



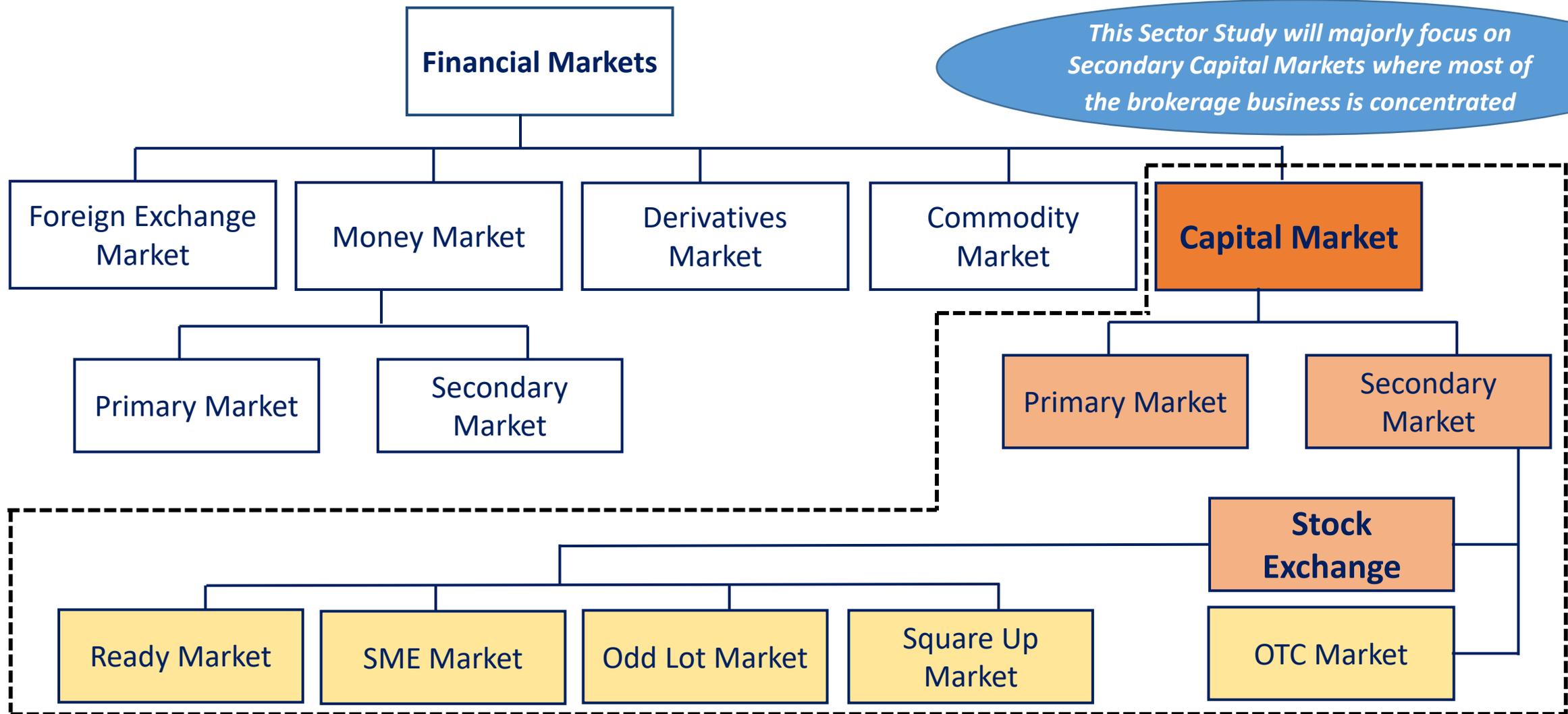
Brokerage Firms

Sector Study

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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, 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 were first introduced in March 2020. There are currently seven ETFs available to investors on the PSX (five conventional equity; one Islamic equity; and one conventional debt).
- **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.

