CEO Review

Ms. Mashmooma Zehra Majeed, CFA, FRM

Chief Executive Officer, Mutual Funds Association of Pakistan

The financial year 2014-2015 continued on the same pathway that was initiated three years ago by the Government through its inconsistent tax policies which has severely affected the growth of the industry. MUFAP is persistently engaged with the SECP and the Government towards addressing these industry issues.

The assets under management slightly increased from PKR 416 billion on June 30, 2014 to PKR 443 billion as on June 30, 2015 after touching a high of PKR 520.61 billion in April 2015.

Economic Review

The economic growth remained broad based. According to provisional estimates the GDP growth during 2014-15 remained at 4.24% as compared to last year 4.03% (based on revised estimates).

Savings and Investments:

Savings improved slightly to 14.5% of the GDP as compared to revised rate of savings to GDP of 13.7%. This however is extremely low as compared to the region and the world (as per the table below) and indicates that rigorous steps are required to promote savings and investments with major focus on investors' awareness and education as well as removing the taxation anomalies and regulatory issues hampering the growth. The Government should encourage long term investments and take measures to incentivize the long term savings.

IMF Estimates

Economies	Savings	Investment
(averages)	*% of GDP*	
World	25.6	25.2
Advanced Economies	21.5	20.8
Emerging Market and Developing Economies	31.9	31.9
Emerging and Developing Asia	42.1	40.0
Middle East, North Africa, Afghanistan, and Pakistan	23.6	25.9

Source: (IMF WORLD ENOCOMIC OUTLOOK - October 2015)

Pakistan's savings rate is much lower than that of the other countries in the Sub continent, namely India at 29.3% and Bangladesh at 28.9%

Capital Markets Review

Equity:

The KSE-100 Index closed at 34,399 points up 16.01% from the last year, making 2014-15 the sixth consecutive fiscal year when the stock market performance remained positive. The KSE-100 Index outperformed most of its regional peers, gold, and average deposit rates by approximately 10%, 22% and 9%, respectively, over the fiscal year.

Debt:

The interest rates continued on its downward trajectory with the policy rate being reduced to 7.0% percent by May 2015. This has been further reduced to 6% in September 2015.

The growth of the economy is directly linked with the well developed corporate bond market which serves as an additional avenue for raising funds to meet their financing requirements. This avenue however remains majorly untapped with not much significant issues being introduced during the year.

Impact of the Budget FY16:

New tax measures introduced continue to target existing tax payers more than bringing new segments into the tax net. For equity investors, the budget was negative as higher than anticipated taxes were imposed on investors and listed companies in the form of 1) higher Capital Gain Tax (CGT), 2) higher tax on dividends, 3) one time super tax on corporate and 4) additional taxes on Banks.

Mutual Funds Industry Review

The assets under management slightly increased from PKR 416 billion on June 30, 2014 to PKR 443 billion as on June 30, 2015. The change in the taxation policies again lead to a decline in the AUMs with a substantial outflow being witnessed in the money market and income categories during the last month of the fiscal year.

Investors remained vary of the Equity category which received net inflows of PKR 2.69 billion only despite showing an average industry return of 21.73% during the year vs a 16.01% return of the KSE 100 Index. Shariah Compliant equity funds continued to remain the investors preferred mode of investment as this category received net inflows of PKR 16 billion during the year.

Voluntary Pension Schemes continued on its path with another asset management company introducing the VPS, bringing the number of VPS manager to 9 and the VPS funds to 17 (both conventional and Shariah Compliant). The VPS registered net inflows of PKR 3.5 billion during the year.

Nineteen Thousand new individual investors' accounts were added during the year. Due to unavailability of the unique identification data, it is difficult to determine the actual numbers that were added. In percentage terms, the holding of individuals in open-end mutual funds in terms of AUMs now stands at 33% which was 25% last year. Retirement Funds holding has increased to 13% as compared to 10% last year.

In terms of returns, all the categories of the mutual funds posted market based returns which were above the respective benchmarked returns. The next challenge for the Industry is to now create awareness amongst the masses about the features and benefits of saving through mutual funds and pension schemes.

