



# Brokerage Firms

## An Overview



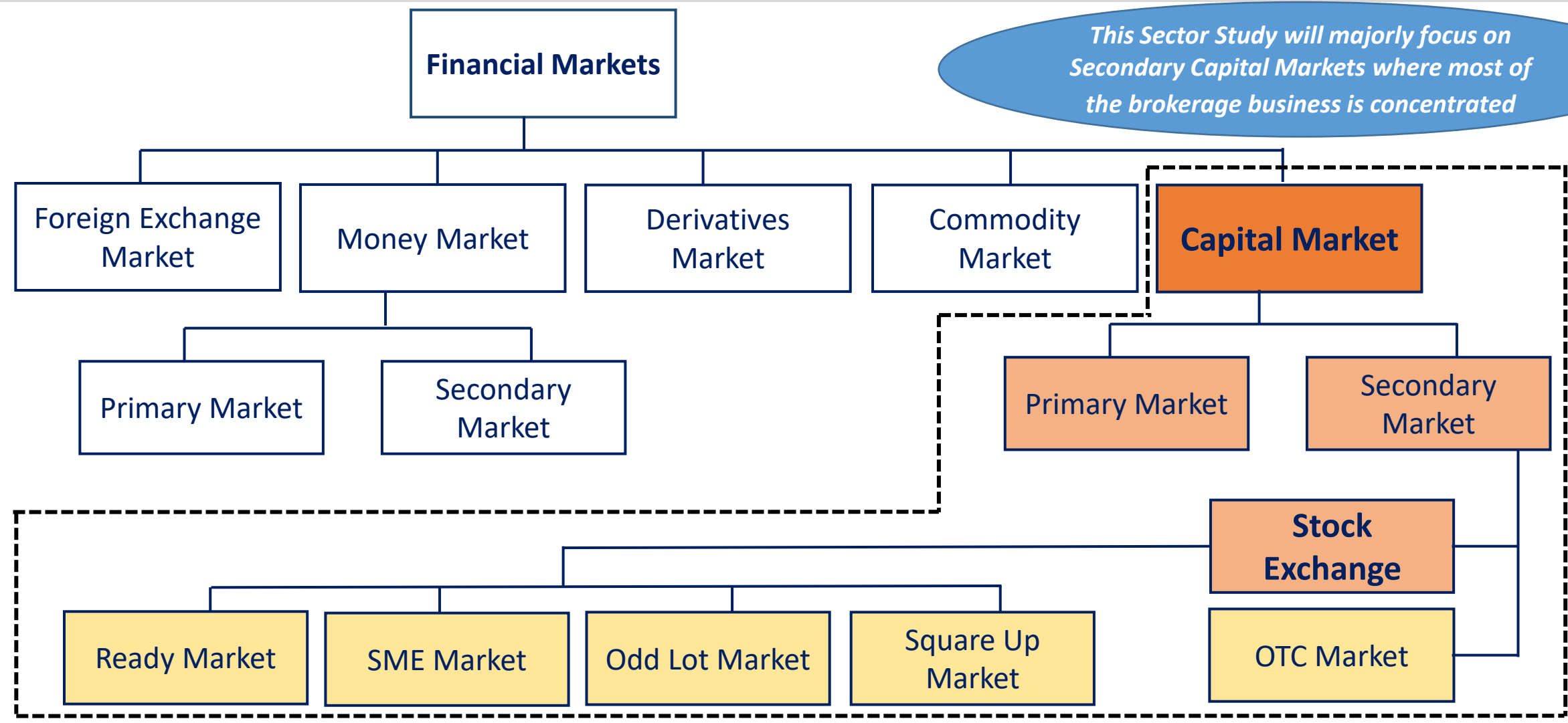
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# BROKERAGE FIRMS | INTRODUCTION

## Types of Financial 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

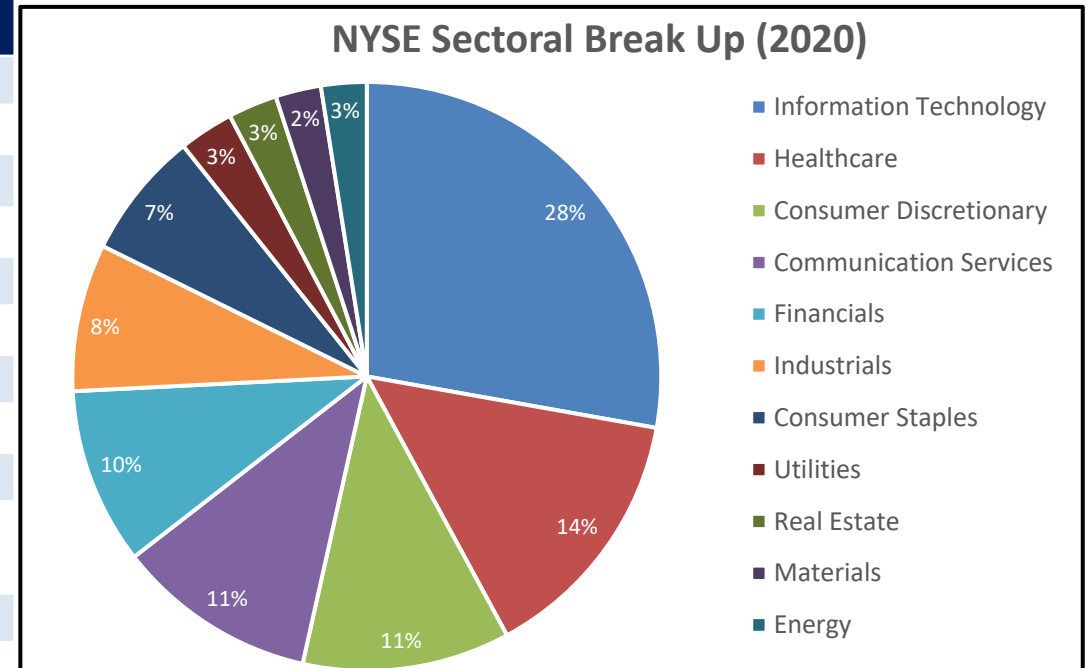
- **Derivatives**
  - **Deliverable Futures Contract (DFC)**: DFCs are forward contracts to buy or sell a certain underlying instrument with actual delivery of the said instrument occurring. The minimum lot for purchasing these shares is 500 shares. Settlement takes place 30 days after the contract is 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 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 the 10 largest stock exchanges in the world in terms of market capitalization along with their 2020 performance. The top 10 exchanges combined represent approximately ~80% of total global market capitalization.
- The US has the two largest exchanges, NYSE and Nasdaq. The NYSE is dominated by the information technology sector which occupies ~28% of the total market. This is due to the presence of companies such as Apple, Microsoft and Amazon, whose individual market capitalization has crossed the trillion dollar mark.