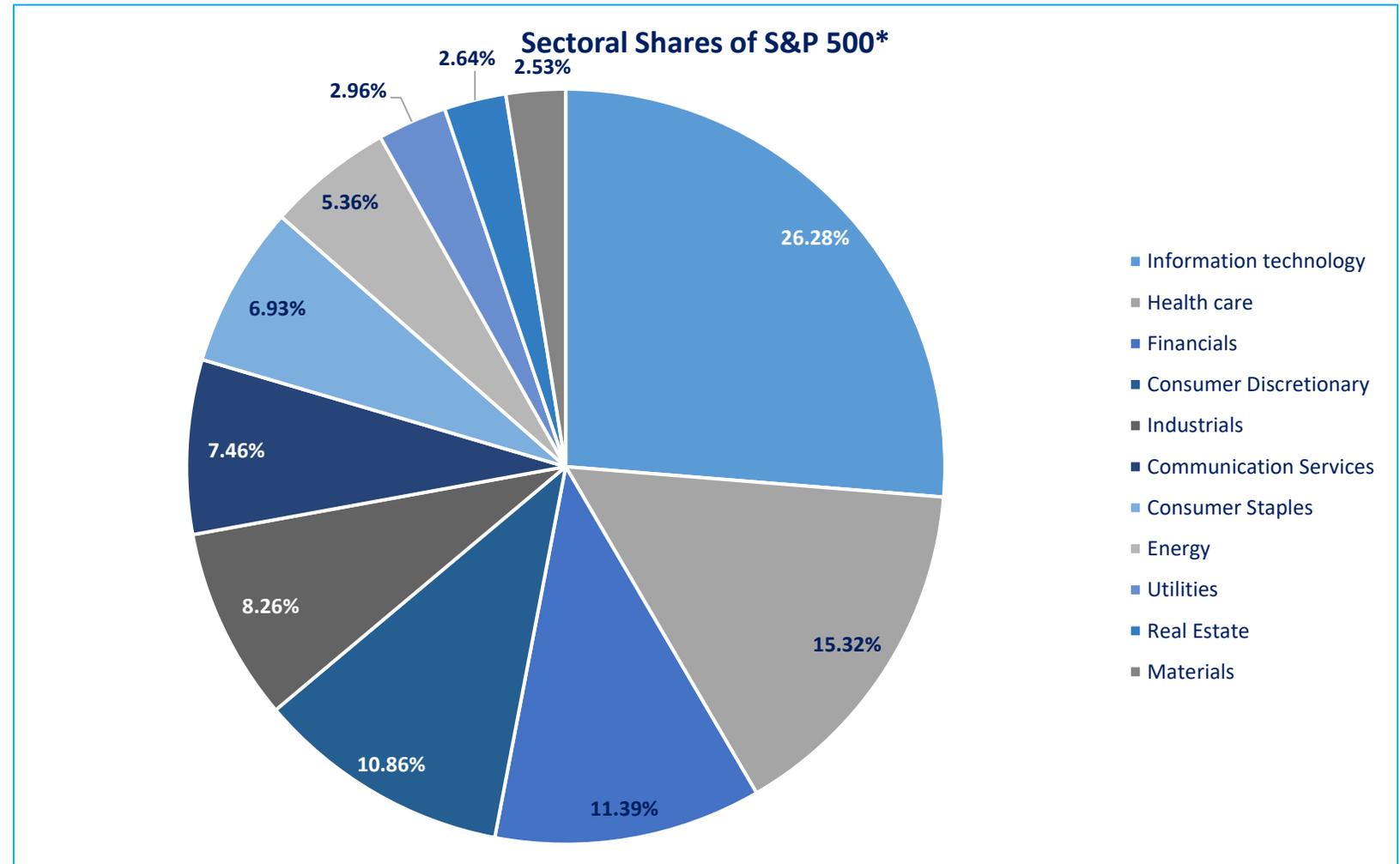
Overview

- The table shows the 10 largest stock exchanges in the world in terms of market capitalization along with their recent performance. The top 10 exchanges combined represent approximately ~80% of total global market capitalization.
- During Dec-22 the lowest returns were earned by the NASDAQ; NIKKEI 225; and S&P500: ~-9%; ~-8%; and ~-6%, respectively.
- Moreover, the lowest returns during CY22 were earned by the NASDAQ and SZSE Composite: ~-34% and ~-25%, respectively.

Stock Exchange	Market Capitalization (USD Trn) [Aug-21]	Index	1 Month Performance (Dec-22)	12 Month Performance (Jan-22 to Dec-22)
New York Stock Exchange	26.64	S&P 500	-6%	-20%
Nasdaq	23.46	Nasdaq	-9%	-34%
Shanghai Stock Exchange	7.63	Shanghai Composite	-3%	-14%
Euronext	7.33	Euro Stoxx 50	1%	-12%
Tokyo Stock Exchange	6.79	Nikkei 225	-8%	-12%
Hong Kong Exchange	6.02	Hang Seng	6%	-11%
Shenzhen Stock Exchange	5.74	SZSE Component	-2%	-25%
London Stock Exchange	3.83	FTSE 100	0%	1%
Bombay Stock Exchange	3.54	SENSEX	-3%	1%
National Stock Exchange of India	3.40	NIFTY 50	-4%	1%
Pakistan Stock Exchange	0.05	KSE 100	-5%	-9%

S&P 500 | Sectoral Composition

- The S&P 500 index is dominated by the information technology sector which occupies ~26% of the total market.
- This is due to the presence of companies such as Apple, Microsoft and Amazon, whose individual market capitalization nearly touch the five trillion dollar mark.



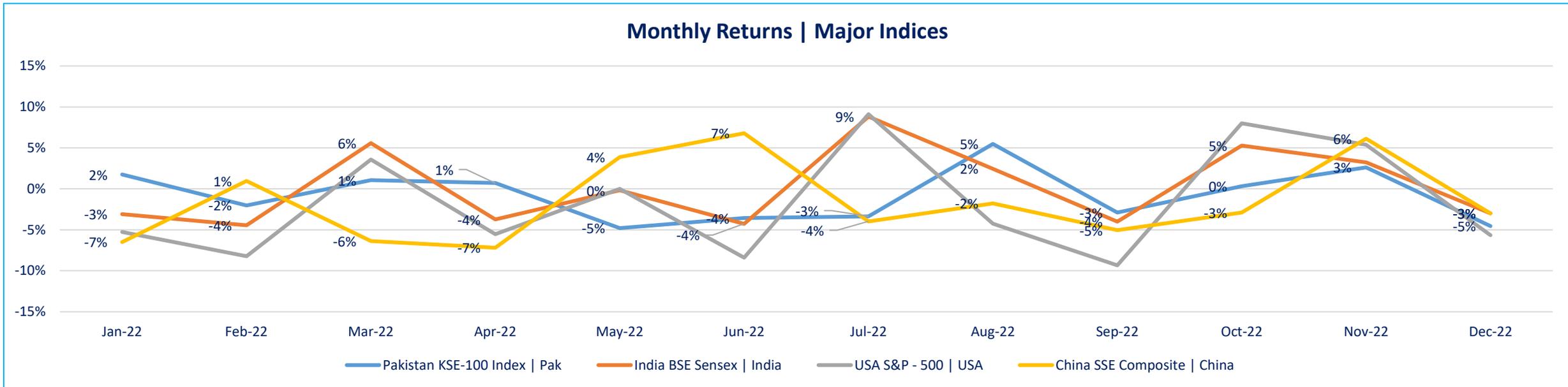
Regional Comparison | INDIA

- 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 1mIn, while for self-clearing members it is INR 10mIn and for trading plus clearing members the minimum capital requirement is INR 25mIn.



Brokerage Firms | Global Indices

Index Performance Comparison



- The performance of Global Stock Indices posted negative returns as a global recession, high inflation; interest rate hikes (particularly the US Fed rate); and the Russian-Ukraine conflict pushed downward pressure on traded stocks.
- During CY22, the US S&P500 had the lowest overall return of ~-20% with average monthly return of ~-2%. CY22 marks the worst year for the US since 2008 ending the US stock market's three-year winning streak. Sticky inflation and high interest rates reversed the market's positive position and weighed in on investor sentiment throughout the year.
- Meanwhile, the KSE-100 had an overall return of ~-9% in CY22 and the SSE Composite had overall returns of ~-14% during the period. China battled with Covid-19 cases and lockdowns for the greater part of CY22 which led to depressed market performance over the greater part of the year.
- Globally, initial public offerings and bond sales slumped during FY22.

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 downgraded from the Emerging Markets Index, where it occupied a weight of 0.02%, to the Frontier Markets Index, where it will reportedly have a weight of ~1.9%.
- 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 ~22 brokerage firms have Entity Ratings while ~31 have Broker Management Ratings and ~13 have Broker Fiduciary Ratings.

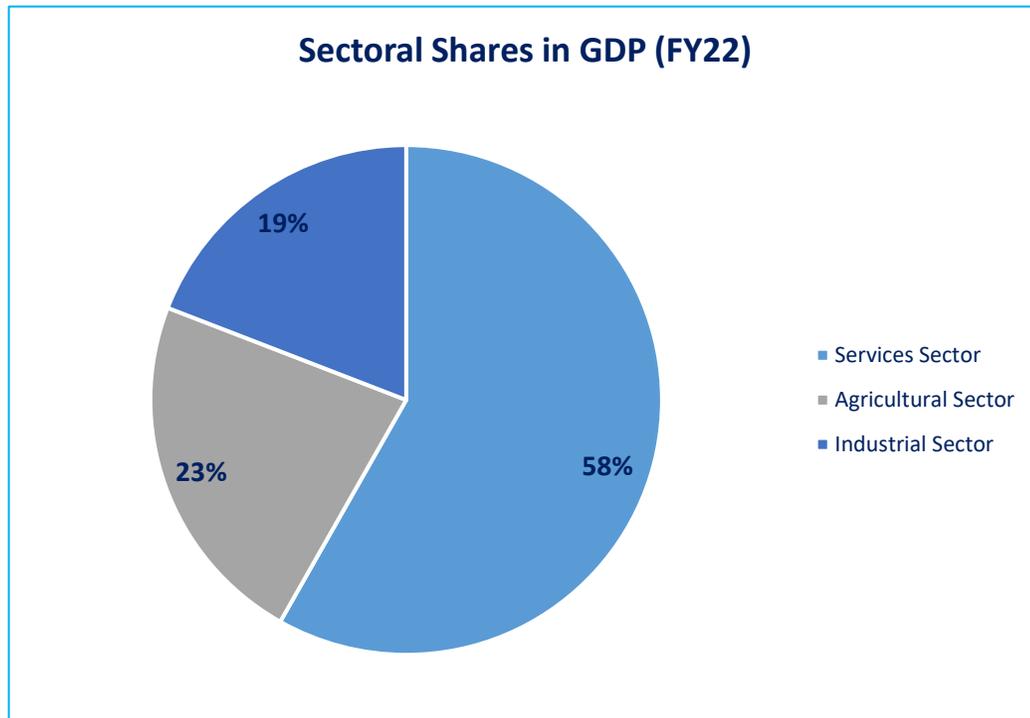
Sector Overview	FY20	FY21	FY22	6MFY23
KSE-100 Index (period end)	34,422	47,356	41,541	40,420
KSE-100 Return	2%	38%	-12%	-9%
KSE-100 Average Volumes (in millions)	135.87	246.96	115.84	94.62
No. of Brokerage Firms	~200 Brokerage Firms			



