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The Financial Sector in Pakistan. With Particular Reference to Investment Finance Banks and Development Finance Institutions.

STUDY UNDERTAKEN

FOR USAID
ISLAMABAD

BY

epru

Economic Policy Research Unit
Lahore, Pakistan

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CONTENTS

EXECUTIVE SUMMARY

i. Pakistan's financial system has evolved through four phases. The first phase witnessed the establishment of basic financial institutions to aid economic development. The commercial banks were set up by the private sector, whereas development finance institutions began operating in the public sector. The second phase was one of nationalisation of financial institutions in response to grievances regarding the concentration of industrial and financial power within a tiny corporate elite. The third phase did not involve a change of ownership but introduced religiously determined instruments and measures into a confused financial system. The current phase is one where the GOP is embarked on a tentative course of financial liberalisation. Attempts are underway to rationalise existing public sector institutions, increase competition and more towards a more market oriented system. Such reorganisation would require prudent regulation, but this would be qualitatively different from the extensive control exercised currently by the government. At present, the country's financial system is under considerable confusion and distress. GOP's efforts at reform acquire particular urgency at a time when the country needs to rely more on domestic resource mobilisation.

ii. This study examines two features of the current liberalisation. First, we examine the prospects of the forthcoming investment finance banks. The second aspect of the study is a review of development finance institutions. The conclusions and recommendations emerging from our study, regarding both subset of institutions, are summarised below.

IFBs : EMERGING ISSUES AND RECOMMENDATIONS.

iii. The first and foremost hindrance that was faced by all parties was the lengthy process of seeking approval. This process has been almost two years in some cases. This poses a constraint for all new aspirants in the field. It is alleged that interested parties are using all sorts of political connections and seeking foreign government recommendations in their bid to obtain letters of intent. The pressure is building up as more applications find their way to the authorities. The experience of the Crescent Group-the only ones that have had the public subscription so far-is a case in point. The stock market with all its inefficiencies gives a premium to the sound reputation of the Crescent Group. This resulted in over subscription and the price of shares being quoted at two or three times the par value. Aspiring sponsors thus also see this as a way to increase the value of their net worth in a short period of time. This explains the interest that has been shown by various parties in obtaining licenses by any possible means. This fact also encourages those whose intentions are only to make a 'quick buck'.

iv. The procedure that companies in Pakistan have to follow in order to have a public offering, whether Investment Banks or others, is aso very tedious and rampant with unnecessary delays. The inherent delays in this process will directly effect the working of IFBs as well when they will underwrite issues of, and act as advisors to clients going public. The present process requires the sponsors of any company to register with the registrar of joint stock companies, go to the controller of capital issue with the memorandum and articles of association, have the same whetted by the Corporate Law Authority, seek State Bank of Pakistan approvals and then put in the prospectus to te Stock Exchange for approval before the actual floatation. The slightest of objections, say at stage 3 would result in going back to stage one in order for them to be approved by the authorities. What would be desirable is the ubiquitous and much desired "one window operation" whereby the sponsors could out together the entire package and then seek a 'blanket approval' from any designated Department of the Ministry of Finance. Going a step beyond this, it has been suggested that the IFBs in particular should be granted approvals to undertake issues on behalf of clients on their own books or by directly placing them in the market. In areas where the regulators wish to retain control there should be a swift approval process which allows transaction to proceed before market condition change.

v. IFBs are allowed to act as traders and brokers of listed securities under section 5 (b)(v) of the SRO. At present stock exchanges are not issuing new membership cards as they do not want to increase membership. The only way out for the IFB is to puchase a card from an existing member. This has led to a monopoly situation for the existing members who have started quoting unrealistic prices for them. It was alleged that they want to sell off cards at exorbitant prices but officially document only a minimal amount in order to make an off-the-book profit.

vi. Nationalized Commercial Banks and Domestic Foreign Banks in Pakistan are regulated by the State Bank of Pakistan. At the time the SRO of Investment Banks was being drawn, it was decided that since Investment Banks are not going to be scheduled banks, therefore they do not need to be regulated by the SBP. Instead it was decided that the Ministry of Finance and in particular the controller of capital issue would be the regulating authority. This decision is responsible for the regulatory confusion that the investment banks are facing today. In particular IFBs do not have access to the money market like other financial institutions. As per section 5(a)(iv) of the SRO, they are allowed to borrow and lend in the call money market (Inter bank). The situation on ground is different, and they cannot participate in the Interbank market which puts them at a relative disadvantage. The more aggressive foreign banks in Pakistan are the traditional borrowers in this market, due to a decline in their share of bank deposits coupled with a more active demand for bank credit. The Interbank or Call Money rate is artificially low. At the peak of the busy season it may exceed the bank rate charged by the SBP. This is due to demand for credit being more than that allowed by SBP and because Call Money does not require collateral. As the name indicates the money is 'on call' but participants in this market have a gentlemen's agreement that it will not be called for some time. To maintain the investment finance banks liquidity position at par with commerical banks it is important that the present situation be amended without delay.

vii. IFBs are allowed to issue short and long term redeemable capital which includes Participation Term Certificates and Term Finance Certificates under section 5 (b)(vii) and 5(c)(xi) of the SRO. However, under section 120 of the Companies Ordinance a company can issue any instrument in the nature of redeemable capital in favour of 'scheduled banks', 'financial institutions' or other persons as may be specified for the purpose by the Federal Government through notification in the Official Gazzette. As an IFB is neither a scheduled bank nor a financial institution, companies cannot issue TFCs in their favour. This situation can be altered only if authorities issue a notification that will amend the existing regulations.

viii. At present IFBs do not have authorization to function as foreign exchange dealers. For this reason they are not in a position to open Letters of Credit on behalf of clients. Thus they would have to have a standing relationship with a commercial bank for this purpose and give up half of the commission that is earned. Their exclusion from this highly lucrative market seems unnecessary. It must be pointed out that foreign banks derive more than two thirds of their income from trade related financing.

ix. IFBs must be eligible for remedies available to commercial banks in cases of default such as access to the banking tribunal. (It is a different matter that the said tribunal is without a judge for the past year and a half). Moreover the existing law regarding foreclosures and taking posession of assets which are pledged as security leave a lot to be desired. Thus recovery mechanisms must be put in place before IFBs can be expected to take on the risk of credit and new ventures.

x. IFBs are not allowed to take deposits that are of less that ninety days maturity nor have checking accounts, which differentiates them from commercial banks. Investment banks want to provide all services under the same roof for their corporate clients. This includes raising short term funds on their behalf, which may be less than 90 days maturity. Similarly Form L ceilings limit short term borrowing. If paper issued by prime corporate customers were excluded from this limit or incorporated as a sub limit, it would encourage entry by companies, help develop markets and create liquidity. It must be realised that the IFBs could play an important role in developing a broad and flexible money market where funds can be channelled where they are most needed.

xi. Specialized credit line from the State Bank are not available to IFBs as they are to NCBs and DFIs. These include concessioanry lines for locally fabricated machinery.

xii. IFBs must be able to take hold and make markets in different kinds of paper without restrictions or impediments. Instead matters appear to have been made artificially complex due to the stamp duties that are imposed on the creation of new instruments. There is a need to build a secondary market in Pakistan. GOP has been showing an interest and a number of studies have been undertaken. IFBs can play an important role if provided with the required incentives. In well developed money markets, liquidity is the 'name of the game'. The only reason why there is a demand for instruments with long term maturitys such as 30 year bonds, is because they can be traded freely. It is recommended that stamp duty on IFB paper products be removed.

xiii. To have IFBs competing with other institutions on a level playing field certain conditions have to be created. Liquidity and tradeability form the critical mass of capital markets. Pakistani authorities will have to take committed steps to fuel the market. For instance the crowding out effect due to unnecessarily advantageous features of certain instruments should be avoided. The WAPDA bonds is a case in point. First, they are guaranteed by the government. Secondly, they are just another source of non bank domestic borrowing. The rate of return does not reflect the operating performance of WAPDA. Infact the bonds prospectus did not contain a financial statement of WAPDA. These long term bonds have features of discounting (after 6 months with FCDC and a tax advantage that will be very difficult to match for any prime corporate borrower). The prime customer will be able to borrow at 12.5% + legal and administrative cost and will thus be driven out of the market. It is ofcourse critical that IFBs have access to cheaper funds as compared to the corporations that they are lending to.

xiv. Since IFBs are not included in the list of scheduled banks there is a number of problems that they are facing. For instance IFBs can provide guarantees on behalf of customers in case equipment is imported, but cannot guarantee the payment of duty through custom debentures, as the law only names scheduled banks as eligible for this function. Section 5(c)(xii) allows IFBs to undertake guaranteeing and counter guaranteeing business, but public sector institutions are resisting the acceptance of guarantees issued by them, as IFBs are absent from the text of the Companies Ordinance 1984. Similarly certain government corporations which have surplus funds cannot place them with IFBs since they have not been given the status of financial institutions in existing law.

xv. The tax status of the IFBs is still not very clear and there has not been any rate disclosure. If the IFBs are taxed like other banks it will be unfair since the quality of the portfolio of the two types of institutions will be very distinct. Secondly the amount of money that the IFBs are spending on the research and development of new products will have an impact on their income thus rendering them incomparable to other banks.

xvi. IFBs are working in a regulated environment where each activity is restricted in quantifiable terms as a percentage of liquid net worth or other similar measures. On the other hand activities of leasing companies and modarabas are not restricted or governed by any regulation. This results in their unlimited and unregulated involvement in activities which essentially lie in the domain of investment banking. These companies are investing in shares, discounting bills, giving margin loans and accepting deposit and lending in an unrestricted manner. This results in unfair competition as the conventional leasing rates are 22 - 24%. Thus leasing companies are in a position to offer competitive deposit rates in the neighbourhood of 16-18%, which are the highest in the market. It is therefore recommended that either Modarabas should be disallowed investment banking activities or should have similar guidelines as those provided to IFBs so as to have fair competition.

xvii. A major problem exists due to the fact that investment banking is a new concept in Pakistan. The market as well as the bureaucracy do not or only partially understand what is entails. Some think of IFBs as being synonymous with the fraudulant investment companies which mushroomed in the past decade. These companies offered tremendous returns and later decamped with the investors's money. This is the chief reason for the extreme caution being exercised by regulatory agencies and the public at large. Thus it is important to educate the target audience, as regards investment banking. The challenge facing the IFBs is, firstly to create a demand for their services and then to create an awareness of their name. Even the professional and fresh graduates who are working in IFBs are only familiar with the academic working of Investment Banks. The experience of well developed capital markets can also not be replicated in their entirety. For this reason, it would be appropriate for organizations such as the Pakistan Banking Council and/or the regulating bodies, alongwith international agencies, to hold seminars and training workshops all over the country for bankers and professionals. Donor agencies could also play an important role by sponsoring workshops, where experienced investment bankers from overseas could be invited to impart training to the aspiring investment bankers in Pakistan or those in the field be sent overseas for a short period of time to gain practical knowledge and experience.

xviii. Donor agencies could lend support to IFBs through various measures. First of all an awareness of the existence of these institutions needs to be created in the donor community. The IFBs came into existence due to World Bank conditionality on liberalization of the financial sector and the role that the private sector could play. It appears that the pressure on regulatory authorities must continue in a similar manner. If the objectives in view are to be achieved, half hearted effort is of no use. Instead the whole process should be monitored at every step. A positive move would be the provision of credit lines. In this regard donor agencies and overseas DFIs should be encouraged to disburse funds through IFBs. The process can start by a few initial projects where final evaluation and approval vests with the foreign DFI. At a later stage dedicated lines of credit could also be made available to IFBs as were given to the government controlled DFIs in the past. Caution must be exercised in this regard to avoid undesirable experiences such as those with state controlled DFIs. For this reason it will be very important to look at the track record of sponsors.

xix. IFB personnel should be sponsored for training courses in other less developed countries such as Thailand and Indonesia. The environment of the financial sector is similar to that in Pakistan, or was recently at a stage where Pakistan is now.

RECOMMENDATIONS FOR IMPROVING DFI PERFORMANCE

xx. DFI performance has to be seen alongwith the infrastructural and other inherent weaknesses of the financial sector. DFIs may be performing similar functions but there is hardly any competition among them. Applicants have also felt free to approach more than one institution. The government must encourage competition within the DFIs. For this it may chose certain target performance measures such as rate of return on assets or rate of recovery. In fair competition it is necessary to reward performance just as it is necessary to penalize poor results. However there must also be a miniimum acceptable level of adverse performance.

xxi. All DFIs must be encouraged to mobilize their own resources and not depend on subsidized credit facilities of the SBP or international agencies. If their mandate does not allow resource mobilization, it should be amended accordingly. At this stage some DFIs may not be in a position to do so, owing to the adverse quality of their loan portfolios.

xxii. Concentration of DFI headquarters in one region has resulted in large projects becoming the prerogative of Karachi businessmen. To have an equitable disbursement of funds DFI headquarters must be moved up country. Initially the headquarters of two institutions should be moved to Lahore and one each to Islamabad, Peshawar and Quetta. This should be coupled with opening of regional offices (as recently announced by ADBP). This step might also lead to a natural division of sectoral lending, for instance DFIs based in Punjab may end up financing more agro based industry and/or cotton textiles. Similarly there might be a natural division on the basis of rural or urban concentration of the projects under consideration. Looking ahead, if the government wants to move towards (say) rural industrialization , DFIs can play an important role in developing infrastructural facilties for industries in selected rural areas.

xxiii. Competition for DFIs is also emerging in the form of private sector Investment Finance Banks. These institutions will undertake project finance activities as well and claim to have turn around time of 10 to 15 days. In order to compete DFIs will be forced to atleast work within the stated 60 day approval cycle and push towards early disbursements.

xxiv. It is recommended that DFIs should create a technical intelligence unit and hire inhouse technical consultants. In this age of rapidly changing technology, such a unit should have the ability to evaluate technological choices, its interaction with other technologies, its relationship with social and economic systems and its impact on the economic viability of the project.

xxv. DFIs must also consider the technological development objectives of the country while evaluating projects. Import substitution, deletion policies and utilization of indigenous capabilities could [illegible] a consideration while considering loans. Related certain quantitative measures and targets could be made prerequisites for disbursal. For instance, they could include graduated deletion of foreign technology import by (say) 5-10% per year.

xxvi. DFI performance has been excessively top management dependant. As is the practice in many other areas of Pakistan society, individual personalities have dominated certain institutions. One way of avoiding this would be by giving more power to the Executive Boards who should have an equal number of internal and external members, thus increasing the chances of dissent. Decentralizing to regional or provincial levels will also decrease the dependence on Head Office and the decision making on one person. Regulatory agencies could keep a check on performance by monitoring the trend in the number of sanctions over time and doing the needful in case there is an extreme movement.

xxvii. Terms and conditions of work and salary structure at DFIs need to be reviewed. Ideally these should be brought in line with private sector terms. Performance criteria and objectives should be decided in consultation with the employees and performance reviews should be carried out regularly. Moreover performance based rewards and promotion must be introduced, as is the case in private banks.

xxviii. New employees should go through intensive training modules along with on-the-job training. This should be similar to the training programs being offered by private sector financial institutions. DFIs could also institute the Account Officer system. (see detail in commercial banking section).

xxix. DFIs must also have ready or on-line access to the credit information network for NCBs. This will enable them to have up_to_date information regarding group accounts and total liabilities outstanding of corporate individuals and groups, and delinquencies ,if any.

xxx. Disbursing institutions must ensure that the recipients of funds are the initial sponsors of the projects. In many cases sanctions have been sold to other non deserving parties or original sponsors are no longer associated with the project when it finally takes off.

xxxi. Certain preconditions must be imposed on borrowers, such as the provision of audited financial statements in a timely fashion. The integrity and sophistication of reporting standards depends on the sophistication of its users. In developed systems it is analysts and institutional stake holders who ensure high quality reporting. Laws regarding timely preparation of accounts are in place in Pakistan, as in other countries, but the implementation is too slow or is non existent.

xxxii. In order to play their due role in capital market development in Pakistan, DFIs could make it a precondition for borrowers to have a public offering. DFIs could provide an all-in-one package to clients. This would also result in better reporting practices.

xxxiii. Internationally employed loan clssification criteria must be adopted by DFIs. The importance of post disbursal evaluation and project monitoring must be recognized in this regard. Having an account officer sytem in place will aid this process greatly.

xxxiv. Over the long term it is recommended that the DFIs be restructured finanacially and administratively. Some measures regarding administrative restructuring have been mentioned earlier. Measures for financial restructuring should include a thorough portfolio audit in each institution as a first step.

xxxv. Secondly the formation of a central management service company or smaller companies is recommended. These should be along the lines of "work-out groups" in some Western countries. The company consists of an independent group of professionals including accountants, financial managers. lawyers, tax advisors which may be hired by the Institution(s). This group usually takes over the management of problem companies which would be similar to our 'sick units'. It carries out a management audit and puts measures in place that may aid in turning it around. In case of a situation beyond redemption, it aids in the filing of bankruptcy proceedings and the final disposal of assets of all creditors. DFIs could have inhouse work out groups if outside consultants are not available.

xxxvi. Institutional retructuring along the lines of commercial banks could also be undertaken. Here each instituion would be divided to form two separate ones. One would retain all the 'good loans' and the other all the classified or sub standard ones. The purpose of the latter would be restricted to that of a collection agency - collecting interest payments and pursuing loan recovery with the aid of the legal sytem. A combined collection agency for all the DFIs could also be set up.

Abbreviations and Definitions

DFI:	Development Finance Institution.
GOP:	Government of Pakistan.
IFB:	Investment Finance Bank.
NCB:	Nationalized Commercial Bank.
SBP:	State Bank Of Pakistan.
ADB:	Asian Development Bank.
ADBP:	Agricultural Development Bank of Pakistan.
BEL:	Bankers Equity Limited.
EPF:	Equity Participation Fund.
FBC:	Federal Bank for Co-operatives.
ICP:	Investment Corporation of Pakistan.
IDBP:	Industrial Development Bank of Pakistan.
NDFC:	National Development Finance Corporation.
NDLC:	National Development Leasing Company.
NIT:	National Investment Trust.
PICIC:	Pakistan Industrial Credit and Investment Corporation.
PLHCL:	Pakistan-Libya Holding Company Limited.
PKICL:	Pak-Kuwait Investment Company Limited.
SAPICO:	Saudi-Pak Industrial and Agricultural Company.
SBFC:	Small Business Finance Corporation.

Definitions

* **BANKS.** Financial institutions that accept funds, principally in the form of deposits repayable on demand or at short notice (such as demand, time, and savings deposits). Under the general rubric "banks" come: commercial banks, which engage only in deposit taking and short- and medium-term lending; investment banks, which handle securities trading and underwriting; housing banks, which provide housing finance; and so on. In some countries there are universal banks, which combine commercial banking with investment banking and sometimes with insurance services.

* **CAPITAL MARKET.** The market in which long-term financial instruments, such as equities and bonds, are raised and traded.

* **COMMERCIAL BILLS.** Short-term debt instruments that are used mainly to finance trade. Examples are promissory notes, by which debtors commit themselves to pay to creditors or to their order a stated sum at a specified date, and bills of exchange, which are drawn up by creditors and accepted by debtors. Commercial bills that are also accepted by banks are known as bank acceptances. Promissory notes issued by large corporations to meet their general financial needs are known as commercial paper.

* **CONTRACTUAL SAVINGS INSTITUTIONS.** Occupational pension funds, national provident funds, life insurance companies, and similar institutions that collect long-term savings on a contractual basis.

* **CURB MARKET.** An unofficial money and capital market.

* **DEVELOPMENT FINANCE INSTITUTIONS.** (DFIs). Financial intermediaries that emphasize the provision of capital (loans and equity) for development. DFIs may specialize in particular sectors-for example, industry, agriculture, or housing. Although most provide only medium- and long-term capital, some, particularly those that specialize in agriculture, also provide short-term finance.

* **DISCOUNT.** A reduction from the face value of a financial contract.

* **EQUITY FINANCE.** The provision of finance in a form that entitles its owner to share in the profits and net worth of the enterprise.

* **FINANCIAL SAVINGS.** The portion of total wealth held in the form of financial assets.

* **FOREIGN PORTFOLIO INVESTMENT.** Investment by foreign residents in domestic capital markets, without the investors' provision of technology and management services that usually occurs with foreign direct investment.

* **FRACTIONAL RESERVE BANKING.** The practice by which commercial banks maintain a reserve of highly liquid assets (usually deposits in a central bank) equal to only a fraction of their deposit liabilities.

* **INDEXATION.** A mechanism for periodically adjusting the nominal value of contracts in line with movements in a specified price index.

* **LEVERAGE.** The ratio of debt to equity or of debt to total capital employed.

* **LIQUID LIABILITIES.** Money plus highly liquid money substitutes, such a savings deposits.

* **MARKET CAPITALIZATION.** The total value of outstanding securities at present market prices.

* **MONEY MARKET.** A market in which short-term securities such as Treasury bills, certificates of deposit, and commercial bills are traded.

* **NONBANK FINANCIAL INTERMEDIARIES.** Financial institutions, such as building societies and insurance companies, that hold less-liquid liabilities not normally regarded as part of the money stock.

* NONPERFORMING LOAN. A loan on which contractual obligations (for example, interest or amortization payments) are not being met.

* **RESERVE MONEY.** Currency in circulation plus deposits (of banks and other residents but not the government) with the monetary authorities.

* **TERM FINANCING.** Equity or medium- and long-term loan finance.

Source: The World Bank's Financial Definitions. Washington, 1989.

List of persons met.

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CHAPTER 1

EVOLUTION OF PAKISTAN'S FINANCIAL SECTOR.

1.01 The current weaknesses in Pakistan's financial sector are the result of a four staged evolution since partition. In 1947, the country's financial system, such as there was, remained confined to short term financing of trade and commercial activities. It was clearly inadequate for the substantive development process launched in subsequent years.

1.02 The first phase of the financial sector's growth contained two features which mirrored the GOP's development strateges. First, the government's major priority was import substituting industrialisation. A host of incentives - such as an artifically high exchange rate, heavy non-tariff and tariff protection - aided this primary objective. Accompanying this pattern of resource allocation was the creation of private commercial banks. These banks,as well as insuracne companies, were owned by the same group of families who were in the forefront of the industrialisation process. The resulting concentration of financial and industrial assets had adverse equity implications. As far as the financial sector was concerned, such lop-sided development implied that credit was by and large confined to a small group of Karachi based entrepreneurs. The second feature of the first phase was the establishment of quasi-public sector financial institutions to direct credit into particular sectors, to finance projects that the private sector was unwilling or unable to. In some cases it was to promote medium and small scale industry. To a great extent, however, the major industrial-financial families were the beneficiaries of state created institutions as well. They were frequently represented on the Boards of these organisations and managed to allocate a fair proportion of sanctions to their units. Thus, the first phase witnessed the evolution of a financial system which to be adequately serving its norrowly defined purpose - providing finance for the few entrepreneurs who were engaged in capital intensive import substituting industrialisation. Financial institutions were involved in little innovation or effort beyond their limited scope. The major achievement of this phase was the beginning of institution building and development of indigenous management for the financial sector. Indeed much of the managerial talent emerging from this phase was to provide the backbone for the development of a major international bank in the seventies - the Bank of Credit and Commerce International (BCCI). Within the public sector, an institutional base was laid out through organisations such as the Industrial Development Bank of Pakistan. Popular resentment against the industrial - financial elite gathered force in the late 1960's. It led to demands for the curtailment of their control over the economy and was responsible in part for the downfall of the regime.

1.03 The People's Party government, which came into power in the truncated Pakistan, nationalized banks and insurance companies in 1974. This public take over of assets heralded the second phase of the financial sector's evolution. The process saw the emergence of five nationalized commercial banks and a proliferation of development finance institutions. Whereas nationalization may have broken the hold of a few families, it led to a number of complications which have debilitated the financial sector. Many of the problems that have emerged are common to the involvement of an inefficient public sector. The root cause of shortcomings has been the use of financial institutions to subsidies government operations. This subsidy takes several forms. Socially desirable projects inevitably involve a trade off with pure profitability concerns. Another form of subsidy is forced lending by nationalized banks to finance a burgeoning budget deficit. This feature has become particularly prominent in recent years, as the deficit - GNP ratio rate rise from 5% to nearly 8%. Funding this deficit through a 'tax' on NCBs is preferable to deficit financing as far as inflation is concerned. But the cost of such a policy is borne by an increasingly constrained and inefficient financial sector.

1.04 Nationlisation of banks has led to a number of additional adverse developments, in the financial sector, which are summarised below :

i. Extensive intervention by a centralised bureaucracy in the functioning of financial markets. This has led to a general lack of innovation due to the absence of incentives for better performance.

ii. Administered interest rates, which have prevented creditors from charging a premium for highly productive but risky projects. It has also biased lending towards creditworthy government guaranteed borrowers. Further, large reserve requirements have adversely affected the profitability of commercial banks. One of the likely benefits of less regulated financial markets would be greater flexibility in financing investment projects, introduction of a larger variety of financial instruments and better deposit rates to attract savings. Recent experience provides evidence of responsiveness of savings to such incentives. The mushrooming of private finance companies led to difficulties not due to lack of funds but due to absence of prudent regulation. The response of savers to attractive interest rates that were offered was somewhat dramatic.

iii. NCBs pay out set minimum deposit rates set by the State Bank . The adjustment has typically lagged behind changes in the economic environment. To some extent this may be due to the inefficiencies of an oligopolistic market structure. But the primary reason appears to be the strict controls on commercial banks which do no provide the necessary incentives for engaging in the mobilisation of deposits. Further, financial layering blunts the incentive to tend to the most profitable borrower and decreases the degree of competition among lenders.

iv. Credit has been used as an important tool for political patronage. Excess demand for credit inevitably involves rationing. When this scarcity is utilised for cultivating political allegiance there are detrimental effects. Two are notable; First, those who receive such credit are not particularly concerned about repayment. The nature of the sanctioning is one where the recipient knows that default will not lead to punishment. Second, those who get credits in this manner help destroy the credibility of financial institutions. Such overt manipulation creates an ethos of favour dispensation which inhibits the development of financial criteria for loan dispersal.

v. The quality of management attracted to the nationalised financial sector often leaves a lot to be desired. Poor remuneration, lack of incentives and better opportunities abroad have deprived the financial sector of good quality staff. Since the quality of management is a key skill in financial services, the migration of Pakistani banking professionals has hampered institutional development.

vi. The banking sector has been used for positive discrimination policies. Promoting disadvantaged groups is desirable but very damaging, to financial institutions who have to take on personnel obviously unsuited to the task. Such personnel policies should in future be targeted at first inducting positive discrimination entrants into rigorous training programmes. Further, banks have been subjected to the unfortunate but common practice as 'employers of last resort'. They carry the burden of a highly overmanned workforce due to normal public sector pressures.

vii. Credits directed to particular sectors have sometimes proved to be useful. However, sectoral allocations require continous adjustments. Not only is there some trade-off with more productive alternatives but these sectoral credits are also amenable to mainpulation by powerful lobbies. In this manner, potentially important sectors may be deprived of credit.

viii. The provision of subsidised credit, through interest rate ceilings, is effectively a tax on the financial sector. The concomitant low deposit rates do not encourage financial savings. Small spreads discourage innovation and the resulting caution restricts credit disbursement to safe and well known parties. The financial sector can be taxed more easily if it remains in public hands. Government's plans to liberalise the financial sector have already been adversely affected by the temptation to retain control over public sector organisations.

1.05 The third phase in Pakistan's financial sector evolution did not involve a change of ownership. Thus the earlier comments made regarding the shortcomings of public sector financial institutions remained valid through this period. The third phase involved new shocks to the financial system from within the public sector. It involved the introduction of Islamic injunctions. Two aspects of the Islamisation of the financial sector are worth noting. First, there was an attempt to abolish the very concept of interest. Second, there was an addition of financial instruments and schemes which emphasised equity participation by the lender. The result of the latter has been an expansion of instruments but the funds raised through these do not appear to constitute additional resource mobilisation. Commercial banks are often reluctant to get involved in equity financing.

1.06 Perhaps the most damaging effect has been the uncertainty created by measures ostensibly to abolish interest. Often all this has involved complex subterfuges to discover ideologically sound nomenclature. But the more pervasive effect has been greater insecurity and incohesiveness within the financial sector - attributes which are anathema to sound development. It is no surprise that Islamisation of the financial sector appears to have made no positive contribution towards raising Pakistan's low savings ratio. The rates on PLS deposits were much lower than those being offered under the interest based system. The country's savings rate is half that of India's 22%. In brief, the net effect of Islamisation has been to introduce an additional shock to a financial system already under considerable duress. Further, these measures were accompanied by accelerated use of politically determined credits, rising default rates and deepening structural malaise during the third phase.

1.07 The current phase represents the fourth in the chain of financial sector evolution. Towards the mid to late eighties, it was evident that the financial system was in need of substantial reform. A worryingly large number of institutions are insolvent and are on an effective subsidy to remain in business. Loan write-offs, rising default rates and persisting political interference have contributed to deep malaise in the financial system. Donors have frozen credit lines to some agencies due to poor pay-back performance of previous loans, which is indicative of the problems prevalent in the sector.

1.08 Pakistan is reaching a stage in its development where it has to rely increasingly on domestic resources. Mobilisation of these resources is extremely important at a time when the net inflow of aid is shrinking. The GOP is well aware of the role that will need to be played by the financial sector to mobilize these resources. The needed liberalisation of the financial system is critically dependent on reducing the hold of the public sector and encouraging greater competition through the active involvement of the private sector. Fortunately, the present government is favourably disposed towards a greater role for the private sector in general. But the process of liberalising the financial sector is complex, particularly since this sector has been effectively subsidising a number of economic activities. Powerful groups stand to lose in a process of adjustment. Nonetheless, these contraints have been overcome in other developing countries. Liberalisation should not be limited to the reform of the banking system but should seek to develop a more broadly based financial system that will include money and capital markets and non-bank intermediaries. A balanced and competitive system of finance contributes to macroeconomic stability by making the system more robust in the face of external and internal shocks. Active securities markets increase the supply of equity capital and long term credit, which are vital to industrial investment. Further, to operate efficiently financial institutions and markets have to be guided primarily by market forces rather than government directives. Competition needs to be strengthened by encouraging the entry of new and innovative providors of financial services, by phasing out interest rate controls and by stimulating the development of money and capital markets.

1.09 Some of the policy challenges faced by the GOP during the course of financial liberalisation are summarised below :

1. An important feature for financial sector reform is the need to control the fiscal deficit. Unless this is done, the pressure on non-bank borrowing will be too intense for a meaningful transition from a regulated to a more liberal financial system.

2. The GOP would need to pay special attention to improve the foundations of a financial system -- this would involve improvement of the legal system. This is crucial, as it will enable contracts to be enforced and swift action can be taken against defaulters. Financial liberalisation can be volatile and would need prudential regulatory bodies to supervise the transition.

3. A move towards a more market based system would involve a reduction in directed credit programmes as well as adjustments in the structure of interest rates. Broader ranges for deposit and lending rates would need to be introduced. It will be more prudent to channel directed credits for activities rather than target specific sectors. Thus exporters in general should have priority over producers in particular sub-sectors.