Stock Exchange	Market Capitalization (USD Trn)	Index	1 Year Performance (CY20)	P/E Ratio
New York Stock Exchange	22.4	S&P 500	16%	41.17
Nasdaq	18.0	Nasdaq	42%	40.01
Shanghai Stock Exchange	7.2	Shanghai Composite	15%	16.31
Tokyo Stock Exchange	6.7	Nikkei 225	18%	26.02
Hong Kong Exchange	6.1	Hang Seng	-2%	13.96
Shenzhen Stock Exchange	5.5	SZSE Component	40%	35.33
London Stock Exchange	4.6	FTSE 100	-10%	17.55
Euronext	4.4	Euro Stoxx 50	-5%	21.12
Saudi Stock Exchange	2.4	Tadawul All Share	5%	35.54
National Stock Exchange of India	0.2	NIFTY 50	17%	35.99
Bombay Stock Exchange	0.2	SENSEX	18%	34.58
Pakistan Stock Exchange	0.05	KSE 100	6%	10.95





## Regional Comparison | INDIA

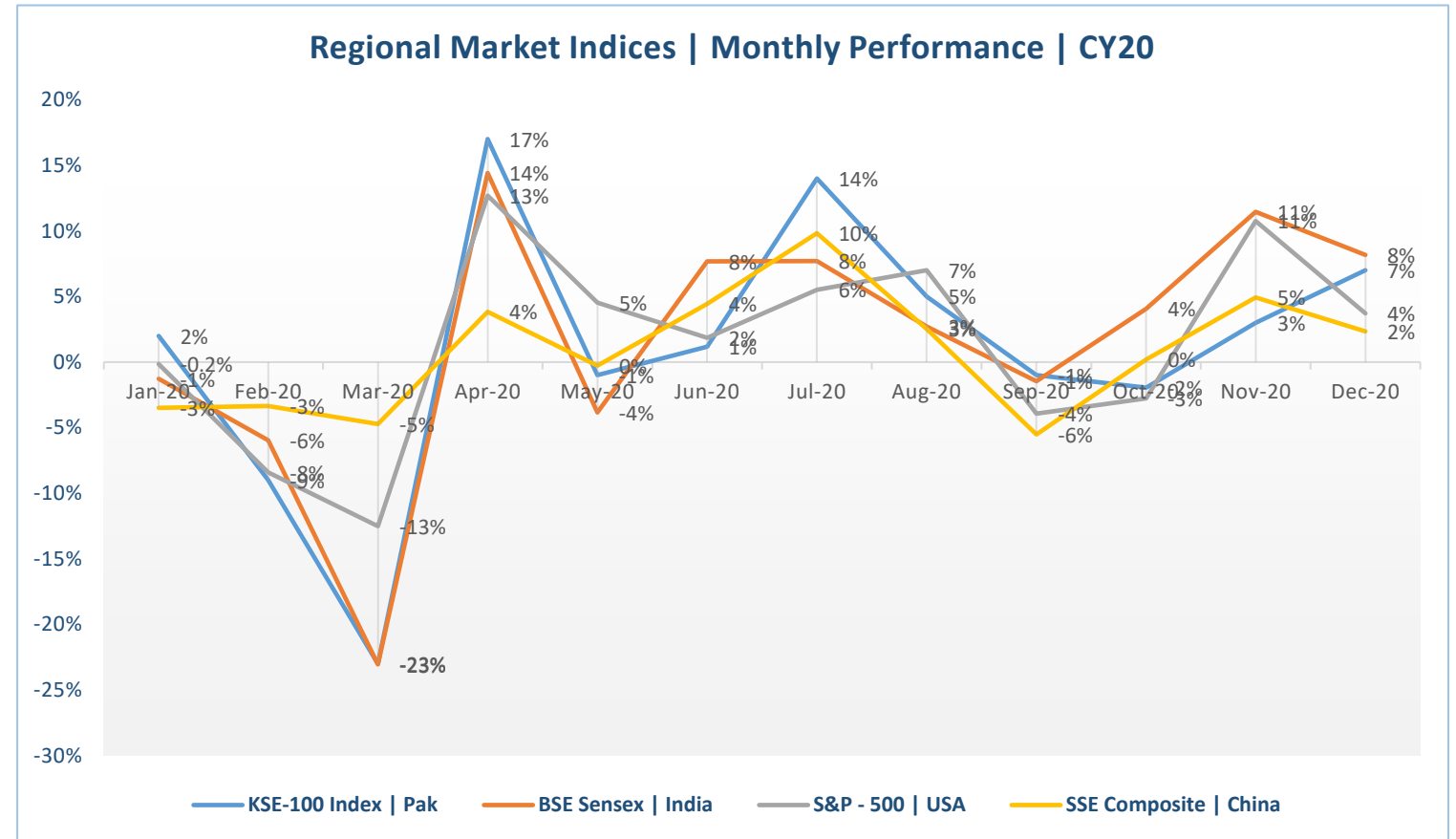
- The Securities and Exchange Board of India (SEBI) is the regulatory body which oversees brokerages in the country. The Securities and Exchange Board of India (Stock Brokers and Sub-Brokers) Regulations, 1992 is the legislation which regulates the brokerage industry.
- The regulation defines 3 categories 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.