Brokerage Firms | Local Industry

GDP Break Up

- Pakistan’s real GDP grew by ~20% in nominal terms in FY22 and stood at PKR~66.9trln as compared to PKR~55.8trln in FY21.
- The top 5 sectors in terms of contribution to GDP are (i) Wholesale & Retail Trade; (ii) Transport, Storage & Communication; (iii) Livestock; (iv) Large Scale Manufacturing; and (v) Other Private Services.



FY22 Sector Wise GDP Break-Up (%)	
Crops	7.84
Livestock	14.04
Forestry	0.49
Fishing	0.32
Total Agricultural Sector	22.68
Mining and Quarrying	1.71
Large Scale Manufacturing	9.24
Small Scale Manufacturing	1.98
Slaughtering	1.21
Electricity Generation + Distribution & Gas Distribution	2.41
Construction	2.56
Total Industrial Sector	19.11
Wholesale & Retail Trade	18.83
Transport, Storage & Communication	11.78
Finance & Insurance	1.86
Housing Services	5.57
General Government Services	4.64
Other Private Services	8.32
Total Services Sector	58.20

Note: GDP value is at constant basic prices of 2015-16

Macro Economic Indicators

	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22	6MFY22	6MFY23
Average Inflation Rate (CPI)	7.40%	8.60%	4.50%	2.90%	4.20%	3.90%	7.30%	10.70%	8.90%	21.30%	9.80%	24.51%
Average KIBOR	9.84%	9.88%	8.85%	6.49%	6.11%	6.39%	10.43%	11.95%	7.43%	10.83%	8.69%	15.99%
Monetary Policy Rate (MPR)	9.91%	9.75%	8.75%	6.04%	5.75%	5.95%	9.69%	11.75%	7.00%	9.67%	7.62%	15.04%
PKRV	9.63%	9.75%	8.67%	6.34%	5.95%	6.26%	10.20%	11.79%	7.28%	10.68%	8.57%	15.81%
Average Exchange Rate	96.83	102.84	101.47	104.37	104.78	110.11	136.45	158.40	160.46	191.87	169.32	220.43
(USD mln)	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22	6MFY22	6MFY23
Current Account Balance	-2,496	-3,130	-2,815	-4,961	-12,270	-19,195	-13,434	-2,970	-1,852	-13,779	-1,515	-620*
Exports	24,802	25,078	24,090	21,972	22,003	24,768	24,257	22,536	25,630	31,792	2,547	2,878
Imports	40,157	41,668	41,357	41,118	48,001	55,671	51,869	43,645	53,785	80,177	6,507	5,633
Trade Balance	-15,355	-16,590	-17,267	-19,146	-25,998	-30,903	-27,612	-21,109	-28,155	-48,385	-3,961	-2,755
Foreign Exchange Reserves	11,020	14,141	18,699	23,099	21,403	16,384	14,482	18,886	24,398	15,537	24,668	13,401

*Based on 5-month average (latest available data)

Macro Economic Indicators | Monthly

	Jan-22	Feb-22	Mar-22	Apr-22	May-22	Jun-22	Jul-22	Aug-22	Sep-22	Oct-22	Nov-22	Dec-22
Average Inflation Rate (CPI)	13.00%	12.20%	12.70%	13.40%	13.80%	21.30%	24.90%	27.30%	23.20%	26.60%	23.80%	24.50%
Average KIBOR	11.32%	10.82%	11.85%	13.52%	14.90%	15.41%	15.66%	15.96%	16.05%	15.81%	16.01%	17.00%
Monetary Policy Rate (MPR)	9.75%	9.75%	9.75%	12.25%	13.00%	13.75%	15.00%	15.00%	15.00%	15.00%	15.50%	16.00%
PKRV	11.13%	10.67%	11.78%	13.13%	14.78%	15.25%	15.39%	15.78%	15.83%	15.64%	15.87%	16.90%
Average Exchange Rate	176.5	175.7	180.1	202.4	214.1	204.4	219.4	220.9	230.5	220.6	222.3	225.0
(USD mln)	Jan-22	Feb-22	Mar-22	Apr-22	May-22	Jun-22	Jul-22	Aug-22	Sep-22	Oct-22	Nov-22	Dec-22
Current Account Balance	-2,531	-545	-1,006	-640	-1,513	-2,169	-1,215	-676	-363	-569	-276	Unavailable
Exports	2,614	2,820	3,763	3,779	2,990	3,770	2,835	3,387	3,021	2,834	2,888	2,304
Imports	6,036	5,907	7,218	7,028	6,550	8,353	6,151	6,649	5,571	5,288	4,978	5,161
Trade Balance	-3,422	-3,087	-3,455	-3,249	-3,560	-4,583	-3,316	-3,262	-2,550	-2,454	-2,090	-2,857
Foreign Exchange Reserves	22,836	22,638	18,545	16,406	15,219	15,537	14,024	14,347	13,310	14,278	13,027	11,421