4. GOP would need to encourage autonomy in the management of those financial institutions which remain in the public sector. It is important that managers in the public sector should have autonomy and be accountable. GOP interference in asset management, personnel policy and loan decisions should be kept to the minimum. To the extent possible, the government should take a bolder initiative towards privatisation of banks. The present policy of offering nearly 20% of equity to the public is likely to lead to a very meagre privatisation programme. Since management remains with the public sector, thus these 20% floats are effectively a form of non-bank borrowing rather than privatisation drives. Admittedly, caution is needed when liberalising financial markets but being over cautious can defeat the whole purpose of the exercise.

5. Competition and efficiency would be encouraged by allowing foreign entry into domestic financial markets. This can be implemented with the provision that local partnership is necessary, to ensure the development of indigenous management capacity. Similarly, new institutions such as investment banks should be encouraged not only because they could add instruments and functions but also because of the competitive pressure they would exert on the public sector.

1.10 The study provides a description of the institutional framework, its evolution and present status. It describes the role played by each set of institutions and their strengths and weaknesses.

1.11 This study focuses on two aspects of the financial sector liberalisation currently being initiated in Pakistan. First, the emerging investment finance banks are examined in section B. The experience of 5 investment banks is enumerated. This section ends with an analysis of future directions for IFBs in Pakistan and necessary steps required to aid their operations. The second component consists of an analysis of the performance of development finance institutions. A survey of their individual performance is followed by the issues emerging from present state of affairs and recommendations for their further development. The recent performance of seven DFIs is summarised. This is followed by a brief of each of the remaining DFIs.

1.12 The study is based on interviews of the Chairmen of 5 investment banks, Ministry of Finance officials, development finance institution personnel, other officials and commentators. The written material consulted consisted of annual reports, articles in periodicals and newspapers and government publications.

CHAPTER 2

SUMMARY ANALYSIS OF FINANCIAL INSTITUTIONS IN PAKISTAN.

FINANCIAL SECTOR IN PAKISTAN - AN OVERVIEW

2.01 The financial sector in Pakistan consists of various institutions namely:

The State Bank of Pakistan
5 Nationalized Commercial banks
3 Specialized Banks
19 Domestic Foreign banks
14 Development Financial Institutions (including the three specialized banks)
7 leasing and Modaraba Companies
2 Stock Exchanges
Insurance Companies
Investment Finance Banks (upcoming)

STATE BANK OF PAKISTAN

2.02 The State Bank of Pakistan (SBP) is the central bank of the country. It governs and monitors the working of the various financial institutions and implements the monetary policy. It was established on July 1, 1948. Under the SBP Act of 1956 it is charged with regulating the monetary and credit systems of the country and foster utilization of its productive resources.

2.03 The Chief Executive is the Governor who is assisted by one or more deputy governors, who are appointed by federal government for a term of five years.

2.04 As the central bank of the country, the functions of the State Bank include;

* Bank of Issue for currency notes of Rs.2 & above.

* Banker to the Government : supplies cash required for salaries and accepts deposits of cash.

* Advisor to the Government on economic, financial and monetary matters; agriculture credit and industrial finance.

* Banker's Bank. It is the lender of the last resort for commercial banks, and maintains a discount window where it offers re-discount facilities of 90 day trade bills and agriculture bills and against government securities.

* Controller of Credit and bank rate.

* Controller of Foreign Exchange : it issues licenses to institutions to function as authorized dealers. It exercises full control over the movement of capital to and from the country and both visible and invisible payments such as foreign exchange for business, travel, medical treatment and education.

2.05 It has the sole authority to process applications for opening new branches of commercial banks, changing the location of existing ones and can move a court of law for liquidation of a bank. The State Bank obtains periodic reports from all nationalized and foreign banks regarding their ceilings and reserves. State Bank auditors also visit branches to inspect credit documents and other books. The Finance Sector Adjustment Loan of the World Bank has required SBP to undertake various measures such as. Introduction of new treasury bills. These bills were to be sold at discount through open auction at regular intervals. The market forces would then determine the rate. So far three auctions were held but bids were declared since rate quoted were considered high. Setting up of an information bureau to meet the needs of having a computerized credit system, accessible to all banks and non-bank financial institutions.

COMMERCIAL BANKS

2.06 There are five Nationalized Commercial Banks (NCBs) namely:
National Bank of Pakistan
United Bank Ltd
Habib Bank Ltd.
Allied Bank Ltd.
Muslim Commercial Bank Ltd

2.07 In addition to the above there are nineteen Domestic Foreign Banks such as Citibank, Bank of America, Bank of Tokyo, Grindlays Bank, Banque Indosuez etc. These along with three specialized institutions form what are known as scheduled banks. A scheduled bank is one that is governed by the Companies Act 1927 and the banking Ordinance of 1962. Section 5 (b) of the Ordinance defines banking as "the accepting for the purpose of lending or investment of deposit of money from the public, repayable on demand or otherwise and withdrawable by check, draft, order or otherwise".

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2.08 Before 1947 the banking sector had been dominated by Hindus with Habib Bank as the only major Muslim banks. At independence the banking system inherited by Pakistan was mainly engaged in financing raw cotton export. The private sector took the task of economic developmental on itself and laid the foundation of the industrial infrastructure. What started with 81 branches in 1947 in the territory which now comprises Pakistan increased to 7,100 branches all over the country and 74 offices in foreign countries at the end of 1988. This phenomenal growth is responsible for the tremendous mobilization of individual saving. Even though Pakistan has one of the lowest rates of savings amongst developing countries, it is the most important source of credit in the country's economy. There are nearly 21 million depositors at present and more than ninety percent are individuals.

2.09 The NCBs operate on a decentralized basis. There are four provinces four federally administered areas, 22 districts, 311 tehsils and 45,719 villages in the country. Each province is politically sub divided into divisions and further into district tehsils union councils and village. The provincial members of the executive board of the NCBs are fully responsible for all banking functions in their respective provinces. The provincial area of operations of each NCB is divided into circles. Each circle is responsible for three to five zones, with each zone responsible for a number of branches. Branches operate at the union-council level. All domestic foreign banks are allowed to have a maximum of three branches in the country except ANZ Grindlays which has eleven branches. This is due to the fact that it came into being after independence as a merger of seven different banks.

2.10 There are three kinds of debt in Pakistan. All rates on Government debt are administratively determined and the rate structure is somewhat distorted.

Floating debt is usually short term with maturity of one year or less. This includes adhoc T-bills which are like an automatic overdraft facility for GOP at 0.5% and held by the State Bank. Regular or eligible T-bill at 6% held by commercial banks to meet their asset reserve requirement and Government Treasury. Deposit Receipts (GTDRs) at 9-10.5% held by the general public. These account for 43% of government debt.
Permanent debt which includes 7 - 20 years loan & bonded debt at 5-12%.

Unfunded debt including the National Savings Scheme. This includes instruments such as Defence Savings Certificates. Special Deposit Certificates ranging from 12% to 15 - 16%. This accounts for 44% of government's domestic debt.

The total debt and rate of return breakup is as follows.

% Of Total Debts	% Rate Of Return
30%	1.5 - 3 %
20	5 - 6.5
20	8 - 12
30	12 - 20

(Source : SBP Annual report)

Recently ineligible T-bill have been auctioned, in order to have a secondary market for the non bank public.

2.11 The financial sector in Pakistan is characterised by an ever increase in bank financing. The increase in the share capital during 1983-88 was only 25% in sharp contrast to the increase in bank financing which over the same period was almost 50%. Five NCBs account for 80 percent of the financial system's assets whereas the foreign banks account for another 10 percent of the asset. The remaining 10 percent is accounted for by the specialized banks and other non bank financial institutions.

2.12 Commercial banks in Pakistan are required to hold the 6 percent T-bills to meet the 'liquid asset' reserve requirement of 30% as stated by the SBP. This is in addition to a 5% cash liquid asset requirement. The reserve requirements combined with the low rate on eligible paper drives up the rates to the private sector borrowers. Deposits of banks are fully guaranteed by the Government of Pakistan (GOP). The legal implication of this guarantee are ambiguous as it is not an outright insurance such as that provided by the FDIC in the United States (up to $100,000).

2.13 The National Credit Consultative Council uses credit ceilings as the key instrument of monetary policy to set specific credit target for commercial banks and ensure credit expansion targets as allocated. In order to ensure compliance by banks the SBP prescribes credit target for individual banks indicating the public and private sector ceilings. Mandatory targets are also set by the SBP for small loans to agriculture, business and industry and low cost housing in the non government sector, in keeping with the desirable money supply targets. Non compliance of these limits result in penalty in the form of return free deposit to the extent of shortfall. It is interesting to note that these targets are based on the market share of both local and foreign currency deposits for the previous period. They are not based on the rate of annual growth in deposits which, if it were a criterion, would be an incentive for the bank to increase deposit mobility. Traditionally the commercial banks concentrated on short term lending but lately have also ventured to medium and long term financing due to credit lines extended by international agencies.

TABLE 1 SCHEDULED BANKS DISTRIBUTION OF DEPOSITS & ADVANCES				
				Rs. in Billion
Size of Acct	Deposit	%	Advances	%
0 - 10,000	82543.9	89.0	4645.3	45.7
100,000 - 50,000	40066.4	9.0	16339.6	34.0
50,000 - 100,000	18522.9	1.18	28339.4	14.2
100,000 - 500,000	24736.4	.6	13656.1	3.8
500,000 - 1000,000	6990.7	.10	7771.8	.6
1000,000 - 10000,000	21752.8	.9	44413.9	1.6
10000,000 & over	25548	03	68386.8	.1
Total	22661.1		169896.8	100

As can be seen 89% of depositors have holdings of less than Rs.10,000 whereas more than 40% of the advances go to .1% of the borrowers.

The following table shows the secheduled bank advances by the nature of security pledged.

SCHEDULED BANKS ADVANCES CLASSIFIED BY SECURITY PLEDGED.		
		Million Rs.
		%
Golb, Bullion	924.1	.5
Shares and Financial Instruments	5754.2	3.39
Merchandize	58065.9	34.2
Fixed Assets including Machinery	19235.1	11.33
Real Estate	37989.3	22.37
Fixed deposit & Insurance Policies	6302.7	3.71
Other Secured Advances	35507.0	20.9
Unsecured Advances	6118.5	3.6
		100.0

2.14 Major milestones in the history of the financial sector were the Nationalization Act of 1974, the setting up of the Development Financial Institutions in 1959 and the implementation of Islamic modes of finance which was fully accomplished in 1985.

NATIONALIZATION

2.15 In the early 1970s credit was concentrated in big accounts and banking was characterized by interlocking of ownership with enterprise. On January 1, 1974 the

Government of Pakistan decided to nationalize the scheduled banks and promulgated the banks Nationalization Act 1974, the stated objectives were;

- To obtain access to use of capital concentrated in the hands of the rich banking elite and channel it to more urgent social welfare projects.
- Coordinate banking policy for joint activity without eliminating healthy competition,
- Equitable distribution of bank credit to different classes, sectors and regions.

2.16 Nationalization completely ensured the exit of the private sector from banking. The general direction and management of affairs being totally handed over to their Executive Boards. Post nationalization the institutioal framework included the setting up of the National Credit Consvetative Council under the auspices of the SBP. The Act further provided for the setting up of the Pakistan Banking Council, as a body parallel to the State Bank. it was assigned various functions, some of which were;

Making policy recommendation to the government for directing banking activities towards national socio-economic objectives.

Formulating policy guidelines for the banks

Laying down performance criteria for banks and taking steps for assuring their observance.

Analyzing and appraising financial performance of the banks and appointing auditors.

Determining areas of coordination of banks.

Assisting the SBP in establishing a Credit Information Bureau and establishing a Research Department.

Developing management information systems and schemes for modernization of banks.

2.17 PBC was established as a buffer between commercial banks and the government. In the mid 1970's the PBC worked on the reorganization of the banking sector which included the reconstitution of a group of banks into a new bank. It was authorized to call for information statements and reports periodically. Over time however there was an overlap between the monitory sole of the SBP will monitor & regulate the foreign branches of Nationalized Banks and the SBP, the local branches. The functions of both these institutions can be seen in the table ahead. Auditing of branch performance and appraisal of crdit procedures continues to be performed by SBP staff. PBC now has a minimal role in regulation. Infect it has become a target of severe criticism and has been labelled as a 'dumping ground' or 'warehouse' for ex commercial bankers from NCBs. Most presidents of NCBs look upon appointment as chairman of the Banking Council as a prestigious pre-retirement perk, at the end of their career. The following table shows the regulating agency and the legislation for various institutions.

INSTITUTION	BODY RESPONSIBLE FOR		GOVERNING LEGISLATION
	REGULATION	INSPECTION	
NCBs	P.B.C	S.B.P	SBP Act 1956 Banking Co Ordinance 1962. Banking Reform Act 1972. Banking (Nationalization Act) 1974.
FOREIGN BANKS	S.B.P	S.B.P	Bank Co Ordinance 1962. Bank Reform Act 1972. Foreign Private Investment Act 1976. S.B.P. Act 1956.
ADBP	S.B.P	S.B.P	ADBP Ordinance 1961
IDBP	S.B.P	M.O.F	Industrial Development Fin Ordinance 1961.
FEDERAL BANK OF COOP.	M.O.F/S.B.P	M.O.F	Establishment of FBC & Regulation of Cooperative Banking Ordinance 1976.
NDFC	M.O.F/S.B.P	M.O.F	NDFC Act 1973
PICIC	S.B.P	S.B.P/CLA	Companies Ordinance 1984
BEL	S.B.P	S.B.P/CLA	Companies Ordinance 1984
HBFC	MOF	MOF	HBFC Act 1952

2.18 The national Credit Consultative Council was set up to ensure the optimum utilization of bank credit in Pakistan and channelize it for development purposes in accordance with national policy. It determines the credit need of various sectors of the economy under a confidential formula and prepares a well defined credit plan before the commencement of each financial year. The plan is then approved and allocations made to various sectors in conformity with priorities set out. The members consist of representatives of the government, banks and financial institution, business and industry. It meets as often as necessary to review the credit plan and adjust the allocation in accordance with the emerging economic situation. The allocation for the private sector are residual after government / public sector borrowing requirements are deducted from the overall credit expansion.

PROBLEMS CONFRONTING COMMERCIAL BANKS

2.19 The working of commercial banks over the last few years has been marred by their inefficient performance, political pressures and huge bad debt portfolios. The major problems being confronted by NCBs can be summarized as follows;

i. There is inadequate competition between them, which leads to inefficient operations. Even the foreign banks do not provide enough competition due to regulations, size of operations, and the small branch network.

ii. Concentration of lending in few hands due to inavailability of credit information. At present none of the commercial banks or DFIs have any system computerized or

So. No.	Name of IFB (Chief Sponsor)	Letter of Intent	Head Office	Incorporation Date	Date of License	Consent for Capital Issue	Clearance of Prospectus.
1.	Crescent Investment Bank Ltd. (Crescent Group)	24.1.1989	Lahore	4.4.89	4.6.89	10.6.89	25.9.89
2.	Trust Investment Bank Ltd. (Nisar Akbar and Rayon Group - Bank of Qatar)	29.3.1989	Lahore	22.6.89	14.9.89		
3.	Regco Qatar Islamic Investment Co.	13.4.1989					
4.	Fidelity Masraf (Investment Finance Bank) Ltd. (Nishat Group-Salman Taseer)	17.4.1989	Faisalabad				
5.	Security Investment Finance Bank Ltd. (Anwar Majeed)	3.5.1989	Islamabad				
6.	Pakistan Northern Investment Finance Company	3.5.1989					
7.	BCC Investment Bank	28.10.1989	Islamabad	14.2.90	17.2.90	19.2.90	
8.	First International Investment Bank (Packages - Amex)	28.10.1989	Lahore	7.2.90	19.3.90.	23.6.90	20.7.90
9.	Islamic Investment Bank Ltd. (Bank of Oman)	8.1.1990.	Peshawar				
10.	Alboraka Investment & Dev Bank	10.1.1990	Lahore				
11.	Pak. Investment Bank Ltd.	30.1.1990					
12.	Atlas Investment Finance Co. (Shirazi Group-Bank of Tokyo)	4.5.1990	Lahore				

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otherwise that contains information such as individual/group exposure. Therefore it is difficult to know the association of individuals with corporate groups or to obtain information on delinquent loans and uncredit worthy borrowers.

iii. Non performing loans due to lack of freedom in the selection of loan portfolio due to political pressure. NCBs have full discretion on only 30 - 75% of interest earning assets. Administered distribution of credit results in crowding out of new small private investors.

iv. Weak organization and lack of managerial policies as regards credit evaluation. There is lack of managerial autonomy and the work force is unionized. NCBs do not have the account officer system that exists in foreign banks whereby an account officer manages and monitors a set of accounts. The loan officer analyzes the reported figure periodically to assess debt capacity and strength of capital structure. Unlike NCBs, Foreign Banks have the standard practice to send out a credit enquiry to all other banks to check the status of any loans and total exposure. Loan officers at Foreign Banks also visit management to determine future plans has his/her evaluation tied to loan performance.

v. Inadequate spread between the rate of lending and rate of borrowing. Banks are able to mobilize savings at around 5% or so but earn only 6% on 35% of their liquid assets.

vi. Under capitalization . Their capital average is 2.9% of assets, which is very low in selection to the riskiness of asset portfolios and in relation to banks of other developing countries.

vii. There have been a large number of cases of willful default in the absence of efficient recovery mechanism. The lack of adequate credit reporting systems reinforces this. There have been instances of loans being granted to small and medium sized businesses in the absence of audited financial statements. Banking tribunals are also ineffective and the litigation process is lengthy and tedious.

viii. Most banks and specialized credit institutions take part in the inter bank market. The more conservative institutions are lenders while the more aggressive ones are borrowers. Mandatory credit ceilings tend to inhibit the growth of the inter bank market as they create surplus liquidity. This surplus is estimated as Rs 40 billion (Subtracting the reserve requirements of all banks from the total deposits and subtracting from this the combined credit ceilings).

2.20 Various recommendations made to increase the efficiency of NCBs under the FSAL of the World Bank include the;

i. Creation of a central credit bureau (already announced by SBP) in order to have an information network on credit of individuals and corporate groups for all NCBs and Non bank financial institutions.

ii. Conducting a comprehensive portfolio audit, in order to classify loans realistically. The FSAL guideline calls for loan classification as sub standard doubtful and uncollectable and calls for a proportionate provision in each case.

iii. Establishment of performance targets such as those employed by private sector banks alongwith issuance of new credit policies and procedures.

iv. Rationalization of the branch network on the basis of income and operating cost.

v. Improvement in the recovery of bad loans.

DEVELOPMENT FINANCIAL INSTITUTIONS

2.21 The credit enquiry committee set up in 1959 to examine the scope and working of the financial sector recommended the formation of specialized financial institutions. Development Financial Institutions or DFIs were set up with the aim of providing medium and long term credits to industry and agriculture. The following are the DFIs presently operating in the country, namely (year established);

Pakistan Industrial Credit and Investment Corporation (1957) - PICIC
Industrial Development Bank of Pakistan (1961) - IDBP
Agriculture Development Bank of Pakistan (1960) - ADBP
National Development Finance Corporation (1973) - NDFC
Investment Corporation of Pakistan (1966) - ICP
National Investment Trust (1962) - NIT
Equity Participation Fund - EPF
Bankers Equity Ltd (1980) - BEL
National Development Leasing Corporation (1985)- Private Sector - NDLC
Pak Kuwait Investment Co (1978)- Private Sector - PKI
Pak Libya Holding Company (1978)- Private Sector - PLHC
Saudi-Pak Industrial and Agricultural Investment
(1981)-Private Sector - SAPICO
Small Business Finance Corporation - SBFC
Regional Development Finance Corporation - RDFC
House Building Finance Corporation - HBFC

2.22 Most DFIs were set up in the late 1960s to address the needs that commercial banks could not serve due to inadequate resources and risk aversion. Industrial investment offered low profitability and the time frame of repayment could well extend to a decade or so. Moreover, the collateral fell short of established security criteria. DFIs in Pakistan were meant to play an important role in the finance sector, an initiative that was expected to lead to a healthy growth of broad based capital markets. They were set up in a parallel semi-government structure where a number of private corporate executives were appointed on their boards in order to ease out conventional bureaucratic delays.

2.23 Most DFIs were created with distinct development objectives such as the area of operation or the size of the project. Besides these they were also engaged in financing large scale units in nationally desirable sectors. DFIs financing criteria included regional development and objectives of development plans such as use of local raw material in projects,purchase of locally manufactured machinery, their impact on the balance of payment, and preference for labor intensive technology. On certain occasions formulae set by external lending agencies were also employed when their funds were used.

2.24 The IDBP and PICIC were set up with a view that they would play a key role in linking the corporate sector with international capital. The IDBP was an institution derived out of the Pakistan Industrial Finance Corporation PIFCO. PIFCO was set up to finance industries which the private sector was unable to undertake either because they were technologically complex or capital intensive. International development agencies such as the IFC and IDA also extended credit lines through the IDBP. PICIC was set up to provide long and medium term financing in local and foreign currencies for industries based on local raw material or are import substitutes. It also aimed at assisting foreign investors to locate suitable investing opportunities and bring them together with local enterprise.

2.25 ICP and NIT were created to stimulate the money and capital markets in Pakistan. The objectives of the NIT was the 'pooling of resources' of a large number of small investors which could then be invested in a diversified portfolio of shares. This was aimed at dispersing share ownership and relieving the small investor from maintaining constant contact with the financial position of companies. The NIT also undertook the underwriting of public issues. ICP was formed in order to undertake underwriting activities (PICIC and IDBP were also authorized to do the same) floating closed end funds, trading in shares or on its own account and providing professional investment advice.

2.26 There are three joint venture DFIs namely Pak-Libya, Pak-Kuwait, and Saudi-Pak which were incorporated in the late 1970 early 1980s. These aim to provide assistance to industrial units, joint venture projects which may or may not be in partnership with the country of the sponsors. SAPICO is particularly interested in financing agro based industries by taking an equity position in the venture.

2.27 Then there are specialized institutions such as the Agriculture Development Bank of Pakistan which provides credit to the agriculture sector, agro based industry and farm related processing units. The House Building Finance Corporation finances the building and purchase of residential property. A detail description of all the institutions follows in chapters 8 & 9.

ISLAMIC MODES OF FINANCING

2.28 The Islamization of the economic system which was initiated on Jan 1, 1981 was fully implemented during 1985. It can be divided into fiscal and financial measures. Fiscal measures include the Zakaat and Ushr Ordinance. Financial measures required banks and other lending institutions co-provide financing on the basis of participation in profit and loss. Under Islamic Law this is a mandatory deduction from saving deposits and profit that remains in the hands of the owners for one full year, which goes into the central Zakaat Fund. This fund is administered by the government which then channels funds to various welfare projects on a nation wide scale. The various instruments of Islamic Finance are along the lines of equity rather than debt, and are designed on the basis of Profit and Loss sharing. Under Islamic banking the cost of credit is fixed for a predetermined period of time, on a markup basis. Financial institutions purchase assets and sell them with a profit margin that is mutually agreed upon with the borrower. The agreed price is payable on a deferred payment basis either in lump sum or installments. Incentives for prompt payment, usually a rebate on the agreed markup are standard. Markup was initially used for providing short term financing and later extended to term financing. Beyond the predetermined period of the loan, the system is not time bound. Finance charges do not accrue after the agreed period so delay or default result in loss of income to the financial intermediary. Loss of the 'prompt payment' rebate is the only penalty for a defaulting borrower. The various instruments introduced in Pakistan include the following;

2.29 Profit and Loss Sharing Deposit Accounts (PLS): There is no maximum limit to the amount of money that can be deposited in a PLS savings account. Under the PLS system the proportion of profit or loss is determined retroactively by the banks once every six months as a function of the banks profitability during the preceding 6 months. Incase of term deposit the depositors are issued a Term Deposit Receipts and if the receipt is encashed before the date of maturity without completing the minimum period of six months, the deposit is withdrawn from the PLS and depositor dces not get share in the profit.

2.30 Musharika or Mark-up financing: Musharika is a kind of temporary partnership where both a customer and a bank in an arrangement of business or financing contribute their money, effort or skills or a combination of all these components. In this arrangement profit is shared in a pre-agreed proportion but loss if any is borne by the capital only. Profit sharing ratios are determined in accordance with the profit projections compatible with the company's past performance or in light of future plans and the general economic climate. The working capital requirements of trade and industry are met through this scheme. The capital provided by the bank is not equity but an investment. NCBs stipulate that capital be in the form of checking account or an overdraft account where the deposits and withdrawal are at the convenience of the borrower. The company has to make payments at the end of each quarter. The traditional debtor creditor relationship is maintained because of the predetermination. The entire management or operation remains with the borrowing company. Banks give due recognition to managerial skills by awarding a portion of the profit as 'management fee' or bonus.

2.31 Hire-Purchase Financing: This scheme is geared towards meeting the fixed investment needs of various sectors such as machinery equipment, and commercial and industrial vehicles. Monthly rental installments are so fixed that the amount invested by the bank alongwith some rental income is fully ammortized during the validity of the agreement and within the normal useful life of the article concerned. The ownership of articles vests in the bank till it is transferred in favor of the hirer on payment of all the agreed installments or incase a settlement is reached.

2.32 Modarabas: Is a general or specific purpose fund which is formed under a limited partnership agreement. It is raised through a public subscription and is managed by a management company like that of a mutual fund. It is designed to pool the entrepreneurial talents of the not so wealthy with the money of the wealthy who may not have any managerial prowess. 'The Modareb' or manager is required to put in ten percent of the capital while the 'Rabbul Mal' or investor contributes ninety percent of it. The arrangement may be for a fixed period or for an indefinite period. The earnings are to be shared on a profit and loss sharing basis. The earnings of a modaraba are exempt from tax if ninety percent of it are distributed to the investors. Modarabas can also have a debt/equity ratio of 80 : 20. There are number of activities that a modaraba can undertake. Lately leasing of industrial assets and motor vehicles is a very popular activity undertaken by the various modaraba companies. At present there are 21 Modaraba management companies registered and up until now Rs 955 million has been raised through 11 funds.

2.33 Lease Financing:The financial institution as lessor provides medium or long term credit for acquiring assets on a deferred payment basis. The lessor retains ownership of the assets and the lessee obtain the possession and use of it and bears all operating risk. Ownership may be transferred at the lessee's option on payment of nominal residual value determined by the lessor. This mode has been used for financing buildings, plants and machinery and tubewells besides commercial motor vehicles.

2.34 Participation Term Certificates: Based on a profit and loss sharing. PTCs are similar to convertible debentures with the difference that the bank is going into a 'partnership' with the borrower and has to participate in the profits as well as losses. The holders of the PTCs, in lieu of losses suffered in any financial year, are issued convertible common shares of the company to the extent of such loss from the term capital created for the issue. Subsequently the term capital is deemed as ordinary capital. The convertible shares may be reduced from the profits of the company in subsequent years, as provided in the agreement. Moreover, these shareholders have the same voting rights as the rest of the common stockholders.

2.35 Term Finance Certificates; TFCs are issued by borrowers to establish a basis for payment for the purchase of assets from bank. Instead of a conventional loan arrangement, the bank or DFI enters into a buy sell agreement whereby it buys assets and re-sells them to customers. The sale price is based on cost plus an agreed rate of profit, established within a range set by the SBP. Cost is paid by customers over a 3 year period (short term) or 3-6 years (long term) by the issue of a series of TFCs with six month maturities. On each payment date a TFC matures, customers pay the bank or DFI the face value of the TFC which is then cancelled.

2.36 The Islamic modes of financing were implemented by the SBP by prescribing a methodology of calculating the maximum service charge (10 to 20%) in case of return free lending by NCBs and DFIs and the maximum and minimum rates applicable to the investment type modes (minimum 10 percent). The Islamization does not apply to foreign branches of NCBs nor to foreign currency accounts kept in Pakistan. All arrangements under interest based system at the time were to be honored till maturity and transactions with foreign governments and international institutions remain interest based till an acceptable system evolves.

THE STATE LIFE INSURANCE CORPORATION

2.37 SLIC has the monopoly of life insurance business in Pakistan. Life insurance is the single most important non-banking source of mobilization of household savings. The Insurance Act of 1938 and the investment rules made thereunder govern the investment of life insurance funds. It was established on November 1, 1972 with a Principle office and three Beema units which were mainly concerned with selling, underwriting, claim settlements and servicing life policies. The three beema units have been replaced by five zonal offices. SLIC is fully guaranteed by the Government and has a small pension division as well. In the public sector pension funds are unfunded and government employees are members of non contributing schemes. By law pension funds are to be invested in Government securities or the NSS. For SLIC the law requires that 40% of the funds be invested in Government or Government approved securities. There are discretionary upper limits to the proportion that can be invested in certain assets. They are as follows;

Qouted companies,these should be large concerns with a proven track record	40%
Propertieds	60%
Term Finance Certificates	60%
Bank Deposits	10%

Actually 70-75% of the insurance funds are invested in Government or approved securities and 25-30% in other assets such as real estate investments. This is in contrast to the western countries where insurance companies and pension funds are the largest investors in all kinds of instruments of investment especially stocks and bonds.

THE SECURITIES MARKET

2.38 Well developed capital markets aid in transferring real economic resources from lender to borrower. The role of a stock market in any economy is of value in that ;

It collects savings that would not otherwise go into financial investments and channels these into productive investments.

It enables companies to obtain equity to match debt for the purpose of growth and expansion.

It enables the government to disinvest equity and attract investors, thus have a wider ownership of enterprise.

2.39 In Pakistan there are two stock exchanges one each at Karachi and Lahore. They are regulated by the Securities and Exchange Ordinance 1969 and the Securities and Exchange rules of 1971. The Corporate Law Authority (CLA) has the dual responsibility of the enforcement of law and surveillance of the stock exchanges and company affairs. It intervenes in the working of the exchanges whenever it is considered necessary in public interest. Insurance companies are listed while banking companies are not listed on the exchanges. The security market is not well developed and evidence is that out of a total number of 21,804 joint stock companies in the country only 1,595 are public limited companies. Out of these only 450 are listed on the Karachi Stock Exchange and only 298 on the Lahore exchange. The exchange in Lahore has a role that is secondary to that of the KSE. According to an estimate almost 90% of the public subscription are from industry that is located in and around Karachi. At present there are two hundred members of the Karachi Stock Exchange out of whom only 87 are active. Lahore Stock exchange has 117 members out of whom only 18 are active. Official figures show the number of shareholders as greater than one million whereas participants estimate it to be around 300,00 only. Some selected statistics regarding the stock market are given below.