Impact of the Budget FY16

Separate tax rates for dividend and capital gains from mutual funds were introduced this year, increasing the rate of tax for corporate for both dividend and capital gains received from mutual funds (other than stock funds) to 25%. The Income Tax laws recognize only two categories of mutual funds, i.e, 'Stock Funds' and 'Other than Stock Funds'. There are several other categories of funds which can be called 'hybrid funds' which invests in both fixed income securities and stocks. These include balanced, asset allocation and capital protected funds. It is therefore necessary that the hybrid category is also recognized where proportionate rate of tax on dividend and rate of tax on capital should apply to make it fair for the investors.

Workers Welfare Fund

The Government announced that the income of Mutual Funds would not be subjected to the Workers Welfare Fund (WWF). Voluntary Pension Schemes were however missed out from the notification. MUFAP has been actively engaged in pursuing with the Government as well as a constitutional petition relating to levy under Workers Welfare Fund (WWF) on the mutual funds as MUFAP has always been clear and had very clear clarifications issued by the Ministry of Labor and Manpower that WWF is applicable on asset management companies but not on mutual funds which are exempted from WWF. While this amendment addresses the matter going forward, the previous years still remain pending as Mutual Funds Constitutional Petition for decision and judgment of the Sindh High Court is pending at the Court since June 30, 2010. We remain optimistic that the final outcome will be favorable for us.

Taxation Anomalies affecting the growth of the Mutual Fund Industry

It had been very unfortunate that the mutual fund industry has been plagued by various taxation anomalies and issues since 2008 that have been growing every year rather than reaching any resolution. It is also unfortunate that the petitions filed in the Honourable Courts have been pending for years now with no outcome. These are adding to the cost of management and affecting the returns of the investor. The Government instead of facilitating savings and investments in the country has been hampering the same through double taxation and other anomalies.

Tax neutrality requires that investors directly investing in underlying securities and those investing through mutual funds should be subject to the same taxes. Mutual Funds have been subject to provincial sales tax, Federal Excise Duty (FED) and Workers Welfare Fund (WWF) which significantly reduces profits of the investors. The same is not applicable to direct investments in stock market, bank deposits and National Savings Schemes which puts the mutual funds investors at a disadvantage.

The various tax issues and anomalies are affecting the growth of the industry need to be resolved at the earliest. Federal Excise Duty (FED) remains the biggest as FED is double taxation and is not tax neutral as the investors in mutual funds are already subject to provincial sales tax on services at 14%. This is not the case in direct investment and needs to be removed. Additionally multiple provinces are claiming their share on the same investment due to difference in the wordings of their respective laws and instead of resolving the issue by developing a sharing formula amongst themselves, are harassing the asset management companies.

Principal component should be removed from dividend definition as the amount invested by an investor includes a principal (capital) component in the price at which he invests. The cash dividend received by him may have been paid out of his principal amount, which will result in extra payment of tax. This tax anomaly should be removed so that the principal component of investment is not taxed as capital is not taxable.

During the year, the Federal Board of Revenue (FBR) issued a clarification to its field offices, making it mandatory for every exempt entity whose income is exempt under clause 47B of Part IV of the Second

Schedule to obtain a tax exemption certificate every year otherwise its tax will be withheld at source and they would thereby need to file refund claims at year end. Collective Investment Schemes, Voluntary Pension Schemes, REIT Schemes, private equity and venture capital funds Modarabas, and all recognized provident, superannuation and gratuity funds will be affected by this circular. This move has only created operational difficulties and departmental inefficiencies and there will be no tax revenue for the Government as the income of these entities is exempt from tax.

20th Asia Oceania Investment Fund Association (AOIFA)

The 20th Asia Oceania Investment Fund Association (AOIFA) meeting was held from March 16 to 20, 2015 in Bangkok and Pattaya, Thailand. 29 delegates from 13 countries in the Asia Pacific region attended the meeting. The conference theme focused on Building Investment Culture with a main focus on retirement/ pension funds and the challenges being faced in the region. Association of Investment Management Companies (AIMC) hosted the wonderful and well organized event.