KSE-100 Returns | Monthly & Annual

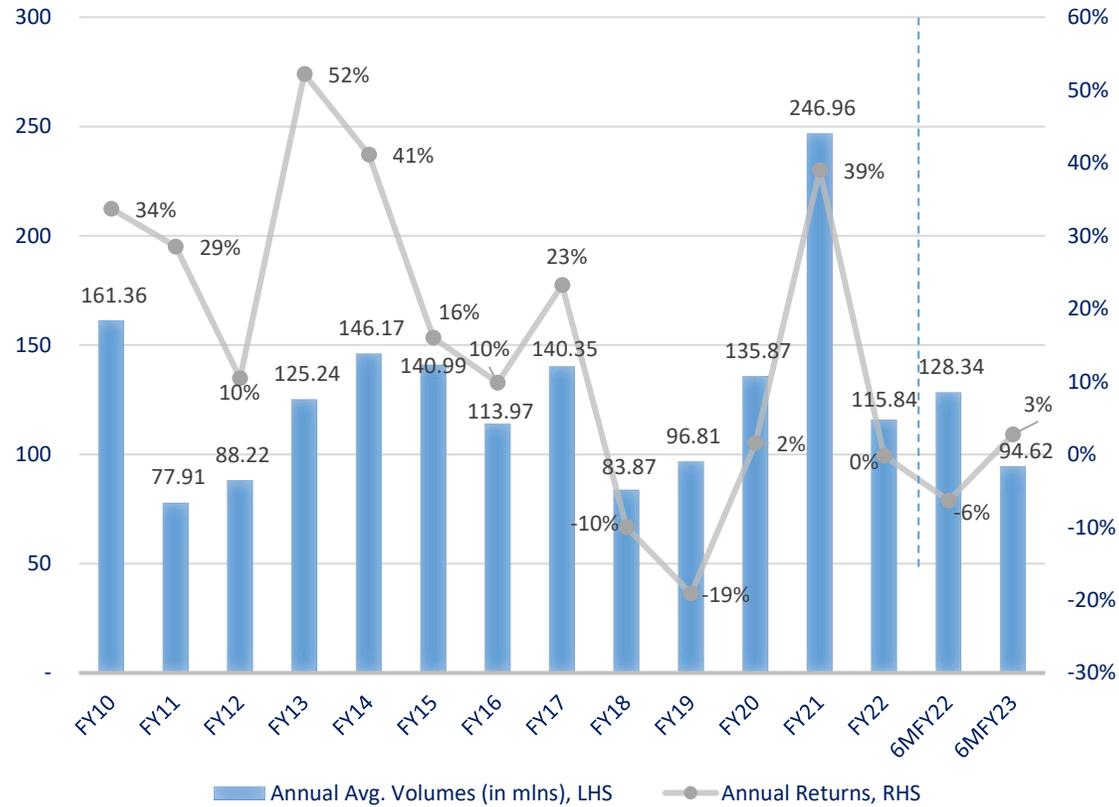
KSE 100 Index	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	FY22	6MFY22	6MFY23
Index Value	21,006	29,653	34,399	37,784	46,565	41,911	33,902	34,422	47,356	41,541	44,596	40,420
Returns (%)	52%	41%	16%	10%	23%	-10%	-19%	2%	38%	-12%	2%	-9%

KSE 100 Index	CY12	CY13	CY14	CY15	CY16	CY17	CY18	CY19	CY20	CY21	CY22
Index Value	16,905	25,261	32,131	32,816	47,807	40,471	37,067	40,735	43,755	44,596	40,420
Returns (%)	49%	49%	27%	2%	46%	-15%	-8%	10%	7%	2.0%	-9%

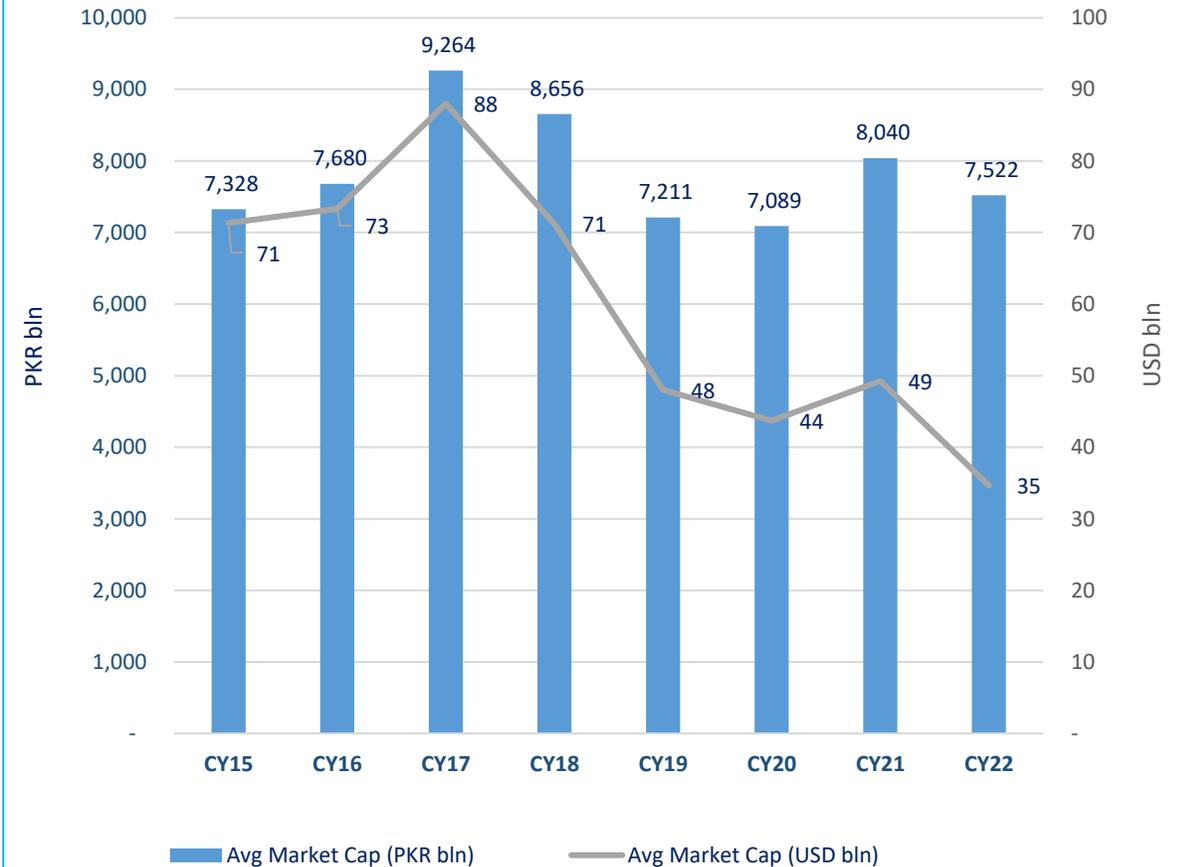
KSE 100 Index	Mar-22	Apr-22	May-22	Jun-22	Jul-22	Aug-22	Sep-22	Oct-22	Sep-22	Oct-22	Nov-22	Dec-22
Index Value	45,375	44,461	44,929	45,249	43,078	41,541	40,150	42,351	41,129	41,265	42,349	40,420
Returns (%)	2%	-2%	1%	1%	-5%	-4%	-3%	6%	-3%	0%	3%	-5%

