher) up to 2.5% of the transaction value. The table shows the broker categories in the New Broker Regime introduced by the government in 2020. The brokers were required to apply for conversion to their applicable categories by July 2020.

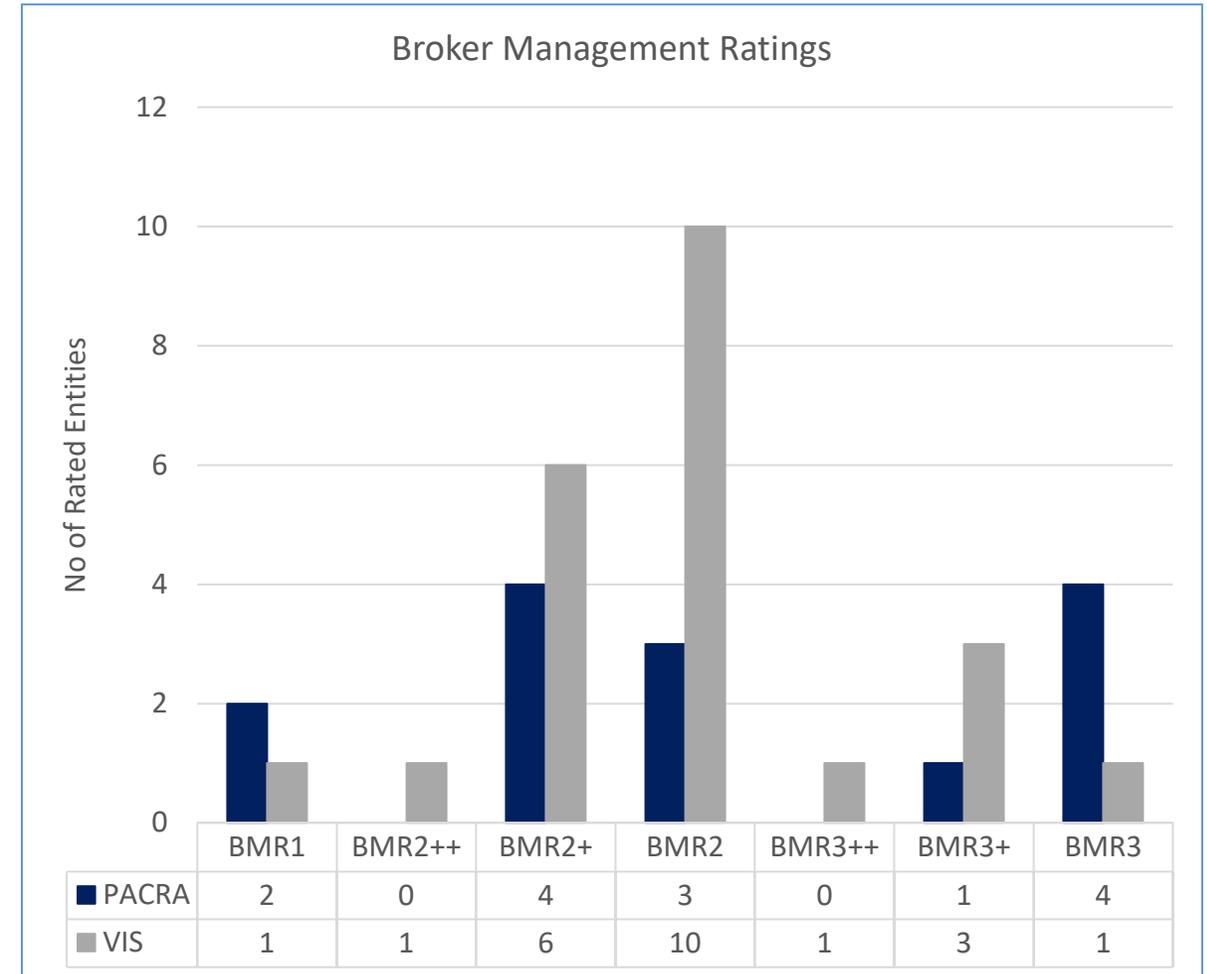
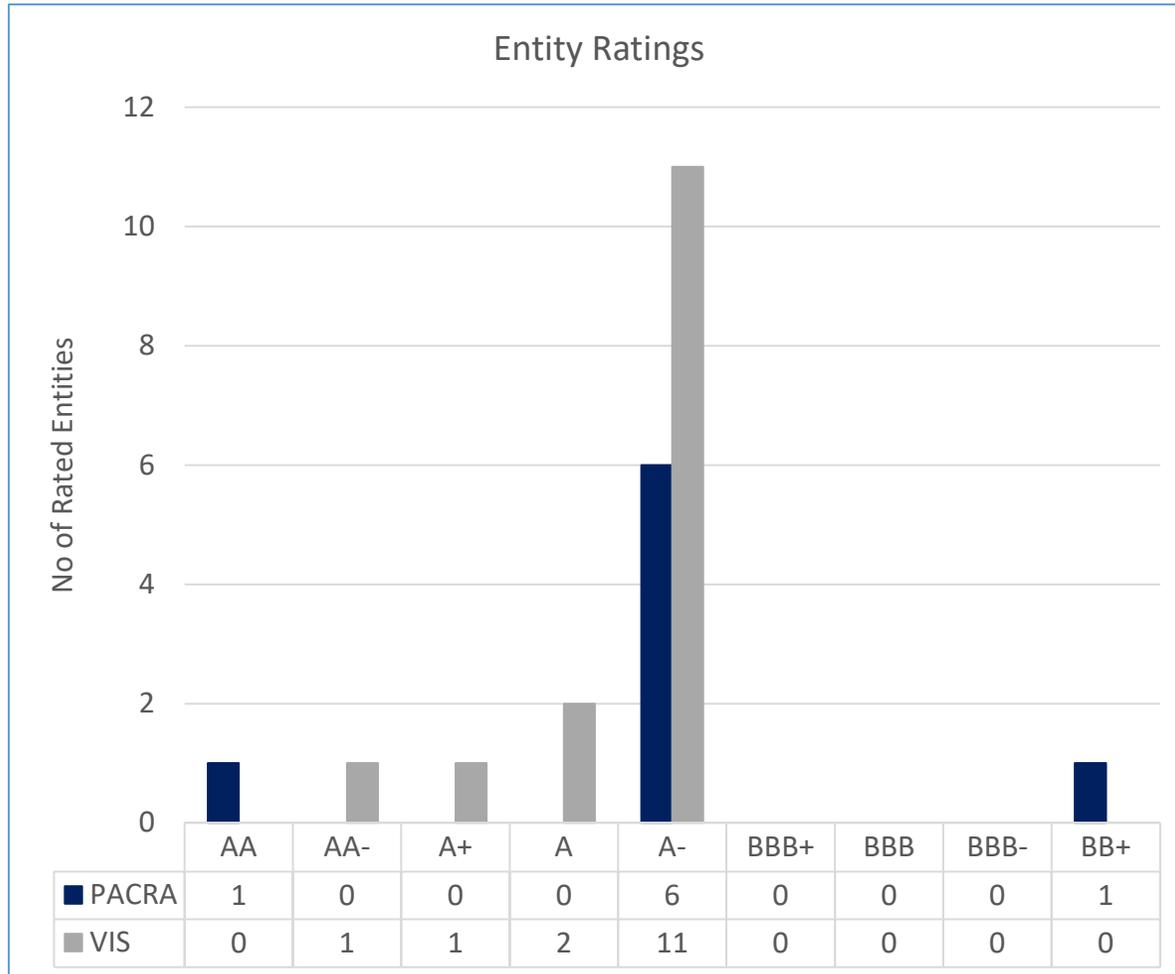
Categories	Trading Only	Trading and Self Clearing	Trading and Clearing
Description	The broker can only execute its proprietary trades and trades on behalf of its customers but cannot settle executed trades or keep custody of securities or money owned by it and its customers.	The broker can execute as well as settle its proprietary trades and trades executed on behalf of its customers and can keep custody of securities and money owned by it and its customers subject to such conditions as may be imposed by the Commission.	The broker can execute as well as settle its proprietary trades and trades executed on behalf of its customers and can keep custody of securities and cash owned by it and its customers subject to such conditions as imposed by the Commission and, in addition, such securities broker can settle trades of other securities brokers and their customers and keep custody of the securities and cash owned by such other securities brokers and their customers.
Minimum Net Worth	PKR 15mIn	PKR 50mIn	PKR 500mIn
Liquid Capital Requirement	PKR 5mIn	PKR 10mIn	PKR 50mIn
Minimum Net Capital Balance	Not Applicable	PKR 10mIn	PKR 15mIn
Assets Under Custody Limit	2 Times of Net Worth	25 Times of Net Worth	35 Times of Net Worth