21st Asia Oceania Investment Fund Association (AOIFA) in 2016 will be hosted by MUFAP in Pakistan

MUFAP will proudly be hosting the 21st Asia Oceania Investment Fund Association (AOIFA) Conference from April 3-7, 2016 in Pakistan.

MUFAP had earlier hosted the 12th AOIFA Meeting in 2007 in Lahore, Pakistan.

Board Meetings/ Attendance

MUFAP's Directors have been extremely generous in giving their time and expertise for industry issues. During 2014-2015 tenure of the Board, fifteen meetings were held of the Board of Directors. The attendance recorded at the meetings of the Board of Directors for 2014-2015 is summarized as below:

S.No	Name of Directors	No. of Meetings Attended
1	Mr. Mohammad Shoaib - Chairman	14
2	Mr. Shahid Ghaffar - Senior Vice Chairman	11
3	Mr. Yasir Qadri - Vice Chairman	14
4	Dr. Amjad Waheed	13
5	Mr. Mir Muhammad Ali	13
6	Mr. Imran Azim	12
7	Mr. M. Habib-ur-Rahman	12
8	Mr. Farid Ahmed Khan	11
9	Mr. Adnan Siddiqui (co-opted from February 24, 2015)	7 out of 9
10	Mr. Ahmed Ateeq (resigned on January 22, 2015)	2 out of 6
11	Mr. Babar Ali Lakhani	0
12	Mr. Enamullah Khan	0
13	Ms. Mashmooma Z. Majeed - Chief Executive Officer	15

Key Challenges

- **Early resolution of Court cases and removal of tax anomalies**

  It is important for the mutual fund industry's survival and growth that the tax anomalies are removed and a conducive environment is present for the industry to do its proper role in the economy as it does internationally. Mutual Funds are the biggest savings avenue worldwide which unfortunately has not been the case over here in Pakistan. While on hand Government is offering high returns on fixed rate Government instruments and schemes making it difficult for market return instruments such as mutual funds to compete, on the other hand it is also imposing double taxation and levies on the mutual funds that are not present on other investment avenues.

  A level playing field between mutual funds and other savings and investment avenues is must for mutual funds and pension funds industry to grow and promote savings and investments in the country which is currently at the lowest in the region.

  MUFAP understands the significance of the issue for investor and industry interest and is actively following up its resolution through the Courts and Government of Pakistan.

- **Public Awareness and Education to expand the Retail Investor Base**

  It is imperative for long term sustainable growth of the mutual funds industry that the retail investor base increases. Asset Management Industry vis-a-vis the Banking Sector presents a bleak picture, not only in terms of assets under management, but also with regard to participation and outreach to the general public. Currently, asset management companies are offering a diversified range of mutual and pension funds to meet the risk appetite of investors, yet the awareness in the masses is lacking of the options available to them.

  The industry's next focus must be on conducting a comprehensive and sustained public awareness campaigns to bring across to the attention of the individual investors, the diverse investment features and benefits that mutual funds and voluntary pension schemes offer to them. The Government and SECP are also required to facilitate asset managers to promote, educate and encourage investors to save.

Acknowledgement

I would like to thank SECP for their continued support. I am particularly grateful to Mr. Zafar-ul-Haq Hijazi Chairman SECP, Mr. Zafar Abdullah Commissioner SECP, Mr. Akif Saeed Commissioner SECP, Mr. Asif Jalal Bhatti, Executive Director Specialized Companies Division, Mr. Muhammad Afzal, Director REITs & Pension, Mr. Imran Inayat Butt, Director AMCs and the entire AMCs, Pensions and Strategy, Development, Investor Education Teams for their proactive role in dealing with issues relating to mutual funds and VPS.

I would like to thank the Chairman Mr. Mohammad Shoaib, Senior Vice Chairman Mr. Shahid Ghaffar, Vice Chairman, Mr. Yasir Qadri and Board of Directors and Committees' Members for their guidance, dedication, teamwork and support. Lastly, my thanks and appreciation is for the management team of MUFAP for their hard work and commitment.