MARKET VOLUMES & CAPITALIZATION

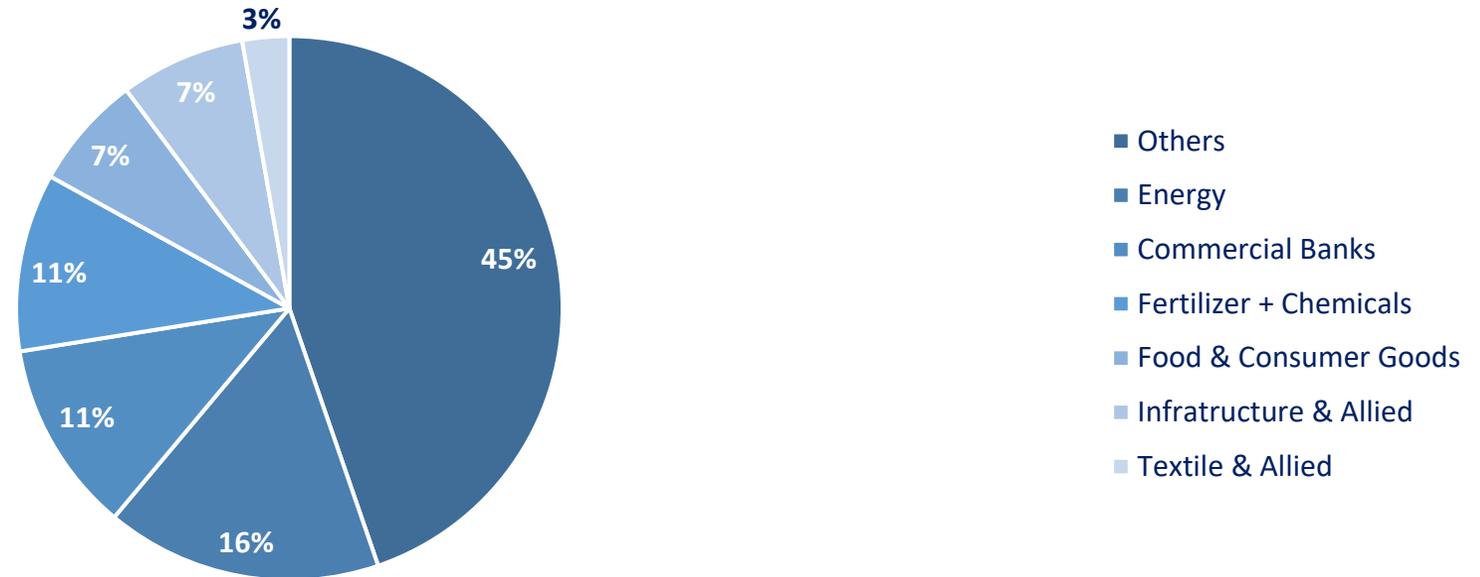
KSE-100 Average Volumes



Average Market Capitalization



Sector Wise Market Capitalization



- This data is based on market capitalization of PKR~7.6trn as on 28th Dec, 2022.
- The largest sector is energy sector which comprises of Oil & Gas Exploration & Production, Oil & Gas Marketing, Power Generation & Distribution and Refineries; the market capitalization stands at PKR~1.2trn and accounts for ~16% of the total.
- Commercial banks, with a market capitalization of PKR~0.9trn, are the next largest sector and contribute ~11% to the total market capitalization.

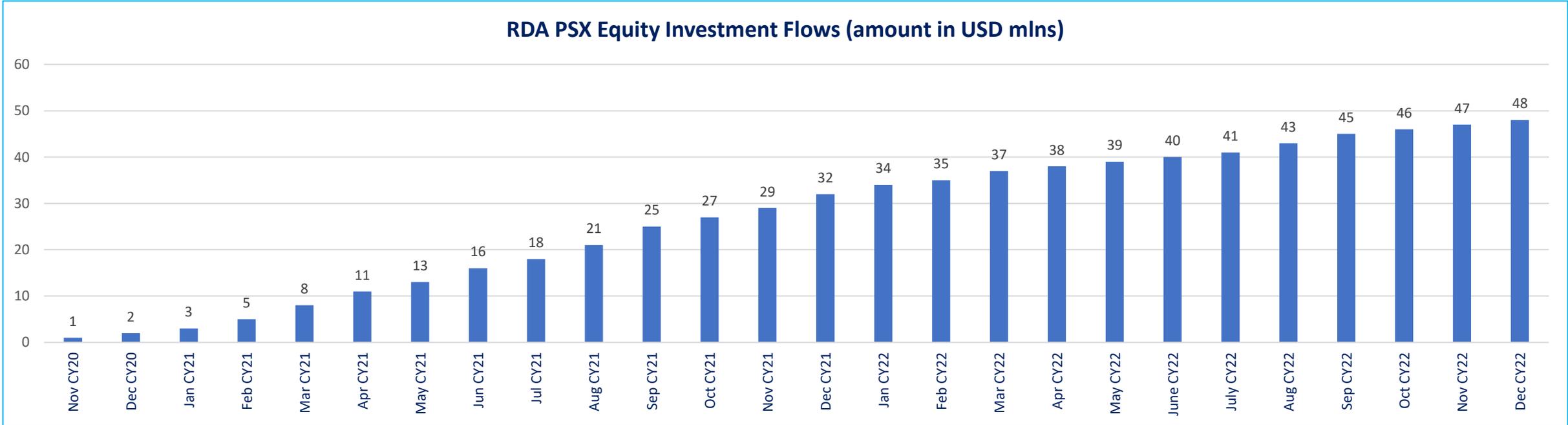
Fee Income

- With effect from 14th Oct, 2019, PSX vide Notice No. PSX/N-1258 dated 9th 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, average daily volumes of the KSE-100 index stood at ~115mln shares in FY22 (SPLY: ~247mln). However, this figure has fallen to ~95mln shares in the 6MFY23 period (SPLY: ~128mln). Trading volumes dropped due to negative market sentiment which prevailed owing to a burgeoning external account deficit; rising inflationary pressures; uncertainty on the political front; and delays in approval of IMF's sixth and seventh review. This negative sentiment carried well into the 6MFY23 period wherein the Aug-22 monsoon flashfloods slowed down economic growth generating economic losses worth over USD 30bln.

Fee Income		
Month	Total Volumes (KSE-100)	Minimum Fee (3 paisa per share)
Mar-22	1,828,537,000	54,856,110
Apr-22	3,411,414,185	102,342,426
May-22	1,962,837,257	58,885,118
Jun-22	2,239,144,805	67,174,344
Jul-22	2,793,671,422	83,810,143
Aug-22	3,116,938,999	93,508,170
Sep-22	2,063,999,753	61,919,993
Oct-22	2,035,711,926	61,071,358
Nov-22	1,718,231,824	51,546,955
Dec-22	1,718,190,544	51,545,716

Brokerage Firms | Local Industry

Roshan Digital Account (RDA)