## The COVID-19 SPELL

- Global Stock Indices took a dip during the first wave of Covid-19, with KSE-100 and BSE-Sensex dropping by ~23% in March'20. China's SSE Composite was the least to decline by ~5% (Mar'20).
- The markets recovered in the next months and have reflected positive growth sentiments barring a few months.
- KSE-100 Index has, on average, reflected a return of ~5% combined in Nov'20 and Dec'20.



## Overview

- The adjacent table shows the MSCI categorization of various international equity markets into developed, emerging and frontier markets.
- In 2017, Pakistan was included in the MSCI Emerging Market Index and has maintained its position ever since.

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



# BROKERAGE FIRMS | LOCAL INDUSTRY

## Overview

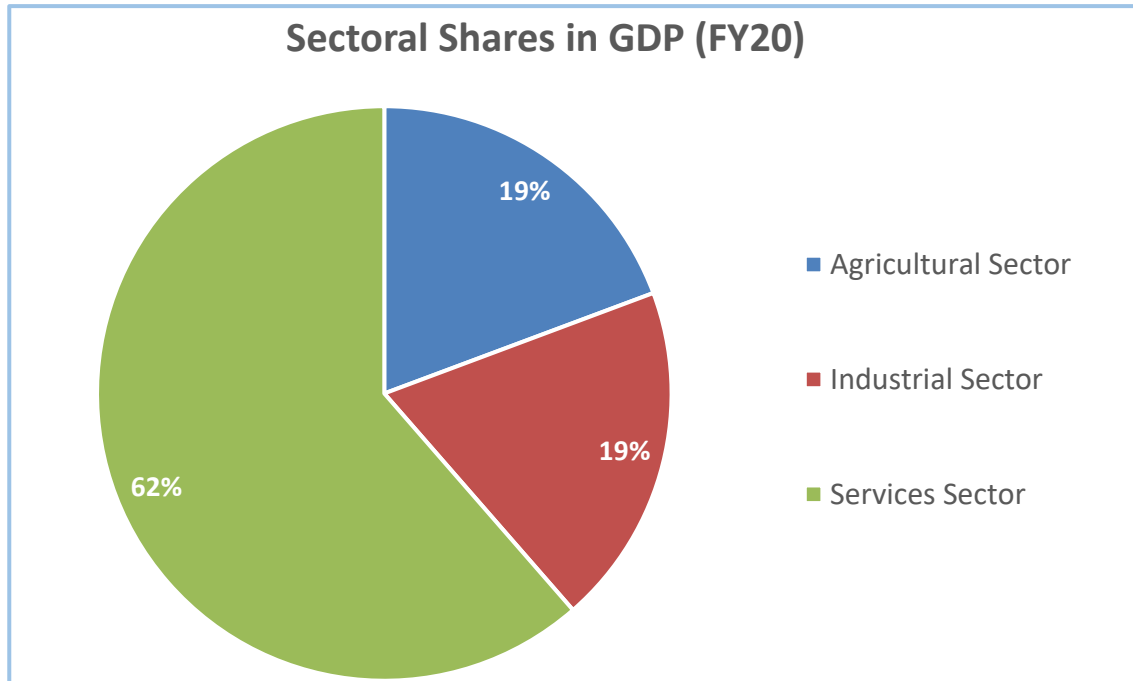
- A broker or brokerage firm acts as an intermediary by matching a customer's buy order with a third party's sell order or vice versa.
- Brokerage firms receive compensation through a commission or fees that is charged once the transaction has been successfully completed. This amount may be paid by the 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 ~204 brokerage firms licensed by the Securities and Exchange Commission of Pakistan (SECP). Out of these 20 brokerage firms have Entity Ratings while 19 have Broker Management Ratings. Moreover, there are 9 brokerage firms listed on the Pakistan Stock Exchange.



# BROKERAGE FIRMS | LOCAL INDUSTRY

## GDP Break Up

- Pakistan's GDP shrunk by 0.38% in FY20 and stood at PKR~12,532bln as compared to PKR~12,580bln in FY19.
- 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.



FY20 Sector Wise GDP Break-Up (%)	
Crops	6.81
Livestock	11.69
Forestry	0.41
Fishing	0.40
<b>Total Agricultural Sector</b>	<b>19.31</b>
Mining and Quarrying	2.51
Large Scale Manufacturing	9.50
Small Scale Manufacturing	2.04
Slaughtering	0.94
Electricity Generation + Distribution & Gas Distribution	1.76
Construction	2.53
<b>Total Industrial Sector</b>	<b>19.28</b>
Wholesale & Retail Trade	18.17
Transport, Storage & Communication	12.31
Finance & Insurance	3.60
Housing Services	6.98
General Government Services	8.60
Other Private Services	11.75
<b>Total Services Sector</b>	<b>61.41</b>

