



NBFIs & Modarabas

An Overview

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NBFIs & Modarabas

Introduction

Non-bank Financial Companies (NBFCs), also known as Non-bank Financial Institutions (NBFIs) are financial institutions that offer various banking services but do not have a banking license. Generally, these institutions are not allowed to take traditional demand deposits—readily available funds, such as those in checking or savings accounts—from the public. This limitation keeps them outside the scope of conventional oversight from federal and state financial regulators.

The NBFIs sector mainly comprises:

- Pension Funds,
- Insurance Corporations
- Other Financial Intermediaries (OFIs) - OFIs include all financial intermediaries that are not central banks, banks, public financial institutions, insurance corporations, pension funds, or financial auxiliaries. They mainly include investment funds, captive financial institutions (A subsidiary financial institution whose primary or sole operation is the provision of credit for customers of the parent company) and money lenders, central counterparties, broker-dealers, trust companies and structured finance vehicles.



Global Overview

NBFIs Across The Globe:

- Total global financial assets were recorded at USD~404trn in CY19 growing by ~6.6% YoY, with the growth of the NBFi sector outpacing that of banks in CY19. The NBFi sector grew by ~8.9% in CY19 to USD~200trn, and the banking sector grew by ~5% to USD~155trn. The NBFi sector accounts for 49.5% of global financial assets, while banks remain the largest single sector of the financial system.
- The Financial Assets of the NBFi Sector accounted for 49.5% of the global financial system in CY19, compared to 42% in 2008 showing an increase of ~7.5% since the global financial crisis. NBFIs play an increasing role in providing financing to the real economy, as well as in managing the savings of households and corporates.

Type	Share of Global NBFi Assets (CY19)
Investment funds (other than MMFs and hedge funds)	24.9%
Insurance corporations (ICs)	17.6%
Pension funds (PFs)	19.6%
Captive financial institutions and money lenders (CFIMLs)	11.4%
Broker-dealers (BDs)	5.2%
Money market funds (MMFs)	3.5%
Hedge funds	2.8%
Structured finance vehicles (SFVs)	2.6%
Finance companies	2.5%
Trust companies	1.9%
REITs	1.4%
Central counterparties (CCPs)	0.3%
Total	100%

In CY20, the global economy suffered due to COVID-19. Since the start of CY21 approval of several vaccines has allowed administrations to ease lockdown measures. It may help economic recovery and sharp rebound has been observed in several regions with China leading from the front. However, the recent resurgence of COVID cases may dampen recover prospects.

In March'20, the GoP rolled out a significantly large stimulus package of PKR~1.24trn that included support for families and businesses hit by the pandemic. The main provisions included: PKR~190bln for Emergency Response; PKR~570bln for Relief to Citizens; and PKR~480bln for support to business and Economy. The package has significantly supported the domestic economic recovery.

Prospects of economic growth have showed visible signs of improvement during Jul-Jan FY21 which strengthen expectations about economic recovery:

Inflation

- Inflation resurged on the back of higher international commodity prices and demand drive in Pakistan. Lately, inflation trend depicts that both YoY and MoM inflation are on a negative trend. The Government implemented policy measures to improve the market mechanism of food commodities and to re-enforce the supply chain of essential food items. These interventions were successful to prevent uptick in prices of daily use items. But with the IMF program active again and rising oil prices during recovery phase of COVID-19, some pressure on prices of essential items will be witnessed. Higher taxes may also lead to inflationary pressure.

Macro Economic Indicators

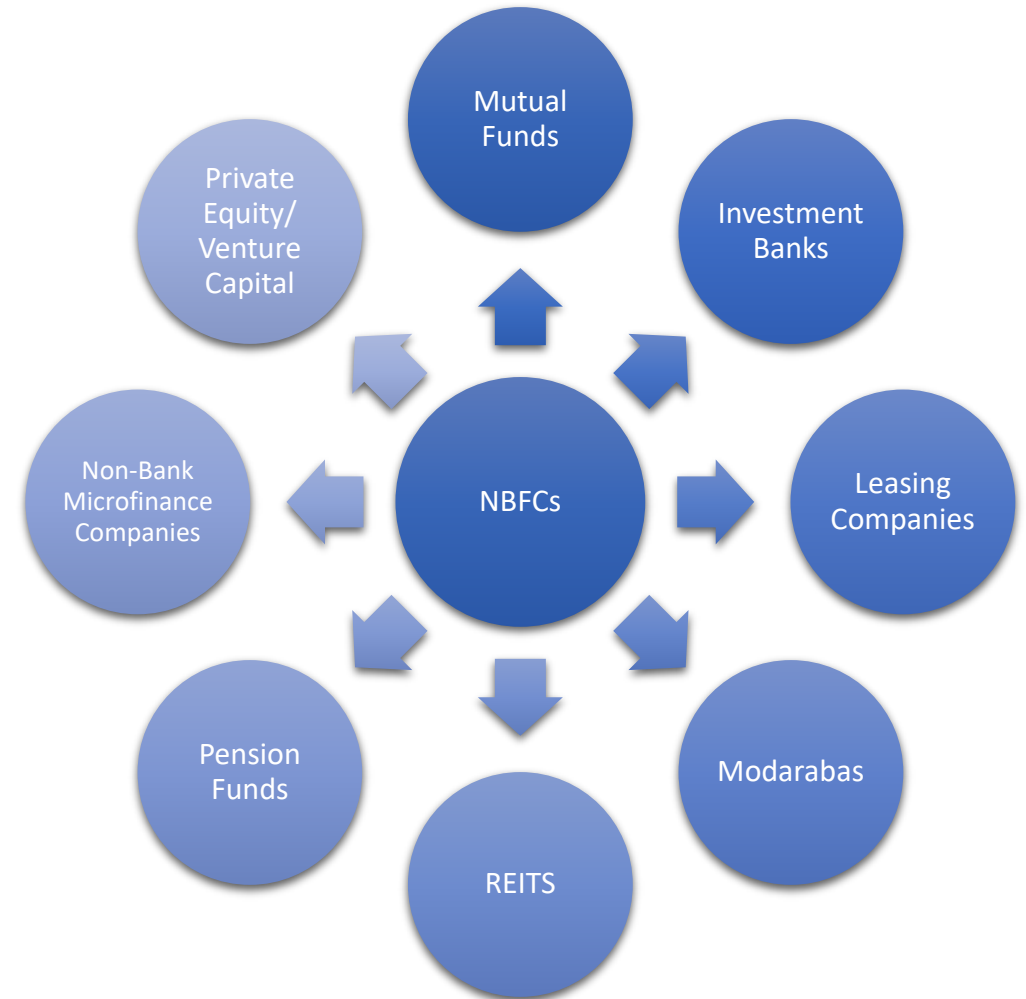
	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	9MFY21
Average Inflation Rate (CPI)	11.90%	11.00%	7.40%	8.60%	4.50%	2.90%	4.20%	3.90%	7.30%	10.70%	8.36%
Average KIBOR	13.45%	12.33%	9.84%	9.88%	8.85%	6.49%	6.11%	6.39%	10.43%	11.95%	7.34%
Monetary Policy Rate (MPR)	13.70%	12.41%	9.91%	9.75%	8.75%	6.04%	5.75%	5.95%	9.69%	11.75%	7.00%
PKRV	13.00%	11.91%	9.63%	9.75%	8.67%	6.34%	5.95%	6.26%	10.20%	11.79%	7.19%
Average Exchange Rate	86.31	89.24	96.83	102.84	101.47	104.37	104.78	110.11	136.45	158.40	162.21
(USD mln)	FY11	FY12	FY13	FY14	FY15	FY16	FY17	FY18	FY19	FY20	8MFY21
Current Account Balance	214	-4,658	-2,496	-3,130	-2,815	-4,961	-12,270	-19,195	-13,434	-2,970	-2,741
Exports	25,369	24,718	24,802	25,078	24,090	21,972	22,003	24,768	24,257	22,507	16,439
Imports	35,796	40,370	40,157	41,668	41,357	41,118	48,001	55,671	51,869	42,417	29,605
Trade Balance	-10,427	-15,652	-15,355	-16,590	-17,267	-19,146	-25,998	-30,903	-27,612	-19,910	-13,166
Foreign Exchange Reserve	18,244	15,289	11,020	14,141	18,699	23,099	21,403	16,384	14,482	18,886	20,105

NBFIs & Modarabas

Local Industry | An Overview

Pakistan’s Non Banking Finance sector consists of conventional and Shariah-compliant non-bank financial institutions namely:

- Modarabas
 - Mutual Funds
 - Pension Funds
 - REITs
 - Leasing companies
 - Investment Finance Services.
- NBFIs and Modarabas provide financial products to individuals and businesses for their financing needs.
 - This Sector Study shall focus on the Asset base of different categories of NBFIs in order of their percentage share in the total NBFIs Assets.