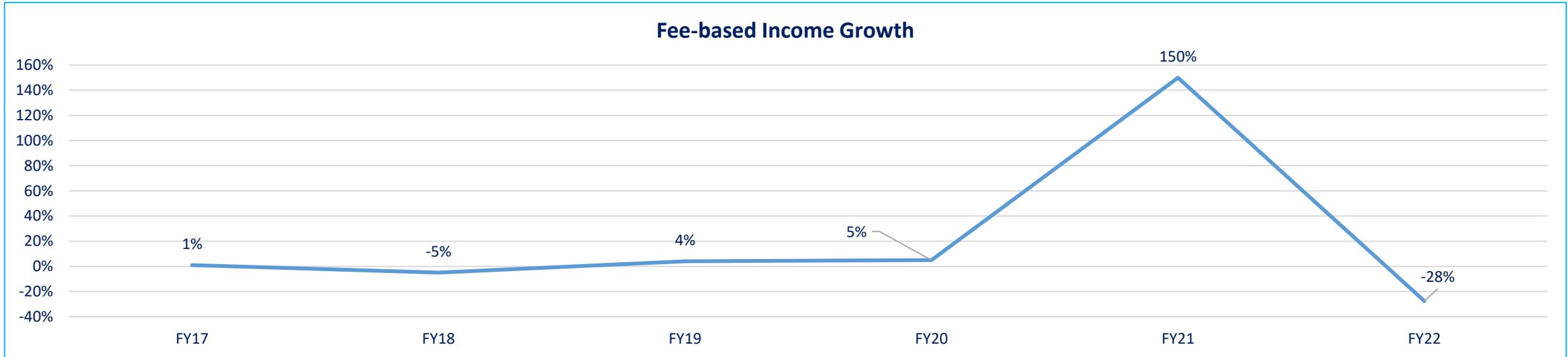
- The SBP in collaboration with Pakistan Stock Exchange (PSX), National Clearing Company of Pakistan Limited (NCLL), brokerage houses and RDA banks offer non-resident Pakistanis to invest in listed securities at PSX remotely through a digital investment account – the RDA.
- RDA funds can be repatriated and investors are permitted to remit their dividend income as well as divest their holdings without prior approval of the RDA and SBP banks.
- Apart from meeting their investment needs, investors can pay their bills, transfer funds, and engage in e-commerce using this single platform.
- While the bulk (~63%) of RDA inflows are in Naya Pakistan Certificates, a portion of the inflows (~1%) is invested in Shariah and non-Shariah compliant listed stocks. The gross inflow into listed securities amounted to USD~48mln in Dec-22 (SPLY: USD~32mln).

NET BUY/SELL

Net Buy/Sell (PKR mln)						
Participants	FY19	FY20	FY21	FY22	6MFY22	6MFY23
Individuals	20,796	34,001	53,276	28,420	12,164	10,605
Companies	14,553	4,245	22,142	20,182	10,421	5,055
Banks / DFIs	9,009	-8,516	-15,412	21,030	4,743	11,431
NBFC	-172	707	27	500	788	-415
Mutual Funds	-20,080	-7,792	1,761	-23,598	-1846	-14,285
Other Organizations	3,423	4,973	6,889	10,481	7,200	3,581
Broker Proprietary Trading	-1,801	-2,105	-5,270	-3,409	-1,987	-1,686
Insurance Companies	17,887	20,179	-1,357	-1,810	11,336	-14,177
LIPI NET	43,615	45,691	62,055	51,796	42,819	110
Foreign Individuals	61	-134	12	662	697	5,464
Foreign Corporates	-44,540	-49,033	-60,141	-63,841	-52,119	-14,789
Overseas Pakistanis	865	3,477	-1,926	11,383	8,603	9,222
FIPI NET	-43,615	-45,691	-62,055	-51,796	-42,819	-102

Net Buy/Sell (USD mln)						
Participants	FY19	FY20	FY21	FY22	6MFY22	6MFY23
Individuals	166	213	332	157	71	48
Companies	111	27	138	111	60	23
Banks / DFIs	63	-55	-95	115	28	50
NBFC	-2	5	0	3	4	-2
Mutual Funds	-146	-50	10	-128	-10	-64
Other Organizations	28	32	45	60	43	16
Broker Proprietary Trading	-15	-13	-32	-20	-12	-7
Insurance Companies	150	128	-10	-1	66	-63
LIPI NET	356	285	387	298	250	1
Foreign Individuals	0	-1	0	4	4	24
Foreign Corporates	-362	-306	-375	-367	-304	-66
Overseas Pakistanis	6	22	-13	65	50	41
FIPI NET	-356	-285	-387	-298	-250	-1

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 ~-28% in FY21 as compared to 150% in FY21. Following a successful year marked by growth in stock market activity, the performance of brokers was impacted by negative investor sentiments where were weighed down by political uncertainty, a deteriorating economic outlook; mounting inflationary pressures; and uncertainty about the resumption of the IMF programme which was putting pressure on Pakistan's FX reserves.
- Another negative contributing factor is the low volume of IPOs in FY22; only three IPOs occurred raising a mere PKR 1.3bln which is the lowest in nine years. In contrast, FY21 witnessed a total of eight IPOs raising PKR 20.0bln. Brokers act as market makers to IPOs which serves as a source of revenue.

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 ~60% in FY21 (FY20: ~65%).
- **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 320% in FY22 (FY21: 217%). 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 ~58% during FY22 (FY21: ~62%).

Industry Average	FY18	FY19	FY20	FY21	FY22
Equity Instrument/Investments	66%	62%	65%	65%	60%
Liquid Assets/Trade Related Liabilities	480%	413%	268%	217%	320%
Equity/Total Assets	67%	62%	58%	62%	58%