## Regulatory Framework | Updates

- The government made certain amendments to the tax structure applicable for brokerage firms through the Annual Budget FY22.
  1. Individuals having turnover of PKR~100mln or more added to the classification of 'withholding agent/prescribed person' for the purpose of collecting tax under section 233 of the Income Tax Ordinance, 2001. Previously, the withholding agent classification included federal, provincial and local governments, companies and association of persons.
  2. In addition, sections 233A and 233AA were both withdrawn in the budget. Section 233A encompassed the collection of advance tax by the stock exchanges on purchase and sale of shares. Meanwhile, section 233AA encompassed the collection of advance tax by NCCPL from margin financiers, trading financiers and lenders in respect of margin financing.
- Recently, the Pakistan Stock Exchange (PSX) introduced a new trading and surveillance platform, called Designated Time Schedule (DTS), and increased the duration of daily shares trading by 30 minutes with effect from 25<sup>th</sup> October, 2021. PSX purchased the software for USD~2.85mln from the Shenzhen Stock Exchange (SZSE) in February 2020 and conducted test runs for 10 months.
- Despite this, the new system experienced technical glitches when it became operational, particularly in the Jade Trading Terminal (JTT). As a result of this, trading volume was significantly lowered in addition to which trading was suspended for a brief period due to technical issues. The PSX in response has reverted to the old system, Karachi Automated Trading System (KATS), as a temporary measure until the technical issues with the new system can be resolved.
- The Securities and Exchange Commission of Pakistan (SECP), recently introduced an amendment to the Securities Brokers (Licensing and Operations) Regulations, 2016. The amendment stipulates that the Minimum Net Worth requirement of Trading and Self Clearing members shall be increased to PKR 60mln with effect from 1<sup>st</sup> April, 2022 and further increased to PKR 75mln with effect from 1<sup>st</sup> April, 2023.