STOCK MARKET - SELECTED STATISTICS

	1984	1985	1986	1987	1988	1989
No. of Companies.	347	362	360	382	411	450
Market Capitalization (Rs. Million)	19647.4	21953.5	24422.4	31617.1	38151.4	43934.9
Index of Share Prices (1980-81 = 100)	182.35	176.32	171.02	222.68	260.59	273.23
Turnover of Shares (Million No.)	N.A.	94.7	147.0	85.4	84.2	172.7

2.40 The causes for the lack luster performance of capital markets can be attributed to a number of factors chief among which are;

Credit policies
Disparities in the interest rate structure

2.41 Family controlled businesses are the norm in the private sector, where sponsors their family and friends own approximately 60% of the equity. Out of the 40% that is offered to the public 20% has to be offered to NIT and 10% to ICP, to 'enable them to carry out the role of ironing out dramatic moves in share prices'. This in turn has a favorable impact on the portfolios of investments of these institutions, due to the CCI pricing formula as discussed later. Family control is reluctant to admit outsiders for which reason they resort to cheap bank credit at low rates of interest. Good banking connections aid in this process which results in a high debt to equity ratio, which in turn makes the venture appear risker to potential shareholders, thus forming a viscous circle. Due to narrow shareholding bids, to takeover poor performing companies are next to impossible.

2.42 Interest rates as already mentioned are highly distorted. The nominal rates vary from 6% to 15-16% on 3 year investments of the National Saving Scheme. For deposits under three years, the Khas Deposit yields 12.5%. The absence of risk and the advantage inherent in the NSS increases their attractiveness to individuals and institutions alike. On the other hand only 15% of the companies pay dividends between 20-30% whereas others have a lower rate and nearly 40% have a record of not paying at all over the last 9-10 years.

2.43 According to economic literature the efficiency of the capital market can be measured along the following criteria;

Allocative Efficiency: this refers to the channelizing of savings into the most productive and profitable uses.

Informative Efficiency: This refers to the fact that prices fully reflect all the information available.

Operational Efficiency: This reflect the day to day operation of the market. It is responsible for keeping transactions cost down and have them determined by market forces.

Second period Efficiency: This arises if market provides fair game to all players. It is when there are equal opportunities of access to price sensitive information and there are no consistent opportunities to make gains at the other investor's expense and so increase the inequality of wealth from one period to another.

2.44 In Pakistan, information as regards companies' accounts and management decisions is published too late and share prices do not reflect the information available. Often the integrity of the accounting profession is also in question. The efficiency of a stock market or the lack of it is a direct reflection of the efficiency of the economy in which it operates. The problems being faced by participants are reflective of the conditions prevalent everywhere. There don't seem to be too many 'fair games' economically, socially or politically, so perhaps asking for fair play on the stock exchanges is.out of context. In an environment where there is lack of law and order, where presence of illegal money and gross tax evasion are facts of life and where the august institution of the civil service is corrupt achieving stock market efficiency might only remain a dream.

2.45 The trend towards having a public issue is on the increase in Pakistan. In 1989, 38 companies were listed. The total market capitalization at present is Rs 49 billion, which is approximately equal to US $2.5 billion. There are a number of reasons why a company would wish to go public. Some of these as follows;

1. Public limited companies are taxed at a lower rate than private limited companies.Prior to 1989 the income of listed companies was taxed at 40% whereas the rate for private companies was 55%. This has been changed to 50% for listed companies as of 1989.

2. Listed companies' dividend income above Rs 15,000 is tax exempt whereas those of unlisted companies are taxed at the regular income tax rate.

3. Companies may be forced to go to the market as the amount of capital required to support a competitive sized business increases

4. In view of the over subscription of issues in the past underwriting is not a pre condition to going public which means issuers will not shy away due to the cost of underwriting.

5. The new generation of businessmen has professional degrees and wish to work in a more professional environment. Thus they are keen to instill reporting standards and have detailed disclosures.

6. Government policy on disinvestment of public business entities is a sign of encouraging the private sector.

7. Securities prices rise immediately to great heights after the issue which is very attractive to entrepreneurs.

8. GOP has changed rules regarding Bridge Financing. Bridge loans are required to be treated as debt as opposed to equity. This amendment would compell companies to go public.

2.46 Inspite of all the above there are various factors which deter potential investors. There are a number of distortions in the securities market in Pakistan, chief among which is the restriction on issuing shares at a premium. The CCI does not allow the premium on shares to exceed 50% of the difference between the intrinsic value (paid up capital and reserves) and the paid up value of the share. This pricing formula has no rationale. Par value, an accounting convenient does not reflect the market value of the company nor all the available information. It results in the over subscription of shares, as investors can make huge gains over night. They also get a tax break. Informal trading of the securities starts before the official trading, where speculative group bidding pushes the price up to enormous heights thus rendering the public offer into a virtual lottery. The institutional investors such as NIT and ICP gain from this arrangement as the allotted shares show immediate appreciation on their books. Thus performance of their portfolios is not a function of asset selection or the expertise of portfolio managers. Thus market forces are not allowed to determine the price and have lead to the creation of a parallel market.

2.47 Insider Trading is another major obstacle to the smooth working of the market. Insider trading by the officers and directors of the company is not a criminal offense in Pakistan as it is in most western countries. Section 244 of the Securities and Exchange Ordinance states that gains made within a period of less than six months be tendered to the company and a report be sent to the CLA. However it provides that 'nothing in section

244 shall apply to a security acquired in good faith in satisfaction of debt previously contracted'. This virtually renders the restrictions of section 244 useless. Insider trading is further encouraged due to the fact that stock brokers are allowed to sit on the board of the qouted companies.

2.48 Some recent measures taken by GOP to encourage participation in the capital market are as under;

1. As mentioned earlier underwriting has been made optional in order to bring down the cost of the issue.

2. Restrictions have been imposed on bridge financing, which is now being treated as debt for the purpose of working out debt and equity ratios.

3. The SBP has stopped general line of credit to financial institutions, indirectly encouraging them to go to raise resources in the market through instruments such as certificates of investment such as TFC & PTCS. SBP has also issued instructions to DFIs regarding debt/equity and current ratios for projects of various sizes.

4. It has been decided to induct institutions such as investment banks as members to improve the quality of brokerage.

5. The privatization program will increase the supply of shares in the market. As a first step 10% shares of the Pakistan International Airlines have been disinvested. 20% shares of one of the commercial banks MCB will also be offered to the general public (this has met opposition from the workers union of this institution).

6. To extend brokerage services to the northern part of the country, it has been decided to set up a stock exchange in Islamabad (the case has been put on hold due to evidence of corruption and nepotism in the sanctioning process).

2.49 The government has recently decided to set up a Pakistan Fund to be sponsored by the Asian Development Bank. This off shore fund of US $50 million is proposed to be listed on London Stock Exchange and is expected to attract institutional investors abroad.

THE UNOFFICIAL FINANCIAL MARKET IN PAKISTAN

2.50 Financed by wealthy landlords and industrialists, Pakistan unofficial or parallel financial sector has developed a lot over the past two decades. As in other developing countries, the system has developed due to the fluctuation in exchange rates, and transactions that are less easily monitored or controlled through the regulatory framework such as arms, deals, narcotics and real estate deals. It generally consists of the following arrangements;

The 'Hundi' system of foreign exchange transactions

Credit arrangements in the non-corporate cotton textile sector (sooter mandi)

Merchant credit operations particularly in the commodities market

Arrangements within the non corporate banking sector Jaurya Bazaar or other Indigenous banks

2.51 The informal sector at one time was restricted to hundis which are informal promissory notes popularized due to the large number of workers overseas. Over time, however, it has become increasingly urban in character and has developed closer and more complex linkages with the formal economy. The sector is extremely fragmented and plays an important role in the transportation and textile sector. The informal sector operates chiefly through brokers who know or identify borrowers who are retailers requiring stock (inventory) financing, cottage industry requiring finance to purchase raw material or commodity traders to finance purchase of grain, spices etc from farmers. There is a sophisticated system of credit control which exists by way of a highly developed communication network among brokers which limits the chances of bad debts. the collection system that exists in this regard is alleged to be similar to that followed by the mafia in certain countries.

2.52 NCBs play a very minor role (if at all) in the informal sector. The market participants do not trust the NCBs due to various reasons. For instance, NCBs cannot issue bearer securities, and tax officials can obtain information regarding identity of account holders.

2.53 The hundi system consists of a 'chitthi' or promissory note given by the foreign exchange dealer to the remitter in return for cash foreign exchange. The chitthi can be encased in Pakistan in domestic currency as a negotiable instrument of exchange.

2.54 The money market in sooter mandi in Faisalabad is an elaborate credit system parallel to the official system where a number of self devised money instruments are used to facilitate transactions. These transactions are estimated at Rs 135 million per day and the total value of these instruments in circulation at any time is estimated at Rs 4 billion (source: Parallel Financial Sector in Pakistan by Ferguson Associates). Cash delivery receipts are a common instrument in this market and the chief participants are;

Yarn commission agents
Cloth commission agents
Cloth exporters
Weavers
Brokers and
Investors

2.55 The Nationalized Commercial Banks are a part of these arrangements in that they issue Cash Deposit Receipts to investors which are encashable during banking hours. Knowledgeable investors open PLS deposits before obtaining CDRs and thus earn a profit. Any new investor only gets a blank endorsed CDR and the accruing profit is earned by the bank staff who have opened a PLS account in the interim. A CDR is usually accepted only if it is issued by a bank branch in one of the eight bazaars surrounding Faisalabad's clock tower. When presented for encashment the banks pay in notes of small denomination, which acts as a deterrent against indiscriminate encashment of CDRs and to ensure their quick return to the system.

2.56 The merchant credit system consists of intermediaries known as 'arthies' who finance forward operations, hedging storage or speculation in specialized commodities such as cotton, wheat and fruit.

2.57 Operations in the noncorporate banking sector date back to the colonial period when indigenous banks provided services to entrepreneurs in large cities. Some went on to become a part of the formal banking sector. Today this sector is considered to be of a substantial size with 12 leaders and operations are streamlined based on interlocking relations.

2.58 In recent years, narcotics and real estate business have provided boost to the informal sector. The reach of these markets are no longer restricted to a single market, city or country. The unofficial market extends overseas. Funds that have been generated through double invoicing of import and export transaction proceeds of drug sales and possibly the proceeds of fraud committed on domestic and international banks are all syphoned off to bank accounts outside the country. The attraction for importers in this market is the fact that they borrow Rs 100 million to pay for imports which are documented to show a value around Rs 10 million which is the basis used for calculating duties.

2.59 Foreign exchange transaction in this sector have thrived due to official restrictions. Inspite of all the restrictions on Foreign Exchange it is fairly easy to obtain the currency of any kind at a little above or below the official rate. Popular currency such as the US dollar and Pound Sterling sell at above the official rate. Various restrictions are also responsible in inflated exchange rates. For instance Banks in Pakistan are not allowed to provide foreign exchange for the purchase of motor vehicle thus people resort to the unofficial market. According to an estimate approximately $232 million (source:Rationalization of DFIs) was financed through this sector last year. Foreign exchange restrictions have been rendered ineffective to a large extent also due to the Foreign Exchange Bearer Certificates (FEBC) Scheme. Under this scheme anyone can buy FEBCs up to an unlimited amount in Pakistan, convert them into foreign exchange through a check or draft and take the proceeds overseas without disclosing the source of funds. In Pakistan these can only be encased in local currency.

2.60 Public transport vehicles such as taxis,trucks and buses etc. are financed through transport entrepreneurs operating out of this market. Real estate deals are also usually not financed through banks. Instead documentation in these deals is usually much below the actual price to avoid wealth tax and buyers do not need to disclose the source of the money.

2.61 Nowadays international financial markets offer a great channel for funds of wealthy individuals regardless of the source. These markets are virtually unregulated and convertible currencies are free to flow around unfettered irrespective of the source. According to a report by J P Morgan non bank sector residents of fifteen developing countries held assets abroad amounting to almost $300 billion at the end of 1987 which was more than half of the foreign debt outstanding of these countries. Wealthy families transfer assets abroad due to lack of confidence in the political and economic climate in the country. These people will keep their assets abroad as long as the exchange rate is over valued and there is a negative real interest rate. The large budget deficit, insofar as it leads to deficit financing through printing of money and high inflation, and the highly inefficient capital markets also contribute to this exodus.

CHAPTER 3

INVESTMENT FINANCE BANKS : BACKGROUND

3.01 Before recounting the experiences of the Pakistani private sector in the field of investment banking it is important to keep in mind the following discusssion.

INVESTMENT/MERCHANT BANKING

3.02 Merchant Baking as it is known as in Europe is identical to the US phraseology of Investment banking. Investment/Merchant banking can be defined as wholesale banking dealing in large deposits and loans. It includes fee based activities such as corporate advice and management of loans and initial public offerings. Typically an investment bank has a small proportion of operational staff and a high proportion of decision makers. It may typically have a limited deposit base. Investment banker organise syndicates and advice on sources of credit, corporate strategy, merger and acquisition activities, leveraged buy out decisions and privatization issues. In developing countries they are usually more active in project financing activities. (Thus acts of financial sophistication and complexity are "business as usual" for them.)

UNIVERSAL VS SPECIALIZED BANKING

3.03 The case for having specialized banking where each institution plays a role that is concieved by the regulating authorities or having universal banking whereby every institution has the mandate to undertake any/all activities is largely a policy choice. On the one hand, we see a more specialized approach to banking in the United States where regulation in the form of the Glass Steagall Act prohibit commercial banks from undertaking activities that would essentially lie in the domain of investment banks. This regulation came in the wake of the stock market crash and was aimed to avoid the exposure of depositor funds to equity risk. It was formulated with a view to matching maturities of deposits and loans and to avoid conflict of interest situations. Commercial banks in the US were allowed to have investment banking subsidiaries outside the United States. Over time, however, due to financial engineering commercial banks are offering products that are very sophisticated and not much different from Investment banking products. The situation is quite the contrary in Europe ,where there are no restrictive laws but commercial banks have separate investment/merchant banking subsidiaries. In general the trend in the world today is increasingly towards universal banking. Thus prohibitions under law are not needed when a situation naturally creates the desired condition. Even in Pakistan there has been a trend towards universal banking where NCBs have extended medium and long term lending to customers through lines of credit provided by the World Bank and the Asian Devlopment bank. On the other hand DFIs have been urged to take deposits and offer checking account facilities to the public. The charter of the proposed IFBs may seem to favor specialized banking but that is not the case for institutions such as modarabas and leasing companies (See detail follows).

INVESTMENT FINANCE BANKS IN PAKISTAN

3.04 Announced in the budget speech of 1987 by the Finance Minister of the time, Investment Finance Banks were given a charter for operation in the private sector. This step was directly in line with the conditions laid out in the Financial Sector Adjustment Loan (FSAL) of the World Bank which stated a need for private sector participation in the Financial Sector. This was done with a view to creating competition for the nationalized commercial Banks who were seen as incompetent and inefficient. This was envisaged by most as a means for the private sector to re-enter the field of banking. The role of these institutions was to provide Project Financing and Merchant Banking facilities to the corporate sector. They were expected to promote capital market development as 'market makers' providing a two way quotation system for all government paper.

3.05 The initial government notification of 1987 attracted a total of 45 applications which were filed in December. By June 1988 Letters of Intent were issued to six of the interested parties. With the change in government, however, the previously awarded letter were withdrawn in November 1988 and new applications were invited. Fifty seven applicants came forward out of which six were given approvals by June 1989. This figure has reached 12 by May 1990.

3.06 According to the Gazzette notification of the government of Pakistan Statutory Regulation - SRO No. 585(I)/87 anyone desirous of commencing operations has to comply with a number of conditons, some of which are as follows (see exhibit for the original text of the notification):

i. It must be registered as a Public Limited company.

ii. It should have a minimum paid up capital of one hundred million rupees and shall be listed on the Stock exchanges in Pakistan.

iii. Its investment policy has to be clearly and concisely stated in its Memorandum and Articles of Association and the prospectus for the public offer of its securities.

3.07 The objects of Investment Finance Banks preclude banking business and Insurance business as defined by the Banking Companies Ordinance 1962 and the Insurance Act of 1938 respectively. As laid out in the gazzette notifications of July and August 1987, the chief objectives and functions are as under:

Money Market Activities

3.08

i. Issuing short term paper or certificates of deposit or investment of not less than 30 days maturity.

ii. Trading in commercial paper issued by it clients, Government securities, promissory notes, Banker's acceptances and other money market instruments acting as a broker or on its own account.

iii. Assisting in the issue of commercial paper, including introdution of companies to the money market, preparation of documentation, distribution and market making.

iv. Acting as a broker or on its own account in the Call Money market.

Project Financing Activites:

3.09

i. Make investments through underwriting of pubic issue, shares, participation term certificates, and term financing certificates.

ii. Guaranteeing and counter guaranteeing loans and obligaton.

Corporate Finance Activities:

3.10

i. Act as advisor and agent in obtainig direct bak loans, export credit, syndicated loans leases and other project financing.

ii. Assisting companies in cash management and private placement of debt and equity.

iii. Assisiting companies in financial restructuring, mergers and Acquisitions and divestiture decisions.

iv. Preparing feasability, market or industry studies and raising equity through venture capital for new and existing companies.

3.11 The afore mentioned cover a wide range of activities, infact the SRO is open to accomodate other activites which may be discussed with the Controller Of Capital Issue. Investment Banks are expected to play a major role in the restructuring of the financial sytem in Pakistan. They have to mobilise new sources of funds and tap into niches peviously ignored by commercial banks and DFIs. They are expected to develop Money and Capital Market operations. In addition they are expected to share the burden of DFIs in providing financial assistance and advisory services.

SANCTION PROCESS

3.12 The sanction process as indicated by nearly all the sponsors interviewed was not devoid of favoritism and political considerations. According to one source four out of the first eight sanctions given in the first six months of the new regime's coming to power were purely political favors Chief among them were Fidelity Masraf (Investment Fianance Bank) Ltd, a favor to the Deputy leader of the opposition in the Punjab assembly. Trust Investment Bank Ltd,given to Nisar Akbar an MNA and Choudry Umar Draz an MPA in the Punjab assembly. The next was Tariq Islam a relation of the highest office in the country and one to Mr Anwar Majeed who had friends in high places. The track record of these sponsors except those of Fidelity Masraf was unknown. Infact, Mr Anwar Majeed, was involved in a court case in one of the Gulf States on charges of embezzlement.
Two other sanctions were given in exchange of contributions made by two of the leadng corporate groups to the funds of the ruling party. Another two were granted due to intervention of the emmisaries of two foreign governments. Thus merit and setting of tangible and measurable criteria was not the path followed by the authorities. On the other hand to say that all the parties who have recieved permissions to operate investment banks are not sound would not be true. This is further substantiated by the fact that most of them belong to corporate groups who can boast outstanding performance. In three cases the same group got sanctions by both regimes. (BCCI, AMEX, ATLAS)

3.13 According to one of the sponsors the IFB sponsors can be divided into two categories; those who are interested in changing the present state of the capital markets in Pakistan. They will be sound professionally, are bound to be interested in the long term viability of their venture and will fight tooth and nail, any unncessary delays in their path. The other category is people who are only interested in the short term benefits they can derive out of setting up investment banks. These were labelled as 'fly-by-night' operations not much different from the investment companies of the late 1970s. In the late 1970's and in later in 1987-88 various finance companies appeared in the market who granted rates of return which were much higher than any offered. These fly-by-night operations put up sign boards all over in large cities that projected their image as large corporate house with diversified portfolios of business. Names such as Pioneer Industries and Samad Enterprises became the subject of conversation with a lot of individuals and retired personnel who were keen in sharing the success of these. This clearly indicates that it is very important for the Government to have checks and balances to avoid institutions or individuals who might take advantage of naive investors and bring a bad name to all of them.

3.14 By the same token it is crucial to give the professional groups enough incentives to operate and flourish. The post nationalization performance of commercial banks and the inefficiency of the public sector DFIs is well known. It is desirable for the government to extend all support to IFBs in recognition of the role they are expected to play in the health of the financial sector.

CHAPTER 4

FIVE CASE STUDIES

4.01 The following is a brief description of five investment banks that are at some stage of initiating operations. Detailed interviews with key executives of these institutions were conducted in order to do so. The various issues and policy recommendations emerging from these discussions follows the description.

CRESCENT INVESTMENT BANK LTD.

4.02 Crescent Investment Bank or Cresbank, with its head office in Lahore is the first investment Finance bank to be set up in the private sector. It is a Joint venture of the Crescent Group and National Development Finance Corporation (NDFC). The equity structure is as follows;

Crescent Group	50%
NDFC	20%
General Public	30%

4.03 The Crescent Group is a reputable and well established corporate group in Pakistan. It has been involved in various industrial ventures and has a successful track record. It has the development and profitable operation of several industrial and commercial ventures to its credit. These include fifteen public limited companies including seven textile units, two sugar mills, distilleries jute, particle board, steel and engineering works, trading, contracting and consulting and insurance and a leasing company. The group has also been dominant in the field of cotton trade and has had close association with leading organizations in Pakistan and overseas. The share prices of companies are adequate reflection of the Group's performance. For instance, Cresecent jute share pice is 107% above face value, whereas other jute mills are selling at well below par. Besides the interest in Insurance and leasing (Pakistan Industrial leasing Corporation) the group had interest in a commercial bank in the pre-nationalization days and also has representation on the board of PICIC.

4.04 The group is the poineer in the field of Investment Banking in Pakistan. A brief history of their experience follows. The group had applied for an IFB when applications had been called by the previous government in 1987, but inspite of a good track record did not recieve permission to operate. After the elected government came into power another application was immediately filed and skepticism was expressed over the lack of justifiable measurable criteria that had been used previously for selection (some sanctions had been given during the last days of the last regime and had been rightfully entitled as 'sanctions at midnight'). All previous permissions were subsequently cancelled and new applications were invited. The Group initially wanted the Asian Development Bank as a partner with a ten percent stake. The groups leasing company also has equity participation of the ADB and has direct lines of credit confirmed with the World bank, the Asian Development bank and the Commonwealth Development Corporation. This arangement, however was not looked at with favor by GOP (this condition was subsequently done away with) and the group was forced to withdraw. It subsequently applied with NDFC as partner and was one of the few to be granted a 'letter of intent' in January 1989. According to a sponsor of one of the banks, the ease of the sanction even this time was not entirely on the basis of measurable criteria, but infact was directly related to the amount of contruibution that a group made to the fund of the ruling party. It is alleged that inspite of being one of the premier corporate groups in the country today, the Crescent Group had to resort to the same.

4.05 Inspite of inherent delays such as the name of the bank (five names were changed in the first eleven months after the letter of intent had been issued), the issue was brought to the public in October 1989. As expected the issue was well recieved by the public and it was over subscribed by 82 times and shares are subsequently being traded at almost two times face value. The Commencement of Business certificate was finally granted in December 1989, and Cresbank opened its doors for business in January 1990. Even after the successful public offer GOP wanted the sponsors to do it over, citing a change in decision regarding the sponsors' minimum equity requirement as Rs 100 million. At this point the sponsors expressed their inability to scratch the previous public offer and go through the entire process over again and GOPs objection was withdrawn.

PRODUCTS AND COMPETITION

4.06 The following is a list of products and services that the bank proposes to offer;

Project Finance
Equity Investment and trading in listed securities
Underwriting issues of corporate debt and equity securities
Guaranteeing loans and other obligations
Loan syndication
Financing trade
Financing securities purchases (Margin Finance)
Issuing certifictes of deposits on its own behalf and on behalf of customers
Discounting of debt securities
Mobilization and management of mutual funds
Investment and Financial advisory services
Provide fee based services like fund management portfolio management, preparation of feasibilities.

4.07 Management realizes at this stage that inspite of the list of allowable activities, most of these require a lot more sophisticated and organized infrastructure than the existing. Initially management may have to undertake activities that are already being undertaken by other institution such as DFIs and NCBs for making inroads into the sector. In other words a client base will initially be built by undertaking conventional activities as it may take up to four or five years for formulating new products, bringing them to market and having people accept them. The management at Cresbank does not want to engage in project finance activities at the scale at which the DFIs perform this activity. Instead they see themselves as being the catalyst in the entire process. Management wants to provide "One Window Operation" for prospective clients. It wants to reduce the time taken for processing project financing requests and provide clients the advantage of obtaining all services under one roof. The bank in turn will be in a position to refer clients to various DFIs and function as an Interface. This would benefit the client who in turn would have a lot more credibility in the eyes of the DFIs. Given the present nature of the approval cycle for a project and the time involved in obtaining DFI approvals, it will be a welcome step for prime corporate clients. Cresbank has also had meetings with some private DFIs such as FMO the Netherlands Development Finance Corporataion and DEG a German DFI to obtain lines of credit. These agencies displayed caution due to the poor performance of DFIs in Pakistan, and cited experiences where donors were forced to freeze lines due to poor performance.

FIRST INTERNATIONAL INVESTMENT BANK LTD.

4.08 First International Bank or Interbank with its head office in Lahore (physically in Karachi) is a joint venture of Packages Ltd., American Express Bank Ltd (AMEX). and the International Finance Corporation (IFC). The equity structure is as follows;

Packages Ltd.	30.1%
American Express	30.0%
IFC	14.9%
General Public	25.0%

4.09 Packages Group is one of the most dynamic industrial groups on Pakistan's business horizon. It has been involved in a number of industrial and commercial ventures most of which have been joint venture arrangements with industrial houses of the West. Often they have been first efforts of their kind, for instance the Tetrapak plant and the Milk plant. In the non profit sector, the group has been one of the chief sponsors of the Lahore University of Management Sciences. This is a private sector undertaking which is providing management education at par with leading business institutions of the world. The operating performance and reputaion of the group can be best judged by the company share prices which for Packages and Milkpak is 340% and 200% of face value. The chairman of the board Syed Baber Ali is the chairman of the Inter bank and is also on the board of the International Finance Corporation.

4.10 The experience of the sponsors as far as sanctions for the bank are concerned were summarized by the chairman who said that the high officials of USAID were well aware of the constraints encountered in this regard. It is pointed out that the AID official had been made aware of the progress at every stage of the process. This sanction, it was alleged could not have been possible without the involvement of the highest representatives of the United States government, and substantial verbal and written exhortations. These stemmed from the interest the US government has in encouraging free enterprise in Pakistan.

4.11 The same partners had put in an application in the pre democracy days and had nearly started operation when the licenses ware revoked and it had to be disbanded. Unnecessary delays were encountered by them at every juncture of the reapplication process, chief among whom was the highest public authority in the ministry concerned who at the time was of the view that foreign partners should not be given the right to repatriate profits. It must be pointed out that this right is safeguarded by the constitution of the country.

4.12 Interbank's chief executive officer is Mr Fredrick Piecoczeck an experienced investment banker appointed by American Express. Inter bank was awarded the letter of intent in October 1989 and hopes to have the public offering on July 19, 1990. At present the CEO is in Karachi eventhough the sanction was given for an office in Lahore. Karachi is the centre of Business & Commerce. The major Stock Exchange is in Karachi as are the corporate headquarters of various private & multinational corporations.

4.13 Management sees the achievement of its objectives subject to the regulatory environment and the encouragement and incentives it may recieve from the authorities. Management sees Inter bank and infact all the IFBs as a force that is capable of exploiting opportunities existing in the Financial sector. It seeks to establish profitable new areas of business given liberalization of markets and the setting up of a regulatory framework condusive to capital market activities. Inter bank has the advantage of having institutional support in the form of the world wide network of AMEX and access to and knowledge of other financial markets of the world. Inter Bank management and other investment banks, see it as the leader in introduction of new financial products in Pakistan. It wants to play a major role in a substantial broadening of the financing options available to the corporate sector. AMEX's prior experience in this regard has been entirely favorable. It was one of the first foreign banks who offered leasing of corporate assets to prime clients. This was done under an unusual arrangement, whereby it went into a tripartite agreement with a Modaraba company - B.R.R Modaraba and the client.

PRODUCTS OFFERED AND COMPETITION

4.14 The products/services that it proposes to offer include;
Assistance in floatation of companies including underwriting of issues.
Arrangement and provision of short term and long term financing through paper issue, Musharikas and markup arrangements
Market making in corporate and government paper
Money market, treasury and Foreign exchange activities (Subject to approval)
Corporate and project advisory work
Floatation of modarabas and mutual funds
Introduction of investors and capital to Pakistani investment opportunities
Loans and equity syndication
Leasing

Management wants to provide competition to nationalized and foreign commercial banks, which might be expected to react by measures such as rate reduction. It also expects Modaraba companies if sufficient in number, to pose competition, given their advantagous tax structure. (please refer to detailed discussion ahead).

ISLAMIC INVESTMENT BANK LTD.

4.15 Islamic Investment Bank Ltd. with its head office in Peshawar is being set up by a group of entrepreneurs and professionals. It will have six corporate directors none of whom will have an absolute majority. One of the key sponsors is the Al-Hurair Group from the Gulf who are investing almost fifteen percent in their personal capacity in this venture. The equity structure is as follows :

Al-Hurair Group	15%
Professional group	45%
General	40%

4.16 The professional group consists of various retired civil servants (ex Governor State Bank of Pakistan, ex Secretary Ministry of Production, ex official of the PIDB etc.), entrepreneurs; (Mr. Fareed a chartered accountant, overseas Pakistanis and an experienced bankers Mr. Sultan Ahmed Khan (Chief Manager Bank of Oman in Dubai). This group does not have equity from any large corporate group in Pakistan and instead the largest shareholding is that of the Bank of Oman. Bank of Oman has a representation in Pakistan and has branches in Karachi, Lahore and Peshawar.

4.17 Management wants to provide "modern services" to the entrepreneurial class. They want to provide innovative products, especially in project finance and claim to have recieved encouragement in this regard from the aministrative authorities in the North West Frontier Province. Management expects to compete with the Development Finance Institutions.The group hopes the Islamic Bank will play a major role in development finance citing profit as not being the prime motive for business. Sponsors strongly believe in the soundness of Islamic banking and its viability in the market place. "Social responsibility" and a "spirit of service to the nation" by locating in a relatively less developed area of the country were reiterated by both sponsors who were interviewed in this regard. They also stressed the fact that they want to play a major role in the development of sectors previously ignored such as housing etc.

4.18 The sponsors indicated fragmented holding and professional management as their competitive advantage. It was proffesionals who initiated the application and then went about looking for sponsors. The entire operations are being conducted solely by Mr. Sultan Khan who is also working in the capacity of legal counsel and corporate accountant. They see investment banking as a viable channel to direct resources away from the unorganized financial sector. In this regard sponsors believe that they will complement the role of NCBs initially and eventually hope to expand operations so as to compete with them. The mandate of Islamic Bank is somewhat unclear, as most activities were those that are undertaken by DFIs or NCBs. Sponsors projects the idea of their bank more as a commercial bank. Moreover the interviewer heard a lot about professionalism yet the professional management team was nowhere in sight.

THE ATLAS GROUP.

4.19 The investment bank being set up by the Atlas group is the most recent entrant in the field. Having obtained the actual permission to operate on May 2, 1990 the Atlas group has been sanctioned its head office in Lahore, but will initially operate out of Karachi (along the lines of Interbank). The proposed equity structure is as follows;

Atlas Group	40%
Bank of Tokyo	20%
Asian Development Bank	20%
General Public	20%

4.20 The Atlas Group was formed in 1962 and in a period of 28 years has become one of the largest corporate groups in Pakistan today. It stood at number nineteen in the list of net assets of top twenty five corporate groups listed on the stock exchange. The group consists of six public limited companies engaged in diverse business. The group is heavily oriented towards engineering and more specifically towards the automotive industry. The group has a number of joint venture projects chiefly with Japanese corporations such as Honda motorcycle, Japan Storage Battery Co. Ltd. and the Bank of Tokyo. The objective of the group has always been to transfer technology into Pakistan and use the international experience of partners to build a professional business venture. The share price of companies in the group such as Atlas Autos and Panjdarya are 250% and nearly 300% of face value. The chairman of the board is Mr. Yusuf Shirazi who prides himself with the team of professionals looking after these companies.