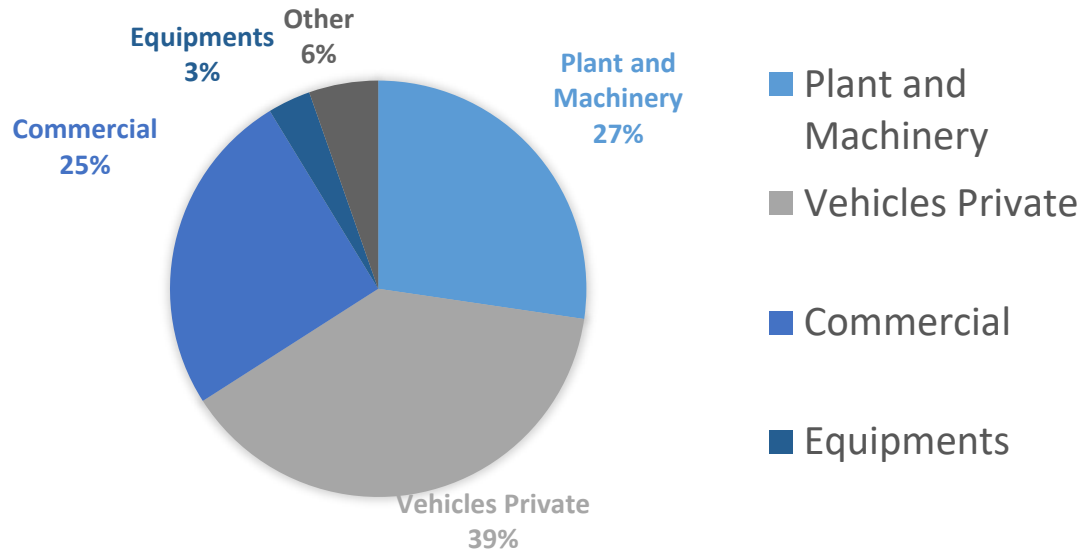


NBFIs & Modarabas

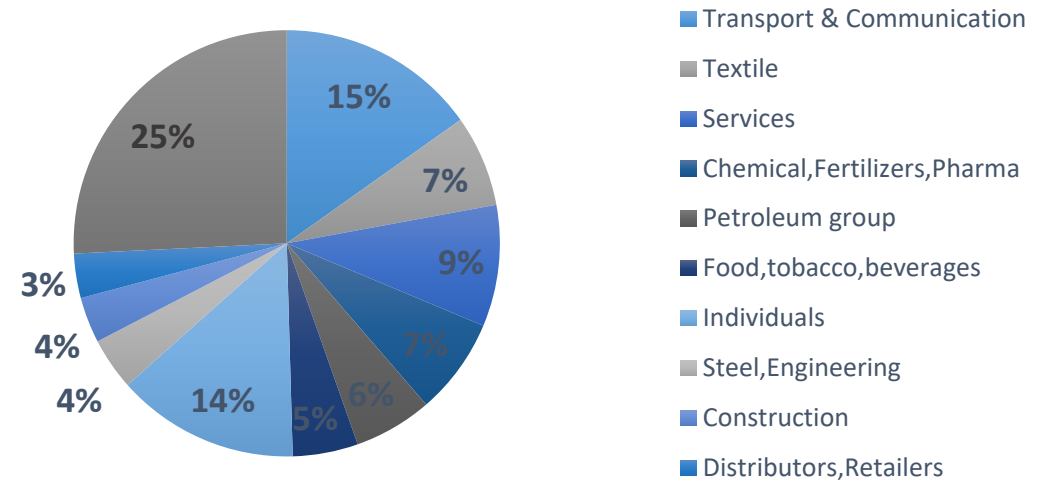
Financing Break-up | Asset Wise & Sector Wise

- NBFIs and Modarabas are essential for the economic development of Pakistan. In Pakistan, there are an estimated 5.2 million small and medium enterprises (SMEs). Their contribution to GDP is estimated to be 40% while that to exports is estimated as 25%¹
- The potential market for SME financing in Pakistan ranges between PKR~3-4trn of which formal finance meets only 15% to 20% while the rest is either financed through informal channels or remains unmet.²
- NBFIs and Modaraba's lending to SMEs was 46% in FY18 and 40% in FY19. This shows that SMEs rely significantly on financing by NBFIs and Modarabas and NBFIs are essential in filling the gap that exists³. Below is the asset and sector wise lending of the Modaraba & NBFC sector during FY19.

ASSETS WISE FINANCING FY19

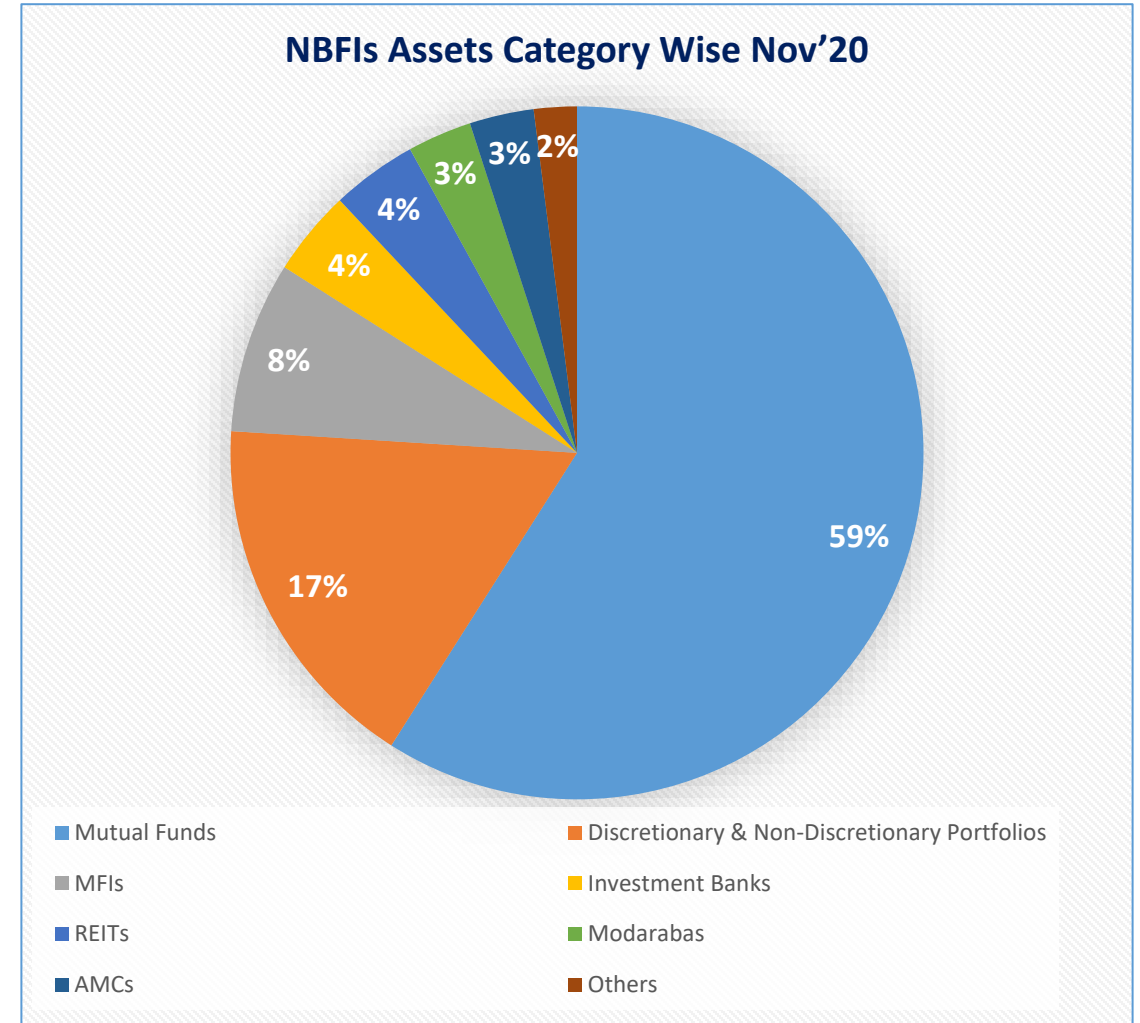
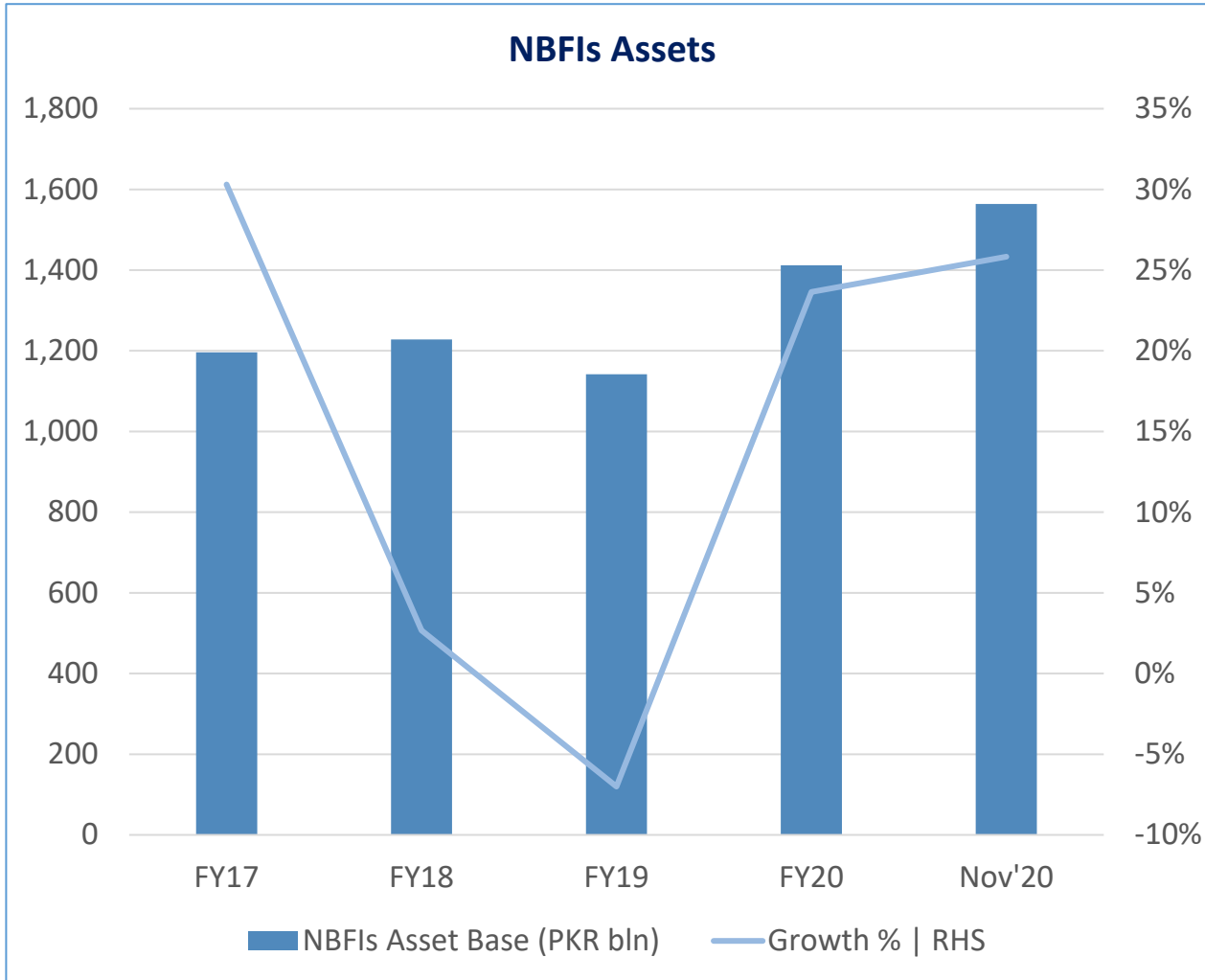