# Brokerage Firms | Local Industry

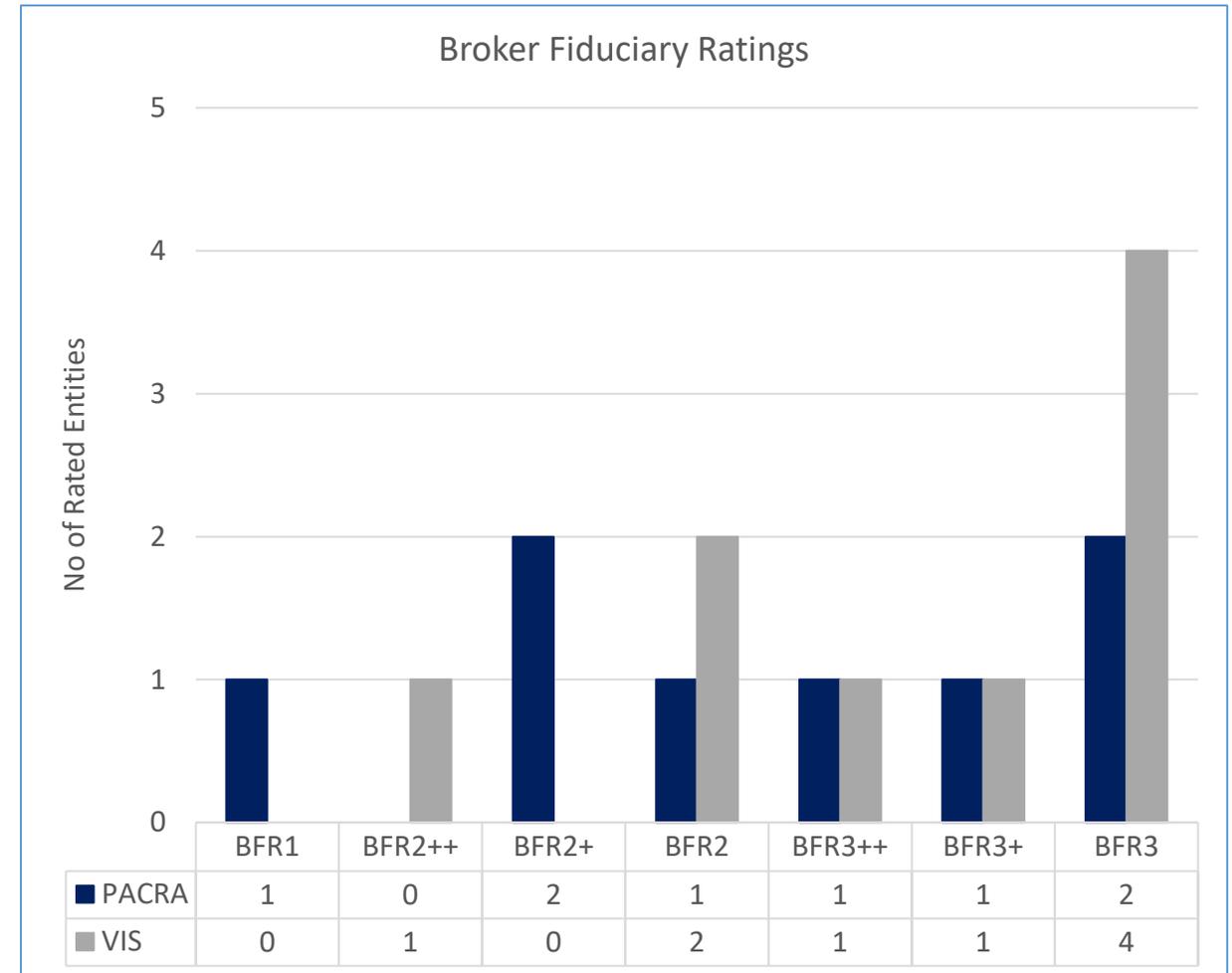
## Rating Scale



# Brokerage Firms | Local Industry

## Rating Scale

- PACRA provides Entity ratings to 8 brokerage firms with a long term rating bandwidth of BB+ to AA.
- In addition, PACRA provides Broker Management Ratings (BMR) ratings to 14 brokerage firms with a long term rating bandwidth of BMR3 to BMR1.
- Moreover, PACRA provides 8 Broker Fiduciary Ratings (BFR) with a long term rating bandwidth of BFR3 to BFR1.





# Brokerage Firms | Local Industry

## SWOT Analysis

- Strong regulatory oversight through SECP and PSX.
- Stock market experienced significant returns during FY21, boosting investor confidence

Strengths

Weaknesses

- Any kind of uncertainty, be it political, social or economic can have a negative impact on the stock market and in turn on the brokerage firms.
- Some of the regulatory requirements, e.g. minimum capital, may be difficult for small brokers to meet.

- Deteriorating economic indicators such as current account deficit, currency depreciation and rising inflation can create negative sentiment in the market.

Threats

Opportunities

- Introduction of new products, such as Exchange Traded Funds.
- The economy is in recovery phase which also bodes well for investors in the stock market as well as brokerage firms.

# Brokerage Firms | Outlook & Future Prospects

## Outlook: Stable

- Pakistan's post economic recovery is exhibited by the GDP growth of ~3.9% during FY21 (based on provisional figures). Among the contributors of GDP growth is industrial activity which has picked up in various sectors with the Large Scale Manufacturing Industries output increasing ~15% YoY during FY21. The sectors which have contributed to this growth are textiles, food & beverages, pharmaceuticals and chemicals. Food & Beverage sector holds a sizable portion of the Index market capitalization, therefore is a positive sign for the Sector.
- During FY21, the stock market has also gradually moved in a positive direction as the economic recovery picked up due to which investor confidence in the market also increased. KSE-100 Index returns for FY21 stood at ~38%, significantly higher than previous year's return of ~2%.
- However, during 6MFY22 various economic indicators exhibited a negative trend. The current account deficit crossed USD~7bln in Nov-21 as the trade deficit increased largely due to rising international commodity price. The inflation levels continue to be on a rising trend with CPI inflation clocking in at a significantly higher ~12.3% during Dec-21 as compared to 11.5% during Nov-21. In addition, the exchange rate has also depreciated ~12% since the start of current fiscal year.
- Moreover, the policy rate has also been increased in successive reviews and now stands at 9.75%, and while the Monetary Policy Committee (MPC) has indicated no further change in short term, the rate is expected to increase further in the medium to long term.
- All these factors combined, created negative sentiments in the market due to which KSE-100 returns for the 6MFY22 period stood at -6%. In addition, the KSE-100 experienced negative returns during Dec-21 of -1.1% due to deteriorating economic indicators as well as the emergence of a new COVID-19 variant.
- Looking ahead, the government has recently introduced the Mini-Budget for FY22 which includes the removal of GST exemptions for a large number of items. While this is designed to restrict imports, it will also likely cause further increase in inflation. Meanwhile, the Mini-Budget along with other prior actions were necessary to satisfy IMF conditions for the Extended Fund Facility (EFF). The sixth review of EFF and next tranche of USD 1bln is expected later this month.

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- BSE India

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