4.21 The group set up a leasing company in 1987 with National Investment Trust and the Bank of Tokyo as partners. It took over the Muslim Insurance Company in 1980 which today, with its network of 27 branches, is one of the leading companies in the industry. It also has an ivestment company dealing in innvestment and trading of financial and other assets.

4.22 The Atlas group had also applied for a license to operate an investment bank during the previous regime. The permission was revoked like all the rest and the group re-applied in 1988. The chief sponsor indicated the lack of positive response from present authorities in the ministry concerned, so much so that sponsors were asked to put up their case to the chief excutive of the country or her family members. This suggestion was turned down by the sponsor and therefore there was no progress. Instead the concerned ministry raised objections on the location of the head office. Sanction was granted nearly two years after the application had been put in, and the visit of the Japanese Prime Minister proved to be a catalyst in this regard. It is alleged that the final approval came when the Emissary of the Japanese government wanted MOF to give them a progress report of all joint venture projects which awaited approvals. At this point the location of the Head office seemed to be of no consequence to the approving authorities.

4.23 The present Chief Executive Mr. Jawaid Iqbal Ahmed has been assocated with the group for a long time and is looking after this project till a professonal management team is hired for the purpose. Management strongly feels that so far bureaucratic controls have inhibited social development in Pakistan instead of encouraging it. It is felt that Development Financial Institutions and the public sector have fallen short of the expected role and only the private sector can now achieve the intended objectives. At the same time management feels it is very important to have checks and balances along the way so as to weed out those who are not seriously committed to the task of nation building and are in it only for the short term. Management wants to play a major role in mobilizing savings in the country and expanding the capital base. It is very conscious of the fact that individuals have a lot of money that is hoarded and invested in non-productive assets.

4.24 Management hopes to introduce innovative mechanisms of investment and deal making through financial engineering. Management expects the leasing company and the investment company as playing a major role in complementing the scope of the investment bank. The Atlas group of companies has a historical relationship with the Bank of Tokyo dating back to almost 27 years and hopes to replicate its transfer of technoogy experience with other Japanese corporate houses in investment banking. They hope to gain from the experience of the Japanese Investment banks and are working on formulationg policy documents and procedural manuals in direct consultation with co-sponsors. The Asian Development Bank is another important partner that has a wealth of resources, the group is seeking to tap this as well. Management realizes the importance of having sound promoters in order to gain the confidence of the business sector and cited its repeated success in the engineering sector by the same token. The management indicated the current dialogue between them and Yamaichi Securities under which they want to study the operating structure of an investment company that the laterhasset up with the help of the ADB in Indonesia.

FIDELITY MASRAF (Investment Finance Bank Ltd.)

4.25 Fidelity having recently obtained the letter of intent from the government intends to start operations with Faisalabad as the head office. The shareholding is divided amongst five individuals / groups and the general public. These include ;

Main Mohammed Mansha	10%
Mean Tariq Saigol	10%
Mr. Jehangir	10%
Sapphire Group	10%
Mr. Salman Taseer	10%
General Public	50%

4.26 The chief sponsors are amongst the top seven companies listed on the stock exchange with the highest net asset. Mian Mansha has been the chairman of All Pakistan Textile Mills Association (APTMA) and Chief Executive of the Nishat Group of companies (listed number 6). Mian Tariq Saigol has also been the chairman of APTMA (listed number 4). The Sapphire group (listed as number 7) Mr. Jehangir a leading stockbroker from Karachi and Mr. Salman Taseer was a partner in the reputable Auditing and Accounting firm of Taseer Handi and Khalid all have an equal stake.

4.27 The experience of the sponsors regarding the application / approval process is fairly straight forward. According to one of the sponsors the initial letter of intent was given by the Prime Minister as political favour to one of them who was a stalwart of the People's Party. He further added that out of a total of six sanctions given during the first half of 1989 four were political favours (please see detail above).

4.28 Inspite of the nature of approval, even this group faced a lot of difficulty and unnecessary delays which were attributed in their entirety to the Ministry concerned. The delay was chiefly due to disagreement on the location of the Head Office. The group had been authorized head office in Multan whereas they had wanted one in Faisalabad.

4.29 IFBs came into being due to World Bank conditionality as stated in the FSAL. The loan report talks of these IFBs developing into full fledged banks ultimately which would provide competition to nationalized banks. GOP has sanctioned one branch initially with the provision of expanding into five branches over time officials have repeatedly mentioned that their role will be restricted to the invigoration of money and capital markets at this stage and for the foreseeable future.

4.30 The interest of various parties such as leading foreign banks provides evidence to the contrary. BCCI, American Express and Bank of Oman have already received approvals, whereas Citibank and Grindlays Bank are keen to obtain approvals at the earliest. Observers see this as a means for them to undertake activities which they were previously prohibited from. These include the issuance of certificates of deposit, underwriting of shares and flotation of modarabas and leasing companies. Foreign banks have also found an opportunity to increase profits through avenues, such as increase in branch network and a reduction in their tax liability.

4.31 The latter can be achieved by transferring a chunk of non-funds based earning to the books of the investment bank. IFBs are listed companies that will be taxed at 40% whereas tax liabilities of foreign banks is sometimes in excess of 75%.

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CHAPTER 5

EMERGING ISSUES AND RECOMMENDATIONS.

PRESENT HINDRANCES TO SUCCESSFUL OPERATIONS.

5.01 The first and foremost hindrance that was faced by all parties was the lengthy process of seeking approval. This process has been almost two years in some cases. This poses a constraint for all new aspirants in the field. It is alleged that interested parties are using all sorts of political connections and seeking foreign government recommendations in their bid to obtain letters of intent. The pressure is building up as more applications find their way to the authorities. The experience of the Crescent Group-the only ones that have had the public subscription so far-is a case in point. The stock market with all its inefficiencies gives a premium to the sound reputation of the Crescent Group. This resulted in over subscription and the price of shares being quoted at two or three times the par value. Aspiring sponsors thus also see this as a way to increasing the value of their net worth in a short period of time. This explains the interest that has been shown by various parties in obtaining licenses by any possible means. This fact also encourages those whose intentions are only to make a 'quick buck'.

5.02 The procedure that companies in Pakistan have to follow in order to have a public offering, whether Investment Banks or others, is aso very tedious and rampant with unnecessary delays. The inherent delays in this process will directly effect the working of IFBs as well when they will underwrite issues of, and act as advisors to clients going public. The present process requires the sponsors of any company to register with the registrar of joint stock companies, go to the controller of capital issue with the memorandum and articles of association, have the same whetted by the Corporate Law Authority, seek State Bank of Pakistan approvals and then put in the prospectus to te Stock Exchange for approval before the actual floatation. The slightest of objections, say at stage 3 would result in going back to stage one in order for them to be approved by the authorities. What would be desirable is the ubiquitous and much desired "one window operation" whereby the sponsors could put together the entire package and then seek a 'blanket approval' from any designated department of the Ministry of Finance. Going a step beyond this, it has been suggested that the IFBs in particular should be granted approvals to undertake issues on behalf of clients on their own books or by directly placing them in the market. In areas where the regulators wish to retain control there should be a swift approval process which allows transaction to proceed before market condition change.

5.03 IFBs are allowed to act as traders and brokers of listed securities under section 5 (b)(v) of the SRO. At present stock exchanges are not issuing new membership cards as they do not want to increase membership. The only way out for the IFB is to puchase a card from an existing member. This has led to a monopoly situation for the existing members who have started quoting unrealistic prices for them. It was alleged that they want to sell off cards at exorbitant prices but officially document only a minimal amount in order to make an off the book profit.

5.04 Nationalized Commercial Banks and Domestic Foreign Banks in Pakistan are regulated by the State Bank of Pakistan. At the time the SRO of Investment Banks was being drawn, it was decided that since Investment Banks are not going to be scheduled banks, therefore they do not need to be regulated by the SBP. Instead it was decided that the Ministry of Finance and in particular the controller of capital issue would be the regulating authority. This decision is responsible for the regulatory confusion that the investment banks are facing today. In particular IFBs do not have access to the money market like other financial institutions. As per section 5(a)(iv) of the SRO, they are allowed to borrow and lend in the call money market (Inter bank). The situation on ground is different, and they cannot participate in the Interbank market which puts them at a relative disadvantage. The more aggressive foreign banks in Pakistan are the traditional borrowers in this market, due to a decline in their share of bank deposits coupled with a more active demand for bank credit. The Interbank or Call Money rate is artificially low. At the peak of the busy season it may exceed the bank rate charged by the SBP. This is due to demand for credit being more than that allowed by SBP and because Call Money does not require collateral. As the name indicates the money is 'on call' but participants in this market have a gentlemen's agreement that it will not be called for some time. To maintain the investment finance banks liquidity position at par with commerical banks it is important that the present situation be amended without delay.

5.05 IFBs are allowed to issue short and long term redeemable capital which includes Participation Term Certificates and Term Finance Certificates under section 5 (b)(vii) and 5(c)(xi) of the SRO. However, under section 120 of the Companies Ordinance a company can issue any instrument in the nature of redeemable capital in favour of 'scheduled banks', 'financial institutions' or other persons as may be specified for the purpose by the Federal Government through notification in the Official Gazzette. As an IFB is neither a scheduled bank nor a financial institution, companies cannot issue TFCs in their favour. This situation can be altered only if authorities issue a notification that will amend the existing regulations.

5.06 At present IFBs do not have authorization to function as foreign exchange dealers. For this reason they are not in a position to open Letters of Credit on behalf of clients. Thus they would have to have a standing relationship with a commercial bank for this purpose and give up half of the commission that is earned. Their exclusion from this highly lucrative market seems unnecessary. It must be pointed out that foreign banks derive more than two thirds of their income from trade related financing.

5.07 IFBs must be eligible for remedies available to commercial banks in cases of default such as access to the banking tribunal. (It is a different matter that the said tribunal is without a judge for the past year and a half). Moreover the existing law regarding foreclosures and taking posession of assets which are pledged as security leave a lot to be desired. Thus recovery mechanisms must be put in place before IFBs can be expected to take on the risk of credit and new ventures.

5.08 IFBs are not allowed to take deposits that are of less that ninety days maturity nor have checking accounts, which differentiates them from commercial banks. Investment banks want to provide all services under the same roof for their corporate clients. This includes raising short term funds on their behalf, which may be less than 90 days maturity. Similarly Form L ceilings limit short term borrowing. If paper issued by prime corporate customers were excluded from this limit or incorporated as a sub limit, it would encourage entry by companies, help develop markets and create liquidity. It must be realised that the IFBs could play an important role in developing a broad and flexible money market where funds can be channelled where they are most needed.

5.09 Specialized credit line from the State Bank are not available to IFBs as they are to NCBs and DFIs. These include concessioanry lines for locally fabricated machinery.

5.10 IFBs must be able to take hold and make markets in different kinds of paper without restrictions or impediments. Instead matters appear to have been made artificially complex due to the stamp duties that are imposed on the creation of new instruments. There is a need to build a secondary market in Pakistan. GOP has been showing an interest and a number of studies have been undertaken. IFBs can play an important role if provided with the required incentives. In well developed money markets, liquidity is the 'name of the game'. The only reason why there is a demand for instruments with long term maturitys such as 30 year bonds, is because they can be traded freely. It is recommended that stamp duty on IFB paper products be removed.

5.11 To have IFBs competing with other institutions on a level playing field certain conditions have to be created. Liquidity and tradeability form the critical mass of capital markets. Pakistani authorities will have to take committed steps to fuel the market. For instance the crowding out effect due to unnecessarily advantageous features of certain instruments should be avoided. The WAPDA bonds is a case in point. First, they are guaranteed by the government. Secondly, they are just another source of non bank domestic borrowing. The rate of return does not reflect the operating performance of WAPDA. Infact the bonds prospectus did not contain a financial statement of WAPDA. These long term bonds have features of discounting (after 6 months with FCDC and a tax advantage that will be very difficult to match for any prime corporate borrower). The prime customer will be able to borrow at 12.5% + legal and administrative cost and will thus be driven out of the market. It is ofcourse critical that IFBs have access to cheaper funds as compared to the corporations that they are lending to.

5.12 Since IFBs are not included in the list of scheduled banks there is a number of problems that they are facing. For instance IFBs can provide guarantees on behalf of customers in case equipment is imported, but cannot guarantee the payment of duty through custom debentures, as the law only names scheduled banks as eligible for this function. Section 5(c)(xii) allows IFBs to undertake guaranteeing and counter guaranteeing business, but public sector institutions are resisting the acceptance of guarantees issued by them, as IFBs are absent from the text of the Companies Ordinance 1984. Similarly certain government corporations which have surplus funds cannot place them with IFBs since they have not been given the status of financial institutions in existing law.

5.13 The tax status of the IFBs is still not very clear and there has not been any rate disclosure. If the IFBs are taxed like other banks it will be unfair since the quality of the portfolio of the two types of institutions will be very distinct. Secondly the amount of money that the IFBs are spending on the research and development of new products will have an impact on their income thus rendering them incomparable to other banks.

5.14 IFBs are working in a regulated environment where each activity is restricted in quantifiable terms as a percentage of liquid net worth or other similar easures. On the other hand activities of leasing companies and modarabas are not restricted or governed by any regulation. This results in their unlimited and unregulated involvement in activities which essentially lie in the domain of investment banking. These companies are investing in shares, discounting bills, giving margin loans and accepting deposit and lending in an unrestricted manner. This results in unfair competition as the conventional leasing rates are 22 - 24%. Thus leasing companies are in a position to offer competitive deposit rates in the neighbourhood of 16-18%, which are the highest in the market. It is therefore recommended that either Modarabas should be disallowed investment banking activities or should have similar guidelines as those provided to IFBs so as to have fair competition.

5.15 A major problem exists due to the fact that investment banking is a new concept in Pakistan. The market as well as the bureaucracy do not or only partially understand what is entails. Some think of IFBs as being synonymous with the fraudulant investment companies which mushroomed in the past decade. These companies offered tremendous returns and later decamped with the investors's money. This is the chief reason for the extreme caution being exercised by regulatory agencies and the public at large. Thus it is important to educate the target audience, as regards investment banking. The challenge facing the IFBs is, firstly to create a demand for their services and then to create an awareness of their name. Even the professional and fresh graduates who are working in IFBs are only familiar with the academic working of Investment Banks. The experience of well developed capital markets can also not be replicated in their entirety. For this reason, it would be appropriate for organizations such as the Pakistan Banking Council and/or the regulating bodies, alongwith international agencies, to hold seminars and training workshops all over the country for bankers and professionals. Donor agencies could also play an important role by sponsoring workshops, where experienced investment bankers from overseas could be invited to impart training to the aspiring investment bankers in Pakistan or those in the field be sent overseas for a short period of time to gain practical knowledge and experience.

5.16 Donor agencies could lend support to IFBs through various measures. First of all an awareness of the existence of these institutions needs to be created in the donor community. The IFBs came into existence due to World Bank conditionality on liberalization of the financial sector and the role that the private sector could play. It appears that the pressure on regulatory authorities must continue in a similar manner. If the objectives in view are to be achieved, half hearted effort is of no use. Instead the whole process should be monitored at every step. A positive move would be the provision of credit lines. In this regard donor agencies and overseas DFIs should be encouraged to disburse funds through IFBs. The process can start by a few initial projects where final evaluation and approval vests with the foreign DFI. At a later stage dedicated lines of credit could also be made available to IFBs as were given to the government controlled DFIs in the past. Caution must be exercised in this regard to avoid undesirable experiences such as those with state controlled DFIs. For this reason it will be very important to look at the track record of sponsors.

5.17 IFB personnel should be sponsored for training courses in other less developed countries such as Thailand and Indonesia. The environment of the financial sector is similar to that in Pakistan, or was recently at a stage where Pakistan is now.

GOP VIEWS.

5.18 The views of various GOP officials was sought in this regards. Some issues as perceived by officials at the Ministry are as under :
MOF realizes the lack of a unitary regulatory authority and had suggested the creation of a special bureau with the SBP. The bureau has been approved as a part of the finance bill now after considerable delay and will be operational by the beginning of next year. MOF sees the role of IFBs distinct from NCBs and does not want them to think they are commercial banks. Thus they do not want this to be perceived as a back door entrance to commercial banking, which is the perception held by the private sponsors.

5.19 The private sector was decribed as being 'capricious and dishonest'. Some officials cast doubts over the seriousness of the efforts of the private sector. He maintained that the delays in setting up operations was indicative of this - only one bank is functioning whereas 12 have been awarded sanctions.

5.20 The official was wary of those groups who appear to be fly-by-night operators. He indicated that the lack of a proper management team and or hired professionals was a proof of their short term committment. Officials also indicated that the team of professionals initially shown in the applications were nowhere in sight.

5.21 The large corporate groups were perceived as only serving self interests. Management was of the opinion that IFBs belonging to the large corporate groups will probably end up serving only the companies of the group, who will thus have a tight control over operations. Certain Officials also alluded to the fact that these may only serve as 'money laundering' outfits for the groups.

5.22 The authorities were not willing to concede to their demands of having checking accounts or being authorized dealers of foreign exchange. IFBs are not commercial banks and that is not their desired role, was the response.

5.23 The IFBs are required to play a distinct role to invigorate the financial sector. It was for this reason that none of them have been given a license to operate with a head office in Karachi. As cited by an Official of the Ministry, more than 70 percent of the deposits are in the NWFP and the Punjab, whereas more thn 80% of the lending is done in Karachi. IFBs are expected to remove this distortion by having operations up country.

5.24 The sponsors have not been straight forward in dealing with the Ministry was another allegation. For instance, one group of sponsors had indicated foreign partners as having a 25% share in equity in the initial application but had shown a 50% participation in subsequent paper work, without pointing out the discrepency to the officials concerned.

5.25 Another sponsor had come to the ministry to demand that the license issued to him should be revoked, as he had fallen out with the original sponsors. Instead he wanted another sanction in his own name. He was asked to resolve his disagreement instead of involving officials of the Ministry in insider bickering.

5.26 Officials expressed concern over the operations of the one bank in the market. It was alleged that they had been turning away potential clients. Moreover they had not advertised any deposit or resource mobiliation schemes in the six month of operation and seem to be involved in only group dealings. The authorities hope to have an SBP audit soon whereby they will get a fair idea of the operations of this bank. The official mentioned that as a last resort measure, if the private sector did not 'shape up' licenses may be revoked.

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CHAPTER 6

SECTOR REVIEW

DEVELOPMENT FINANCIAL INSTITUTIONS - SECTORAL SUMMARY

6.01 There may not be a single quantifiable measure by which a comparison of the working of all DFIs is possible. However, the strengths and weaknesses of each can be weighed against their stated objectives. Their performance has been a source of concern for the government and international agencies who have had to resort to extreme measures. PICIC is a case in point where the lines of credit that were once available from the World Bank have been frozen. More recently the Asian Development Bank undertook a study in order to investigate the rationalization of Development Financial Institutions. The final report and recommendations are still awaited by the concerned ministry.(1) The following is a brief attempt to explain the working of DFIs and some reasons that have hampered their performance over the years.

6.02 At the time Pakistan came into being, the muslim businessmen chiefly belonged to the trader-merchant class who were involved in the export of raw cotton, retail of cotton produce and similar activities. The trader merchant class was gradually moving into industrial ventures and transforming into a financial-industrial class. The policies of the military ruler Field Marshall Ayub provided a critical stimulus to this process. Institutions such as the PIDC, PICIC and the IDBP were formed in the wake of those policies. The financial-industrial groups that emerged in the late 1950s and early 1960s, such as the Dawoods, the Crescent group and the Valikas, were the prime beneficiaries of these policies. A large portion of the loans of institutions like the IDBP and PICIC went towards these groups.

6.03 In addition the board of the PICIC was dominated by representatives of these large industrial houses. From its inception PICIC did not risk providing capital to new groups, instead it relied on tried and tested industrial houses which further aided in concentrating wealth in the hands of the chosen few. These industrial groups were later identified among the famous 22 families in 1968 in whose hands lay more than 80% of Pakistan's economic wealth.

6.04 The National Investment Trust (NIT) and the Investment Corporation of Pakistan(ICP) were created to have broad based capital markets with wide share ownership. They were set up to encourage individual savings to be invested in money and capital market instruments. These institutions were also meant to conform to the risk/investment profile of the investors. Over the years, however these two institutions have not only been denied the membership to the stock exchanges but have also not fulfilled their mandate. NIT has performed very well, but its success is not due to its efficient investment portfolio but due to the various concessions by the government. For instance a fixed percentage of any new share issue in the market has to be offered to the Trust. Since the price of issues generally goes up to double or more in a short period, the value of the Trust's holding goes up without any astute decision making by the portfolio managers. This has prevented the development of financial expertise in the institution. As a result the institution has not been able to provide the necessary impetus to money and capital market development.

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1. It is over due and Ministry of Finance Officials have labelled it almost as an exercise in futility after seeing the draft. EPRU staff had the opportunity to briefly review it at the ADB office In Islamabad. It seemed to suffer from being repetitive and somewhat incoherent. The recomendations made thereunder also seemed contradictory at times.

6.05 The ICP has floated numerous mutual funds over the years. The effective annual yield of these 17 funds varies from 15 percent to greater than 40 percent. There are no minimum standards and the annual reports do not expound on the quality of management or the profile of potential investors. This is in contrast to the practice elsewhere in the world, where the general asset composition is disclosed. The risk profile of investors determines whether they want to invest in a conservative or an aggressive fund. Further there is no mention of the reasons why one fund has a high rate of return and the other low.

6.06 NDFC was initially created in 1972 to provide financing to State Owned Enterprises, especially the balancing modernization and expansion activities of the nationalized industrial units. Similarly Banker's Equity was set up to provide direct equity support and under writing facilities to private enterprise. NCBs are members of BEL and are chiefly responsible for its creation. Prior to BEL, NCBs used to take part in consortium financing with other DFIs such as in ICP, BEL ad NDFC have also moved away from their main objectives in a similar fashion to that of IDBP and PICIC in the past. NDFC undertook project financing in the more lucrative private sector with hardly any restriction on the nature or size of the projects. BEL went into project financing over and above the bridge financing and underwriting activities.

CHAPTER 7

CASE STUDY : AGRICULTURE DEVELOPMENT BANK OF PAKISTAN.

AGRICULTURAL CREDIT-SECTORAL REVIEW

7.01 As mentioned earlier the NCCC estblishes aggregate ceilings for credit expansion which are alocated among the economy's various sectors. These ceiings cover the maximum amount f loans to all sector that a bank is authorized to disburse during the priod For agricuture the process involves the Agric ıltural Credit Advisory Council and the State bank, after having recieved the approval from the inistry of Finance. The ACAC assesses credit requirement for various agricultural purposes as detailed in annua targets of the 5 year pan. The NCCC fixes and the SBP administers the over all credit allocations for the sector. Ceiling for the ADBP like other DFIs and FBC are based on their absorptive capacity for loan disbursement and lon recovery performance.

7.02 The instituional structure of the agricultural credit system is dominated by the Government of Pakistan. Agriculture credit flows through three main chanels

The Agricultural Development bank of Pkistan
The Nationalized Commercial Banks
Federal Bank for Cooperatives

Table I shows the source wise break up of Institutional Agricultural credit for 1988-89:

7.03 The NCBs and their branch network have been discussed earlier, here an attempt is made to describe the cooperative credit, the Agriculture Development Bank of Pakistan and its role in the agricultural sector.

COOPERATIVE BANKS

7.04 A Cooperative Bank means a banking society registered under the Cooperative Societies Acts 1912 and 1925. The movement started in Indo-Pak towards the end of the niineteenth century. Initially set up to provide credit to farmers in order to save them from village money lender, cooperatives were organized to encourage self help to persons of limited means through the Cooperative Act of 1904. Cooperatives are organized on a three tier system.

Cooperative Societies
Provincial cooperative Banks (PCB)
Federal bank for Cooperatives (FBC)

7.05 State Bank funds are channeled through FBC which is an extention of the SBP. It is vested with developmental and supervisory functions over cooperatives. The four provinces and two federally administered areas are served by one Provincial Cooperative bank each. A general manager is the chief executive of each PCB. The credit function of loan processing, approval and collection are performed by personnel of the cooperative department, which has reduced the role of PCBs to mere disbursing units. The cooperatives societies have an average membership of thirteen and are channels of credit at the village level. They get loans from the PCB and lend it to indvidual members. These are essentially village organizations with meager equity and the risk of loan repayment is borne by all its members.

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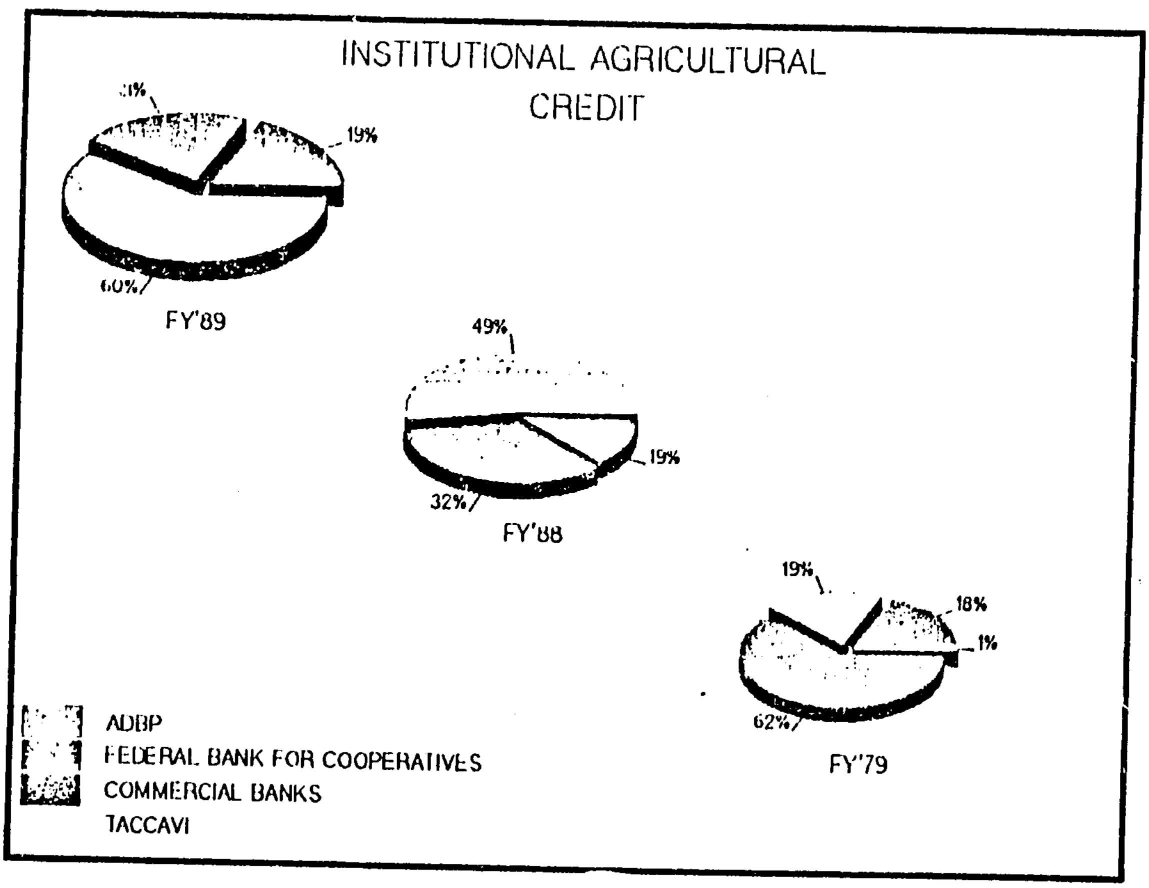
Table 1
Institutional Agricultural Credit 1988-89
Source-wise

(Rupees-Million)

Institution	Production Loans	Development Loans	Total	Share (%)
* Agricultural Development Bank of Pakistan	2109.526	6557.997	8667.523	60.0
** Commercial Banks	2706.500	347.600	3054.100	21.1
Federal Bank for Cooperatives	2638.000	92.710	2730.710	18.9
Total:	**7454.026**	**6998.307**	**14452.333**	**100.0**

* Includes Rs. 593.027 million for agribusiness loans.

** Net of Rs. 369.500 million for tobacco marketing.



THE AGRICULTURE DEVELOPMENT BANK OF PAKISTAN-CASE STUDY

ORGANIZATION

7.06 ADBP was established under the ADBP Ordinance in 1961 through the merger of the Agriculture Development Finance Corporation set up in 1951 and the Agriculture Bank of Pakistan set up in 1957. The stated objectives included the provision of better credit facilities to agriculturists and persons who had set up agro-based cottage industry. It has an authorised capital of 40 crores and subsribed capital of 36 crores. The policies and operations of the Bank are supervised by a Board of Directors consisting of 12 memebers, incuding Federal Government, officials from the Ministry of Finance and the Ministry of Food and Agriculture, representatives of the provincial government, representatives of the State Bank and one from the Azad Jammu and Kashmir.

7.07 Organizationally the bank is structured into 10 divisions. Executive Directors are the Division heads who control the affairs of the division within the financial and administrtive powers delegated to them. Each diviision is sub divided into departments headed by directors. There are 42 departments such as Economic Research, Planning, Project and Consultancy, training and manpwer development etc. These departments are operating units for routine business, preparation of plans and transmission of policy guidelines. Field operations are condcted by a network of 42 regional offices 250 branches and a team of almost 1400 Mobile Credit Officers (MCOs).

7.08 ADBP is a scheduled bank and therefore has to abide by the credit and monetary policies and directions issued by the SBP. It is authorized to accept deposits but is prohibited from engaging itself in trade or having direct interest in industrial or other undertakings. The bank is authorised to advance short term loans repayable within 18 months, medium term loans to be repaid between 18 months to 5 years and long term loans to be reapaid within a period exceeding five years. It charges 12 percent interest and incase of default a 2% penal charge and an additional 2% recovery charge. Table II shows the total loan portfolio of ADBP as on June 30, 1989. The largest portfolio is that of loans in the Punjab.

7.09 ADBP depends on SBP for its borrowings. It also has direct credit lines from the World Bank ,the IDA and the Asian Development Bank. The government has, what are essentialy soft loans at 3/4 or 1 percent service charge available from these agencies. These are repayable in about 50 year with a grace period of 10-15 years.