SECTOR WISE FINANCING FY19



NBFIs & Modarabas

Total Assets Break-up



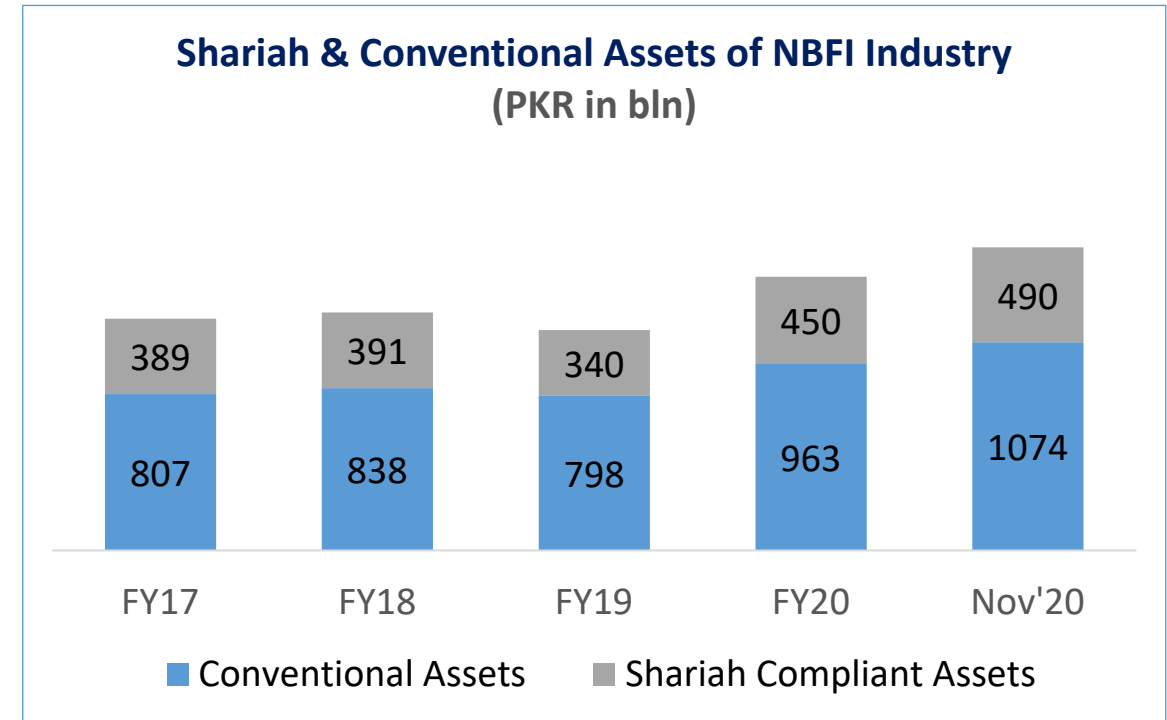
Total Assets

Type	FY18			FY19			FY20			Nov'20		
	No of Entities	Total Assets (PKR in bln)	% Assets Share in NBFCs & Modarabas	No of Entities	Total Assets (PKR in bln)	Assets Share in NBFCs & Modarabas	No of Entities	Total Assets (PKR in bln)	Assets Share in NBFCs & Modarabas	No of Entities	Total Assets (PKR in bln)	Assets Share in NBFCs & Modarabas
Mutual Funds	190	679	55%	203	578	51%	220	802	57%	227	917	59%
Discretionary & Non-Discretionary Portfolios	-	153	12%	-	198	17%	-	229	16%	-	258	17%
Real Estate Mgmt Cos/Trusts	6	47	5%	6	52	4%	8	55	4%	8	58	4%
Asset Mgmt. Companies	21	39	3%	23	37	3%	23	40	3%	23	43	3%
Pension Funds	19	27	2%	19	27	2%	19	31	2%	19	34	2%
Private Equity	4	5	-	7	7	1%	9	7	0	9	8	1%
Investing Institutions Total	240	950	77%	258	899	78%	279	1,163	82%	286	1,318	84%
Non-Bank Microfinance Companies	25	157	13%	26	117	10%	25	122	9%	26	121	8%
Investment Banks	10	58	5%	10	63	6%	12	65	5%	12	64	4%
Modarabas	29	53	4%	28	53	5%	28	51	4%	28	50	3%
Leasing Companies	7	10	1%	6	10	1%	7	11	1%	7	10	1%
Lending Institutions Total	71	278	23%	70	243	22%	72	249	17%	73	246	16%
NBFI's Total	311	1,228	100	328	1,142	100	351	1,412	100	359	1,564	100

NBFIs & Modarabas

NBFIs Assets | Shariah & Conventional

Description (PKR in bln)	FY17	FY18	FY19	FY20	Nov'20
Conventional Assets	807	838	798	963	1,074
Shariah Compliant Assets	389	391	340	450	490
Total Assets	1,196	1,229	1,138	1,412	1,564
Share of Conventional Assets	68%	68%	70%	68%	69%
Share of Shariah Compliant Assets	33%	32%	30%	32%	31%



- Share of Shariah compliant assets has remained almost constant close to ~30% in the past 5 periods. CAGR of Conventional and Shariah assets during FY17-Nov'20 was recorded at 6% and 5% respectively.