# BROKERAGE FIRMS | LOCAL INDUSTRY

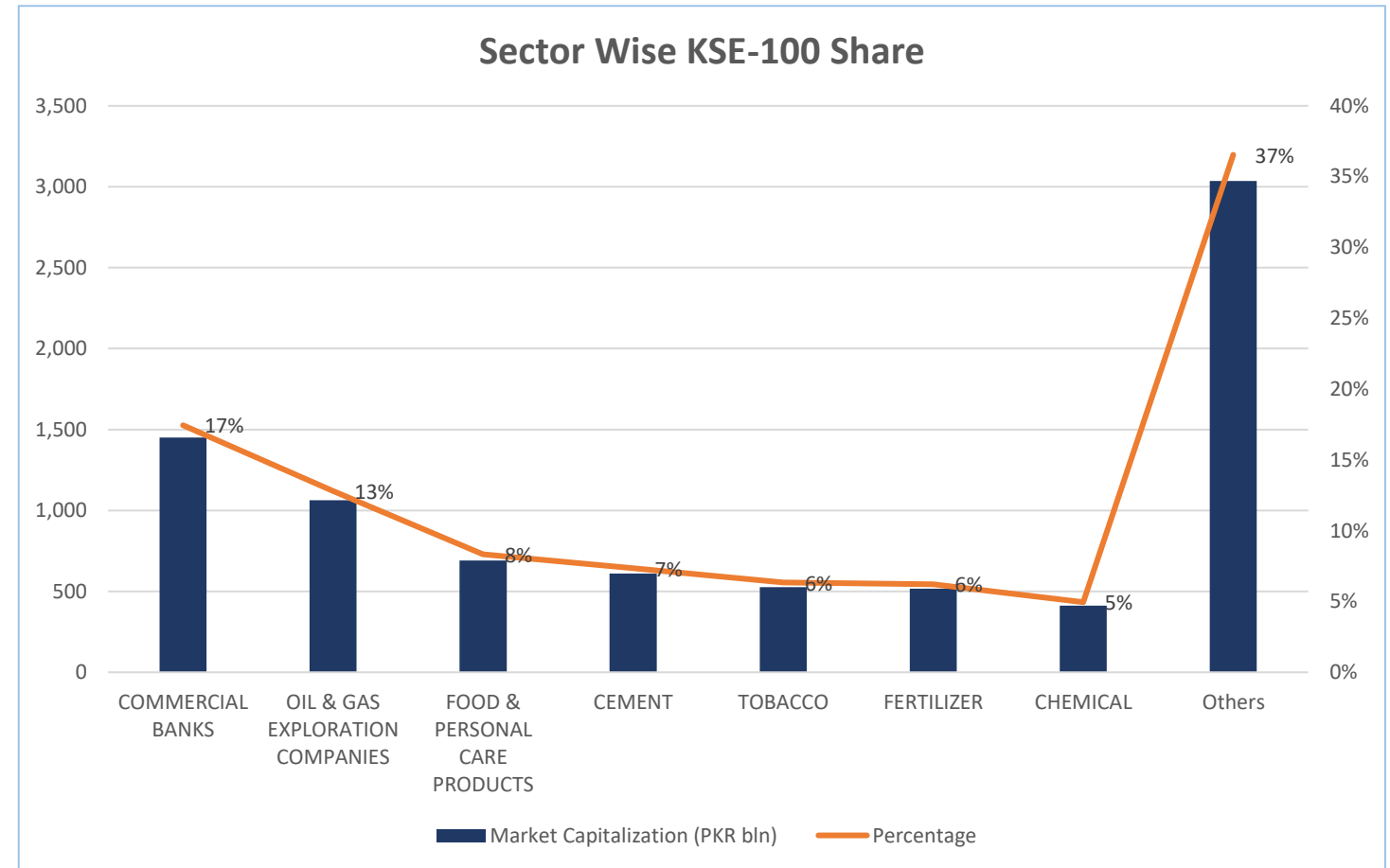
## Macro Economic Indicators

	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	1HFY21
<b>Average Inflation Rate (CPI)</b>	11.90%	11.00%	7.40%	8.60%	4.50%	2.90%	4.20%	3.90%	7.30%	10.70%	8.74%
<b>Average KIBOR</b>	13.45%	12.33%	9.84%	9.88%	8.85%	6.49%	6.11%	6.39%	10.43%	11.95%	7.22%
<b>Monetary Policy Rate (MPR)</b>	13.70%	12.41%	9.91%	9.75%	8.75%	6.04%	5.75%	5.95%	9.69%	11.75%	7.00%
<b>PKRV</b>	13.00%	11.91%	9.63%	9.75%	8.67%	6.34%	5.95%	6.26%	10.20%	11.79%	7.15%
<b>Average Exchange Rate</b>	86.31	89.24	96.83	102.84	101.47	104.37	104.78	110.11	136.45	158.40	164.11
(USD mln)	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	1HFY21*
<b>Current Account Balance</b>	214	-4,658	-2,496	-3,130	-2,815	-4,961	-12,270	-19,195	-13,434	-2,970	1,640
<b>Exports</b>	25,369	24,718	24,802	25,078	24,090	21,972	22,003	24,768	24,257	22,507	9,550
<b>Imports</b>	35,796	40,370	40,157	41,668	41,357	41,118	48,001	55,671	51,869	42,417	18,163
<b>Trade Balance</b>	-10,427	-15,652	-15,355	-16,590	-17,267	-19,146	-25,998	-30,903	-27,612	-19,910	-8,613
<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	20,512

\*Current Account, Export, Import and Trade Balance are up till Nov-20

## KSE-100 | Sectoral Composition

- This data is based on market capitalization of PKR~8.3trn as on 8<sup>th</sup> Jan, 2021.
- Top seven (7) Sectors contribute ~63% to the total Market Capitalization of KSE-100 Index in which Commercial Banks take the lead.