7.10 Lending is done with the aid of three types of appication forms depending on the nature of the security.these are;

Credit against personal surety or crops
Credit against a mortgage
Credit under the pass book cheme

7.11 Loans are provided to individuals and corporate bodies engaged in agriculture or contribute towards the development of agriculture. Small farmers are usualy unwillng to take investment for increasing productivity without suitable arrangement for marketig surplus. In order to facilitate this and ensure that farmers get a fair price, credit is

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Table 2

Total Loan Portfolio as on 30.06.1989: Area-wise

(Rupees-Million)

Province/Area	Amount Outstanding	Share (%)
1. Federal Capital Area	323.508	1.1
2. Punjab	17554.719	61.4
3. Sind	6383.562	22.3
4. N.W.F.P	2703.324	9.5
5. Baluchistan	1150.304	4.0
6. Azad Kashmir	213.622	0.8
7. Federally Administered Northern Areas	175.691	0.6
8. Head Office	97.165	0.3
Total:	28601.895	100.0

disbursed to organizations that have undertaken processing and marketing of agriculture produce, and activities such as dairy development, poultry farming and live stock development. The total loans disbursed upto June 30, 1989 since inception can be seen in table III:

7.12 Upon receipt of of an apppication, an appraisal mission is sent to collect information from office records through observation and field visits. After this a government delegation including representatives of institutions visit the concerned branch for negotiations and end up with an agreed set of minutes. The loan proposal is then placed before the Board of Governors for consideration and is declared 'effective' when terms and conditions are agreed to by both parties. Any expenses in utilizing funds are reimbursed while items required to be purchased internationally are purchased through competitive bidding.

7.13 The ADBP has to monitor loans and provide the lending instituion with information on financial activities, lending operations and recovery. Administrative and procedural changes are also to be conveyed. Review and supervision missions start visiting the country after the utilization of funds has started. The term of loans is flexibe and negotiable and can be extended. The Government of Pakistan bears the risks arising out of changes in the exchange rate.
Table IV shows the cumulative recovery of loans upto June 30, 1989 since inception:

7.14 In 1979 a senior banking executive became the chairman of the bank. On review at the time it was revealed that since 1961 only 7 lac agricuturists had been assisted which came to about 19% of total farmers in the country. Moreover there were huge arrears that had accumulated over the years. Major restructuring of the organization took place under new management, some of the salient features were as follows;

(i) Branches were rationalized and it was decided not to open any new branches

(ii) A lot of attention was given to the needs of small farmers who were hesitant to come to towns and cities.

(iii) The novel concept of Mobile Credit Officers was introduced to provide door to door credit to farmers Each MCO was provided with a motor cycle. They reported to regional managers who were incharge of 15-20 villages and controlled six branches each.

(iv) The MCO system promoted customer-banker relationship, ensured regular field visit and a well organized feed back system. Lately the introduction of the new cadre of Functional Mobile Credit officers or FMCOs has also proven to be an excellant way to introduce new technologyto farmers and motivate them to modernize their farms. MCOs assist borrowers in fulfilling borrowing formalities, sanction loans on the spot and supervise its utilization. They also ensure the recovery of dues through the assistance of the District Revenue Administration incases of default.

IMPACT OF ISLAMIC BANKING

7.15 Based on the mark up system, Islamic financing replaced the conventional interest based lending in 1985. The lender becomes the seller of inputs at a 'cash price' to the bank and the 'credit price' paid by farmer/borrower incudes cash price plus a mark up of an amount intended to cover its costs plus a profit margin. The farmer is offered a 'prompt

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Table 3

Loans Disbursed Since Inception Upto June 30,1989

(Rupees-Million)

	Province/Area	No. of Loan Cases	Amount Disbursed	Share (%)
1.	Federal Capital Area	3462	362.989	0.8
2.	Punjab	948164	27496.124	61.7
3.	Sind	476551	11121.251	25.0
4.	N.W.F.P	120225	3533.021	8.0
5.	Baluchistan	44210	1428.494	3.2
6.	Azad Kashmir	19147	349.070	0.8
7.	Federally Administered Northern Areas	9567	238.110	0.5
Total:		**1621326**	**44529.059**	**100.0**

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Table 4

Cumulative Recovery Since Inception
Upto June 30,1989

(Rupees-Million)

Province/Area	Amount due for Recovery upto 30.06.1989 (since inception)	Amount Recovered upto 30.06.1989 (since inception)	Past Dues as on 30.06.1989	Recovery Ratio (%) (since inception)
Federal Capital Area	147.564	120.176	27.388	81.4
Punjab	18199.075	17051.772	1147.303	93.7
Sind	8734.994	7430.624	1304.370	85.1
N.W.F.P.	1901.537	1635.185	266.352	86.0
Baluchistan	737.014	558.353	178.661	75.8
Azad Kashmir	225.641	199.917	25.724	88.6
Federally Administered Northern Areas	122.912	109.510	13.402	89.1
Total:	**30068.737**	**27105.537**	**2963.200**	**90.1**

payment price'as an incentive for timely repayment. There is no concept of compounding returns in Islamic banking and the mark up may be charged only for a 210 day 'cushion period' following due date, beyond which there is little or no incentive to repay.

7.16 ADBP and NCBs adopted Islamic modes of financing in 1985. Because the World Bank reimburses ADBP for part of the loans disbursed to farmer, the modes of financing, interest rates and purposes for which the loans are made are part of the legal agreement. The World Bank put the condition that the ADBP lending under service charge and profit and loss sharing modes would not exceed 2 percent of its total lending in any one year.

7.17 Markup free credit programs in NCBs has also been criticized because of the alleged misuse of loans intended for the subsistence farmers. It has been singled out as the most costly program with the greatest negative impact on the GOP budget.

SUPERVISED AGRICULTURE CREDIT PROGRAMME

7.18 This program was introduced in 1972 after the Banking Reform Act 1972, which compulsorily involved commercial banks in agriculture lending. It emphasized productivity based aproach to lending.Special credit officers were appointed in this regard and it limited itself to small farmers.

AGRO BASED PROJECT LENDING

7.19 ADBP financing of small and medium Agro processing industries started in 1980-81. Project financing was undertaken with rupee resources and subsequently the Asian Development Bank provided assistance. This assistance was for the preparation of feasibility studies to develop agro-based project lending and agro servicing sector. This facility was extended subsequently to provide foreign exchange credit for financing the establishment of such industry in the private sector.

WOMEN IN AGRICULTURE

7.20 Women have been identified as having the major responsibility of work in activities related to livestock, poultry, cottage industry, vegetable farming and produce storage. They have also been identified as principal decision makers in these activities. They perform a number of tasks in the pre and post harvest season as well. Their access to credit is limited, however, and where they may have access, as in the case of cooperatives, their requests are denied.

7.21 In 1985 ADBP introduced the Couple Mobile Credit Officers Scheme where wives of MCOs would disburse,monitor, and recover credit to women. There has also been an inclination towards hiring female credit officers and training them if their qualificatons fall short of the requirements.

EMERGING ISSUES

7.22 The ariculture holdings in Pakistan are dominated by the landed aristocracy. These feudals have successfully survived three land reforms over the last forty years. Infact it is alleged that they have been able to strengthen their holdings as a result of reforms. At the time of reforms, land was transferred in the name of tenant farmers and peasants for the purposes of book entries alone. These landlords have also dominatd the political scenario. Most of these families have atleast one or two members in the provincial and national assemblies. Their political clout precludes the need for having a well organized lobby to plead their cause in the parliament, as might be the case in western democracies. Instead these people have been successful in setting the tone for policy reforms or the lack of the same. Their strength has resulted in the non implementation of the contraversial agriculture tax which has been recommended by many objective authorities. These feudals have also exerted a lot of pressure on various lending institulons of the country and since all of them are engaged in agriculture leading ADBP has been a major target of their pressures.

7.23 The ADBP is not able to mobilize deposits for the expansion of its future lending due to the cost of fund under savings and time deposits schemes. Instead it relies heavily on SBP funds. In FY 1986-7 SBP refinanced Rs. 4.86 billion or 81% of the Rs 6.03 billion disbursed to the sector. Its present resource mobilization efforts might be ineffective in light of its lending policies. If it offers rates comparable to the market on deposits (except demand deposts) it is bound to face a negative spread.

7.24 ADBP along with FBCs has become unduly dependant on low cost funds which are avialable at only 5 percent per annum. This rate is well below the market rates which has led to its misuse.

7.25 ADBP operations are centralized in the corporate office in Islamabad. All Decison are made by top management along the same lines as other DFIs. Most medium and long term loan sanctions are the priveledge of management in Islamabad. There is a need for regional offices with more autonomy and sanctioning authority. An announcement has recently been made in this regard.

7.26 ADBP FBC and NCBs seem to be offering funds to the same clientelle for the same purpose according to their accessability. This leads to all three instituitons lending for all types of needs seasonal and non seasonal to borrowers of all sizes.

7.27 Land is the primary collateral used by most institutions,incase of ADBP the pass book system is used in this purpose. The transaction costs for pass book accounts are prohibitive for farmers. The acquisition in case of default is a complicated and long drawn procedure. The second most common form of collatral is personal guarantees or sureties. The recovery mechanism leaves a lot to be desired. Foreclosures are constrained by cultural factor and various permissions from the Board of Revenue.

7.28 There is a need for more qualified and trained personnel. In order for supervised credit to be more widespread. This in turn will ensure an improvement in recovery ratios as well.

RECOMMENDATIONS

7.29 In view of its initial efforts to mobilize deposits any impediments should be removed or minimized by the concerned authorities.. The cost of funds mobilized may be prohibitive if the existing liquidity and cash reserve reuirements are adhered to. Initially it may be necessary to remove this temporarily and then only a reduced percentage be implemented.

7.30 ADBP needs to wean itself off SBP financing. It should aim to do so by bringing its administrative costs under control. Moreover SBP should replace 100 percent refinancing with interest rate subsidies. These subsidies may even be linked with resource mobilization performance.

7.31 There is need for making agriculture lending competitive with trade and industry.

This can be done by either increasing lending rates or decreasing costs by ensuring better credit monitoring and minimal loan losses.

7.32 ADBP, NCBs and the FBC need to specialize in the type of clientelle that each serves. By catering to the different markets there can be specialization of the training requirements and evaluating abilities of each type of institution. This objective can, however, only be achieved if the said instituion can reach out to the target market through its branch network.

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CHAPTER 8
REVIEW OF SEVEN DFIS

HISTORY

8.01 The Industrial Development Bank of Pakistan originated from the Pakistan Industrial Finance Corporation (PIFCO). PIFCO was established in 1949 to finance industries which the private sector could not undertake either because they were technologically complex or capital intensive. It was the first Development Finance Corporation in Pakistan and was a joint venture of the Government and private sector. PIFCO financed only those industries which were very large or already established. It did not finance new industries or give foreign currency loans.

8.02 To overcome these set backs, the Credit Enquiry Commission recommended that PIFCO should be converted into a development bank. To mobilize and allocate foreign exchange resources and cater for the long and medium term loans of the private industrial sector, especially medium and small industries. The Government converted PIFCO into the Industrial Development Bank of Pakistan in August 1961. The Bank has had the continuous support of the Government and State Bank. Since its inception, new industrial development financial institutions have been set up in Pakistan.

OBJECTIVES

The main objectives of IDBP are

8.03 To provide medium and long term loan for establishment of new industrial units and to expand, balance, modernize or replace existing units.

8.04 To collaborate with the Boards of Provincial Small Industries Corporation in financing small industrial units.

8.05 To provide short term loans (upto 25%) for working capital.

8.06 Encourage the growth of small and medium size units in less-developed areas by administering the Equity Participation Fund established under the ordinance of the Federal Government in 1970. Also to encourage Government financed industrial trading estates located in the country except in Karachi.

8.07 Gives IDA credits for Small Scale Industrial Units.

8.08 Helps the borrowers in solving their complex problems by giving them financial, technical and managerial advice in planning and execution of projects.

8.09 Industrial projects approved by the Non-repatriable Investment (NRI) are financed by IDBP.

8.10 Local machineries are encouraged by providing loans at a reduced rate for the purchase of local machinery.

8.11 Industries which are import substituting are encouraged by the Bank.

8.12 It was only recently that IDBP decentralised the processing of loan applications to regional offices to maintain better contact with the sponsors, effectively monitor projects, improve the quality of appraisal and improve regional profitablility.

OPERATIONS

8.13 IDBP prescribes an Industrial Investment Schedule whereby credits are given to industrial enterprises. The financial targets for each industrial sector and province is outlined in the schedule. The Bank grants loans according to the Investment Schedule. It can even obtain sanctions from the Government for special loans.

8.14 For limited loans the ceiling of loaning one project is Rs 4 million with a foreign currency requirement which does not exceed Rs 3 million. For partnerships or sole ownerships, the upper limit is Rs 11.5 million with a foreign currency component below one million rupees. The lending ceiling does not apply to mining cotton, jute, inland transport and shipping. The upper lending limit can be relaxed with the consent of the Federal Government. The Bank's lending does not have a lower limit.

8.15 IDBP offer a higher rate of interest than commercial Banks. The rate of local currency is between three to four percent above the Bank rate. Private industries in less developed areas are especially encouraged and special rates are offered to them.

8.16 On foreign currency loans, the rate of interest is 2% above the rate of the loans which is given by the agency. It is subject to a minimum of nine and a half percent or as specified by the Government.

8.17 In the case of local currency loans, the loans have to be repaid over a period from five to ten years. For foreign currency loans, the period of repayment is between ten to fifteen years, depending upon the term of foreign loan and earning capacity of the project. Loans can be repaid in half yearly installments, the first installment in twenty eight months from the date of opening of letter of credit and/or payment of the first instalment of local currency loan.

TABLE 1					
Loans Disbursed by Industrial Sub-sectors (Rs in Million)					
Sub-sectors		1985-86 Amount	1986-87 Amount	1987-88 Amount	1988-89 Amount
Milling Industries		34.89	44.94	45.31	31.41
		(6.3)	(4.9)	(4.6)	(3.3)
Food Industries		156.33	204.04	93.01	134.97
		(28.2)	(22.4)	(9.5)	(14.0)
Baverage Industries			2.23	0.58	1.17
			(0.2)	(..)	(0.1)
Mfg. of Cotton Textile	15.87	122.67	306.99	260.22	
(Spinning,weaving etc)	(2.9)	(13.4)	(31.6)	(27.0)	
Mfg. of Other Textiles	34.58	19.71	18.91	16.85	
		(6.2)	(2.2)	(1.9)	(1.7)
Footwear			2.75	1.29	2.58
			(0.3)	(0.1)	(0.2)
Other Weaaring Apparel	2.35	16.93	24.00	8.71	
and Made-up Textiles		(0.4)	(4.8)	(2.4)	(0.9)
Mfg. of Wood Cork &		0.65			9.64
Allied Products		(0.1)			(1.0)
Furniture and Fixtures	2.88	1.80	6.24	4.97	
		(0.5)	(0.2)	(0.6)	(0.5)
Paper & Paper Products	56.09	21.37	61.49	128.18	
		(10.1)	(2.3)	(6.3)	(13.3)
Printing Publishing &	4.10	29.22		5.04	
Allied Products		((0.7)	(3.2)		(0.5)
Mfg. of Leather &		7.31	12.21	24.92	3.45
Leather Products		(1.3)	(1.3)	(2.5)	(0.3)
Mfg of Rubber Products	20.16	13.29	31.94	11.49	
		(3.6)	(1.5)	(3.3)	(1.2)
Mfg of Chemicals &		47.37	62.87	43.48	69.32
Chemical Products		(8.5)	(6.9)	(4.4)	(7.2)
Non-Metallic Mineral		43.82	133.46	71.05	48.20
Products		(7.9)	(14.5)	(7.3)	(5.0)
Basic Metal Products		16.26	17.28	12.23	29.86
		(2.9)	(1.9)	(1.2)	(3.1)
Mfg. Of Metal Products	16.28	12.38	13.53	21.21	
(Except Machinery)		(3.0)	(1.4)	(1.4)	(2.2)
Machinery		1.73	12.25	7.58	0.33
		(0.3)	(1.3)	(0.8)	(..)
Electrical Machinery		6.91	18.57	80.78	34.52
		(1.2)	(2.0)	(8.2)	(3.6)
Transport Equipment		7.96	28.74	17.48	34.55
		(1.4)	(3.1)	(1.8)	(3.6)
Cotton Ginning &			1.06	2.34	3.26
Pressing			(0.1)	(0.2)	(0.3)
Hotels and Motels		11.36	35.01	25.14	10.14
		(2.1)	(3.8)	(2.6)	(3.1)
Cold Storage including	6.15	10.88	14.50	4.31	
Ice Plants		(1.8)	(1.2)	(1.5)	(0.4)
Transport Service			0.96		

Loans Disbursed by Industrial Sub-sectors

(Rs in Million)

Sub-sectors	1985-86 Amount	1986-87 Amount	1987-88 Amount	1988-89 Amount
		(0.1)		
Other Service Industry 18.41	9.82	36.49	46.22	
	(3.3)	(1.1)	(3.7)	(4.8)
Mining & Quarrying	1.26	20.72	5.79	28.80
	(0.2)	(2.3)	(0.6)	(3.0)
Other Miscellaneous Industries	17.95	41.40	34.29	14.61
	(3.2)	(4.5)	(3.5)	(1.5)
TOTAL	553.51	916.13	979.36	963.98

(figures in parenthesis give the percentage of total amount)

TABLE 2

Recoveries by Sub-sectors

Rs in Million

Sub-sector	1985-86	86-87	87-88	88-89	% change in 88-89 over 87-88
Cotton Textile	136.12	186.02	158.44	120.48	-23.96
Other Textile	50.75	59.94	71.86	91.74	+27.76
Chemicals	76.25	79.46	100.13	39.26	-60.79
Food, Baverages	133.12	144.30	171.42	146.38	-14.61
Engineering	29.39	24.67	31.48	41.15	+30.72
SICs/Board Projects	8.36	6.32	5.41	1.50	-72.27
Miscella-neous	67.76	88.90	165.65	130.25	-21.37
Total	501.75	589.61	704.39	570.76	-18.97

8.18 Over the past five years the major industries which were funded by IDBP were Food, cotton textiles, paper, non-metallic minerals and chemicals. The share of the Food Industry in disbursements (by industrial sub-sector) was the highest in 1985-86. The Industry accounted for 28% of the disbursements. The percentage share of the Food Industry in disbursements reduced to 22.4% in 1986-87 and 9.5% in 1987-88. However the recoveries in this sector increased by only 8% in 1986-87 since 1985-86. The recoveries improved by 16% in 1987-88. There was increase in the percentage share of disbursement by 14% in 1989 but the recoveries declined by 14%.

8.19 The share of Cotton textile industry in total disbursements (by industrial subsector) has shown an increase from 2.9% in 1985-86 to 13.4% in 1986-87. The recoveries in this sector also increased by 37% during this year. However, from 1986-87 to 1987-88 the share of cotton industry in disbursements increased by 31.6%, whereas the recoveries decreased by 15% over the last year. The disbursement in this sector decreased by 27% in 1988-89 and the recoveries also declined by 23.9%.

8.20 The chemical industry accounted for 8.5% of the loans disbursed by IDBP in 1985-86. The trend in the percentage share of chemical industry in disbursements remained the same over the next five years. The recoveries however improved by 31% from 1985-86 to 1987-88. There was a sharp decline in recoveries by 60% in 1988-89.

8.21 The share of miscellaneous industries in 1986 to 1987 increased from 3.2% to 4.5%. The recoveries increased by 31% in the same year. However from 1987 to 1988 the share in disbursements declined by 3.5% whereas the recoveries increased by 86%. In 1989 the disbursements declined by 1.5% and the recoveries by 30.225%.

8.22 The share of paper industry in the total disbursements (by industrial sub-sector) was 10.1% in 1985-86. The percentage share decreased by 2.3% in 1986-87 and kept increasing until it was 13.3% in 1988-89.

8.23 Non-metallic minerals accounted for 14.6% of the disbursements in 1986-87 but the percentage share non-metallic minerals in total disbursements steadily decreased to 5% in 1988-89.

8.24 Keeping in view the objective of the Bank, IDBP should be financing new industries. The Bank should move away from traditional industries like textile and concentrate on promoting non-traditional and diversified projects.

TABLE 3

Loans disbursed by provinces

Period	1985-86	1986-87	1987-88	1988-89
Sindh	31.2%	31.2%	24.1%	32.5%
Punjab	40.5%	40.5%	60.1%	51.0%
NWFP	11.9%	11.9%	9.7%	10.6%
Balochistan	16.4%	16.4%	6.1%	5.9%

8.25 A total of 3775 loans were given to the provinces over the past four years. Punjab has had the largest share of disbursement which is 48.3% over the past four years. 32.2% of the total amount (from 1985-89) were for Sindh, 11.9% for NWFP and 7.6% for Balochistan.

8.26 Punjab and Sindh have had the largest share of disbursements.

TABLE 4			
Loans sanctioned by purpose			
			Rs in millions
Period	1986-87	1987-88	1988-89
Loans to New Units	80.0%	82.5%	78.9%
Loans for expansion	10.4%	10.8%	9.5%
Loans for BMR purposes	9.6%	6.7%	11.6%

8.27 The Table shows that the largest amount (in loans sanctioned by purpose) were allocated for new units. The average annual percentage of loans for new units from 1986-89 was 80.5%.

8.28 Also keeping in view the objective of the Bank,IDBP disbursed 77% of the total local currency loans for the financing of locally manufactured machinery in 1988. In 1989 the percentage share was 73% of the total local currency loans. Figures for the previous years are not available. The following are some key performance ratios of IDBP.

PERFORMANCE RATIOS					
					(Rs in millions)
Period	84-85	85-86	86-87	87-88	88-89
Loans disbursed.	265.4	358.3	532.3	979.4	963.9
Return on capital	50%	44%	.6%	23.7%	23.4%
Return on assets	.02%	1%	1%	3%	.01%
Disbursements per staff number	0.68	0.69	1.12	1.17	1.16
Op Profit/adm cost	95%	112%	140%	163%	150%
adm cost/staff No	.07	.07	.08	.09	.11

8.29 The Table shows that the loans disbursed by IDBP amounted to Rs 963.9 m in 1988-89. The loans increased at an average annual rate of 41.8% percent from 1984-87. However from 1987-88 to 1988-89 disbursements declined by 1.6%. The return on capital was very high, 50% in 1984-85 but decreased over the years. It was very low, 0.6% for the year 1986-87.

8.30 Return on assets has been very low (an average of 1.02%) over the past five years. The disbursements per staff number were Rs 680,000 per staff member in 1985 and 1986 but increased to Rs 1.12 million in 1987. There was a further increase to Rs 1.17 million in 1988. Total operating profit as a percentage of total administrative cost was 95% in 1985 and showed a favourable trend until it was 163% in 1988. The total administrative cost as a percentage of the total number of staff members has been about Rs 70,980 from 1985-89.

PROBLEMS

8.31 Loans are given due to political pressure. The employees cannot be held responsible for bad loans because they are not given on a professional basis.

8.32 Even though the Bank has been sanctioning loans to new units, locating new entrepreneurs is a difficult process because it involves risk.

8.33 Insufficient data on the market in evaluating projects. IDBP goes largely by what the sponsors say.

8.34 The World Bank suspended financial assistance to IDBP to provide loans to medium size investors.

8.35 No action is taken if objectives are not followed.

8.36 Management changes frequently due to political pressure.

8.37 Legal proceedings take a long time to settle.

IDBP's CONTRIBUTION TO THE GROWTH OF DFIs

8.38 IDBP's share in aggregate channelization of resources by DFI's fell from 11.8% in 1984 to 10.7% in 1988. IDBP's share in advances of DFIs decreased from 13% in 1984 to 12% in 1988. Its share in investments of DFIs increased from 3.2% in 1984 to 3.9% in 1988.

8.39 The share of IDBP in aggregate resources mobilized by DFIs decreased slightly from 11.2% in 1984 to 11.1% in 1988. THe share of IDBP in equity and borrowing of DFIs fell from 4% and 15.2% respectively in 1984 to 3.5% and 13.6% in 1988. Its share in deposits of DFIs improved from 7.6% in 1984 to 12.3% in 1988.

HISTORY

8.29 Pakistan Industrial Credit and Investment Corporation Limited (PICIC) was established in October 1957 with the support of the government of Pakistan and the World Bank. It is a public limited company and finances the private industrial sector in the form of long or medium term loans in local or foreign currencies. In this way it helps in the expansion and modernization of private industrial enterprises and assists in the growth of the capital market. It is also involved in equity participation, purchase of debentures and underwriting any public issue of shares and debenture. It arranges participation of local and external finance from private and institutional investors. Besides it provides managerial, financial and technical services to industry in the private sector.

8.30 PICIC aims at broadening the base of the industrial ownership in the country and thereby developing the stock market. It provides loans both in foreign and local currencies for industrial projects in the private sector which are financially feasible. Purchase of local plants and machinery and establishment of industries in the backward areas is especially encouraged.

8.31 To generate resources PICIC borrows both in foreign and local currencies. Borrowing in local currencies are the loans from the Government and the State Bank of Pakistan. International Financial Institutes such as the World Bank, Asian Development Bank and DFW (Germany) provide loans in foreign currencies. Loans are also given by a number of other countries. These loans are given in accordance with the purchase of machinery from the countries. A line of equity has also been provided by the Islamic Development Bank of Pakistan.

8.32 Foreign investment in PICIC's share capital includes investments by International Finance Corporation, Washington, an affiliate of the World Bank and Common Wealth Development Finance Company Ltd. London.

OBJECTIVES

* PICIC gives long term and medium term loans in foreign and local currencies and in this way assists the private sector industry in Pakistan. It provides assistance for acquisition of fixed assets. It does not give loans for refunding operation or for working capital.

* It makes direct participation in shares, debentures stock and underwriting public issues of shares and other securities.

* PICIC assists foreign investors to locate suitable opportunities for investment in Pakistan. It also helps Pakistani entrepreneurs to obtain suitable foreign investment in their enterprises. It gives funds to entrepreneurs in the preparation of investment proposals.

* It gives financial, technical and managerial advice to the industries which have been financed and helped by it.

* PICIC helps entrepreneurs through the implementation and operational stage of the project. It takes any remedial steps if there are any financial or technical problems.

* It finances industries which are based on local raw material and are export oriented or would generate import saving.It diversifies investment both by region and industry.

* It gives preference to less developed areas.

* Non traditional industries are encouraged so that new entrepreneurship can develop in the country.

OPERATIONS

TABLE 1					
Cumulative No of Projects					
Period	1985	1986	1987	1988	1989
No	873	896	933	959	1013

8.33 The cumulative number of projects financed by PICIC show a steady increase from 1985-89. The average annual percentage increase of projects was 5.6% over the past five years.

TABLE 2

INDUSTRY WISE DISTRIBUTION OF LOANS SANCTIONED

Rs in Million

INDUSTRY	1985	1986	1987	1988	1989
Agriculture & Forest					
Food Products	159.67 (14.4)	58.24 (4.5)	193.75 (8.9)	42.68 (2.2)	28.20 (0.5)
Sugar	83.55 (3.6)	46.76 (7.5)	108.85 (5.0)	463.56 (23.6)	564.31 (10.2)
Paper & Printing		103.15 (8.1)	116.84 (5.4)	1.17 (0.1)	0.13 (..)
TEXTILES Cotton	432.66 (38.5)	658.05 (51.3)	1517.77 (69.8)	1059.94 (54.0)	3429.35 (61.8)
Jute	15.00 (1.3)		3.50 (0.2)		
Other	48.60 (7.7)	98.98 (4.4)	12.61 (0.6)	22.67 (1.2)	131.50 (2.3)
Leather & Rubber	2.15 (0.2)	27.00 (2.1)	2.90 (0.1)	0.15 (..)	
Engineering	120.56 (10.8)	51.42 (4.0)	98.87 (4.5)	55.19 (2.8)	361.61 (6.5)
Chemicals	66.49 (6.0)	160.28 (12.5)	73.74 (3.4)	269.55 (13.7)	536.42 (9.7)
Minerals		101.32 (9.1)	7.62 (0.3)		183.98 (3.3)
Cement, Ceramics	53.82 (4.8)	65.80 (5.1)		47.42 (2.4)	138.24 (2.5)
Tourism					
Shipping					
Miscellaneous	32.86 (3.0)	13.42 (1.1)	39.04 (1.8)		177.80 (3.2)
TOTAL	1112.68	1283.10	2175.49	1962.33	5551.54

(figures in parentheses give the percentage of total amount of loans disbursed)

8.34 Some of the major industries which have been funded by PICIC were Food, Sugar, Textile cotton, Engineering and the Chemical Industry. Food Industry accounted for 14.4% of the total disbursements in 1985. The percentage share of Food industry in disbursements decreased to 4.5% in 1986. The percentage share of Engineering industry in disbursements also decreased from 10.8% in 1085 to 4.0% in 1986. While more importance was given to the Sugar, Textile cotton and chemical industry. The percentage share of sugar industry in disbursements increased from 3.6% to 7.5% from 1985 to 1986. the share of textile industry increased from 38.5% to 51.3% and the chemical industry increased from 6% to 12.5%.

8.35 In 1987 the percentage share of food industry in disbursement increased to 8.9% but decreased to 2.2% in 1988 and 0.5% in 1989. The cotton textile industry was given more funds. Its share increased to 69.8% in 1987 and than declined to 54.0% in 1988 and increased to 61.8% in 1987. The share of chemical industry in disbursements decreased to 3.4% in 1987 and increased to 13.7% in 1988 and than 9.7% in 1989.

8.36 Keeping in view the objective of PICIC, it should be financing new industries instead of traditional ones like the textile industry. They have been giving preference to traditional industries only. This clashes with the policy of promoting new, non-traditional and diversified projects.The World Bank has recently put a credit squeeze on PICIC barring it from financing the textile industry especially spinning units. PICIC discourages diversification because of the risk involved in encouraging new projects. However locating and nurturing new entrepreneurs should be an important area of responsibility for PICIC because it is a development bank.

TABLE 3

Province wise distribution of loans sanctioned

Rs in million

Period	1985	1986	1987	1988	1989
Sindh	541.47	454.42	396.31	438.8	1453.4
Punjab	409.77	582.55	1574.2	1476.9	3170.4
NWFP	34.87	28.88	16.62	16.40	642.7
Balochistan	126.57	196.25	187.7	30.2	24.48
Islamabad					126.50
Azad Kashmir		21.00	0.70		134.1

8.37 The percentage share of loans sanctioned to provinces was the highest for Punjab over the past five years. In 1986 Punjab accounted for 41% of the loans sanctioned by PICIC. The share of Sindh in the loans sanctioned was 35%, NWFP 2% and Baluchistan 15% in 1986. In 1987 the share of Punjab increased to 72% while that of Sindh was reduced to 18% NWFP 1% and Baluchistan 2%. In 1988 Punjab again accounted for 75% of the loans sanctioned, while Sindh accounted for 22% and NWFP and Baluchistan 1% each. In 1989 the loans sanctioned to Punjab decreased to 57%. Sindh was sanctioned 26% of the loans, NWFP 11.5% and Baluchistan 0.4%.

8.38 Even though one of the main objective of the bank is to support less developed areas, people are not encouraged to put up industries in these areas due to the lack of infrastructure facilities. It is only when the government provides these facilities that industrialization can begin in these areas.

TABLE 4	
Annual Recoveries of Loans	
Period	Rs in Millions
1980	306.00
1981	350.00
1982	406.00
1983	440.00
1984	484.00
1985	538.00
1986	652.00
1987	778.00
1988	942.00
1989	1138.00

8.39 The amount of loans disbursed by PICIC increased from 1985-87. The annual recoveries of loans also show an improvement. In 1985 loans worth Rs 643 million were disbursed while recoveries were Rs 538 million. In 1986 loans worth Rs 722 million were disbursed while recoveries were Rs 652 million.