NBFIs & Modarabas

Mutual Funds | Overview

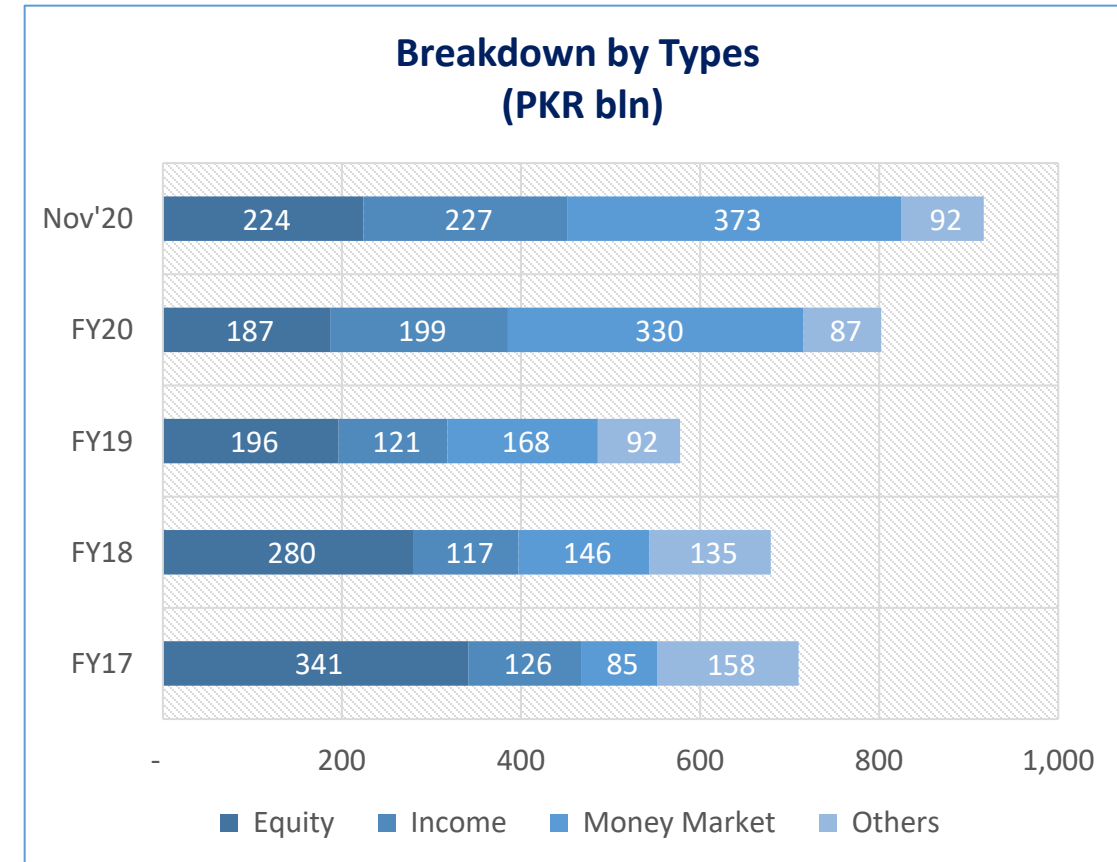
- The share of Mutual Funds Assets in NBFIs and Modarabas was recorded at ~59% as at 30th Nov,20. Mutual Funds hold the highest share in the NBFi assets space with total assets of PKR~917bln (Nov'20). CAGR of Mutual Funds Assets during FY17-Nov'20 was recorded at ~5.3%

Description	FY17	FY18	FY19	FY20	Nov'20
Total Assets (PKR bln)	710	679	577	802	917
Growth (YoY)	29%	-4%	-15%	39%	14%
Number of Mutual Funds	177	190	203	220	227
Number of Plans	51	72	94	89	85
Total Number of Mutual Funds & plans	228	262	297	309	312

NBFIs & Modarabas

Mutual Funds Asset Categories

Description (PKR bln)	FY17	FY18	FY19	FY20	Nov'20
Equity	341	280	196	187	224
Income	126	117	121	199	227
Money Market	85	146	168	330	373
Others	158	135	92	87	92
Total	710	679	578	802	917



NBFIs & Modarabas

Mutual Funds | Investor Accounts Breakup

Description	No. of investor accounts as at Nov 30, 2020	Value of Investment as at Nov 30, 2020 (PKR bln)	% of total Investment Value
Resident			
Individuals	336,179	299	33.63%
Associated Banks/DFIs/AMCs	57	35	3.94%
Other Banks/DFIs	170	12	1.35%
Insurance Companies	320	39	4.39%
Other financial institutions	131	17	1.91%
Other Corporates	2571	330	37.12%
Fund of Funds	58	11	1.24%
Retirement Funds	2595	110	12.37%
Trusts/NGOs etc.	1110	30	3.37%
Foreign			
Individuals	615	3	0.34%
Non-Individuals	16	0	0.01%
Total	343,822	889	100.00%

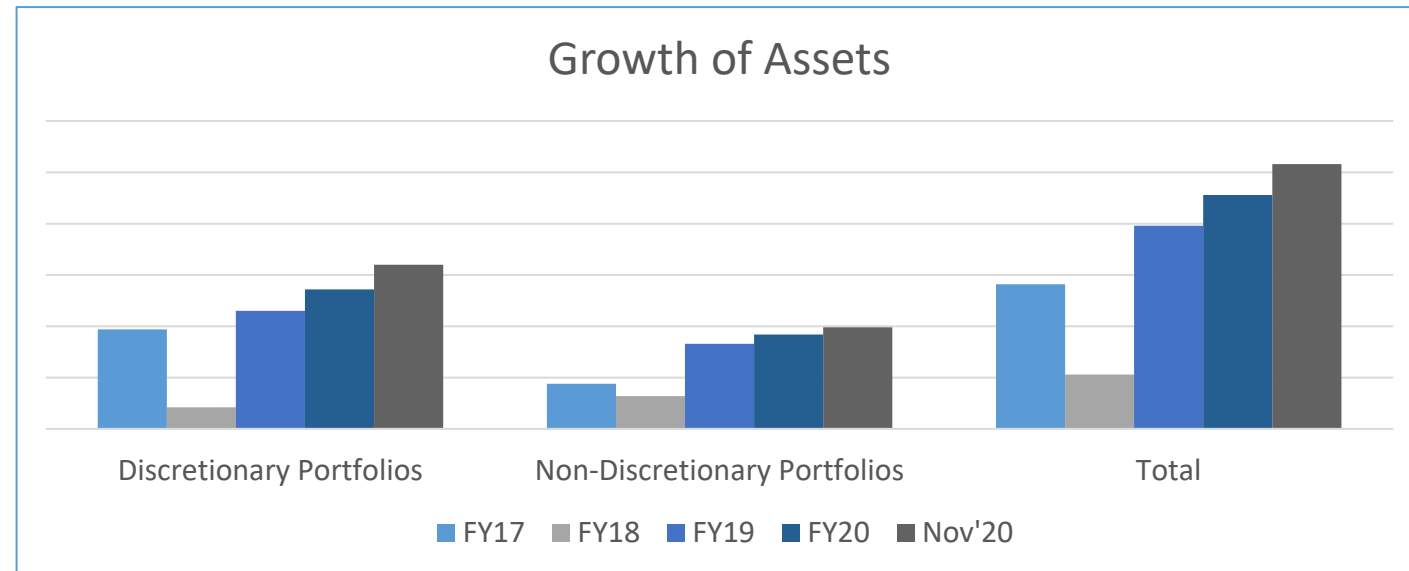
Note The above table shows the number of investor accounts in open end mutual funds only.

NBFIs & Modarabas

Discretionary/Non-Discretionary Portfolio

- In discretionary portfolios, the portfolio manager individually and independently manages the funds and securities of each client in accordance with the needs of the client. Under non-discretionary portfolios, the portfolio manager manages the funds in accordance with the directions of the client.
- In Pakistan these portfolios hold the second highest weight in the NBFIs sector with asse base of PKR~258bln (Nov'20).

Assets (PKR in bln)	FY17	FY18	FY19	FY20	Nov'20
Discretionary Portfolios	97	21	115	136	160
Non-Discretionary Portfolios	44	32	83	92	99
Total	141	53	198	228	258