# BROKERAGE FIRMS | LOCAL INDUSTRY

## KSE-100 Returns | Monthly & Annual

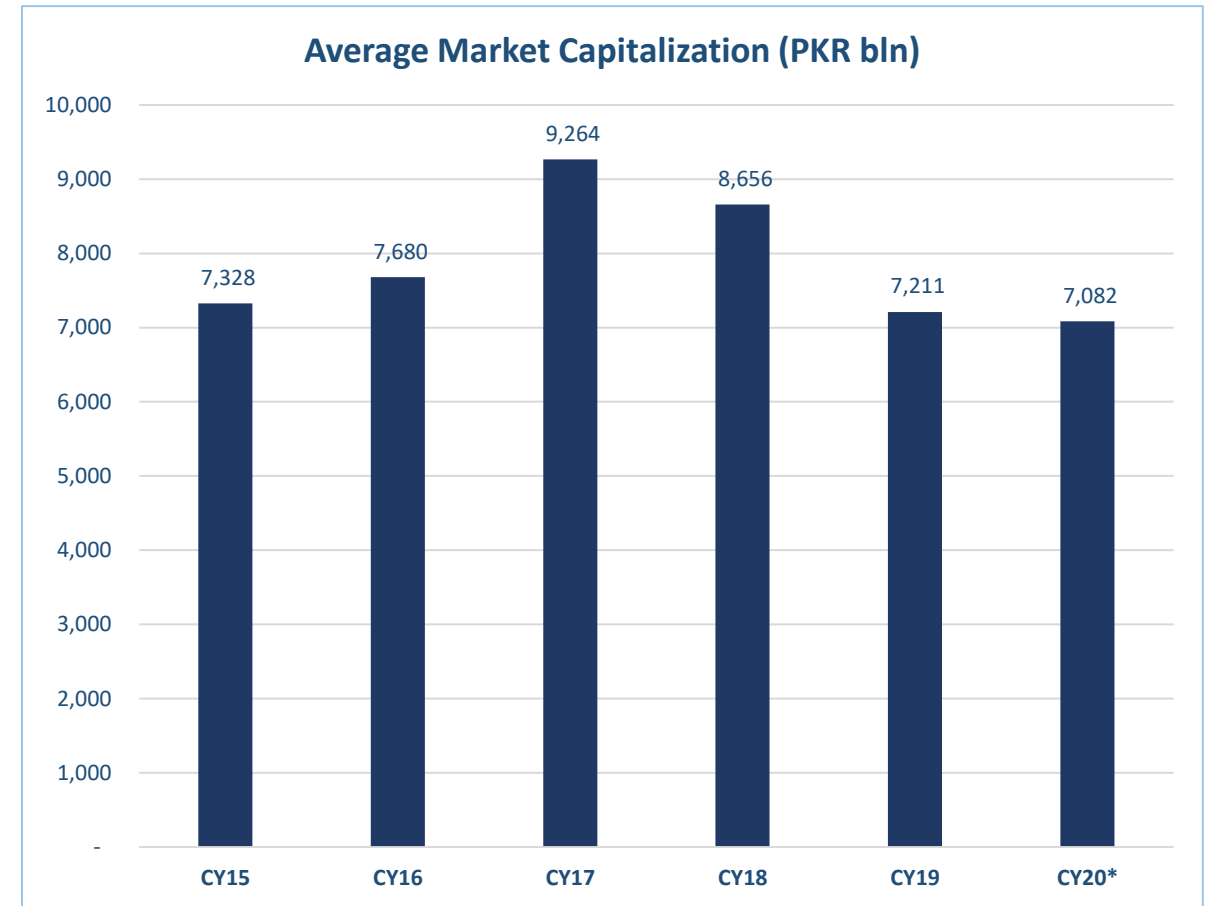
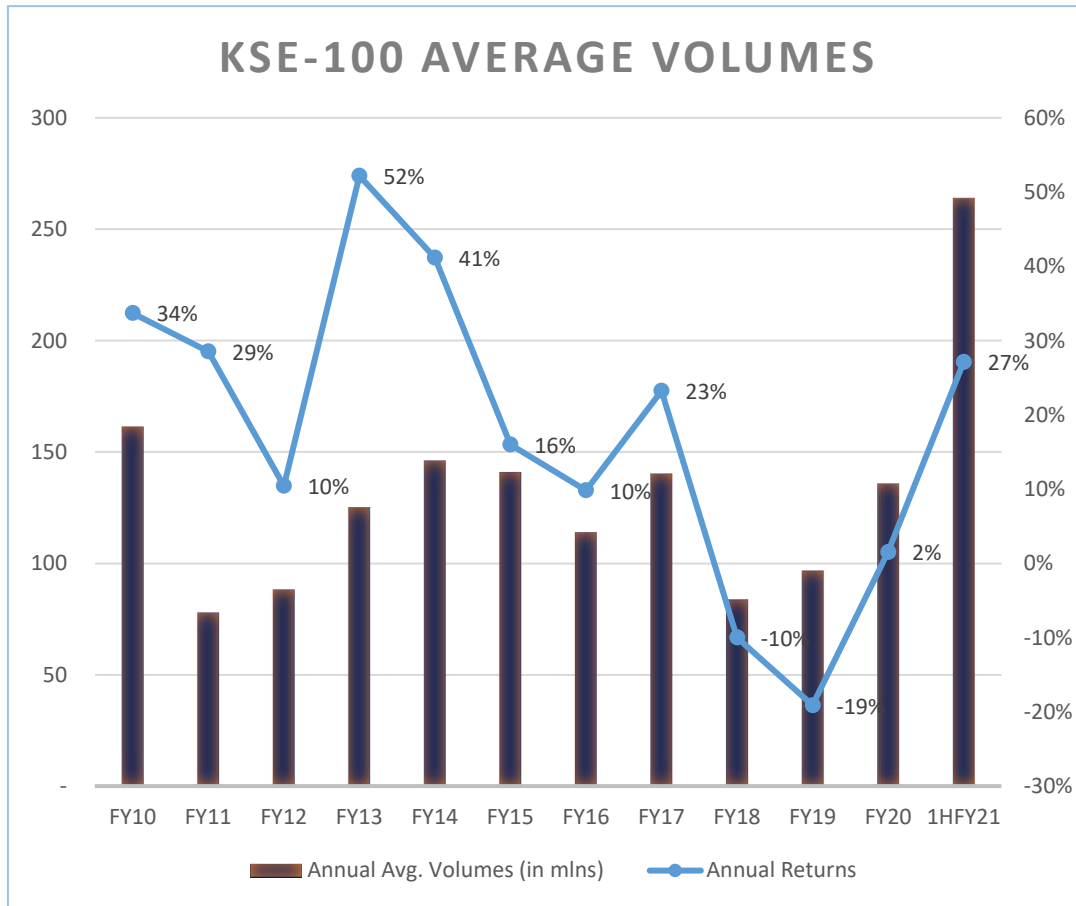
KSE 100 Index	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	1HFY21
Index Value	12,496	13,801	21,006	29,653	34,399	37,784	46,565	41,911	33,902	34,422	43,755
Returns (%)	29%	10%	52%	41%	16%	10%	23%	-10%	-19%	2%	27%

KSE 100 Index	CY11	CY12	CY13	CY14	CY15	CY16	CY17	CY18	CY19	CY20
Index Value	11,348	16,905	25,261	32,131	32,816	47,807	40,471	37,067	40,735	43,755
% Change	-4%	49%	49%	27%	2%	46%	-15%	-8%	10%	7%

KSE 100 Index	Jul-19	Aug-19	Sep-19	Oct-19	Nov-19	Dec-19	Jan-20	Feb-20	Mar-20	Apr-20	May-20	Jun-20	Jul-20	Aug-20	Sep-20	Oct-20	Nov-20	Dec-20
Index Value	31,938	29,672	32,079	34,204	39,288	40,735	41,631	37,984	29,232	34,112	33,931	34,422	39,258	41,111	40,571	39,888	41,069	43,755
% Change	-6%	-7%	8%	7%	15%	4%	2%	-9%	-23%	17%	-1%	1%	14%	5%	-1%	-2%	3%	7%

# BROKERAGE FIRMS | LOCAL INDUSTRY

## MARKET VOLUMES & CAPITALIZATION



\*CY20 Market Capitalization is till 6<sup>th</sup> Nov, 2020





## Fee Income

- With effect from 14<sup>th</sup> 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, the brokerage firms have gone into profits from core operations in the current 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.