8.40 From 1986-87 the loans disbursed increased by 8% while recoveries increased by 19%. From 1987-88 loans disbursed increased by 44% while recoveries increased by 21%. In 1988 to 1989 loans disbursed decreased by 6% while recoveries increased by 20%.

8.41 Figures for the recoveries of loans targeted for a particular year are not given in the annual reports. Therefore, an evaluation of the Bank regarding its loan loss ratios or overdues is not possible. The following are some key performance ratios for PICIC.

PERFORMANCE RATIOS				
				Rs in millions
Period	1985-86	1986-87	1987-88	1988-89
Loans disbursed	722.0	781.0	1126.7	1059.7
Return on Capital	1.15%	1.3%	1.1%	1.2%
Return on Assets	2%	2%	2%	2%
Op Profit/adm cost	367%	315%	359%	346%

8.42 The Table shows that return on capital has been very low over the past five years. One reason could be that DFIs are not profit oriented institutions. They donot aim at making profit like other commercial banks. The return on assets which is the profit as a percentage of loans is also very low. It has remained 2% over the past five years. The operating profit as a percentage of the administrative cost was 367% in 1986. It decreased to 315% in 1987 and then increased to 359% in 1988.

PROBLEMS

- Bad and doubtful loans are given due to political pressure. The employees cannot be held responsible for giving bad loans because decisions are not made on professional basis.

- Weak data base for market analysis. Sponsors donot give the right information when they apply for loans.

- Estimates of people directly involved in the project are not reliable because they donot want competitors. Government statistics are not upto date and donot give the right figures. It is difficult to find out the background of the sponsors.

- Projects sometimes are not in a position to satisfactorily service their debts. These include cost and time over runs during the implementation stage, technical defects, changes in government policies and inefficient management. PICIC takes a variety of actions to remedy the problems. In case of managements difficulties, it coordinates with other banks and financial institutions and puts credit squeeze on the sponsoring group, which extends not only to the particular project but goes to cover all their business and industrial undertakings. If this fails the alternative is to take the company into liquidation.

- Sometimes the borrowers default deliberately in servicing debts. From 1971-82 (latest figures are not available) the overdues against the borrowing companies continued to grow, and their dividend payouts tended to become larger. This deteriorated the relationship between PICIC and the clients. The number of cases which had to be filed in court swelled considerably. There were problems in seeking adjudication of the courts. The legal procedures are such that it takes a very long time to get results. In many cases, the judgement of the court comes after years of litigation and then the execution of the decision takes a number of years and by that time the assets get substantially eroded in value. A Law called the Bank's Loan Recovery Law was promulgated a few years back. It was hoped that the loan recovery suits would be disposed of within a few months with the promulgation of this law, but it still takes a long time for the cases to be settled.

- There is no in-service management development training programme in PICIC. In a few cases, officials are sent abroad to attend courses run by the World Bank and Development Banking Institute. Officials are not kept informed of new developments taking place in the world.

- Slow process of sanctioning of loans. Due to this the prices of plants and machinery go up and the cost of project increase. New competitors appear in the market.

- Time lag between the time the loans are sanctioned and disbursed. This problem occurs because of non-availability of funds. Sometimes the sponsors have to fulfill certain conditions which cannot be met. Due to this problem it takes time before the loan is actually disbursed.

- The administration is very weak which has a negative effect on the organization. In the last five years, four managing directors have changed. Most of them are in their last years of retirement. Even promotions cannot be carried through without the approval of the bureaucracy.

* There is an absence of vigorous follow-up of underlying objectives of the bank as seen in the annual reports and interviews with bankers.

PICIC's CONTRIBUTION TO THE GROWTH OF DFI's.

8.43 PICIC's share in the aggregate resources of DFIs fell from 11.2% in 1984 to 9.7% in 1988. Its share in equity and deposits of DFIs increased from 6.3% and 1.0%, in 1984 to 7.1% and 1.1% in 1988. However, its share in borrowing by DFIs declined from 16% in 1984 to 13% in 1988.

8.44 PICIC's share in the aggregate channelization of resources by DFIs also deteriorated from 12.3% in 1984 to 10% in 1988. Its share in advances and investments of DFIs declined from 13.6% and 3.7% in 1984 to 11.5% and 3.0% in 1988.

HISTORY

8.45 Sponsored by the Government of Pakistan, the National Investment Trust was established in 1962. The National Bank of Pakistan acts as its Trustee, and the Trust is managed by the National Investment Trust Limited known as the Management Company. The Board of Directors consists of three leading industrialist, Presidents of four major nationalized commercial banks, Chief Executives of three D.F.Is', Chairman Pakistan Insurance Corporation, representative of the Federal Government and the Managing Director who is appointed by the Board with the approval of the Federal Government. One of the Directors is appointed by the Federal Government as the Chairman of the Trust. The Trust started its operation from 1 January, 1963.

OBJECTIVES

8.46 When Pakistan was made, most of the large enterprises were family owned. A gradual monopolization of industry had led to concentration of economic power. It was therefore necessary to broaden the industrial base and energize small investors' capital formation. But the government lacked resources as well as the technical know how to withstand the manipulations of those who exercised control over the capital market.

8.47 To overcome these obstacles the National Investment (Unit) Trust was set up. It is the only open-end Mutual Fund in Pakistan. Its main objectives are:-

* To mobilize saving mainly of common people through sales of Certificates (NIT Units)
* To meet the growing needs of corporate sector and achieve broad-based investment
* To bring about a diffusion of corporate ownership

OPERATIONS

8.48 The Trust Fund is divided into Units, called 'NIT Units'. Each Unit represents an equal proportion of the assets of the Trust. The main function of the management company is to promote the sale of Units for investment in profitable industrial enterprises in the corporate sector in order to broad base the share ownership of the companies listed on the Stock Exchanges.

8.49 The income received from the investment of the Trust Fund and capital gains realized from its operations are distributed among investors holding NIT Units as on the 30th June, annually as dividend.

8.50 The volume of the Trust's property expands or shrinks according to the quantum of sales and re-purchases. The Units are sold and repurchased by the National Bank of Pakistan and seven other leading banks. The issuing banks register the certificates, effect transfers and carry out consolidation, subdivision or cancellation of certificates. Stock brokers and others have been appointed as sales agents on commission basis in various cities, centers of business and industry. A center register is maintained by the Trustee and the management company on the basis of weekly returns furnished by the issuing banks.

8.51 The NIT Units are 'Approved Securities' and 'Approved Investments' for the purpose of the Insurance Act, 1938 and the Companies Ordinance, 1984. They provide security of capital and initiate capital appreciation depending upon the performance of the Stock Market.

There are two kinds of Units viz Registered Units and Bearer Units.

Registered Unit Certificates

8.52 The NIT offices and authorized branches of banks sell Registered Units on application. Individuals (in single or joint names) and companies and trust funds can invest in these Units.

Dividend on Registered Units is paid annually by means of Income Distribution Warrants.

Registered Units are issued in denomination fo 5, 10, 20, 30, 40, 50, 100, 200, 300, 400, 500, 1000, 5000, 10000, 25000, 50000 and 100000 Units.

Cumulative Investment Plan

8.53 Holders of Registered Units can reinvest their dividend and obtain additional Units at concessional rate (less by 10 paisa per Unit on the opening sale price) under the Cumulative Investment Plan. According to the Income tax ordinance 1979, CIP Units provide tax relief in the following year.

Bearer Unit Certificates

8.54 The authorized bank branches and NIT Offices sell Bearer Units against cash payment without completion of any form or disclosure of identity. There is no responsibility in case of lost, stolen and destroyed Bearer Unit Certificates or dividend coupons.

Dividend on Bearer Units is paid annually (on presentation of the dividend coupons attached with the Bearer Unit Certificates) at any authorized branch of National Bank of Pakistan. The rate of dividend is the same as that of Registered Units.

Bearer Units are issued in denomination of 5, 50, 100, 200, 300, 400, 500, 1000, 5000, 10000, 25000, 50000 and 100000 Units.

UNIT PRICE

8.55 The price at which the Units are sold and repurchased are announced on each Saturday by the Management Company through the Press and are also published in the Official Ready Board Quotation Sheet of the Stock Exchanges at Karachi and Lahore.

ISLAMISATION OF NIT

8.56 NIT was one of the first institutions chosen by the government for the Islamisation of the Financial System. Since 1st July, 1979 NIT has stopped investment of its funds in interest bearing securities and investments. It invests in schemes which are approved by the State Bank of Pakistan as an interest-free mode. Investment is made in Stock Market Shares, Modaraba Certificates, PTCs, TFCs and Morabaha and Leasing Financing arrangement for financing trade and industries.

The Government promulgated Zakat and Ushr-Ordinance on 21st June, 1980. The Unit holders who are defined as the 'Saheb-e-Nisab' according to the Ordinance have to pay Zakat at the rate of two and a half percent of the repurchase value of NIT Units. This is deducted from NIT's annual dividend fund.

STATISTICAL OVERVIEW

Sales of Units

8.57 During the period from June'84 to June'89 the number of Units have increased from 20.501 million Units to 112.009 million Units. The net sales of Units in 1988-89 amounted to Rs 1362.491 million as against Rs 241.337 million in 1983-84 which means an increase of 360% over the past five years. The number of units sold increased by 52.2% from 1984-85 and the net salses of units also increased by 53%. From 1986 to 1987 there was a decline in sales of units by 27%. In 1987-88 the net sales again increased by 118% and then declined to 29% in 1988-89.

TABLE 1

SALES OF UNITS

Figures in Millions

Years	No. of Units		Net Sales of Units Value (Rs.)	
84-85	20.501		41.337	
85-86	31.177	(52.2%)	368.325	(53%)
86-87	39.633	(27%)	464.160	(26%)
87-88	86.462	(118%)	1035.647	(122.9%)
88-89	112.009	(29%)	1362.441	(31%)

(figures in paranthesis give the percentage increase over the previous year)

Income Distribution

8.58 The amount of income available for distribution was Rs.842.193 million in 1988-89 compared to Rs 255 m in 1983-84, representing a growth of 271.32% over the past five years. From 1984 to 1986 there was a steady increase in the amount of income from 7.05% to 27% in 1986. From 1987 to 1988 the income increase by 41% and increased again by 42% in 1988-89. The Trust declared dividend of Rs 1.90 per Unit as compared to Rs 1.50 per Unit in 1983-84.

TABLE 2				
INCOME DISTRIBUTION (Figures in Millions)				
Period	Ammount of Income in (Rs.)		Rate of Income Distribution / Unit	
1983-84	255.000		1.50	
1984-85	273.000	(7.05%)	1.60	(6%)
1985-86	332.800	(22%)	1.65	(3%)
1986-87	422.373	(27%)	1.75	(6%)
1987-88	596.629	(41.1%)	1.82	(4%)
1988-89	842.193	(41.2%)	1.91	(5%)

Investments

8.59 The net investment at cost has increased by 232.2% since 1984. It includes shares of Joint Stock Companies, Modaraba Certificates, Participation Term Certificates/Term Finance Certificates, Morabaha, PLS deposits etc.

The following table shows that the net investment at cost stood at Rs 4382.4 million in 1988-89 against Rs 1319.204 million in 1983-84. The highest increase in net investment was in 1987-88 when it went up by 37%.

TABLE 3		
Investment at cost. Figures in millions		
Period	Investment at cost in Rs.	
1983-84	1319.204	
1984-85	1583.828	(20%)
1985-86	2058.414	29%)
1986-87	2803.800	(36%)
1987-88	3838.000	(37%)
1988-89	4382.371	(14%)

Income of the Trust

8.60 The following table represents the annual income earned by the Trust since 1983-84.

TABLE 4

Income of the Trust

Figures in millions

Period	Income in Rs.	
1983-84	229.000	
1984-85	284.500	(24%)
1985-86	337.668	(18.7%)
1986-87	419.221	(22%)
1987-88	596.186	(42.2%)
1988-89	861.461	(44%)

8.61 The total income of the Trust on its investment has registered an increase of 276.2% over the past five years. The highest increase in income was in 1987-88 when it went up by 42% and in 1988-89 when it further increased by 44% since the previous year.

NIT's CONTRIBUTION TO THE GROWTH OF DFI's.

8.82 The share of NIT in aggregate resources mobilised by DFIs increased from 6% in 1984 to 7.6% in 1988. The share of NIT in equity of DFIs recorded a rise of 10.4% from 23.4% in 1984 to 33.8% in 1988.

NITs contribution to the aggregate channelisation of resources by DFIs improved from 5.1% in 1984 to 7.8% in 1988. The share of NIT in advances by DFIs increased from 0.1% in 1984 to 3.2% in 1988, but its share in investments of DFIs decreased quite sharply falling from 38.7% in 1984 to 29.8% in 1988.

HISTORY

8.83 The National Development Finance Corporation (NDFC) was established in 1973 with its Head Office in Karachi. It was originally created to finance public sector corporations but its charter was subsequently amended to provide finance to the private sector also.

The traditional role played by DFIs in Pakistan was only to provide development funds to feasible development projects. NDFC from its very inception was expected to assume and discharge larger responsibilities. It mobilized resources independently to a great extent and employed them for economic development of the country. It offered a wide range of services expected of specialized development, investment and commercial banks.

NDFC has also received permission to set up financial affiliates and subsidiary companies and has since established the following companies:

- National Development Leasing Corporation (NDLC)
- Regional Development Finance Corporation (RDFC)
- Asian Leasing Corporation (ALC)
- BRR Investments Limited

OBJECTIVES

* Promote industrial expansion and economic growth in the country by providing financial and technical assistance and consultancy services for the establishment of new enterprises as well as for the balancing, modernization, replacement and expansion of the existing enterprises and financing working capital requirements.

* Identify, promote and develop new projects and investment proposals.

* assist the government in rehabilitation of sick and problem projects

* administer and supervise the loans provided by the government and foreign institutions to projects in the country.

OPERATIONS

8.84 NDFC offers different forms of financing as well as working capital financing. The Corporation has evolved the "one window style" operation. Participation of other banks and financial institution is often necessitated. To avoid any inconvenience, borrowers are assisted in obtaining commitments from the participating banks and institutions. It also provides bridge financing so that there is no delay in the release of funds. This approach ensures minimizing the chances of implementation delays and cost overruns.

8.85 The Corporation offers financial and consultancy services. This includes loans of short, medium and long maturities, guarantees, underwriting, equity participation, syndication, working capital assistance, export financing of local machinery, trade financing of commodities between Pakistan and other members of the Islamic Development Bank and consultancy services. In this way NDFC can attract new customers and build up a clientele so that it can exercise greater choice in picking up projects for financing.

8.86 NDFC has devised successfully market innovative deposit schemes. One such scheme is the Bearer Certificate of Deposit which has been selling at the average rate of nearly a million rupees a day since it was launched in 1983. There are other deposit schemes which have been very successful and have not only lent stability to NDFCs resource base but have also helped in its growth over the years.

8.87 NDFC was the first institute to arrange trade financing between the member countries of the Islamic Development Bank under a deferred payment plan and the first in the country to enter into large scale financing of plant and equipment export from Pakistan and to mobilize development loans from the Euro-dollar market.

8.88 NDFCs approach to business development is market oriented. In making market evaluation, it first finds out what the customer wants and designs the product that suits his need. This kind of a financial assistance is "customer driven". The customers are treated as mere borrowers and the depositors are taken as investors.

8.89 The Corporation also gets help from the government and its assisted enterprises. It has evaluated the problems of certain public sector enterprises irrespective of its business interest in the concerned projects. This has helped the government in identifying weaknesses and evaluating alternatives for some of the difficulties faced by public sector enterprises. It has identified new business opportunities, made appraisals of industrial projects and identified, formulated and financed downstream projects for the country's only steel mills near Karachi. It has also involved itself in the planning of the annual credit budget participation in the management of selected public sector enterprises through the appointment of nominee directors and various other assignments given by the government. It also recommends policy changes to the government to improve the performance of the public sector.

8.90 NDFC makes sure that the projects are followed up after they are sanctioned. The project cost budgets are planned tightly to discourage overspending. Local and foreign consultants are engaged in this to assist in-house staff. The Corporation has used the plan of working capital lending so that projects can be followed on almost a day-to-day basis.

8.91 NDFC makes sure that its staff is fully trained. Out of 158 officers presently employed, 63 have undergone training in Pakistan and abroad in various aspects of development banking.

8.92 A new system is being designed to manage major accounts and quantitative projects appraisals to serve as a reliable data bank to facilitate monitoring of budgets and plans and to help in making day to day decisions. With this new information system, the Corporation hopes to improve its efficiency and client relationship.

TABLE 1				
FINANCIAL ASSISTANCE DISBURSED				
SECTOR/INDUSTRY	1985 %	1986 %	1987 %	1988 %
CONSTRUCTION	0.5	1.1	2.1	0.4
ENERGY	15.3	10.0	4.8	7.6
Electricity	2.8			1.1
Oil	4.0	2.1		
Gas	8.5	7.9	4.8	6.5
MANUFACTURING	75.1	80.7	86.0	82.4
Agrobased			25.8	39.0
Sugar	13.2	7.9	10.3	9.3
Dairy & Poultry	0.5	0.3	0.3	0.0
Oil and Vegetable ghee	9.5	12.0	13.6	28.7
Others	1.2	1.6	1.6	1.1
Automobile	7.9	9.2	9.3	5.3
Cement	12.0	8.6	7.4	3.9
Chemicals	9.9	20.1	21.5	17.7
Steel & Engineering	8.6	9.8	9.4	10.3
Textiles	4.7	10.5	8.8	4.5
Others	7.5	0.7	3.8	1.7
HEALTH CARE	4.1	2.6	1.4	0.3
MINING	0.1			
TRANSPORT		0.7		2.6
OTHERS	5.0	4.9	5.7	6.5

(figures for 1989 are not available)

8.93 The manufacturing sector received the highest share in disbursements, about 82.8% from 1985-88. In the manufacturing sector the sugar, oil & vegetable ghee, chemical and steel & engineering industries were given preferences. The percentage share of the sugar industry in total disbursements has remained almost constant over the past five years. It was about 10.2% from 1985-89. The oil and vegetable industry accounted for 9.5% of the total disbursements and the percentage share kept on increasing until it was 13.6% in 1987 and 28.7% in 1989. The share of the chemical industry in disbursements was 9.9% in 1985 and increased to 20.1% in 1986 but declined to 17.7% in 1989. The steel and engineering industry accounted for 8.6% of the total disbursements and by 1989 the percentage share had slowly increased to 10.3%.

TABLE 2				
REGIONAL DISPERSION OF TERM FINANCIAL ASSISTANCE APPROVALS				
Province	1985 %	1986 %	1987 %	1988 %
Sind	54.6	44.0	31.4	64.0
Punjab	28.04	43.0	58.6	35.0
NWFP	4.6	1.45	9.0	9.0
Baluchistan	12.14	11.0	9.12	3.0
Azad Kashmir	0.6	0.4		

(figures for 1989 are not available)

8.94 The highest number of loans were approved for Sind and Punjab. In 1985 Sind accounted for 54.6% of the loans. In 1987 the percentage share reduced to 31.4% but again increased to 64.0% in 1988. Punjab accounted for 28.04% of the approvals in 1985 and percentage share increased to 43% in 1986 and 58% in 1986 but again reduced to 35% in 1988. The share of Baluchistan in the number of approvals was 12.14% in 1985 but the percentage share kept on reducing until it was only 3.0% in 1988. NWFP got only about 6% of the share in approvals from 1985-88.

The following are key performance ratios of NDFC over the period 1985-89.

PERFORMANCE RATIOS				
				Rs in million
Year	1985	1986	1987	1988
disbursements	5002.5	7698.9	8521.8	11548.7
Return on capital	27.8%	36.1%	63.0%	33.0%
Return on assets	2.5%	2.5%	2.5%	2.5%
disb/staff No	9.14	11.8	11.9	14.51
Op profit/adm cost	628%	628%	675%	535%
adm cost/staff No	0.07	0.07	0.08	0.11

(figures for 1989 are not available)

8.95 The disbursements of funds have increased from 1985-88. In 1985 disbursements were about Rs 5002.5 million. Disbursements increased to Rs 7698.9 million 1986 and Rs 8521 million in 1987. In 1988 there was a further increase to Rs 11548.7 million. The return on capial was 27.8% in 1985 and increased to 63% in 1987 and then decreased to 33% in 1988. The return on assets has been about 2.5% from 1985-88. The disbursement per staff member have not varied considerably over the past four years. The disbursements per staff member remained at an average of Rs 11.8 million from 1985-88. The operating profit as a percentage of the administrative cost has also remained almost constant. It was about 616.5 over the past four years. The administrative cost per staff member was Rs 70,000 in 1985 and 1986 but increased to Rs 80,000 in 1987 and Rs 110,000 in 1988.

NDFCs CONTRIBUTION TO THE GROWTH OF DFIs

8.96 The share of NDFC in aggregate resources mobilized by DFIs ranged between

21.7% and 23.8% during the period under review. Its share in equity, deposits, and borrowing of DFIs decreased from 9.1%, 75.3% and 13.2%, in 1984 to 7.0%, 65.0% and 11,.6% in 1988.

8.97 The share of NDFC in channelization of resources by DFIs declined marginally from 23% in 1984 to 21.2% in 1988. In sharp contrast, NDFC's share in investment of DF's increased from 18% in 1984 to 29.7% in 1988, while its share in advances of DFIs decreased from 24% in 1984 to 17.2% in 1988.

HISTORY

8.98 The Small Business Finance Corporation was established in 1972 with the aim of financing firms to encourage them to establish new business or to expand the existing ones. The aim of the Bank is to reduce unemployment among the educated people. The Bank gives short, medium and long term loans to persons of small means who possess skill but have meagre resources to utilize them apart from the small transporters plying trucks, tankers, buses, wagons, taxis and rickshaws, the Corporation provides finances to small scale industry whose fixed assets, including the cost of land, do not exceed Rs 2 million and also small businesses having net assets not exceeding Rs 300,000.

8.99 The State Bank of Pakistan has extended special lines of credit to the Bank. In 1980, its operations were Islamized with the introduction of financing on profit-and-loss sharing basis and hire-purchase system. The loans are granted under the Islamic Principles of Financing and are repayable in easy instalments within a period ranging from three to five years with appropriate grace period. The finance provided by the Corporation takes the form of both local and foreign currencies. The maximum maturity period is eight years. Following are the objectives of the Bank.

OBJECTIVE

* to provide loans for Cottage industries, small industries, traders/shop keepers and skilled people.

" loans are given to professionals like doctors, Engineers or Lawyers to establish or expand offices etc. Small scale industries and professional offices are given for rural areas. Loans are also given for the purchase of cars.

OPERATIONS

TABLE I

Disbursements of Financial assistance

Rs in Million

Period	1884	1985	1986	1987	1988
Small businessmen& Professional	28.65 76%	60.18 75%	100.04 86%	180.22 95%	126.6 84.5%
Cottage/Small Industry	8.72 23%	19.82 25%	15.73 13%	10.20 5%	20.24 3%
TOTAL	37.43	80.00	115.77	190.42	149.80

8.100 The average annual percentage share of cottage industries in the total number of loans disbursed has been 13.8% from 1984-88. The percentage share of cottage industry was the lowest in 1988 when it accounted for only 3% of the total loans disbursed. In 1987 the percentage share of loans disbursed to cottage industry was 5%. 95% of the loans were for small businessmen and professionals during the same year. The average annual percentage of loans for businessmen/professionals was 85.5% from 1984-89.

TABLE 2					
PROVINCE WISE BREAK UP OF FINANCIAL ASSISTANCE (AS PERCENTAGE OF TOTAL AMOUNT)					
Period	1984	1985	1986	1987	1988
Punjab	45%	43%	42%	33%	49%
Sind	36%	38%	39%	49%	30%
NWFP	10%	12%	14%	12%	11%
Baluchistan	4%	5%	3%	5%	5%
Azad Kashmir	3%	1%	1%	.01%	3%

8.101 Punjab got the highest share of loans in the past five years. Punjab accounted for nearly 50% of the loans in 1988, and the percentage share has remained steady over the five years. In 1987 Sind received 49% of the loans and Punjab received 33%. The percentage share of Sind in the loans disbursed was about 40% from 1984-88 and the percentage share has remained steady over the past five year. The percentage share of NWFP, Baluchistan and Azad Kashmir in the total number of loans disbursed has also remained steady from 1984-88. The average annual distribution of loans for NWFP from 1984-88 has been about 11.8%, for Baluchistan 4.4% and for Azad Kashmir 1.6%.

TABLE 3					
RECOVERIES Rs in Million					
Period	1984	1985	1986	1987	1988
Recoveries	38.20	44.57	54.24	96.93	114.23

8.102 From 1984-85 disbursements increased by 113.7% but recoveries increased only by 17%. In 1986 the disbursements increased by 44% and recoveries by 22%. In 1987 disbursements went up by 64% and recoveries by 78%. In 1988 recoveries increased by 18% and disbursements decreased by 21%.

PERFORMANCE RATIOS				
(Rs in million)				
Year	1985	1986	1987	1988
tot disb	80	115	190.42	149.8
Return on capital	7%	8%	9%	9%
Return on assets	5%	4%	3%	3%
disb per staff No	0.48	0.66	1.01	0.79
Op profit/adm cost	151%	169%	110%	125%
adm cost/staff No	0.04	0.04	0.07	0.07

8.103 The total disbursement increased from Rs 80 million in 1985 to Rs 190 million in 1987. In 1988 there was a decrease in disbursement to Rs 149 million. The return on capital has not been very high over the past five years. It was 7% in 1985 and increased to 8% in 1986 and 9% in 1989. The return on assets has been about 3.8% over the past five years. The disbursements per staff member were about Rs 480,000 in 1985 and increased to Rs 660,000 in 1986. In 1987 the disbursements per staff number further increased to Rs 1.01 million but declined to Rs 790,000 in 1989. The administrative cost per staff member was about Rs 50,000 from 1985-88.

HISTORY

8.104 The Banker's Equity Limited was established in October 1979, but started its operation in February 1980. It was incorporated as a public limited company and sponsored by the State Bank of Pakistan, the Pakistan Banking Council and the nationalized commercial banks including Habib Bank Limited, United Bank Limited, National Bank of Pakistan, Muslim Commercial Bank Limited and Allied Bank of Pakistan Limited. Originally forty per cent of its capital was contributed by the State Bank of Pakistan and the balance sixty per cent by the Pakistan Banking Council and the nationalized commercial banks. To privatize Bankers Equity, a portion of the share capital was offered to the general public in 1987.

8.105 The policy formation, control and supervision of Bankers Equity is vested in its Board of Directors which comprises of the State Bank of Pakistan, the Pakistan Banking council and Presidents of the five nationalized commercial banks and the Managing director of Bankers Equity. The Governor of the State Bank of Pakistan is the Chairman of Board of Directors.

8.106 The Bank was formed to promote and accelerate industrial financing in the private sector and develop capital market in the country. Since its inception, Banker's Equity has been financing a wide range of medium and large scale industrial projects. It offers specialized services in the field of syndicated financing, merchant banking, leasing and modaraba finance.

OBJECTIVES

* The main objective of Bankers Equity is to bridge the gap in industrial finance arising from the heavy cost of projects. This is achieved by mobilizing the entire resources for the project as a whole through syndication with the nationalized commercial banks and other financial institutions. Both national and international institutions may be partners irrespective of whether it is equity, bridging loan, or underwriting rupee funds or foreign currency loans, normal, long and short term financing or concessional financing or financing short term.working capital requirements.

* It provides assistance in a single package thereby curtailing the time lag in the execution of projects to a great extent. The packaging capability is strengthened by the availability of concessional refinance facility from the State Bank of Pakistan for locally manufactured machinery and export of machinery. Multiple lines of credit and equity from Asian Development Bank, the Islamic Development Bank and other external financing agencies and the co-financing arrangements with the local development finance institutions and the international financing agencies are also available.

* It provides new techniques for investment financing within the frame-work of the Islamic Financial System being developed in the country. One scheme is the Participation Term Certificates. The concept of PTC and discounting of shares was introduced keeping in view the pattern of long term finance in the corporate sector in the country within the frame work of the report of the Council of Islamic Ideology on the elimination of interest from the economy. The PTC replaced the existing instrument of long term financing which was debentures.

* BEL accords high priority to the high value added-export oriented and labour intensive industries.

* It promotes high-tech and pioneering industries more particularly in electronics, chemical and petrochemicals.

* It encourages investment in Down Stream steel-based and engineering goods industries, industries based on agricultural waste and those with specific indigenization targets such as automobiles.

* It aims to simplify the existing financial procedures and to overcome the delays in the implementation of projects caused by the multiple system of project financing in the country.

OPERATIONS

8.107 Bankers Equity Limited has the distinction of pioneering the concept of one-stop unified package financing in the country. It offers the entire range of financial services extending from direct equity investment and underwriting of public issues of shares to the provision of term financing in both local and foreign currencies, short term working capital finance, modaraba finance, leased-based financial assistance and guarantees of foreign exchange.

8.108 Bankers Equity provides financing to those industrial projects which are sponsored by the private sector solely or co-sponsored by the private sector jointly with the public sector and seek public subscription of shares together with being listed on the stock exchange. The projects having a total capital cost of Rupees ten million and above are eligible for financing. While the minimum financing limit per project is for the time being fixed at Rupees two and a half million. There is no upper limit on the amount of financing packaged by Banker Equity for individual projects. For balancing, modernization and replacement of existing units, the minimum financing limit is relaxed to Rupees one and a half million. There is no minimum limit for successive additional financing of the projects assisted by Bankers Equity. To be eligible for obtaining financial support from Bankers Equity the client should organize itself as a joint stock company.
Before financing a project, the Bank makes a detailed investigation of the projects such as economic, technical, financial, and managerial aspects. Projects which are not technically sound are declined during the preliminary examination. The past performance of the sponsors is an important criterion.

8.109 The Bankers Equity provides the following facilities to companies who desire to establish medium and large scale industries in Pakistan.

* Direct equity support and advance loans on profit sharing basis through the instrument of Participation Term Certificates. It is aimed at providing term financing on PLS basis to projects. PTCs are negotiable and marketable financial instruments. It provides Term Finance Certificates which are redeemable long-term instruments based on mark-up prevailing in the market. The certificates are issued by the sponsors and purchased by Bankers Equity. They are repurchased by the sponsors from Bankers Equity over a period upto ten years.

* Foreign currency requirements of projects are arranged by Bankers Equity at rates applicable for respective credit line. Such rates are inclusive of exchange risk cover.

* It provides working capital to the industrial and trading concerns.

* It finances leases to projects on the basis of periodical payments.

* It promotes and co-sponsors projects on a mutually agreed basis.

* It manages investment portfolios.

* It provides guarantees against supplier/buyers credit in lieu of foreign currency loan. This loan is arranged by the sponsors of the project.

* Syndicate stocks and term loans both in local and foreign currencies.

* Underwrites public issues. An arrangement is made under which an institutional underwriter such as a bank of DFIs makes a commitment to purchase the unsubscribed shares offered to the general public. The most commonly practised technique of underwriting is "stand-by" underwriting.