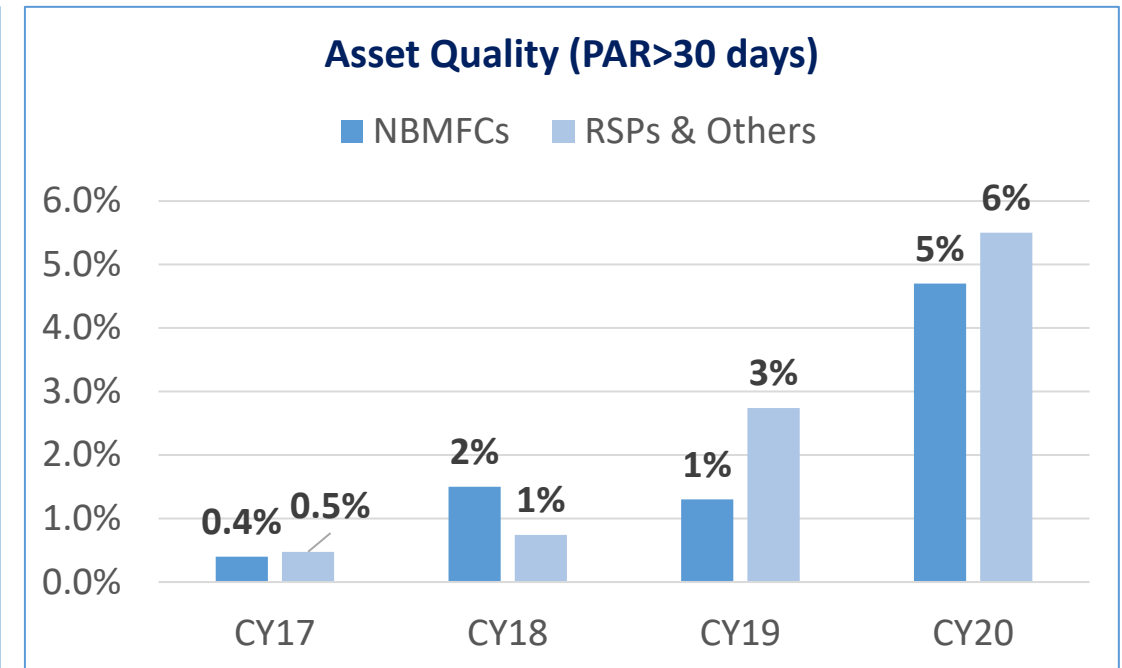
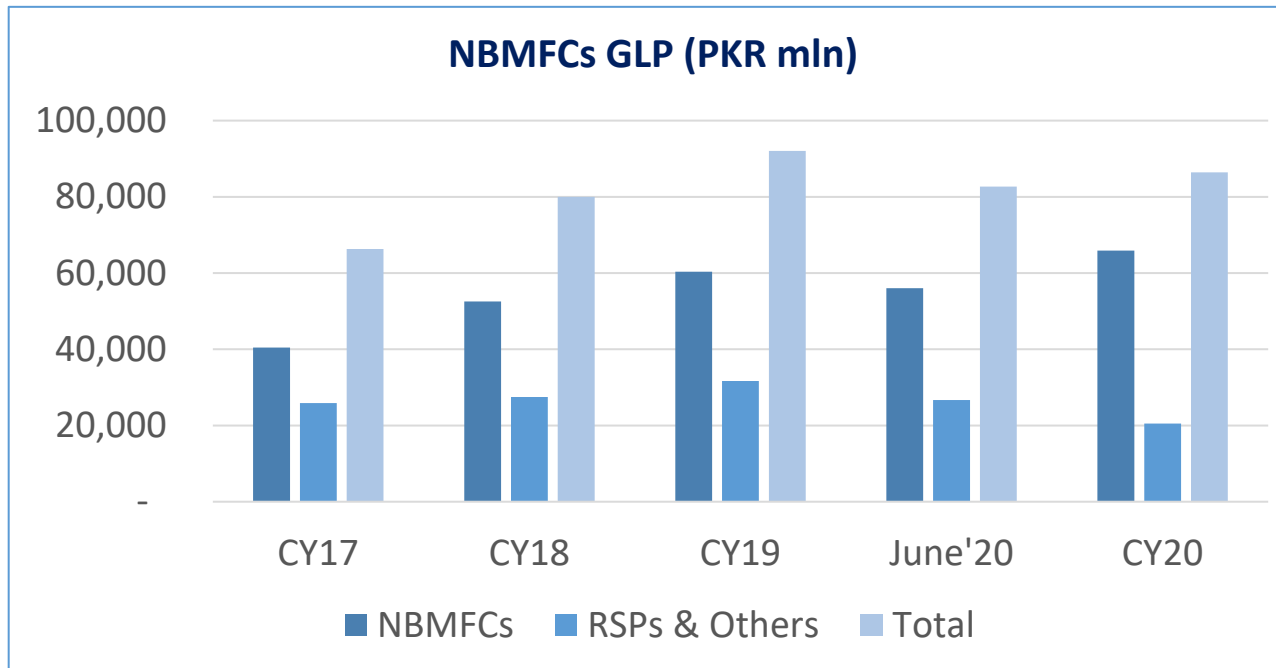


NBFIs & Modarabas

Non-Bank Microfinance Companies (NBMFCs) | Overview

- Non-Bank Microfinance Companies hold the third highest weight by assets in the NBFi sector contributing 8% to the total assets of NBFIs. They are 26 in number and their assets are worth PKR~121bln.
- The Gross Loan Portfolio (GLP) of NBMFCs (including RSPs & Others) was recorded at PKR~86bln in CY20 (PKR~92bln in CY19). The decrease was attributed to the effect of COVID-19.

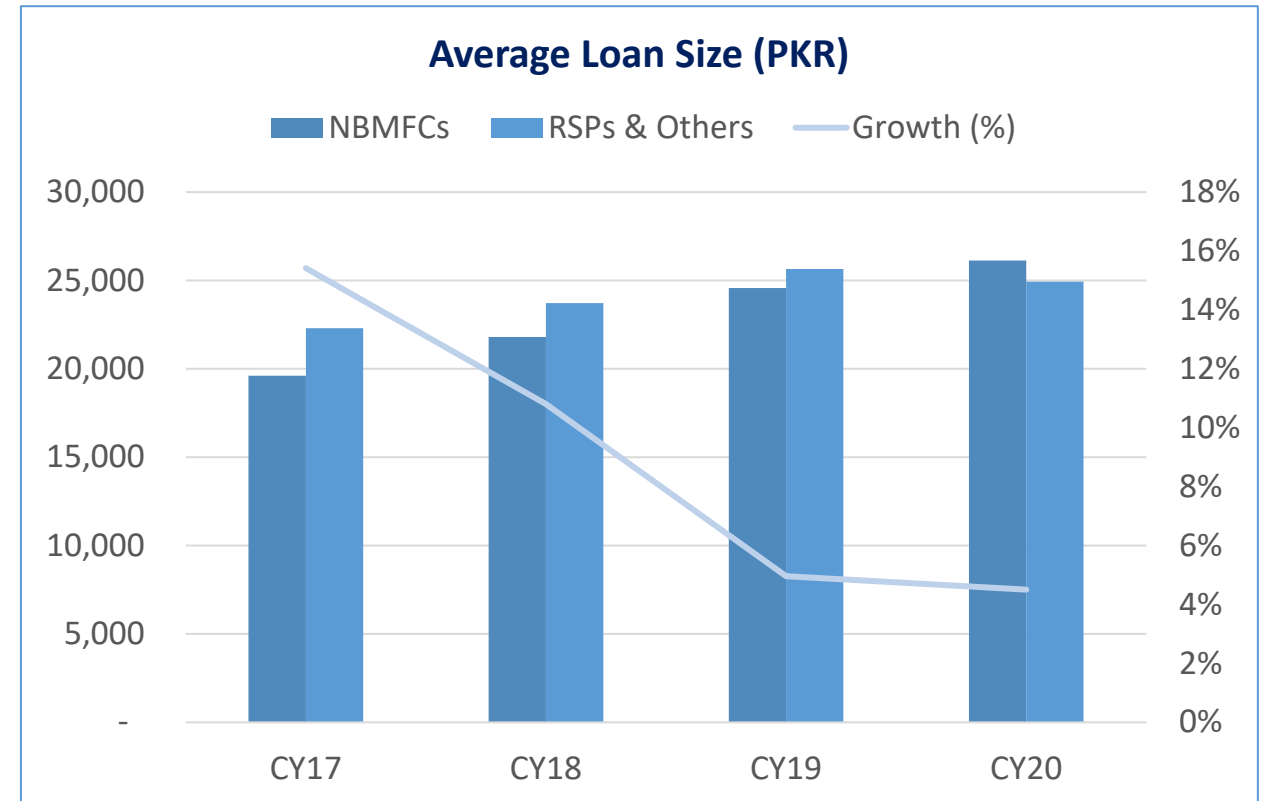
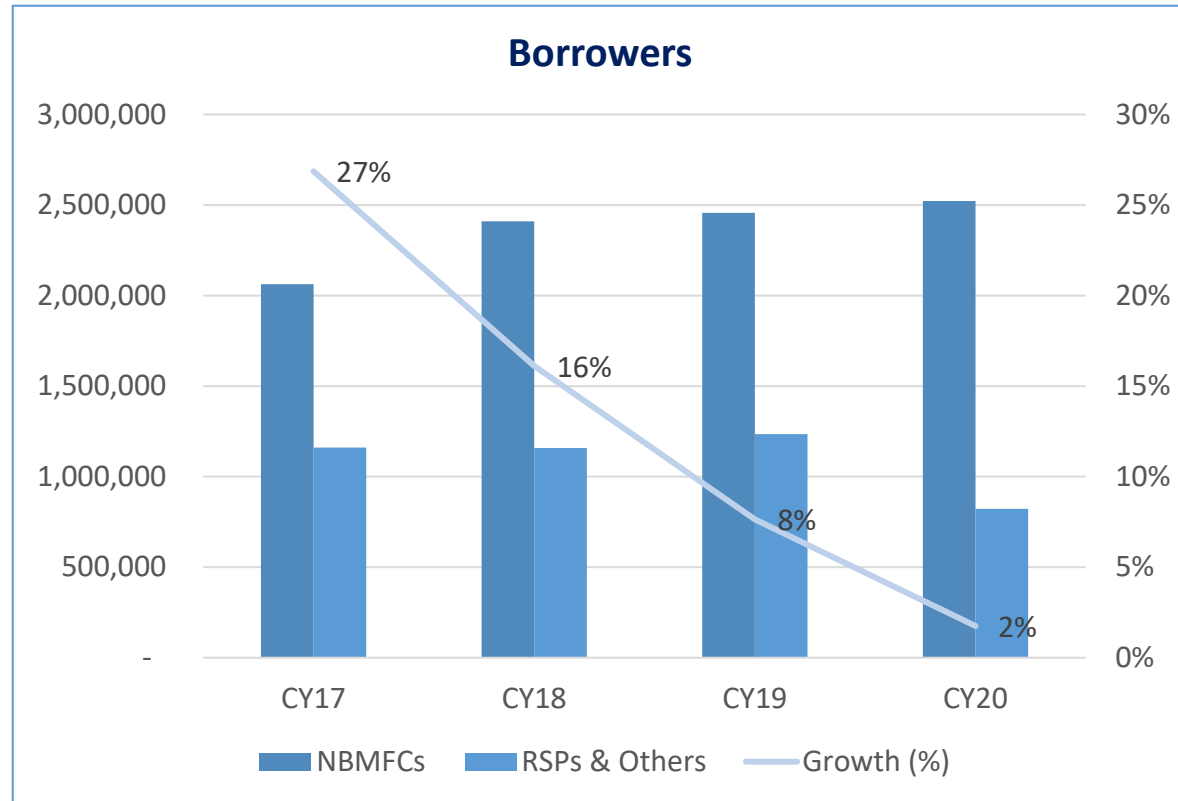
Period	FY17	FY18	FY19	FY20	Nov'20
NBMFCs Asset Base (PKR bln)	122	157	117	122	121