Months	Average Volumes (KSE-100)	Minimum Fee (3 paisa Per Share)*
Oct-19	125,373,723	3,761,212
Nov-19	186,241,057	5,587,232
Dec-19	194,287,061	5,828,612
Jan-20	168,350,902	5,050,527
Feb-20	114,219,097	3,426,573
Mar-20	178,992,296	5,369,769
Apr-20	161,345,897	4,840,377
May-20	139,906,300	4,197,189
Jun-20	114,903,339	3,447,100
Jul-20	250,330,852	7,509,926
Aug-20	292,090,393	8,762,712
Sep-20	354,844,167	10,645,325
Oct-20	257,128,176	7,713,845
Nov-20	161,094,871	4,832,846
Dec-20	265,752,275	7,972,568

\*Effective Date - 14th Oct, 2019

## Market Performance

- The adjacent table shows performance ratios for the KSE 100 index for the latest calendar year.
- The price to earnings ratio of the index clocked in at 10.95 per share. Meanwhile, the price to book ratio stood at 1.28 per share. In addition, the Earnings Per Share currently stand at PKR~4,164 per share.
- The return of the KSE 100 index over the 12 month period of CY20 stood at 5.97%.
- Moreover, the total market capitalization of the entire stock exchange stands at PKR~8,298bln.

KSE 100 Indicators	
Ratios	CY20
Price to Earnings (P/E)	10.95
Price to Book (P/B)	1.28
Earnings Per Share (EPS)	4,164
1 Year Return	5.97%
Market Capitalization* (PKR bln)	8,298

\* Market Capitalization is for entire market while other ratios/return is for KSE 100 index

## NET BUY/SELL

Net Buy/Sell (PKR mln)						
Participants	FY16	FY17	FY18	FY19	FY20	1HFY21
Individuals	13,287	-5,526	580	20,796	34,001	26,087
Companies	-9,136	13,354	10,853	14,553	4,245	14,595
Banks / DFIs	-686	-19,648	-1,139	9,009	-8,516	-11,316
NBFC	19,498	-631	-907	-172	707	180
Mutual Funds	3,927	60,460	-3,550	-20,080	-7,792	3,394
Other Organizations	4,144	2,043	8,547	3,423	4,973	507
Broker Proprietary Trading	-2,233	-626	-4,852	-1,801	-2,105	-1,607
Insurance Companies	-	23,142	22,817	17,887	20,179	13,381
<b>LIPI NET</b>	<b>6,430</b>	<b>68,483</b>	<b>32,349</b>	<b>43,615</b>	<b>45,691</b>	<b>45,220</b>
Foreign Individuals	328	-513	256	61	-134	26
Foreign Corporates	-5,512	-70,198	34,936	-44,540	-49,033	-40,191
Overseas Pakistanis	-1,246	2,241	2,351	865	3,477	-5,055
<b>FIPI NET</b>	<b>-6,430</b>	<b>-68,483</b>	<b>32,349</b>	<b>-43,615</b>	<b>-45,691</b>	<b>-45,220</b>

Net Buy/Sell (USD mln)						
Participants	FY16	FY17	FY18	FY19	FY20	1HFY21
Individuals	128	-53	5	166	213	159
Companies	-84	127	100	111	27	91
Banks / DFIs	-6	-187	-10	63	-55	-69
NBFC	188	-6	-8	-2	5	1
Mutual Funds	39	576	-35	-146	-50	20
Other Organizations	40	-19	78	28	32	3
Broker Proprietary Trading	-22	-6	-44	-15	-13	-9
Insurance Companies	0	220	204	150	128	83
<b>LIPI NET</b>	<b>62</b>	<b>652</b>	<b>289</b>	<b>356</b>	<b>285</b>	<b>279</b>
Foreign Individuals	3	-5	2	0	-1	0
Foreign Corporates	-53	-669	-312	-362	-306	-247
Overseas Pakistanis	-12	21	21	6	22	-32
<b>FIPI NET</b>	<b>-62</b>	<b>-652</b>	<b>-289</b>	<b>-356</b>	<b>-285</b>	<b>-279</b>

## 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 specific category by July 2020. The cutoff date for implementation of LC requirement was extended till May 2021 by the SECP.

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 100mIn*	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

\* This will increase to PKR 125mIn from July 1, 2021

# BROKERAGE FIRMS | LOCAL INDUSTRY

## Applicable Tax Laws

### On Brokerage and Commission Income

<b>Section</b>	233 Brokerage & Commission
<b>Responsible Person</b>	Fed / pro/ local Govt company, AOP constituted by or under any law
<b>From Whom</b>	Recipient of brokerage or commission
<b>Nature of payment / Transaction</b>	Brokerage and commission income (Including – resident agents.
<b>Rate</b>	10 % of the amount of payment 5 % in case of advertising agents
<b>Adjustable / Final</b>	Final
<b>Payment of Tax deducted or collected (Rule 43)</b>	Provincial Government - the same day. Other – Within seven days from the end of each week ending on every Sunday
<b>Statements to be filed (Rule 44)</b>	Monthly - within 20 days of end of each month. Annual – within two months of end of financial year. Extension can be sought from Commissioner u/s 165 (4).