* It provides technical, financial and consultancy services to the companies projects

* It assists in take overs, merger, dis-investment, re-organizing and rehabilitation of companies

* Floats Modaraba and mutual funds. Modaraba is a concept of Islamic finance in which funds are provided by one or a group of investors for business to be carried out by another party providing skill and effort to run the business.

TABLE 1

PERCENTAGE DISTRIBUTION OF DISBURSEMENTS BY INDUSTRIAL SECTORS

Period	1984-85	1985-86	1986-87	1987-88	1988-89
Food,Tobacco, Baverages	24.88	35.74	20.6	11.8	13.2
Textile	13.7	12.34	21.0	38.4	13.2
Leather Paper& Pulp	9.25	11.6	5.2	0.9	2.7
Chemicals, Pharmaceutical &Fertilizer	8.56	40.39	16.0	19.6	6.4
Cement&Non-Metallic Minerals	38.94	23.34	16.9	10.2	8.4
Basic Metals	1.05			7.1	
Metal Products other than Machinery	1.48	1.56	2.0	1.9	1.2
Machinery	0.31	0.79			1.0
Electrical Machinery		0.85	0.5	3.2	0.7
Electronic Industry					2.3
Miscellaneous Industry	2.89	2.06	10.1	10.9	31.9

(figures give percentage of total amount of loans)

8.110 In 1985-86 the Food, Tobacco and Beverage Sector accounted for the largest share in disbursement of funds. These industries accounted for 35.74% of the total disbursements, followed by Cement and Non-metallic Minerals and Products Sector at 23.34%. The Paper and Pulp Sector was 11.16%. In 1986-87, the textile, food, tobacco and baverages sectors accounted for the largest share in disbursement of funds at 21% and 20.6%. The cement and other non-metallic minerals and chemicals and pharmaceuticals sectors accounted for 16.9% and 16% of the total disbursements.

8.111 In 1987-88 the textile sector had the largest share in disbursements 38.4%, followed by chemicals, pharmaceuticals, and fertilizers at 19.6%. Food, tobacco and beverages accounted for 11.8% of the total disbursements. In 1988-89 there was a shift to the share of miscellaneous industries which accounted for 31.9% of the total disbursements, followed by 30.6% for the textile and 13.2% for the food, tobacco and beverages sectors.

8.112 One of the main objectives of BEL was to support high-tech industries especially electronics, chemicals and petrochemicals. BEL has not accorded priority to these industries over the past five years. The figures from the annual reports show that the percentage share of chemical, pharmaceutical and fertilizer industry in the total disbursements was the highest in 1986. They accounted for 40.4% of the total share in disbursements. However from 1987-89 the share in disbursements declined considerably from 16% in 1987 to 6.4% in 1989.

8.113 Other high-tech industries like the ones which are steel based have not been given priority. These include the electronic industry which did not contribute to the share in disbursements until 1989 when the percentage share was only 2.9%. The machinery industry accounted for an average of 0.7% of the total disbursements and the metal industry accounted for about 1.6% of the disbursements.

TABLE 2

REGIONAL DISPERSAL OF INVESTMENTS APPROVED BY BANKER'S EQUITY

Province	1985-86	1986-87	Net change
Sind	16	28	148.9
Punjab	52	50	76.9
NWFP	21	8	-32.1
Baluchistan	10	2	42.2
Azad Kashmir		12	

(figures give percentage of total amount)

8.114 In 1986-87 the total financing approval for Sind rose 2.5 times since the previous year. Similarly, the financing approved for Punjab and Baluchistan have also risen by 76.9% and 42.2%. The financing approved for NWFP declined by 32.1% during 1986-87.

TABLE 3

REGIONAL DISPERSAL OF INVESTMENTS APPROVED BY BANKERS EQUITY

Province	1987-88	1988-89	Net change
Sind	22	24	54.3
Punjab	61	36	-3
NWFP	6	13	228.4
Baluchistan	9	23	233.8
Azad Kashmir	1	3	210.4

(figures give percentage of total amount of loans disbursed)

8.115 In 1988-89 the financing for Punjab approved by Bankers Equity declined by 3% since the previous year. That of NWFP and Baluchistan increased by 228.4% and 233.8% in 1988-89. The disbursements approved for Azad Kashmir also rose by 210.4% although the total share in disbursements was only 3% in 1988-89. The disbursements for Sind rose by 54.3% over the previous year.

8.116 It is seen that Punjab and Sind get the highest number of loans. This is because these two provinces receive the highest number of applications. Also lack of infrastructure facilities in the less developed areas discourage industrialists from financing in these areas.

PERFORMANCE RATIOS (Rs in Millions)

Year	1985-86	1986-87	1987-88	1988-89
Disbursements	926.502	1856.7	2315.25	2734.01
Return on Assets	6%	7%	4%	4%
disb/tot staff	5.01	7.45	7.44	8.26
Op Profit/tot adm cost	746%	813%	359%	359%
adm cost/staff no	0.11	0.12	0.15	0.16

8.117 The disbursements of funds have increased over the past five years. The increase was the highest in 1986-87 when disbursements went up by 100.4%. In 1987-88 the increase was 24.7% and 18.1% in 1988-89.

8.118 The Return on assets has been an average of about 5% from 1986-89. The disbursements per staff number have increased from Rs 5.01 million in 1986 to 7.45 million in 1987 and Rs 8.26 million in 1989. The administrative cost per staff member was Rs 110,000 in 1986 and kept increasing until it was Rs 160,000 in 1989. The total operating profit as a percentage of the administrative cost was 746% in 1986 and increased to 813% in 1987. It decreased to 359% in 1988 and 1989.

PROBLEMS

* There is an absence of vigorous follow up of underlying objectives and recoveries.
* Loans given due to political pressure often become substandard and doubtful.
* Market evaluations are weak due to non-availability of data.
* Legal proceeding take a long time.

BEL's CONTRIBUTION TO THE GROWTH OF DFIs

8.119 BEL's share in aggregate resources of DFIs increased from 4.6% in 1984 to 6% in 1988. Its share in aggregate deposits and borrowing of DFIs increased from 2.5% and 3.2% in 1984 to 3.6% and 6.8% in 1988. Its share in equity of DFIs increased from 9.3% in 1984 to 11% in 1986 but then fell to 4.6% in 1988.
The share of BEL in channelization of resources of DFIs increased from 3.8% and 3.2% in 1984 to 6% and 5.6% in 1988.

HISTORY

8.120 The National Development Leasing Corporation was established in 1985 as a joint venture of the Asian Development Bank and National Development Finance Cooperation. It is the first leasing company and was set up under the auspices of the Government of Pakistan to introduce leasing in the country as part of the Islamic financial system. Leasing, which is akin to long term financing is ideally suited for a non interest based financial system. Since its inception thirteen new leasing companies have been established. It is operating in the private sector and is managed by an independent professional management.

8.121 NDLC provides lease facilities for acquisition of productive assets in the industrial, energy , mining, construction, commercial and services sector by employing a whole range of financial services. These include among others direct purchase lease, asset lease transfer, leveraged and syndicate lease, sales lease back, and lease advisory services.

8.122 Lease presents a viable and sound alternative to conventional debt financing. The lessee acquires most of the economic values associated with outright ownership of the asset, even though the lessor retains title to it. In addition leasing allows capital conservation upto 100% financing, improves cash flow position, provides a tax shield, is self-liquidating and preserves existing credit lines.

OBJECTIVES

* To extend leasing facilities to financially sound and established enterprises.

* To upgrade the technology of the existing industries through BM&R and expansion programmes. Support is mainly provided for balancing, modernization, replacement and expansion programmes.

* To utilize local technology through leasing the locally fabricated equipment.

* To achieve the objective of the Government in contributing towards promoting leasing in the country and thereby advancement of the Islamic economic system. The Council of Islamic Ideology has declared leasing conformed to the principles of Sharia.

* To provide equity support and underwriting service to the private sector enterprises and broad base the capital market.

OPERATIONS

8.123 Any capital equipment, listed below can be leased through NDLC.

<u>Industrial Equipment and Plants.</u>

Metal making and processing machinery, textile machinery, woodworking and plastic machinery, construction equipment, scarf-folding, cranes, forklifts, racks, chemical and pharmaceutical plants, power plants and boiler, anti-pollution equipment and installation.

Office Equipment

Office equipment in general, computer and peripheral equipment, software, electronic data processing equipment, facsimile, electronic PABX systems, accounting machines, copiers and calculators.

Industrial Vehicles

Forklifts, cranes, earth-moving equipment, concrete mixer, reefer trucks, fire trucks and ambulances.

8.124 NDLC also offers assistance to overseas Pakistanis. Leasing of industrial equipment to be purchased in foreign and local currencies and loans for similar purpose. The letters of credit from the foreign banks for the payment of rentals on leased equipment and interest and repayment of loan can also be accepted as a valid security The extent of the security is negotiable.

The objective is to allow the overseas Pakistanis to keep protected their savings in foreign exchange and at the same time establish and manage industry in Pakistan with financial assistance from NDLC.

8.125 The Corporation has developed a financial instrument for the mobilization of savings as per the permission of the Government of Pakistan. It is based on the principal of profit and loss sharing and consists of certificates of investment that may be bearer or registered for a term of three months to ten years.

8.126 It launched in June 1989 Rs. 100 million M Jaraba Fund under the name of Long Term Venture Capital Modaraba. According to the Annual Report of 1988 the leases are satisfactorily serviced. Thus the Corporation has 100% recovery.

TABLE 1 INDUSTRY WISE DISBURSEMENTS OF LEASES (AS PERCENTAGE OF TOTAL AMOUNT)			
SECTOR	1986 (%)	1988 (%)	1989 (%)
ENERGY	12.95	7.16	4.31
Oil	10.62	6.57	4.31
Gas	2.33	0.59	
MANUFACTURING	80.85	79.74	83.04
AGROBASED	50.01	45.92	52.0
Tobacco	8.13	4.21	2.01
Textile & Allied	16.59	22.72	22.95
Sugar	24.90	16.47	19.23
Food and Allied	0.39	2.53	7.82
ALL INCLUSIVE	30.85	33.82	31.04
Cement	8.61	7.66	4.83
Steel and Engineering	7.25	12.76	17.32
Jute & Allied	1.04	1.01	0.51
Pharmaceutical	4.11	1.91	1.01
Paper and Board	5.82	4.91	0.88
Other	4.01	2.39	5.31
TRANSPORTATION AND COMMUNICATION	1.93	0.00	
CONSTRUCTION	0.10	1.18	0.50
MINING	0.00	0.00	0.00
PROFESSIONAL SERVICES	1.66	1.94	4.94
HOTEL & TOURISM	16.59	22.72	1.08
HOSPITALS & CLINICS	0.00	5.14	5.52
MISCELLANEOUS	5.52	0.40	

8.127 The manufacturing sector was given a priority over all other sector. The share of the manufacturing sector in total leases has been 80% over the past four years. The Agrobased industry.accounted for about 50% of the leases from 1986-89. The textile industry accounted for about 20% of the total leases and the sugar industry about 20%. There has been no major shift in the sectoral disbursements of leases.

PERFORMANCE RATIOS					
Period	1985	1986	1987	1988	1989
tot disb		258.0		1016.4	1609.0
Return on capital	25%	35%	81%	54%	46%
Return on Assets	3%	4%	4%	2%	1%
dis per staff No		8.60		2.42	2.682
Op profit/ adm cost	254%	482%	592%	402%	2389%
adm cost/ staff No	0.08	0.14	0.18	0.22	0.03

(disbursements for 1985 and 1987 are not available)

8.128 The return on capital was the highest in 1987. The profit earned by NDLC as a percentage of capital was 81% during that year. The return on capital was 25% in 1985. It increased to 35% in 1986 and then decreased after 1987 to 54% in 1988 and 46% in 1989. The return on assets was averaged 2.8% from 1985-89. The disbursements per staff member were Rs 8.6 million in 1986 but declined to Rs 2.6 million in 1988 and 89. The operating profit as a percentage of the administrative cost was 254% in 1985 but kept increasing until it was 592% in 1987 and increased to 2389% in 196[illegible]. The administrative cost per staff member was Rs 80,000 in 1985 and kept increasing until it was Rs 220,000 in 1988 and decreased to Rs 30,000 in 1989.

PROBLEMS

* Cross-border leasing: In Pakistan's case, this refers to foreign lessors leasing to Pakistani lessees. Under the existing law, a with-holding tax has to be deducted by the lessee and deposited with the government on the entire rental paid to the foreign lessor. In the case of a finance lease, the rental consists of both capital repayment and profit payment, and hence the with-holding tax is being deducted not only on the profit but also on capital repaid - an obviously unacceptable situation to the foreign lessor. This treatment should be such that in the case of foreign loan, the with-holding tax is deducted only on the interest portion. In order not to discriminate against the leasing alternative, the government should review its policy on with holding tax and rules so that on cross border leases this tax is deducted only on the profit portion.

* It is difficult to make market evaluations due to the lack of data.

CHAPTER - 9

SUMMARY INFORMATION ON REMAINING DEVELOPMENT FINANCE INSTITUTIONS

9.01 This chapter reproduces the summary information on the remaining DFIs provided by the Ministry of Finance, Government of Pakistan. The sequence of presentation reflects chronology of the dates of commencement.

ICP

INVESTMENT CORPORATION OF PAKISTAN

HISTORY AND OBJECTIVES

The Investment Corporation of Pakistan (ICP) was established in February 1966 through an Ordinance of the Federal Government of Pakistan, as a development institution with the objectives of broadening the base of equity investments and developing the capital market. Soon after its establishment, the Corporation invited applications from sponsors seeking finances through underwriting of share issues and placement of debentures. This enabled the enterpreneures to meet the equity and local currency requirements of funds of their projects.

In January 1967, the Corporation launched its Investors Scheme in order to broaden the base of equity investments. The objective was further strengthened with the floatation of First ICP Mutual Fund in June, 1967. The Corporation has up till June 30, 1988 launched 17 such Funds and has thus mobilized savings of Rs.190.0 million.

The Corporation seeks to meet the following objectives :

i) Underwrit public issues of shares, provide financial assistance through purchase of Term Finance Certificate /Participation Term Certificate to enable the enterpreneures to meet the equity and local currency requirement of funds for financing their projects and also for the purchase of locally manufactured machinery.

ii) Open and maintain investment accounts with a view to broadbasing share ownership and widening the base of capital market for the purchase and sale of shares of public limited companies. Further, with the introduction of Sharing Account Scheme the Corporation provides an opportunity to the investors to invest in shares jointly with ICP on 'profit and loss sharing basis.

iii) Buying and selling shares on the stock market with a view to providing strength to the stock exchange and help in maintaining stability in share values.

MANAGEMENT STRUCTURE

The Board of Directors consists of 13 members. Eight members including the Chairman and the Managing Director are appointed by the Federal Govecnement and five are elected by the shareholders.

CAPITAL STRUCTURE

The authorised capital of the Corporation is Rs.200 million. The issued and subscribed capital amounted to Rs.100 million on June 30, 1987. The shares are held by the nationalized banks, foreign banks and insurance corporations/companies.

INCOME STATEMENT

	(Rs. million) Year Ended 30 June 1988	1987	%Change
Operating Income			
Interest on Loans, Discounts and Return on Non-Interest Bearing Accounts	72.629	73.928	(1.75)
Gain on Sale of Investments	53.435	52.010	2.73
Service and Commitment Charges	19.756	19.782	(.13)
Others	78.817	92.349	(14.65)
	224.637	238.069	(5.64)
Operating Expenses			
Interest on Borrowings & Return on Non-Interest Bearing Accounts	122.919	116.758	5.27
Salaries, Allowances and Benefits	37.665	30.183	24.78
Other Expenses	42.380	41.967	.98
Depreciation	1.543	3.344	(53.85)
Loss on Sale of Investments	1.760	.603	191.87
	206.267	192.855	6.95
Operating Profit/(Loss)	18.370	45.214	(59.37)
Net Profit/(Loss) before Taxation	18.370	45.214	(59.37)
Taxation			
Prior Years	-	(5.871)	(100.00)
	-	(5.871)	(100.00)
Net Profit/(Loss) after Taxation	18.370	51.085	(64.04)
Accumulated Profit/(Loss) B/F	93.313	54.228	72.07
Profit Available for Appropriation	111.683	105.313	6.04
Appropriation			
Dividends Paid and Proposed	-	10.000	(100.00)
Transfer to Other Reserves	2.000	2.000	-
	2.000	12.000	3.33)
Accumulated Profit/(Loss)	109.683	93.313	7.54

MANAGEMENT INFORMATION

	(Rs. million) Year Ended 30 June 1988	1987	%Change
LOANS, ADVANCES AND PROFIT SHARING ARRANGEMENTS			
Regional Breakdown of total advances approved during year			
- Punjab	154.355	51.496	199.74
- Sind	202.797	108.861	86.29
- N.W.F.P.	-	13.950	(100.00)
- Baluchistan	6.650	10.900	(38.99)
- Azad Kashmir and Northern Areas	29.800	-	-
Total	393.602	185.207	112.52
Regional Breakdown of total advances disbursed during year			
- Punjab	29.486	56.475	(47.79)
- Sind	93.936	118.167	(20.51)
- N.W.F.P.	3.000	6.350	(52.76)
- Baluchistan	.167	32.082	(99.48)
- Azad Kashmir and Northern Areas	19.800	5.000	296.00
Total	146.389	218.074	(32.87)
DEPOSITS AT YEAR END			
- Over 1 year	202.294	193.252	4.68
Total	202.294	193.252	4.68
NUMBER OF EMPLOYEES (AT YEAR END)			
Management			
- Executive	19	17	11.76
- Non-Executive	271	239	13.39
Total	290	256	13.28
Permanent Non-Management Staff			
- Other	273	289	(5.54)
Total	273	289	(5.54)
Total	563	545	3.30
FURTHER ANALYSIS OF PERMANENT NON-MANAGEMENT			
- No. of Unionised Staff	273	289	(5.54)
Total	273	289	(5.54)
WAGES BILL			
Management			
- Executive	1.603	2.150	(25.44)
- Non-Executive	11.635	7.352	58.26
Total	13.238	9.502	39.32
Permanent Non-Management Staff			
- Other	9.693	8.959	8.19
Total	9.693	8.959	8.19
Total	22.931	18.461	24.21
FURTHER ANALYSIS OF PERMANENT NON-MANAGEMENT			
- Unionised Staff Wage Bill	9.693	8.959	8.19
Total	9.693	8.959	8.19

MANAGEMENT INFORMATION

SPECIFIC INFORMATION - BANKS & DFI.
INVESTMENT CORPORATION OF PAKISTAN

1.TERM ADVANCES APPROVED DURING THE YEAR

	PRIVATE SECTOR 1988	PRIVATE SECTOR 1987	PUBLIC SECTOR 1988	PUBLIC SECTOR 1987	TOTAL 1988	TOTAL 1987
Manufacturing						
-Cement	-	-	-	-	-	-
-Sugar	134.900	-	-	-	-	-
-Fertilizer	-	-	-	-	-	-
-Energy	-	-	-	-	-	-
-Textile	196.972	29.570	-	-	-	-
-Engineering	33.600	7.500	-	-	-	-
-Others*	28.130	148.137	-	-	-	-
Agriculture,Forestry Hunting and Fishing	-	-	-	-	-	-
Mining & Quarrying	-	-	-	-	-	-
Construction	-	-	-	-	-	-
Electricity, Gas & Water	-	-	-	-	-	-
Commerce	-	-	-	-	-	-
Services	-	-	-	-	-	-
Others						
TOTAL	393.602	185.207	-	-	-	-

* includes paper & board, Chemicals & Pharmaceutical and Vanaspati & allied.

2.BRANCH NET WORK AT YEAR END

	NO OF BRANCHES 1987	NO OF BRANCHES 1988	SHARING INVESTORS DEPOSIT 30-6-88 1987	SHARING INVESTORS DEPOSIT 30-6-87 1988	NON-SHARING INVESTOR DEPOSIT 30-6-88 1987	NON-SHARING INVESTOR DEPOSIT 30-6-87 1988	ICP DEPOSIT* 30-6-88	ICP DEPOSIT* 30-87
Sind Urban	2	2	70.1	71.0	39.0	35.3	105.1	106.3
Sind Rural	-	-	-	-	-	-		
Punjab Urban	5	5	85.4	82.2	64.4	50.7	127.8	123.1
Punjab Rural	-	-	-	-	-	-		
N.W.F.P Urban	1	1	7.6	7.6	9.7	9.2	11.4	11.4
N.W.F.P Rural	-	-	-	-	-	-		
Baluchistan Urban	1	1	2.0	2.1	1.0	0.4	3.0	3.2
Baluchistan Rural	-	-	-	-	-	-		
Azad Kashmir & Northen Areas Urban	-	-	-	-	-	-		
Azad Kashmir & Northen Areas Rural	-	-	-	-	-	-		

* Sharing Account only.

(Rs in millions)

DEPOSITS.

Deposits at year end.

Deposits from banks and Development. Finance institutions.		
Other deposits for period		
- Less than 3 months	-	-
- 3 months - 1 year		
- Over 1 year	202.294	193.252
Total (Agree with line 218 of form B2)	202.294	193.252

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RATIOS

	Year Ended 30 June 1988	1987
Net Profit After Tax/Net Shareholder's Equity	7.27 %	21.82 %
Total Income/Net Shareholder's Equity	88.97 %	101.69 %
Net Profit Before Tax/Net Shareholder's Equity	7.27 %	19.31 %
Salaries and Benefits/Total Operating Expenses	18.26 %	15.65 %
Dividend Rate	-	10.00 %
Operating Profit/Total Income	8.17 %	18.99 %
Net Shareholder's Equity/Total Assets	8.75 %	8.46 %
Borrowing Ratio	666.30 %	685.04 %
Liqiid Assets/Total Deposit Liabilities	6.4406 : 1	6.3243 : 1

EPF

EQUITY PARTICIPATION FUND

HISTORY AND OBJECTIVES

The Equity Participation Fund (EPF) was established by a special legislation of the Federal Government in 1970 to foster and accelerate the growth of small and medium-sized industrial enterprises in the private sector in the less developed areas of Pakistan and providing equity support to the entrepreneurs of moderate means who are unable to raise funds for industrial activity from the capital market. For the purpose of the Ordinance, less-developed areas are spread over the whole of Pakistan excluding the areas specified below but not excluding the Government financed industrial trading estates located in any of those areas other than Karachi: (i) Islamabad Capital Territory, (ii) Karachi Division, (iii) Lahore District, (iv) Tehsil of Ferozwala, (v) Tehsil of Gujranwala, (vi) Tehsil of Sialkot, (vii) Tehsil of Faisalabad, (viii) Tehsil of Multan, (ix) Tehsil of Rahimyarkhan, (x) Tehsil of Rawalpindi, (xi) Taluka of Kotri, (xii) Taluka of Hyderabad, (xiii) such areas adjoining Karachi Division and Lahore District as may be specified by the Central Board of Revenue.

MANAGEMENT STRUCTURE

The overall control of the EPF vests in its Board of Directors which is composed of the Chairman who is nominated by the Federal government, four Provincial Secretaries - Industries nominated by the Provincial governments, one member representing the Federal Government, another State Bank of Pakistan, two Senior Executives from institutional investors, and one Executive Director nominated by the IDBP who is the also the Executive Director of the Fund.

CAPITAL STRUCTURE

The authorised share capital of the Fund is Rs.200 million out of which Rs.155 million was paid-up as on 30.6.88. The Fund can, however, augment its resources by raising funds through issue of debentures and/or by raising loans from the Federal Government. The Federal Government has allowed a special facility in the form of tax credit for the companies which purchase shares or debentures of the fund.

BALANCE SHEET

ASSETS	(Rs. million) Year Ended 30 June 1988	1987	%Change
Cash and Bank Balances	8.051	28.220	(71.47)
Advances/Profit Sharing Arrangements			
Loans for Project Financing	1.650	1.650	-
	1.650	1.650	-
Investments - at Cost			
Shares of Companies	144.436	127.765	13.04
Other Investments	42.262	29.115	45.15
	186.698	156.880	19.00
Other Assets	19.486	14.966	30.20
Fixed Assets	.383	.122	213.93
Net Assets in Bangladesh	51.386	51.386	
	267.654	253.224	5.69
EQUITY AND LIABILITIES			
Equity			
Paid Up Share Capital	155.000	155.000	-
Accumulated Profit/(Loss)	.005	.004	25.00
Capital Reserves	47.104	34.959	34.74
Revenue Reserves	30.113	27.746	8.53
	232.222	217.709	6.66
Borrowings			
Debentures and Bonds	35.000	35.000	-
	35.000	35.000	-
Other Liabilities	.432	.515	(16.11)
	267.654	253.224	5.69
Contingencies and Commitments	91.496	88.876	2.94

INCOME STATEMENT

	(Rs. million) Year Ended 30 June 1988	1987	%Change
Operating Income			
Interest on Loans, Discounts and Return on Non-Interest Bearing Accounts	4.910	3.790	29.55
Interest on Bank Deposits	1.816	2.513	(27.73)
Premium on Disinvestment of Funds' Holdings	.127	.131	(3.05)
Service and Commitment Charges	4.705	4.517	4.16
Others	.393	.059	566.10
	11.951	11.010	8.54
Operating Expenses			
Salaries, Allowances and Benefits	1.334	.926	44.06
Other Expenses	.600	.415	44.57
Depreciation	.061	.049	24.48
	1.995	1.390	43.52
Operating Profit/(Loss)	9.956	9.620	3.49
Net Profit/(Loss) before Taxation	9.956	9.620	3.49
Net Profit/(Loss) after Taxation	9.956	9.620	3.49
Accumulated Profit/(Loss) B/F	.004	.004	-
Profit Available for Appropriation	9.960	9.624	3.49
Appropriation			
Transfer To(From) General Reserve	2.000	-	-
Transfer to Other Reserves	7.955	9.620	(17.30)
	9.955	9.620	3.48
Accumulated Profit/(Loss)	.005	.004	25.00

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MANAGEMENT INFORMATION

	(Rs. million) Year Ended 30 June 1988	1987	%Change
LOANS, ADVANCES AND PROFIT SHARING ARRANGEMENTS			
Approvals (during the year)			
- Equity Investments	35.610	54.450	(34.60)
Total	35.610	54.450	(34.60)
Disbursements (during the year)			
- Equity Investments	22.760	25.750	(11.61)
Total	22.760	25.750	(11.61)
Portfolio (year end)			
- Other Loans	1.650	1.650	-
- Equity Investments	144.436	127.765	13.05
Total	146.086	129.415	12.88
Regional Breakdown of total advances approved during year			
- Punjab	14.110	22.200	(36.44)
- Sind	10.350	12.800	(19.14)
- N.W.F.P.	9.950	11.350	(12.33)
- Baluchistan	-	6.600	(100.00)
- Azad Kashmir and Northern Areas	1.200	1.500	(20.00)
Total	35.610	54.450	(34.60)
Regional Breakdown of total advances disbursed during year			
- Punjab	12.710	8.450	50.41
- Sind	2.600	2.200	18.18
- N.W.F.P.	3.550	9.800	(63.78)
- Baluchistan	2.700	4.800	(43.75)
- Azad Kashmir and Northern Areas	1.200	.500	140.00
Total	22.760	25.750	(11.61)
NUMBER OF EMPLOYEES (AT YEAR END)			
Management			
- Executive	1	1	-
- Non-Executive	8	6	33.33
Total	9	7	28.57
Permanent Non-Management Staff			
- Other	10	8	25.00
Total	10	8	25.00
Total	19	15	26.67
FURTHER ANALYSIS OF PERMANENT NON-MANAGEMENT			
- No. of Unionised Staff	10	8	25.00
Total	10	8	25.00
WAGES BILL			
Management			
- Executive	.108	.094	14.89
- Non-Executive	.732	.483	51.55
Total	.840	.577	45.58
Permanent Non-Management Staff			
- Other	.494	.349	41.55
Total	.494	.349	41.55
Total	1.334	.926	44.06
FURTHER ANALYSIS OF PERMANENT NON-MANAGEMENT			
- Unionised Staff Wage Bill	.494	.349	41.55
Total	.494	.349	41.55

RATIOS

	Year Ended 30 June 1988	1987
Net Profit After Tax/Net Shareholder's Equity	4.28 %	4.41 %
Total Income/Net Shareholder's Equity	5.14 %	5.05 %
Net Profit Before Tax/Net Shareholder's Equity	4.28 %	4.41 %
Salaries and Benefits/Total Operating Expenses	66.86 %	66.61 %
Operating Profit/Total Income	83.30 %	87.37 %
Net Shareholder's Equity/Total Assets	86.76 %	85.97 %
Borrowing Ratio	15.07 %	16.07 %

FBC

FEDERAL BANK FOR COOPERATIVES

HISTORY AND OBJECTIVES

The Federal Bank for Cooperatives (FBC) was established under the Establishment of Federal Bank of Cooperatives and Regulation of Cooperative Banking Ordinance of 1976 to improve and regularise the working of Cooperative Banks in particular and strengthen the cooperative movement in the country in general.

Some of the major objectives of the Bank are summarised below:-

i) Make secured loans and advances to the provincial cooperative banks and multi-unit cooperative societies.

ii) Lay down policy guidelines in relation to the business of the Provincial Cooperative Banks.

iii) Assist the Federal Government and the Provincial Governments in formulating schemes for the development and revitalisation of the cooperative movement in the country in general and the Provincial Cooperative Banks in particular.

iv) Assist Provincial Cooperative Banks in preparing their seasonal and developmental loaning programmes and conduct appraisal and undertake feasibility study of projects covered by such loaning programmes.

v) Encourage the development of special cooperative projects, the objects and areas of operation of which may extend to more than one Province.

vi) Organize training in cooperation and cooperative banking for the employees of the Provincial Cooperative Banks and the Cooperative Societies.

vii) Carry out research in the problems of rural credit and on such other matters as have bearing on the development of the cooperative movement in the country.

viii) Ensure proper utilization of loans obtained from the Bank.

ix) Inspect the affairs of Provincial Cooperative Banks and issue guidance for the improvement of their working.

x) If necessary, contribute to the Share Capital of the Provincial Cooperative Banks.

MANAGEMENT STRUCTURE

The FBC is administratively under the control of the Ministry of Finance. The Governor of State Bank of Pakistan, is the Chairman of the Board of Directors. Seven other Directors are nominated by the State Bank while the Federal Government nominates the Managing Director and 12 Directors including the Federal Secretaries of the Ministries of Finance and Food and Agriculture and the Provincial Secretaries for Cooperatives.

CAPITAL STRUCTURE

There are 2000 ordinary shares of Rs.100,000 each; 75 percent of the shares are held by the State Bank of Pakistan, 10 percent by the Federal Government and the rest by the Provincial Governments.