NBFIs & Modarabas

NBMFCs Borrowers and Loan Size

- Total Borrowers of NBMFCs and RSPs were recorded at ~2.5mln and 0.8mln respectively in CY20.
- Average Loan Size for NBMFCs and RSPs is recorded at PKR~26k and PKR~25k respectively (CY20).



- Both Real Estate Management Companies (REITs)/Trusts and Investment Banks hold ~4% share each in the total assets of the NBFIs Industry.
- There are 7 Real Estate management companies in the Sector, 1 Real Estate Trust (scheme) and 12 Investment Banks.
- The assets of only one REIT (Dolmen City REIT) worth PKR~52bln (Nov'20) constitutes ~90% of total asset base of all REITs and shall be used for discussion purpose in this Study.
- The collective asset base of all Investment banks is recorded at PKR~64bln in Nov'20.

Assets (PKR in bln)	FY17	FY18	FY19	FY20	Nov'20
REIT	42	42	46	49	52
Investment Banks*	21	58	63	65	64

*Includes Investment Banks which did not file online returns.

Note. Total assets, total liabilities, equity and deposits, etc. of investment banks increased significantly in February 2018 mainly due to change of license status of one leasing company from leasing to investment finance services

Investment Banks | Asset Breakup and Financial Position

- Asset Allocation of Investment Banks as at 30th November, 2020 is as below:

PKR in mln	Cash & Bank	Investments	Loans & Advances	Lease	Investment Property	Operating Assets	Other Assets	Total
Investment Banks	901	5,955	29,175	14,040	441	3,344	5,044	58,900

- Financial Position of Investment Banks at 30th November,2020 is as below:

PKR in bln	Equity	Liabilities	Total Assets	Equity as % of Total Assets	Liabilities as % of Total Assets
Investment Banks*	29	26	59	49%	45%

*Note: Information pertaining to two Investment Banks, which did not file online returns, is not included in above table
Equity and liabilities do not include deficit / surplus on revaluation of fixed assets



In Pakistan Modarabas operate under a unique model with the following features:

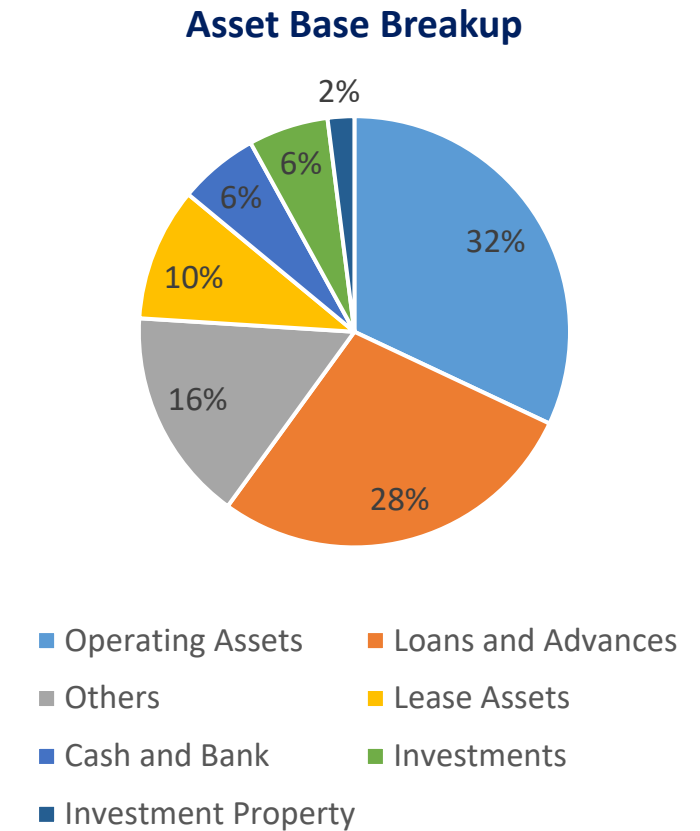
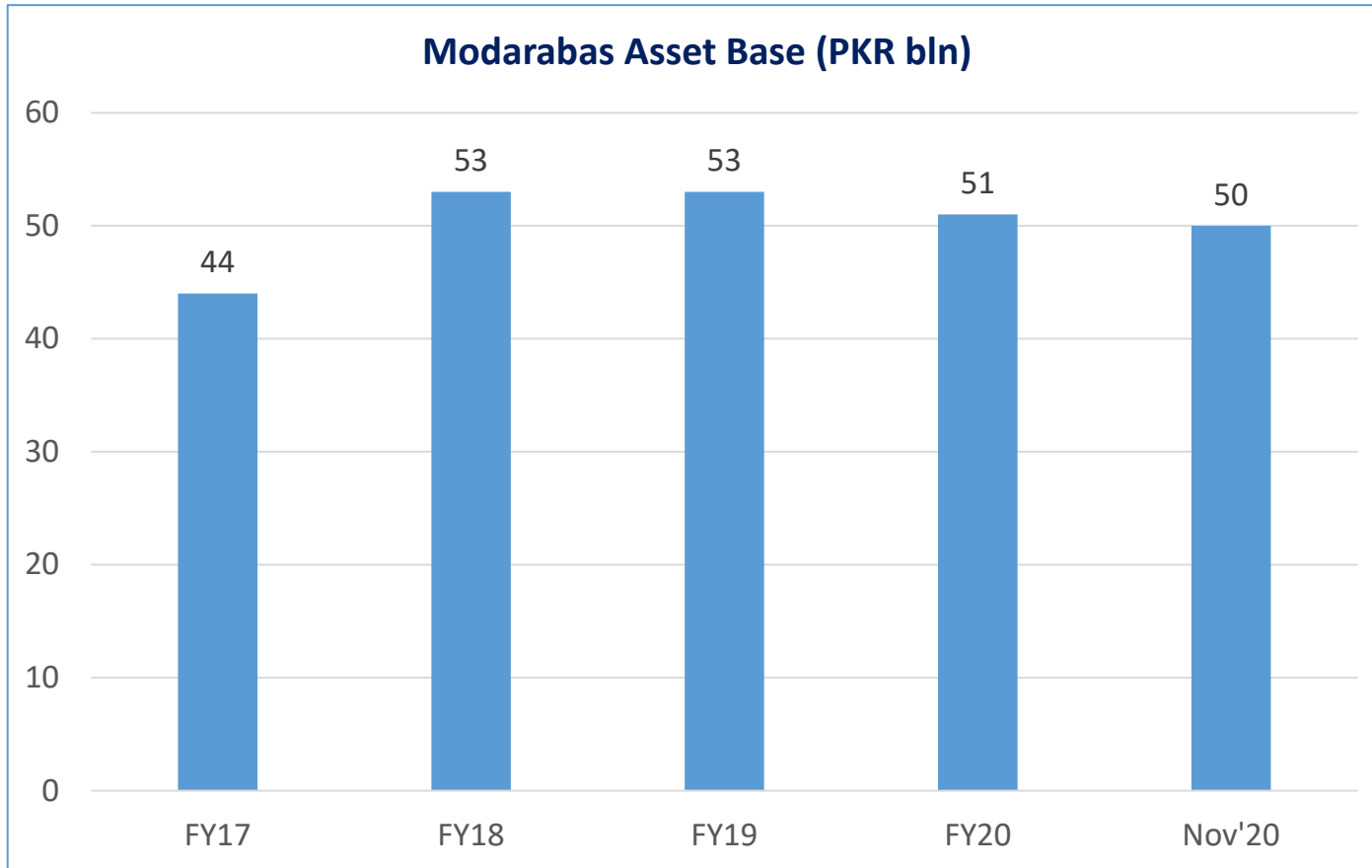
- Modarabas are allowed to offer any financial product or conduct any business based on Islamic concept provided it is Shariah compliant and approved by the Religious Board.
- Modarabas can invest in stock markets, trading of halal commodities, project financing activities etc.
- Modarabas can raise funds in the form of Certificates of Modaraba and Certificate of Musharaka. Modarabas can also issue Sukuk and Musharaka based TFCs.
- In multipurpose Modarabas, transactions are based on Ijarah, Musharaka, Diminishing Musharaka, Murabaha, Musawama, Salam and Istisna, whereas specific purpose Modarabas are designed to handle nominated projects.