### On the Purchase/Sale of Shares

<b>Section</b>	233-A Collection of tax by Stock Exchange			
<b>Sub-Section</b>	<b>233-A (1)(a)</b>	<b>233-A (1)(b)</b>	<b>233-A (1)(c)</b>	<b>233-A (1)(d)</b>
<b>Responsible Person</b>	PSX	PSX	PSX	PSX
<b>From Whom</b>	Member of PSX	Member of PSX	Sellers of shares through members of PSX	Finance through members of PSX
<b>Nature of payment / Transaction</b>	On purchase of shares in lieu of the commission earned by its Members.	On sale of shares in lieu of the commission earned by its Members.	From its Members in respect of trading of shares.	From its Member in respect of financing of carryover trade in shares business
<b>Rate</b>	0.01%of purchase value.	0.01%of sale value.	0.01%of traded value.	10 % of carryover charge
<b>Adjustable / Final</b>	Minimum tax	Minimum tax	Minimum tax	Adjustable
<b>Payment of Tax deducted or collected (Rule 43)</b>	Within 7 days from the end of each week ending on every Sunday.			
<b>Monthly Statements to be filed (Rule 44)</b>	Within 20 days of end of each month.			
<b>Annual Statements to be filed (Rule 44)</b>	Within 2 months of end of financial year.			

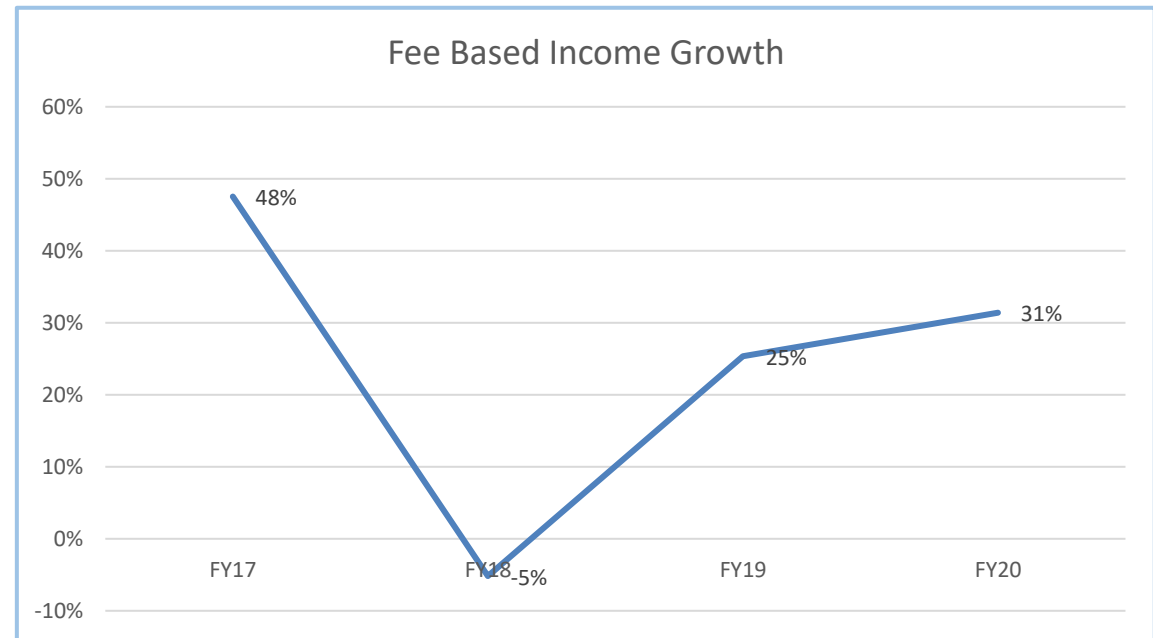


# BROKERAGE FIRMS | LOCAL INDUSTRY

## Business Risk

- This risk 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.
- While the industry’s average fee based income has been volatile, it has remained positive apart from FY18.
- The industry’s fee based income growth stood at ~31% in FY20 as compared to ~25% in FY19. A stable level of growth reflects positively on earnings sustainability and reduced business risk.
- 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 profits from core operations turned positive during the previous fiscal year after facing a dip in FY18.