Regulatory Framework

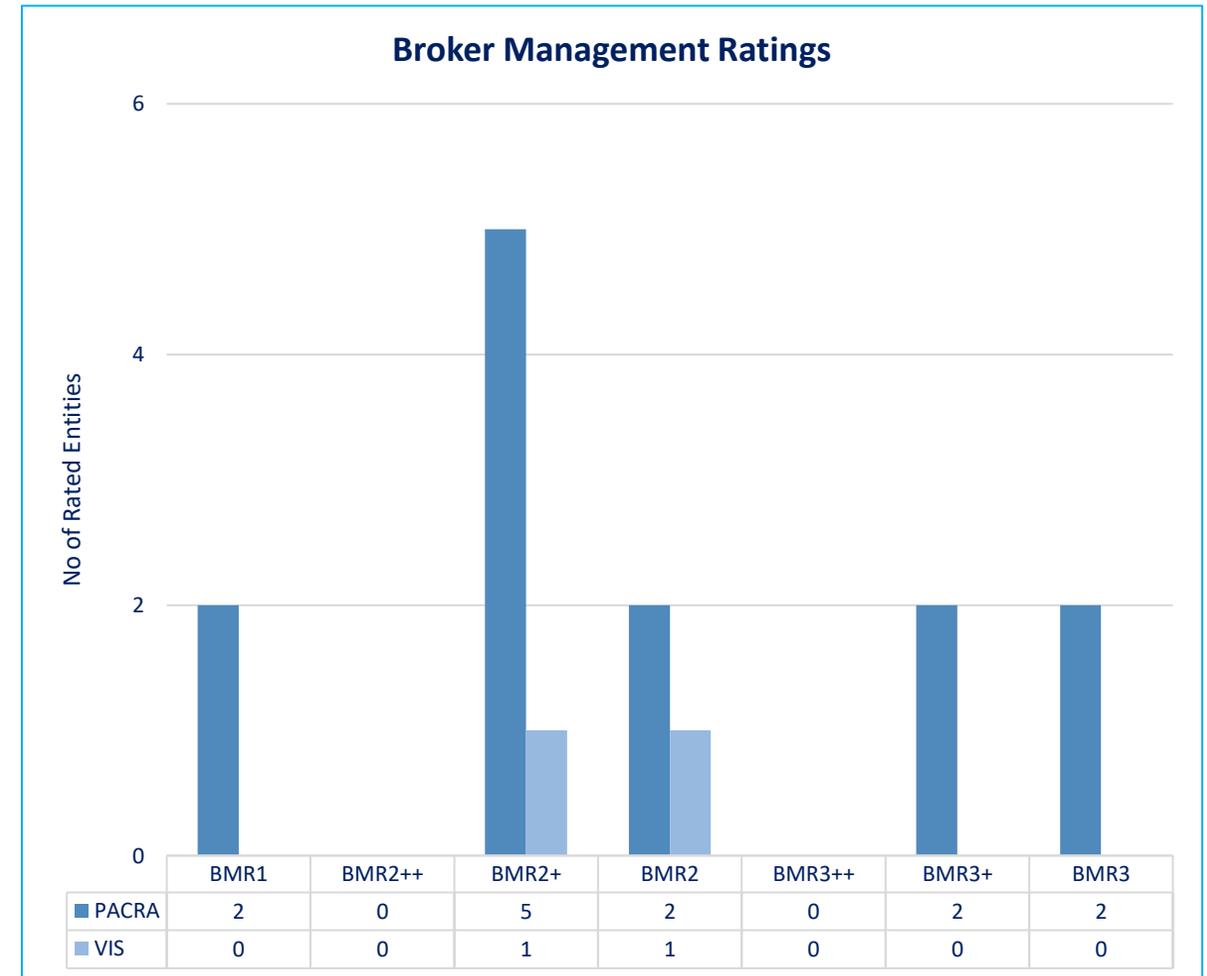
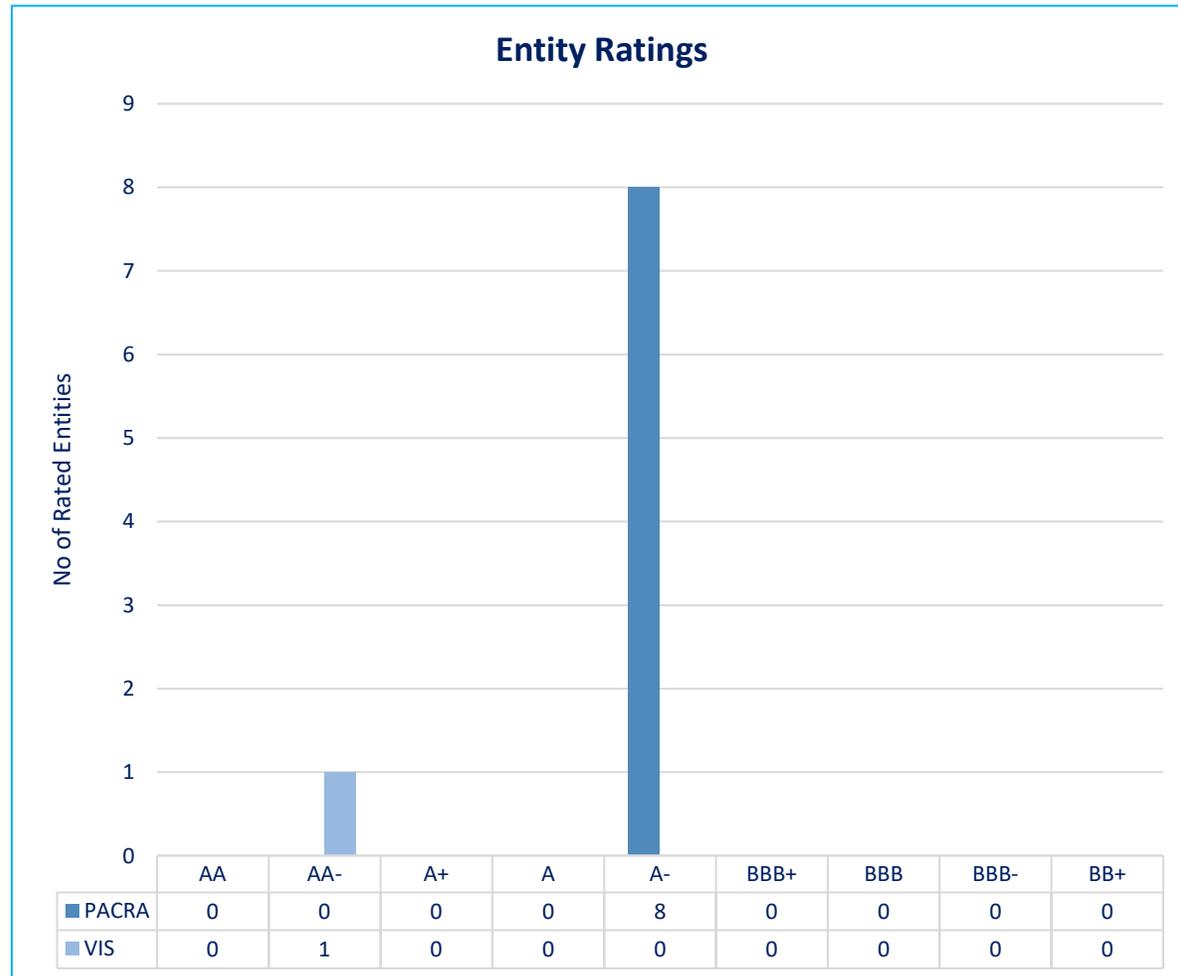
- The primary regulatory body for brokers is the Securities and Exchange Commission of Pakistan. There are a comprehensive set of regulations that govern the activities of brokers. These include the Securities Brokers (Licensing and Operations) Regulations 2016, the SECP Act 1997, the Anti-Money Laundering 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 125mIn	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	Not Applicable	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 25th 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.