NBFIs & Modarabas

Modarabas | Assets

- In Pakistan, there are a total of 28 Modarabas with an asset base of PKR~50bln (Nov'20). Total Assets of Modarabas have remained stagnant over the years and show no promising signs of growth. Asset base of Modarabas have grown at CAGR ~3% since FY17.



AMCs, Pension Funds & Others | An Overview

- Asset Management Companies, Pension Funds, Leasing Companies and Private Equity companies are also an integral part of the NBFIs of Pakistan and hold 3%, 2%, 1%, 1% share of total assets. Asset Management Companies are 23 in number and have assets of PKR~43bln.

Pension Funds:

Trend of Total Assets

PKR bln	FY17	FY18	FY19	FY20	Nov'20
Pension Funds	26	27	26	31	34

Trend of Category Wise Position of Total Assets

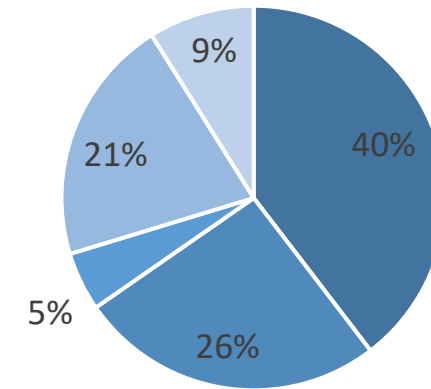
PKR bln	FY17	FY18	FY19	FY20	Nov'20
Equity Sub-Fund	15	14	11	11	13
Debt Sub-Fund	7	8	8	9	9
Money Market Sub-Fund	4	5	7	11	12
Commodity Sub-Fund	0.17	0.14	0.18	0.25	0.27
Total	26	27	26	31	34

NBFIs & Modarabas

Pension Funds | Shariah Vs Conventional

Description (PKR in bln)	FY17	FY18	FY19	FY20	Nov'20
Shariah Compliant Pension Funds	16	17	17	20	22
Conventional Pension Funds	9	10	10	11	12
Total Assets	25	27	27	31	34
Share of Shariah Pension Funds	64	64	64	64	65
Share of Conventional Funds	36	36	36	36	35

Breakdown of Assets Nov'20



- Equities
- Govt Securities
- Debt Securities
- Bank Balances
- Other Assets

- CAGR of Shariah Pension Funds and Conventional Pension Funds from FY17-Nov'20 was recorded at ~7% and 6% respectively.

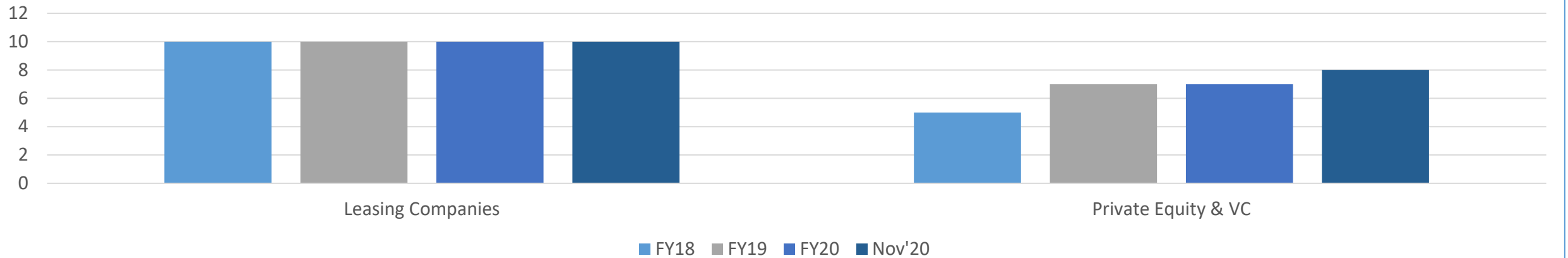
NBFIs & Modarabas

Leasing Companies & Private Equity | Assets

- Leasing Companies and Private Equity/ Venture Capital Funds have 1% of total assets each, they hold PKR 10 billion and PKR 8 billion worth of assets.
- There are 7 leasing companies and 9 Private Equity/ VC funds.

Assets (PKR in bln)	FY17	FY18	FY19	FY20	Nov'20
Leasing Companies	43	10	10	10	10
Private Equity & VC	-	5	7	7	8

Assets Trend (PKR bln)



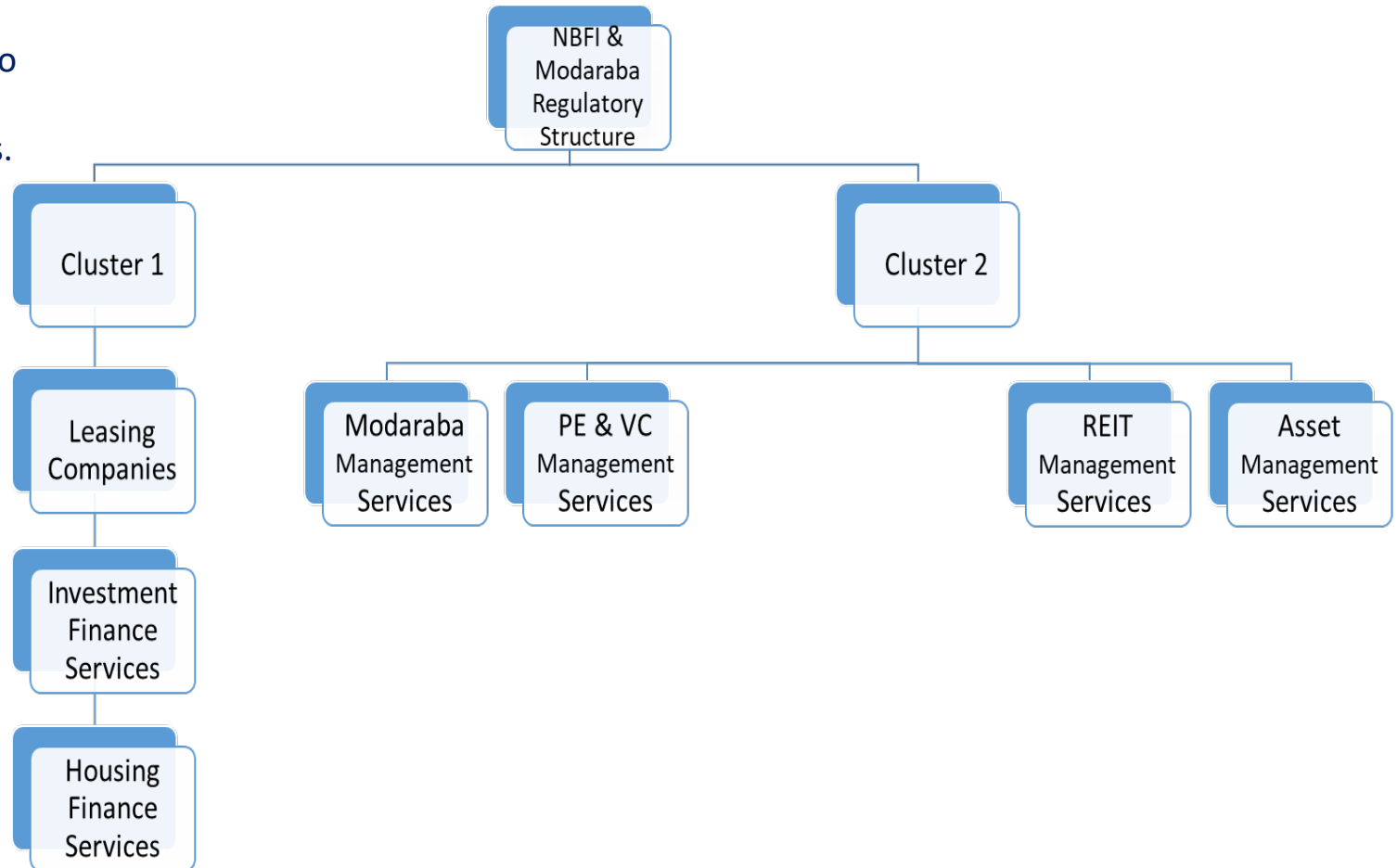
NBFIs & Modarabas

Regulatory Framework

The Sector Structure of NBFIs as per SECP is divided in two Clusters: Cluster 1 is for non-banking financial services while the second cluster is for fund management services.