Industry Average	FY17	FY18	FY19	FY20
Fee Based Income Growth	48%	-5%	25%	31%



*Note: Industry Averages are based on 10 Listed/Rated firms*

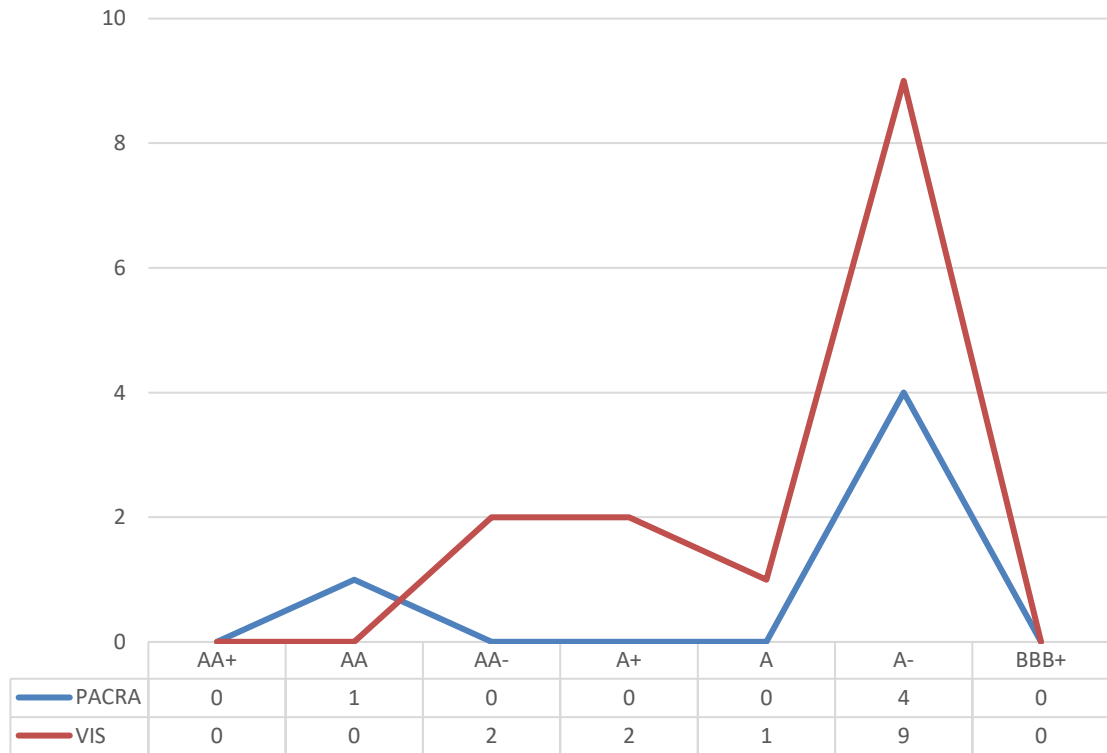
## Financial Risk

- **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 ~32% in FY20 (FY19: ~49%).
- **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 short-term borrowing and trade related liabilities ratio. The industry has an average ratio of 128% in FY20 (FY19: 165%). 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 ~34% during FY20 (FY19: ~39%).

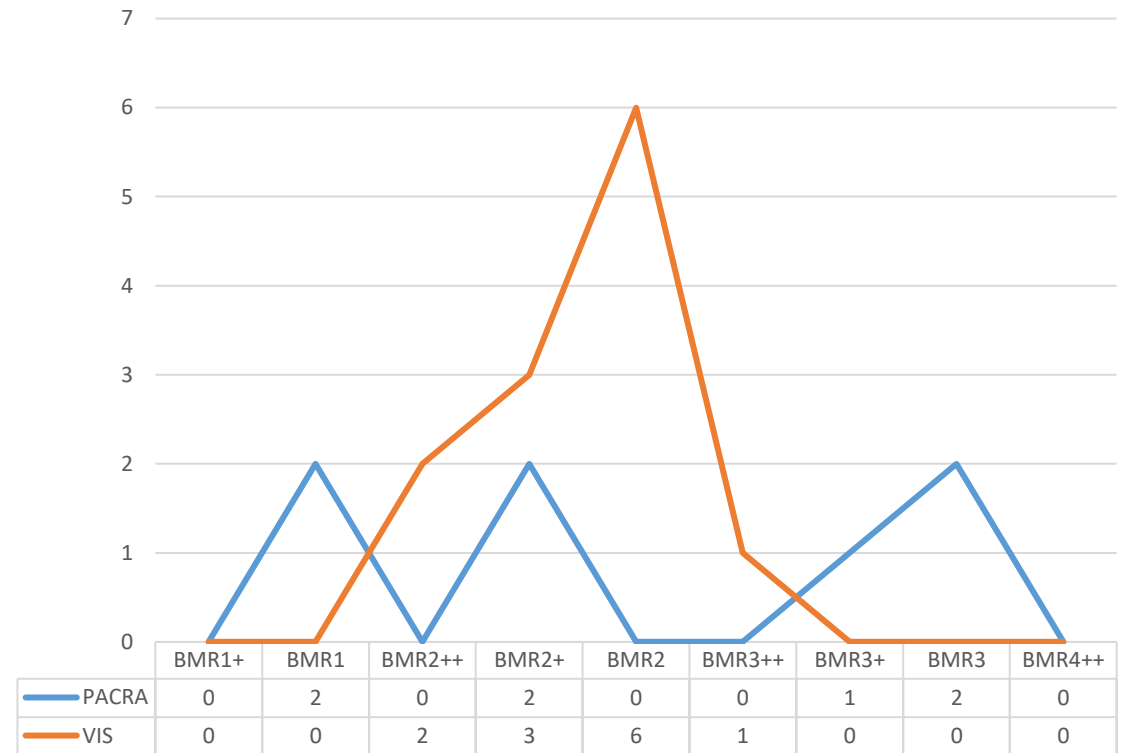
Industry Averages	FY17	FY18	FY19	FY20
Equity Instruments/Investments	24%	28%	49%	32%
Liquid Assets/(STB+Trade Related Liabilities)	109%	74%	165%	128%
Equity / Total Assets	42%	44%	39%	34%

## Rating Scale

### Entity Ratings | PACRA vs VIS



### Broker Management Ratings | PACRA vs VIS







# BROKERAGE FIRMS | LOCAL INDUSTRY

## SWOT Analysis

- Strong regulatory oversight through SECP and PSX.
- Stock market is in recovery phase in the last few months as investor confidence is growing.

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.

- Uncertainty in the market and amongst investors due to second wave of COVID-19.
- Delay in availability of vaccination could hamper economic recovery.

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.

## Outlook: Stable

- The domestic economy has started to gradually recover from the impact of the COVID-19 pandemic which slowed down industrial activities and brought various businesses to a halt.
- Industrial activity has picked up in various sectors with the Large Scale Manufacturing Industries output increasing ~5.46% YoY during the first four months of 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.
- As a result, the stock market has also gradually moved in a positive direction as the economic recovery has picked up due to which investor confidence in the market has also increased. KSE-100 Index return for the month of Dec'20 was recorded at ~7% and is expected to continue growth trajectory in the absence of any major uncertainty. Following a sluggish movement of over two fiscal years, the KSE-100 benchmark has crossed over 45,000 points (*12-Jan-21*).
- The decision taken by the State Bank of Pakistan (SBP) to lower the policy rate by 625bps to 7% in the last quarter of FY20 has lowered the finance costs incurred by brokerage firms.
- The inflation level in the country has also declined. The average inflation rate during the 1HFY21 stood at ~8.74% as compared to an average inflation rate of ~10.7% during FY20. Moreover, the exchange rate is also expected to remain stable in the near future.
- However, there is still significant uncertainty in the market due to second wave of COVID-19 across the globe. While global capital markets are also showing signs of recovery, a strict lockdown or closure of business activities across major economies can have an indirect impact on Pakistan's market where the country's export destinations are concentrated. In addition, there is no clarity regarding timeline as to when vaccines may become available in the country and mechanism to inoculate the general public.

- 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)
- PACRA Database
- Investing.com
- Securities and Exchange Board of India (SEBI)
- BSE India
- Bloomberg
- <https://www.hl.co.uk/news/articles/how-tech-dominates-the-us-stock-market>

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