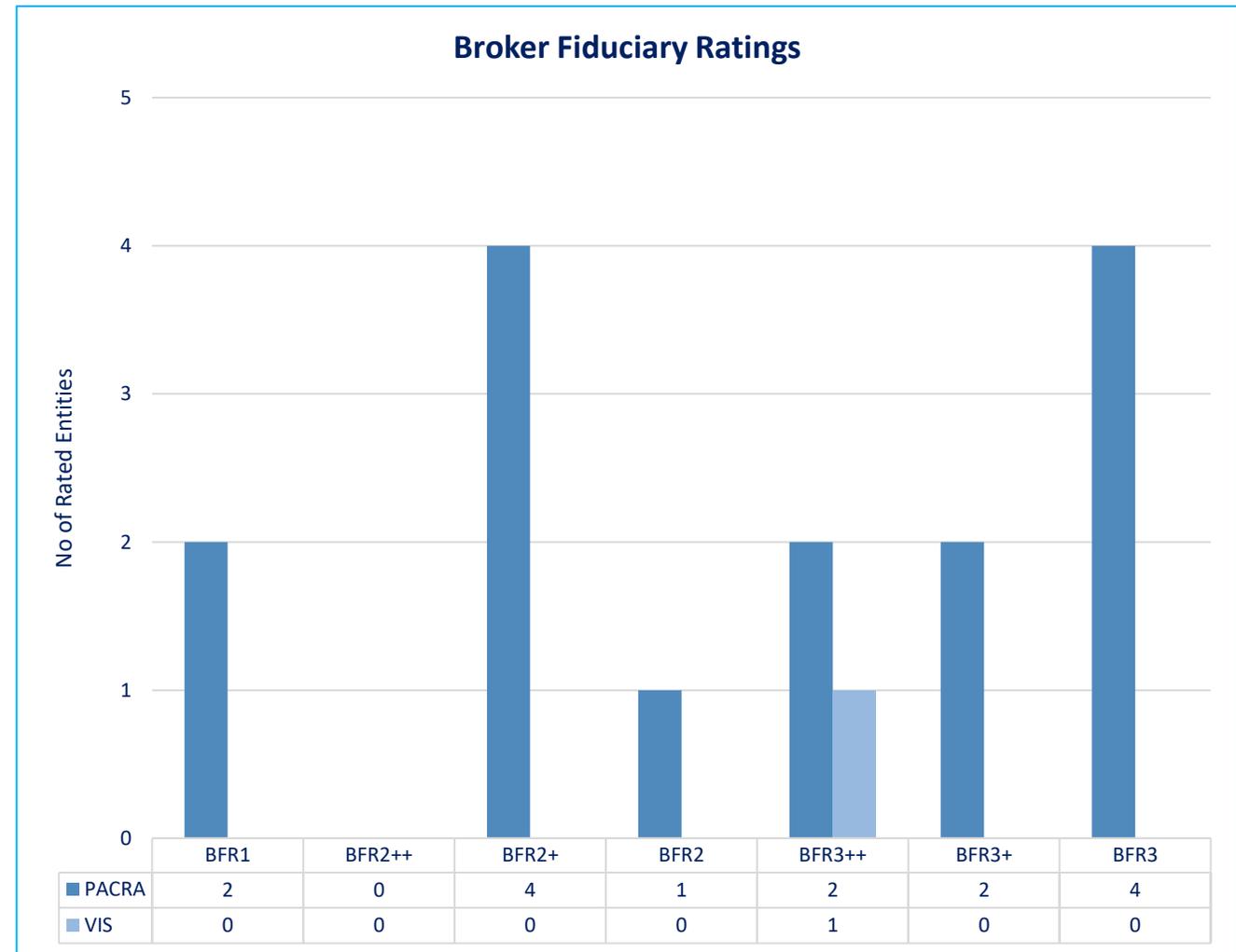
Rating Scale



Brokerage Firms | Local Industry

Rating Scale

- PACRA provides Entity ratings to 7 brokerage firms with a long term rating bandwidth of BBB+ to AA-.
- In addition, PACRA provides Broker Management Ratings (BMR) ratings to 13 brokerage firms with a long term rating bandwidth of BMR3 to BMR1.
- Moreover, PACRA provides 15 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

- 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.

- Pakistan is a highly volatile economy; such an environment can create potential opportunities for earning high returns.

Outlook: Stable

- In FY22 Pakistan's GDP grew by ~20.0% and to PKR ~66.9trln, in nominal terms, (FY21: ~17.5%; PKR ~55.8trln) while the LSM index grew by ~12.0% (SPLY: ~11.6%). FY23 commenced by a catastrophic set of events as unprecedented monsoon rainfalls triggered massive flash flooding across Pakistan destroying infrastructure and affecting the lives of more than 33mln people.
- The estimated economic loss, loss from flood damages, and reconstruction costs from the flash floods has been placed at USD ~14.9bln, USD ~15.2 bln, and USD ~16.3bln, respectively. As a consequence, loss in potential GDP is estimated to be ~2.2% of FY22 GDP. The SBP estimates the FY23 GDP growth at ~2% after incorporating the post-disaster needs assessment of the floods.
- FY23 was marked by significantly high levels of inflation with the average 6MFY23 standing at ~24.5% (SPLY: 9.8%). Inflation spiked in immediately following the flash floods with the national CPI hitting ~27.3%. Inflationary pressures since then have slowly eased due to the rampant restrictive policy measures undertaken by the SBP.
- In FY23 the SBP increased the policy rate on two occasions with the first increase in Jul-22 followed by another in Nov-22. Consequently, the average policy rate in 6MFY23 is ~15.0% compared to ~7.6% in the SPLY. In this high interest rate environment, average KIBOR and PKRV also increased to ~16.0% and ~15.8%, an increase of ~7.3% and ~7.2%, respectively from the SPLY.
- When comparing Pakistan's stock market to global markets, the KSE-100 index demonstrated a similar behavior posting a return of ~-9.4% in both CY22 and 6MFY23 (SPLY: ~1.9% for each period). The brokerage and securities sector was severely impacted by the dire macroeconomic situation, global commodity super cycle, and political uncertainty which commenced in FY22 and continued well into the 6MFY23 period. This precarious set of circumstances became deeply rooted in investor sentiment and was reflected in KSE-100 average index volumes which fell by ~53.0% and ~26.3% in FY22 and 6MFY23, respectively, compared to the SPLY. This negative sentiment can be directly reflected in broker income growth in FY22 of ~-28% sharply in contrast to FY21 wherein growth was ~150%.
- Furthermore, the low volumes of IPOs in CY22 compared to the SPLY meant a further reduction in income earning opportunity for brokers.
- In the 6MFY23 period, both the LIPI and FIPI declined by ~99.7% compared to the SPLY while this decline was ~16.5% in FY22. The RDA account investments in the stock market increased by ~17.1% in the 6MFY23 period. In the SPLY this amount was ~77.8%. While this may sound encouraging, the growth in investment is slowing down since Oct-22 reflecting reduced investing interest.
- The Special Convertible Rupee Account, which reports the inflows and outflows by foreign investors into Pakistan's equity market, reported a cumulative net outflow of USD~62.9mln in the 5MFY23 period compared to USD ~406.7mln in the SPLY. Most concerning is the drop in foreign investment in the equity market which dropped by ~77.0% in the 5MFY23 period compared to the SPLY.
- With a reduced foreign and local interest in investing and reduced IPO activity, coupled with deteriorating macroeconomic fundamentals the near-term performance of the sector rests on the revival of investor sentiment.

- Pakistan Bureau of Statistics (PBS)
- Pakistan Stock Exchange (PSX)
- State Bank of Pakistan (SBP)
- Federal Board of Revenue (FBR)
- National Clearing Company of Pakistan Limited (NCCPL)
- Securities & Exchange Commission of Pakistan (SECP)
- Mutual Funds Association of Pakistan (MUFAP)
- PACRA Database
- Investing.com (<https://www.investing.com/indices/major-indices>)
- Fidelity Research (https://eresearch.fidelity.com/eresearch/markets_sectors/sectors/sectors_in_market.jhtml)
- The News (<https://www.thenews.com.pk/print/889819-msci-downgrades-pakistan-to-frontier-markets>)
- Tribune (<https://tribune.com.pk/story/2327120/psx-to-revert-to-old-trading-system>, <https://tribune.com.pk/story/2326005/psx-adopts-new-trading-system>)
- Securities and Exchange Board of India (SEBI)
- BSE India

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