Modarabas are observing all laws and regulations promulgated in the following:

- Modarabas Ordinance, 1980 (updated 2012)
- Modaraba Companies and Modaraba Rules
- Prudential Regulations (updated 2008)
- Shariah Compliance and Shariah Audit Mechanism (SCSAM)



Latest Developments

REITs

SBP has now made changes to certain provisions of existing Prudential Regulations for Corporate & Commercial Banking to encourage enhanced participation and investment of banks/DFIs in the Real Estate Investment Trusts (REITs). The specified parameters for REIT schemes under the previous regulations tended to encourage developmental REITs and large-sized rental REIT schemes. The new regulations tend to encompass the whole spectrum of schemes

- Entry barriers have been lowered whereby capital requirements for starting an RMC have been revised downwards from PKR 200 million to PKR 50 million. Limits on single investor ownership of fund units (IPOs capped at 5 percent and Pre-IPOs at 10 percent of fund units) has been done way with to facilitate admission of large-scale REIT projects. Concept of strategic investor has been introduced making RMC and the strategic investors the fallback entities which are to hold the specified investments units in blocked accounts until the winding up of the scheme. The scheme's fund size has been linked with the listing regulations of the relevant exchange.
- Utilization of customer advances has been capped to a percentage of construction cost as specified in the business plan and offering document. Unsecured borrowing for capital expenditures and to meet cost overruns has been permitted to the extent of 30 percent of land/real estate value. This resulting reliance on capital market for liquidity is expected to deepen capital markets and protect unit holder's right on the underlying property as it avoids excessive leveraging of a high-ticket business.

NBMFCs/Modarabas

In CY20, SECP allowed NBMFCs to defer repayment upon written request of principal loan before 30th Sep,2020 amount by one year provided that the borrower will continue to service the mark-up amount as per agreed terms and conditions.

Latest Developments

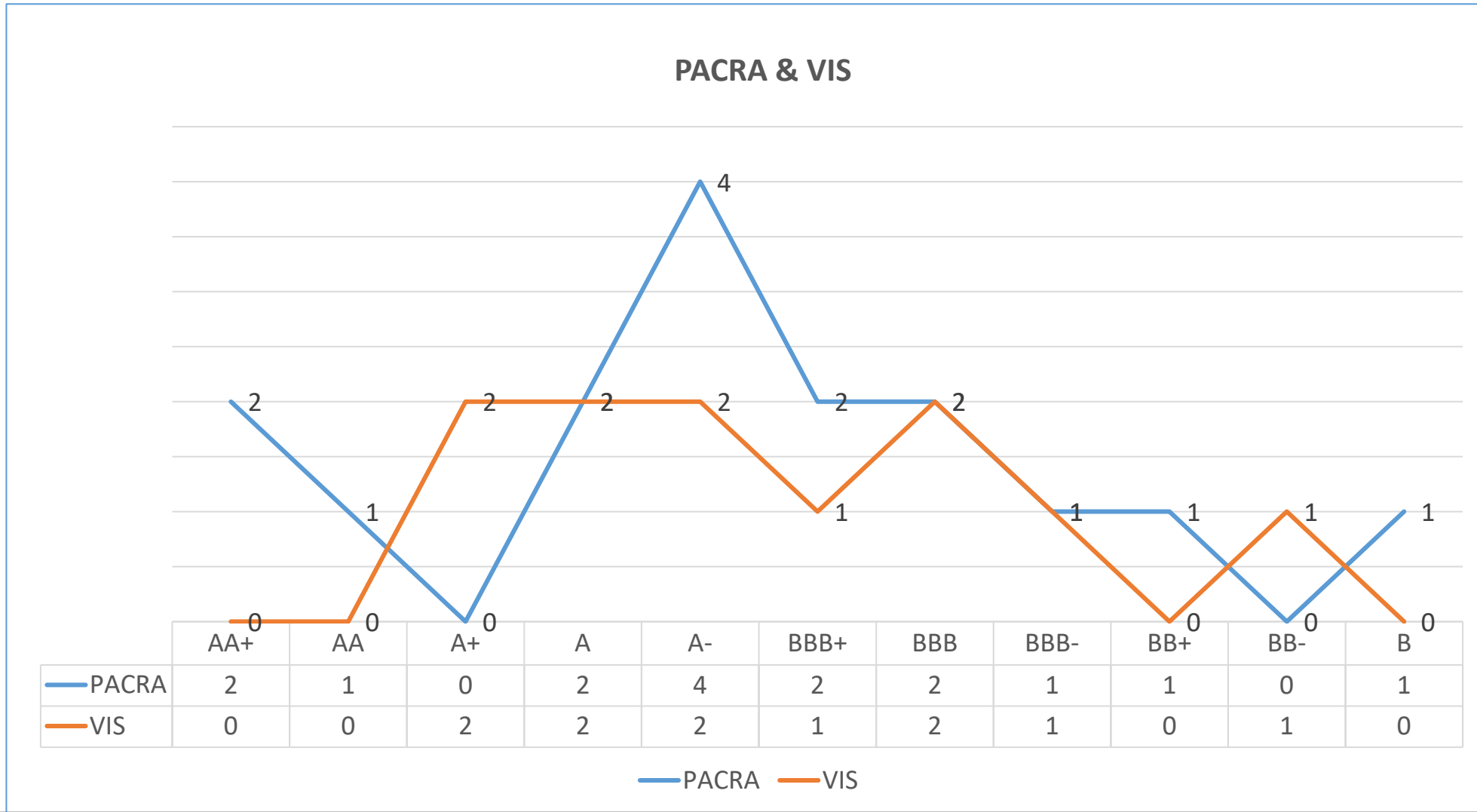
The financing facilities of such borrowers who were unable to service the markup amount or needed deferment exceeding one year, was also allowed to be rescheduled/restructured. If the restructuring was done within 90 days of the loans being overdue in case of NBMFCs and within 180 days of the loans being overdue in case of other financing facility, such facilities were continued to be treated as regular and reported in the ECIB accordingly. The aforesaid relaxations expired on March 31, 2021. Afterwards, the prevailing provisions of NBFC Regulations have been applicable, which makes it critical to assess the actual credit quality of the lending institution in the ongoing period.

AMCs & Mutual Funds

In CY20, SECP extended time to AMCs for compliance with requirements for assessing suitability and Risk Categorization of Collective Investment Schemes till 24th July,2020 as they were facing challenges due to COVID-19. Time period for submission of quarterly financial statements was also extended and time to ensure compliance with minimum fund size requirement was increased to 180 days for open end schemes.

Income Tax Amendment Bill 2021: Following the approval of 'The Income Tax Second Amendment Bill 2021' income tax exemptions available to Modaraba companies, Real Estate Investment Trusts (REITs), Pakistan Mortgage Refinance Company, Venture Capital Funds, and IT services and IT-enabled services will be withdrawn. Moreover, the collective investment schemes will also be subject to normal tax. The impact of this change is yet to be determined.

Rating Curve



Including NBMFCs



NBFIs & Modarabas

SWOT Analysis

- Organized Sector with listed players.
- Major share in lending to SMEs
- Offers smaller investors access to professionally managed and diversified portfolios.
- There is a large variety of funds and investors who can make choices according to their specific objectives.

Strengths

Weaknesses

- Slow growth rates
- High Management Fees
- Lack of awareness for potential investors and borrowers
- Low financial inclusion

- Mainstream banks have the might to take away business.
- Market Risks
- Asset Quality Deterioration for Small Lenders in times of crisis.

Threats

Opportunities

- Ample room to grow.
- Introduction of new products, such as Exchange Traded Funds.

Outlook: Stable

- The Modarabas & NBFIs sector outlook remains stable keeping in view its historical performance. Although there is still sufficient room to grow for the industry, the pace is still slow. The Industry's total assets have grown at a single digit growth rate (6% since CY18).
- Since CY18, Microfinance institutions have lost assets at a compound annual rate of 6%, which is critical as NBMFCs hold the third highest weight in total assets in the industry. This decline can be attributed mainly to higher NPLs and provision losses. Overall, lending Institutions combined have shed 3% which has been absorbed by Investing Institutions overtime.
- Investing Institutions have gained at a CAGR of 9% since CY18 and major contribution comes from Mutual funds which have the highest share in the overall asset base of the industry, gaining 8% even in challenging conditions with regards to the equity market. Discretionary & Non Discretionary portfolios gained 14% during the period which is the highest change among all categories.
- Analyzing the number of players in the lending space there has not been much change i.e. this shows that the traditional players have held on strongly. Similarly, considering the number of players in the investing institutions category, excluding number of mutual funds, there is not much change other than in REITs and Private Equity companies. However, they have a small portion of assets and make up only 5% of total assets of the industry. This also predicts that there is room to expand as the advent of digitization and rise of e-commerce as well as easier access presents several opportunities.
- Going forward, the sector's performance indicators are expected to remain stable considering the trend reflected in the past performance which has well absorbed economic shocks in the long run.

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