CEO Review

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Industry Overview

A weak economic landscape dominated FY 2019, with the Government missing all major targets including GDP growth, inflation, revenue collection, budget deficit, savings and investments by a wide margin. Economic challenges dominated with pressures on the fiscal and external account impacting growth momentum. GDP growth slowed down to 3.3%, lowest since 2008 which was primarily a consequence of drastic, but warranted stabilization measures undertaken by policy makers to arrest widening macro-imbalances (i.e. Current Account and Fiscal Deficits). Sector-wise, all major macro constituents considerably underperformed, with agriculture, industrial and services sectors registering paltry growth of 0.85% YoY, 1.4% YoY and 4.7% YoY against respective targets of 3.8% YoY, 7.6% YoY and 6.5% YoY. Pak Rupee lost more than one third of its total value during FY 19 and closed at Rs. 160 after hitting an all-time low of Rs. 164. Inflation rose considerably to 7.3% in FY 19 due to the lagged impact of exchange rate depreciation, hike in fuel and food prices. Keeping in view the rising inflation, high CAD and slow pace of fiscal consolidation, the State Bank of Pakistan (SBP) raised the policy rate to 13.25% reflecting a cumulative increase of 750 basis points. The PSX 100 index continued its losing streak and closed at 33,901 points in June 2019 which brings CYTD/FYTD market return to (8.5)% & (19)% respectively with low volumes, showcasing the worst equity market performance in a decade.

The impact of this bleak economic environment was seen in the mutual funds industry. The total assets under management (AUM) of the mutual fund industry stood at PKR 540 bn, depicting a decline of 11.5% over the last year. A lot of switching was seen from equity funds towards money market funds as the equity markets continued to plummet while the rising interest rates improved the money market fund returns. Despite the shifting between categories, a net outflow of PKR 23 billion was also seen in the industry. During the year, the industry also witnessed a launch of 37 new funds under Shariah Compliant Equity, Shariah Compliant Fund of Funds, Shariah Compliant Fund of Funds- CPPI, Shariah Compliant Money Market, Shariah Compliant Asset Allocation, Shariah Compliant Income, Conventional Fund of Funds - CPPI, Capital Protected- Income, Equity, Income and Asset Allocation category, 4 funds matured and 2 were converted from Closed-End Funds to Open End funds during the year.

As at June 30, 2019, there were 19 Asset Management Companies managing 290 funds including Open End, Closed-End funds and Voluntary Pension Schemes with PKR 512.83 bn in open-end funds, PKR 1.24 bn in closed-end funds, PKR 25.89 bn in pension funds, PKR 114.61 bn in discretionary and PKR 83.02 bn in non-discretionary portfolios.

Voluntary Pension Schemes remained around PKR 25 bn for the third year with PKR 9.1 bn in conventional and PKR 16.7 bn in Shariah compliant category. A net inflow of PKR 1.25 bn was witnessed, mainly in the Shariah Compliant VPS funds. This year the catch-up incentive of additional tax credit for persons over the age of 45 expired and the inflows are expected to further decline in the coming years unless the Government and Regulatory bodies focus on developing and growing this product.

Around 56 Thousand individual investor new accounts were added during the year primarily in the Equity Funds. 24 Thousand additional accounts pertain to the opening of the two closed-end funds into open-end funds during the year. In percentage term, the holding of individuals in open-end mutual funds in term of AUMs (excluding fund of funds) has increased slightly and now stands at 40.07% versus 38.05% the last year.

Key Regulatory developments during the year to promote growth of the Mutual Funds Industry

A very proactive approach was continued by the Securities and Exchange Commission of Pakistan (SECP) and 8 meetings of MUFAP's Board were held with the Chairman SECP, Commissioner Specialized Companies Division (SCD) SECP and SCD Team over the year leading to a resolution of a number of long outstanding issues as well as initiating discussions on new matters. We strongly believe that continued interaction between SECP and MUFAP would be mutually beneficial in the development and growth of this industry and enable us to address issues at the very start and move forward in a progressive manner.

- **Key Amendments in the NBFC Regulations 2008**

SECP over the year notified some key amendments to NBFC Regulations 2008 in consultation with MUFAP. These include enhancing the expense ratio cap for equity funds from 4% to 4.5% of the net assets, removing all sub caps particularly regulatory caps imposed on the management fee within the expense ratio. In addition to facilitate the expansion of outreach of mutual funds, AMCs have been allowed to charge Selling and Marketing expenses including Alternative Delivery Channels expenses to all categories of funds without any time and sub-limit.

Further, to reduce the operational burden on AMCs the Commission has also removed different requirements of regulatory approvals for mutual funds. AMCs are now allowed to make changes in Constitutive Documents (other than changes in the Fundamental Attributes of the fund) including the changes with respect to change of regulatory requirements without the approval of the Commission. Separate requirement for approval of the Commission for appointment of trustee of each new CIS has also been withdrawn. The validity of the Commission's approval for constitutive documents has been extended from 60 days to 120 days.

The SECP also took a major step in significantly reducing its annual monitoring fee for mutual funds which will improve investor returns and allow the AMCs to spend more on marketing and awareness activities.

MUFAP also did a comprehensive review of the entire NBFC Regulations 2008 and proposed amendments on the same which were comprehensively discussed with SECP and a final version was agreed upon. The same were notified by SECP in June and October 2019.

- **Voluntary Pension Schemes**

In VPS, the Pension Fund Manager is again allowed to charge front end fee on subsequent contributions made by participant directly, through employer or online maximum up to 3%.

MUFAP has also done a comprehensive review of the VPS Rules and related circulars and shared our proposed amendments with SECP. A meeting has been held to discuss and finalize the same.