BALANCE SHEET

	(Rs. million) Year Ended 30 June 1988	1987	%Change
ASSETS			
Cash and Bank Balances	14.419	6.277	129.71
Money at Call and Short Notice	-	3.623	(100.00)
Advances/Profit Sharing Arrangements			
Loans for Project Financing	247.462	136.000	81.95
Other Loans and Advances	2,925.574	2,258.288	29.54
	3,173.036	2,394.288	32.52
Investments - at Cost			
Securities/Treasury Bills of Federal/Provincial Governments	19.569	19.569	-
Shares of Companies	49.243	49.243	-
Other Investments	4.196	3.406	23.19
	73.008	72.218	1.09
Other Assets	5.990	4.205	42.44
Fixed Assets	3.721	2.739	35.85
	3,270.174	2,483.350	31.68
EQUITY AND LIABILITIES			
Equity			
Paid Up Share Capital	200.000	200.000	-
Accumulated Profit/(Loss)	.061	.257	(76.26)
Revenue Reserves	194.462	175.462	10.82
	394.523	375.719	5.00
Deposit and Other Accounts			
Current/Contingency Accounts	.908	4.557	(80.07)
	.908	4.557	(80.07)
Borrowings			
Local	2,810.559	2,043.443	37.54
	2,810.559	2,043.443	37.54
Other Liabilities	64.184	59.631	7.63
	3,270.174	2,483.350	31.68
Contingencies and Commitments	75.000	75.000	

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INCOME STATEMENT

	(Rs. million) Year Ended 30 June 1988	1987	%Change
Operating Income			
Interest on Loans, Discounts and Return on Non-Interest Bearing Accounts	50.568	31.527	60.39
Interest on Bank Deposits	.359	.534	(32.77)
Interest on Government Securities	2.042	2.039	.14
Others	.525	.199	163.81
	53.494	34.299	55.96
Operating Expenses			
Interest on Borrowings & Return on Non-Interest Bearing Accounts	10.930	8.244	32.58
Salaries, Allowances and Benefits	10.147	7.688	31.98
Other Expenses	12.693	11.114	14.20
Depreciation	.868	.702	23.64
	34.638	27.748	24.83
Prior Period Adjustments	(.053)	(3.939)	(98.65)
Net Profit/(Loss) before Taxation	18.803	2.612	619.86
Net Profit/(Loss) after Taxation	18.803	2.612	619.86
Accumulated Profit/(Loss) B/F	.257	.145	77.24
Profit Available for Appropriation	19.060	2.757	591.33
Appropriation			
Transfer To(From) General Reserve	18.999	2.500	659.96
	18.999	2.500	659.96
Accumulated Profit/(Loss)	.061	.257	(76.26)

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MANAGEMENT INFORMATION

	(Rs. million) Year Ended 30 June 1988	1987	%Change
LOANS, ADVANCES AND PROFIT SHARING ARRANGEMENTS			
Approvals (during the year)			
- Term Loans	150.000	75.000	100.00
- Other Loans & Bebentures	3,000.000	2,421.000	23.92
Total	3,150.000	2,496.000	26.20
Disbursements (during the year)			
- Term Loans	134.580	75.000	79.44
- Other Loans	2,885.700	2,419.750	19.26
Total	3,020.260	2,494.750	21.07
Portfolio (year end)			
- Term Loans	247.462	136.000	81.96
- Other Loans	2,914.798	2,250.753	29.50
Total	3,162.260	2,386.753	32.49
Regional Breakdown of total advances approved during year			
- Punjab	2,384.000	1,937.000	23.08
- Sind	211.500	246.000	(14.02)
- N.W.F.P.	390.000	244.000	59.84
- Baluchistan	-	9.000	(100.00)
- Azad Kashmir and Northern Areas	164.500	60.000	174.17
Total	3,150.000	2,496.000	26.20
Regional Breakdown of total advances disbursed during year			
- Punjab	2,335.590	1,851.300	26.16
- Sind	95.000	201.600	(52.88)
- N.W.F.P.	433.830	323.930	33.93
- Azad Kashmir and Northern Areas	155.860	117.920	32.17
Total	3,020.280	2,494.750	21.07
Advances made under Small Loans Scheme (during year)			
- Agriculture	2,885.700	2,419.750	19.26
Total	2,885.700	2,419.750	19.26
DEPOSITS AT YEAR END			
- Less than 3 months	.908	4.557	(80.07)
Total	.908	4.557	(80.07)
NUMBER OF EMPLOYEES (AT YEAR END)			
Management			
- Executive	1	1	-
- Non-Executive	59	52	13.46
Total	60	53	13.21
Permanent Non-Management Staff			
- Other	156	138	13.04
Total	156	138	13.04
Temporary Staff			
- Other	12	15	(20.00)
Total	12	15	(20.00)
Total	228	206	10.68
FURTHER ANALYSIS OF PERMANENT NON-MANAGEMENT			
- No. of Unionised Staff	156	138	13.04

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MANAGEMENT INFORMATION

	1988	1987	%Change
	(Rs. million) Year Ended 30 June		
Total	156	138	13.04
WAGES BILL			
Management			
- Executive	.103	.097	6.19
- Non-Executive	4.302	3.792	13.45
Total	4.405	3.889	13.27
Permanent Non-Management Staff			
- Other	5.538	3.668	50.98
Total	5.538	3.668	50.98
Temporary Staff			
- Other	.204	.131	55.73
Total	.204	.131	55.73
Total	10.147	7.688	31.98
FURTHER ANALYSIS OF PERMANENT NON-MANAGEMENT			
- Unionised Staff Wage Bill	5.538	3.668	50.98
Total	5.538	3.668	50.98

SPECIFIC INFORMATION - BANKS & DFI.
FEDRAL BANK FOR COOPERATIVES

1.TERM ADVANCES APPROVED DURING THE YEAR

	PRIVATE SECTOR 1988	PRIVATE SECTOR 1987	PUBLIC SECTOR 1988	PUBLIC SECTOR 1987	TOTAL 1988	TOTAL 1987
Manufacturing						
-Cement	-	-	-	-	-	-
-Sugar	-	-	-	-	-	-
-Fertilizer	-	-	-	-	-	-
-Energy	-	-	-	-	-	-
-Textile	-	-	-	-	-	-
-Engineering	-	-	-	-	-	-
-Others	-	-	-	-	-	-
Agriculture,Forestry Hunting and Fishing	134.580	75.000			134.580	75.000
Mining & Quarrying	-	-	-	-	-	-
Electricity, Gas & Water	-	-	-	-	-	-
Commerce	-	-	-	-	-	-
Services	-	-	-	-	-	-
Construction	-	-	-	-	-	-
Others						
TOTAL	134.580	75.000	-	-	134.580	75.000

RATIOS

	FBC Year Ended 30 June 1988	1987
Net Profit After Tax/Net Shareholder's Equity	4.76 %	.69 %
Total Income/Net Shareholder's Equity	13.55 %	9.12 %
Net Profit Before Tax/Net Shareholder's Equity	4.76 %	.69 %
Salaries and Benefits/Total Operating Expenses	29.29 %	27.70 %
Operating Profit/Total Income	35.24 %	19.09 %
Net Shareholder's Equity/Total Assets	12.06 %	15.12 %
Borrowing Ratio	712.39 %	543.87 %
Liqiid Assets/Total Deposit Liabilities	26.4185 : 1	4.2723 : 1

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BALANCE SHEET

	(Rs. million) Year Ended 30 June 1988	1987	%Change
ASSETS			
Cash and Bank Balances	235.012	233.701	.56
Money at Call and Short Notice	1,067.885	988.499	8.03
Investments - at Cost			
Shares of Companies	480.324	473.442	1.45
Debentures and Bonds	.009	.052	(82.69)
	480.333	473.494	1.44
Other Assets	476.016	473.494	.53
Fixed Assets	3.762	3.464	8.60
Net Assets in Bangladesh	99.080	99.080	-
Net Assets of Mutual Fund	205.457	182.293	12.70
Net Assets of State Enterprise Mutual Fund	316.383	310.888	1.76
	2,883.928	2,764.913	4.30
EQUITY AND LIABILITIES			
Equity			
Paid Up Share Capital	100.000	100.000	-
Accumulated Profit/(Loss)	109.683	93.313	17.54
Revenue Reserves	42.798	40.798	4.90
	252.481	234.111	7.84
Deposit and Other Accounts			
Other Deposits	202.294	193.252	4.67
	202.294	193.252	4.67
Borrowings			
Local	858.090	795.722	7.83
Participation Term Certificates / Musharika Arrangements	824.193	808.052	1.99
	1,682.283	1,603.774	4.89
Other Liabilities	746.870	733.776	1.78
	2,883.928	2,764.913	4.30

PKIC

PAKISTAN KUWAIT INVESTMENT COMPANY LIMITED

HISTORY AND OBJECTIVES

The Government of Pakistan and the Government of Kuwait signed a protocol in July 1976 for the establishment of a company to be known as Pakistan Kuwait Investment Company Limited with a view to carrying on investment activities in Pakistan in a profit - oriented manner. An agreement in respect of the joint venture was signed in Kuwait on March 8, 1978, which was followed by the signing of the Memorandum and Articles of Association of the proposed Company on December 23, 1978. The document was signed by the Secretary, Ministry of Finance, on behalf of the Government of Pakistan and the Deputy Managing Director, Kuwait Foreign Trading Contracting and Investment Company (KFTCIC), as a nominee of the Government of Kuwait. The company was incorporated in March 1979 as a private limited company.

The main purpose of the company is to promote and expand economic and investment collaboration between Pakistan and Kuwait. It provides financial assistance for industrial enterprises in the private as well as public sectors.

MANAGEMENT STRUCTURE

The management and superintendence of the Company vests in a Board of Directors consisting of six Directors including the Managing Director, who is the Chief Executive. Three Directors are nominated by each shareholder. The Chairman is the nominee of KFTCIC while the Managing Director is named by the Government of Pakistan. Each of the two parties has the right to appoint, re-appoint, replace or remove any of its representatives on the Board of Directors. Besides the Managing Directors, Controller of Capital Issues and Executive Director, the State Bank of Pakistan, represents the Pakistan side on the Board.

CAPITAL STRUCTURE

The company has an authorised capital of Rs.1,000 million. The paid-up capital is Rs. 378.100 million.

BALANCE SHEET

	(Rs. million) Year Ended 31 December 1987	1986	%Change
ASSETS			
Cash and Bank Balances	39.985	42.615	(6.17)
Advances/Profit Sharing Arrangements			
Loans for Project Financing	24.402	23.850	2.31
Participation Term Certificates	6.742	7.186	(6.17)
Other Loans and Advances	145.123	150.219	(3.39)
	176.267	181.255	(2.75)
Investments - at Cost			
Securities/Treasury Bills of Federal/Provincial Governments	5.000	5.000	-
Shares of Companies	212.059	213.862	(.84)
Debentures and Bonds	5.000	5.344	(6.43)
Other Investments	71.907	26.700	169.31
	293.966	250.906	17.16
Other Assets	27.053	22.783	18.74
Fixed Assets	29.895	29.194	2.40
	567.166	526.753	7.67
EQUITY AND LIABILITIES			
Equity			
Paid Up Share Capital	378.100	343.750	9.99
Accumulated Profit/(Loss)	.492	1.164	(57.73)
Revenue Reserves	149.447	173.854	(14.03)
	528.039	518.768	1.78
Other Liabilities	39.127	7.985	390.00
	567.166	526.753	7.67
Contingencies and Commitments	58.897	71.436	(17.5

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INCOME STATEMENT

	(Rs. million) Year Ended 31 December 1987	1986	%Change
Operating Income			
Interest on Loans, Discounts and Return on Non-Interest Bearing Accounts	52.747	50.673	4.09
Commission, Exchange, Fees and Brokerage	.389	4.148	(90.62)
Gain on Sale of Investments	3.459	5.000	(30.82)
Interest on Bank Deposits	7.761	5.688	36.44
	64.356	65.509	(1.76)
Operating Expenses			
Interest on Borrowings & Return on Non-Interest Bearing Accounts	.425	.991	(57.11)
Salaries, Allowances and Benefits	2.599	2.124	22.36
Other Expenses	14.680	8.075	81.79
Depreciation	.298	.226	31.85
	18.002	11.416	57.69
Other Income	.136	.068	100.00
Net Profit/(Loss) before Taxation	46.490	54.161	(14.16)
Net Profit/(Loss) after Taxation	46.490	54.161	(14.16)
Accumulated Profit/(Loss) B/F	1.164	1.094	6.39
Profit Available for Appropriation	47.654	55.255	(13.75)
Appropriation			
Dividends Paid and Proposed	37.810	-	-
Proposed Bonus Shares	-	34.375	(100.00)
Transfer To (From) General Reserve	-	5.000	(100.00)
Transfer to Other Reserves	9.352	14.716	(36.45)
	47.162	54.091	(12.80)
Accumulated Profit/(Loss)	.492	1.164	(57.7[illegible]

MANAGEMENT INFORMATION

LOANS, ADVANCES AND PROFIT SHARING ARRANGEMENTS	(Rs. million) Year Ended 31 December 1987	1986	%Change
Approvals (during the year)			
- Term Loans	10.705	30.831	(65.28)
- Equity Investments	19.188	1.932	889.58
Total	29.893	32.770	(8.78)
Disbursements (during the year)			
- Term Loans	1.257	58.280	(97.84)
- Equity Investments	6.283	3.940	59.47
Total	7.540	62.220	(87.88)
Portfolio (year end)			
- Term Loans	295.826	288.000	2.72
- Equity Investments	236.518	230.000	2.83
Total	532.344	518.000	2.77
Regional Breakdown of total advances approved during year			
- Punjab	15.836	20.145	(21.39)
- Sind	6.283	10.939	(42.56)
- Baluchistan	.133	1.686	(92.11)
Total	22.252	32.770	(32.10)
Regional Breakdown of total advances disbursed during year			
- Punjab	2.931	57.595	(94.91)
- Sind	6.283	2.939	113.78
- Baluchistan	.133	1.686	(92.11)
Total	9.347	62.220	(84.98)
NUMBER OF EMPLOYEES (AT YEAR END)			
Management			
- Executive	4	4	-
- Non-Executive	11	10	10.00
Total	15	14	7.14
Permanent Non-Management Staff			
- Other	24	20	20.00
Total	24	20	20.00
Total	39	34	14.71
FURTHER ANALYSIS OF PERMANENT NON-MANAGEMENT			
- No. of Non-Unionised Staff	24	20	20.00
Total	24	20	20.00

1. TERM ADVANCES APPROVED DURING THE YEAR

	PRIVATE SECTOR 1988	PRIVATE SECTOR 1987	PUBLIC SECTOR 1988	PUBLIC SECTOR 1987	TOTAL 1988	TOTAL 1987
Manufacturing						
-Cement	0.851	0.133			0.851	0.133
-Energy	-	4.283			-	4.283
-Textile	16.743	12.905			16.743	12.905
-Others	12.402	2.931			12.402	2.931
Construction	0.835	-			0.835	-
Services		2.000			-	2.000
TOTAL	30.831	22.252			30.831	22.252

RATIOS

	Year Ended 31 December 1987	1986
Net Profit After Tax/Net Shareholder's Equity	8.80 %	10.44 %
Total Income/Net Shareholder's Equity	12.21 %	12.64 %
Net Profit Before Tax/Net Shareholder's Equity	8.80 %	10.44 %
Salaries and Benefits/Total Operating Expenses	14.43 %	18.60 %
Dividend Rate	10.00 %	-
Operating Profit/Total Income	71.87 %	82.48 %
Net Shareholder's Equity/Total Assets	93.10 %	98.48 %

PLHC

PAK-LIBYA HOLDING COMPANY LIMITED

HISTORY AND OBJECTIVES

The establishment of Pak-Libya Holding Company Limited (PLHC) as a Joint Stock Company on October 14, 1978 with its registered office at Karachi was the outcome of a mutual agreement signed on February 8, 1976 between the Governments of Pakistan and Libya. The Company commenced business operations in October 1980.

To achieve its prime objective of facilitating industrial investment in Pakistan, PLHC provides a comprehensive package of various modes of financing. Its operational sphere includes provision of local and foreign financing, equity participation, underwrting of public issues and bridge finance facilities, short-term investment, co-sponsoring of joint ventures, and also participation in financial packages in consortium with other financial institutions and financing projects by way of Islamic modes of financing particularly on the basis of Participation Term Certificates (PTCs) both for local and foreign currency financing. To further broaden PLHC's sphere of investment activities other Islamic modes of financing are also being explored such as lease financing, modaraba, musharika, mark-up, etc. In order to encourage greater utilization of indigenous machinery the company also extends financing facilities to prospective entrepreneures for locally fabricated machinery under State Bank of Pakistan's Refinancing Scheme.

MANAGEMENT STRUCTURE

The executive authority for the conduct of the Company's business vests in its Board of Directors on which three Directors each have been nominated by the two Governments including its Chairman, the Managing Director and Deputy Managing Director.

CAPTIAL STRUCTURE

The paid-up share capital of PLHC in 1987 was Rs.1000 million.

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BALANCE SHEET

ASSETS	(Rs. million) Year Ended 31 December 1987	1986	%Change
Cash and Bank Balances	10.436	14.539	(28.22)
Money at Call and Short Notice	27.307	87.307	(68.72)
Advances/Profit Sharing Arrangements			
Loans for Project Financing	483.424	589.980	(18.06)
Participation Term Certificates	507.410	222.987	127.55
Other Loans and Advances	.334	.633	(47.23)
	991.168	813.600	21.82
Investments - at Cost			
Securities/Treasury Bills of Federal/Provincial Governments	80.000	32.500	146.15
Shares of Companies	180.152	147.407	22.21
Debentures and Bonds	110.792	135.222	(18.06)
Other Investments	31.011	42.462	(26.96)
	401.955	357.591	12.40
Other Assets	171.858	146.804	17.06
Fixed Assets	29.430	28.035	4.97
	1,632.154	1,447.876	12.72
EQUITY AND LIABILITIES			
Equity			
Paid Up Share Capital	1,000.000	1,000.000	-
Accumulated Profit/(Loss)	1.059	4.181	(74.67)
Capital Reserves	144.000	102.000	41.17
Revenue Reserves	210.165	183.011	14.83
	1,355.224	1,289.192	5.12
Borrowings			
Local	159.181	47.422	235.66
	159.181	47.422	235.66
Other Liabilities	117.749	111.262	5.83
	1,632.154	1,447.876	12.72

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INCOME STATEMENT

	(Rs. million) Year Ended 31 December 1987	1986	%Change
Operating Income			
Interest on Loans, Discounts and Return on Non-Interest Bearing Accounts	140.694	113.544	23.91
Commission, Exchange, Fees and Brokerage	2.300	2.273	1.18
Gain on Sale of Investments	4.555	4.418	3.10
Interest on Bank Deposits	6.503	25.737	(74.73)
Interest on Government Securities	20.964	9.081	130.85
Service and Commitment Charges	9.226	10.471	(11.88)
Others	7.391	11.921	(38.00)
	191.633	177.445	7.99
Operating Expenses			
Interest on Borrowings & Return on Non-Interest Bearing Accounts	2.908	1.866	55.84
Salaries, Allowances and Benefits	4.546	3.921	15.93
Other Expenses	2.729	2.996	(8.91)
Depreciation	.417	.396	5.30
	10.600	9.179	15.48
Operating Profit/(Loss)	181.033	168.266	7.58
Net Profit/(Loss) before Taxation	181.033	168.266	7.58
Net Profit/(Loss) after Taxation	181.033	168.266	7.58
Accumulated Profit/(Loss) B/F	4.181	13.155	(68.21)
Profit Available for Appropriation	185.214	181.421	2.09
Appropriation			
Dividends Paid and Proposed	115.000	110.000	4.54
Transfer To(From) General Reserve	27.155	25.240	7.58
Transfer to Other Reserves	42.000	42.000	-
	184.155	177.240	3.90
Accumulated Profit/(Loss)	1.059	4.181	(74.67)

MANAGEMENT INFORMATION

	(Rs. million) Year Ended 31 December 1987	1986	%Change
LOANS, ADVANCES AND PROFIT SHARING ARRANGEMENTS			
Approvals (during the year)			
- Term Loans	148.339	341.256	(56.53)
- Other Loans & Debentures	52.750	112.000	(52.90)
- Equity Investments	44.500	39.300	13.23
Total	245.589	492.556	(50.14)
Disbursements (during the year)			
- Term Loans	210.471	179.700	17.12
- Other Loans	60.050	29.440	103.97
- Equity Investments	33.800	12.100	179.34
Total	304.321	221.240	37.55
Portfolio (year end)			
- Term Loans	480.911	587.469	(18.14)
- Other Loans	507.410	222.987	127.55
- Equity Investments	180.152	147.407	22.21
Total	1,168.473	957.863	21.99
Regional Breakdown of total advances approved during year			
- Punjab	95.914	186.905	(48.68)
- Sind	148.675	234.676	(36.65)
- N.W.F.P.	1.000	70.975	(98.59)
Total	245.589	492.556	(50.14)
Regional Breakdown of total advances disbursed during year			
- Punjab	152.582	165.015	(7.53)
- Sind	137.366	24.175	468.22
- N.W.F.P.	4.373	1.950	124.26
- Baluchistan	10.000	30.100	(66.78)
Total	304.321	221.240	37.55
NUMBER OF EMPLOYEES (AT YEAR END)			
Management			
- Executive	4	4	-
- Non-Executive	3	2	50.00
Total	7	6	16.67
Permanent Non-Management Staff			
- Other	46	43	6.98
Total	46	43	6.98
Temporary Staff			
- Other	1	6	(83.33)
Total	1	6	(83.33)
Total	54	55	(1.82)
FURTHER ANALYSIS OF PERMANENT NON-MANAGEMENT			
- No. of Non-Unionised Staff	46	43	6.98
Total	46	43	6.98
WAGES BILL			
Management			
- Executive	.616	.529	16.45
- Non-Executive	.339	.391	(13.30)
Total	.955	.920	3.80

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MANAGEMENT INFORMATION

	(Rs. million) Year Ended 31 December 1987	1986	%Change
Permanent Non-Management Staff			
- Other	2.001	1.516	31.99
Total	2.001	1.516	31.99
Temporary Staff			
- Other	.008	.067	(88.06)
Total	.008	.067	(88.06)
Total	2.964	2.503	18.42
FURTHER ANALYSIS OF PERMANENT NON-MANAGEMENT			
- Non-Unionised Staff Wage Bill	2.001	1.516	31.99
Total	2.001	1.516	31.99

L.TERM ADVANCES APPROVED DURING THE YEAR

	PRIVATE SECTOR 1987	1988	PUBLIC SECTOR 1987	1988	TOTAL 1987	1988
Manufacturing						
-Cement	-	-	-	-	-	-
-Sugar	-	124.275	-	-	-	124.275
-Fertilizer	-	-	-	-	-	-
-Energy	-	-	-	-	-	-
-Textile	17.000	106.896	-	-	17.000	106.896
-Engineering.	-	15.000	-	-	-	15.000
-Others	80.939	241.385	-	-	80.939	241.385
Agriculture, Forestry Hunting and Fishing	-	-	-	-	-	-
Mining & Quarrying	-	-	-	-	-	-
Construction	-	-	-	-	-	-
Others	147.650	5.000	-	-	147.650	5.000
TOTAL	245.589	492.556	NIL	NIL	245.589	492.556

RATIOS

	Year Ended 31 December 1987	1986
Net Profit After Tax/Net Shareholder's Equity	13.35 %	13.05 %
Total Income/Net Shareholder's Equity	14.14 %	13.76 %
Net Profit Before Tax/Net Shareholder's Equity	13.35 %	13.05 %
Salaries and Benefits/Total Operating Expenses	42.88 %	42.71 %
Dividend Rate	11.50 %	11.00 %
Operating Profit/Total Income	94.46 %	94.82 %
Net Shareholder's Equity/Total Assets	83.03 %	89.04 %
Borrowing Ratio	11.74 %	3.67 %

SAPICO

SAUDI-PAK INDUSTRIAL AND AGRICULTURAL INVESTMENT COMPANY

HISTORY AND OBJECTIVES

Saudi-Pak Industrial and Agricultural Investment Company (SAPICO) has been established to meet the financing requirements of industrial and agricultural sectors, promote and accelerate industrial development and establish agro-based industries. It is a joint venture between the Kingdom of Saudi Arabia and the Government of Pakistan, and was incorporated as a private limited company under the Company Law on December 23, 1981.

The objectives of the company are investment in the industrial and agro-based industrial fields in the Islamic Republic of Pakistan on commercial basis through the carrying out of industrial and agro-based industrial projects and marketing of their products in Pakistan and abroad.

MANAGEMENT STRUCTURE

The overall control and supervision of SAPICO vests in its Board of Directors comprising three Pakistanis and three Saudi Directors. The Pakistani Directors are nominated by the Federal Government of Pakistan. The Federal Finance Ministry is responsible for the affairs of the company. The Chief Executive officer is also appointed by the Federal Government.

CAPTIAL STRUCTURE

The share capital of the company as authorised by the Government is Rs.1,000 million, of which Rs.800 million has been paid against the first and second calls by the respective governments.

BALANCE SHEET

	(Rs. million) Year Ended 31 December 1987	1986	%Change
ASSETS			
Cash and Bank Balances	31.681	24.084	31.54
Money at Call and Short Notice	519.431	534.935	(2.89)
Advances/Profit Sharing Arrangements			
Loans for Project Financing	312.915	222.994	40.32
	312.915	222.994	40.32
Investments - at Cost			
Securities/Treasury Bills of Federal/Provincial Governments	159.364	163.011	(2.23)
Shares of Companies	81.800	69.700	17.36
Other Investments	84.000	86.500	(2.89)
	325.164	319.211	1.86
Other Assets	54.321	41.732	30.16
Fixed Assets	16.916	6.103	177.17
	1,260.428	1,149.059	9.69
EQUITY AND LIABILITIES			
Equity			
Paid Up Share Capital	800.000	800.000	-
Accumulated Profit/(Loss)	.289	.946	(69.45)
Revenue Reserves	449.625	343.625	30.84
	1,249.914	1,144.571	9.20
Other Liabilities	10.514	4.488	134.26
	1,260.428	1,149.059	9.69
Contingencies and Commitments	397.842	382.747	3.94

INCOME STATEMENT

	(Rs. million) Year Ended 31 December 1987	1986	%Change
Operating Income			
Interest on Loans, Discounts and Return on Non-Interest Bearing Accounts	49.024	26.050	88.19
Interest on Bank Deposits	41.388	41.648	(.62)
Interest on Government Securities	16.250	13.298	22.19
Service and Commitment Charges	4.560	1.567	191.00
Others	7.806	36.706	(78.73)
	119.028	119.269	(.20)
Operating Expenses			
Salaries, Allowances and Benefits	3.739	2.735	36.70
Other Expenses	9.148	9.041	1.18
Depreciation	.798	.492	62.19
	13.685	12.268	11.55
Operating Profit/(Loss)	105.343	107.001	(1.54)
Net Profit/(Loss) before Taxation	105.343	107.001	(1.54)
Net Profit/(Loss) after Taxation	105.343	107.001	(1.54)
Accumulated Profit/(Loss) B/F	.946	3.945	(76.02)
Profit Available for Appropriation	106.289	110.946	(4.19)
Appropriation			
Transfer To(From) General Reserve	-	74.000	(100.00)
Transfer to Other Reserves	106.000	36.000	194.44
	106.000	110.000	(3.63)
Accumulated Profit/(Loss)	.289	.946	(69.45)

MANAGEMENT INFORMATION

	(Rs. million) Year Ended 31 December 1987	1986	%Change
LOANS, ADVANCES AND PROFIT SHARING ARRANGEMENTS			
Approvals (during the year)			
- Term Loans	194.087	121.366	59.92
- Equity Investments	66.213	53.000	24.93
Total	260.300	174.366	49.28
Disbursements (during the year)			
- Term Loans	101.989	152.135	(32.96)
- Equity Investments	17.932	22.587	(20.61)
Total	119.921	174.722	(31.36)
Portfolio (year end)			
- Term Loans	312.914	222.994	40.32
- Equity Investments	101.340	78.408	29.25
Total	414.254	301.402	37.44
Regional Breakdown of total advances approved during year			
- Punjab	233.656	126.438	84.80
- Sind	12.505	35.796	(65.07)
- N.W.F.P.	12.954	4.500	187.87
- Baluchistan	1.185	7.632	(84.47)
Total	260.300	174.366	49.28
Regional Breakdown of total advances disbursed during year			
- Punjab	90.221	150.090	(39.89)
- Sind	20.796	23.000	(9.58)
- Baluchistan	8.904	.982	806.72
- Azad Kashmir and Northern Areas	-	.650	(100.00)
Total	119.921	174.722	(31.36)
NUMBER OF EMPLOYEES (AT YEAR END)			
Management			
- Executive	5	4	25.00
- Non-Executive	10	10	-
Total	15	14	7.14
Permanent Non-Management Staff			
- Production	19	14	35.71
Total	19	14	35.71
Total	34	28	21.43
FURTHER ANALYSIS OF PERMANENT NON-MANAGEMENT			
- No. of Non-Unionised Staff	19	14	35.71
Total	19	14	35.71
WAGES BILL			
Management			
- Executive	432.671	448.036	(3.43)
- Non-Executive	1,004.264	650.921	54.28
Total	1,436.985	1,098.959	30.76
Permanent Non-Management Staff			
- Production	485.334	474.822	2.21
Total	485.334	474.822	2.21
Total	1,922.269	1,573.781	22.14
FURTHER ANALYSIS OF PERMANENT NON-MANAGEMENT			
- Non-Unionised Staff Wage Bill	485.334	474.822	2.21
Total	485.334	474.822	2.21

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MANAGEMENT INFORMATION

1. TERM ADVANCES APPROVED DURING THE YEAR

	PRIVATE SECTOR		PUBLIC SECTOR		TOTAL	
	1988	1987	1988	1987	1988	1987
Manufacturing						
-Cement	-	-	NIL	NIL	-	-
-Sugar	-	-			-	-
-Fertilizer	-	-			-	-
-Energy	-	-			-	-
-Textile	1.300	-			1.300	-
-Engineering	182.387	152.276			182.387	152.276
-Others	5.000	22.090			5.000	22.090
Agriculture, Forestry Hunting and Fishing	-	-			-	-
Mining & Quarrying	-	-			-	-
Construction	-	-			-	-
Services	7.000	-			7.000	-
Others	64.613	-			64.613	-
TOTAL	260.300	174.366	NIL	NIL	260.300	174.366

RATIOS

	Year Ended 31 December 1987	1986
t Profit After Tax/Net Shareholder's Equity	8.42 %	9.34 %
tal Income/Net Shareholder's Equity	9.52 %	10.42 %
t Profit Before Tax/Net Shareholder's Equity	8.42 %	9.34 %
laries and Benefits/Total Operating Expenses	27.32 %	22.29 %
erating Profit/Total Income	88.50 %	89.71 %
t Shareholder's Equity/Total Assets	99.16 %	99.60 %

CHAPTER 10

EMERGING ISSUES AND RECOMMENDATIONS.

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10.01 Over time, there has been a considerable overlap between functions of separate DFIs as their mandates were expanded to permit similar activities. Their various functions and the overlap has been summarized in Table 1. Many reasons have been cited for the overlap of functions, some of which are:

i. There is a scarcity of credit in Pakistan for financing industrial ventures. There will always be a large number of prospective clients chasing the few sources. Therefore financing industrial ventures will always be an attractive prospect.

ii. DFIs in Pakistan have taken little initiative in building infrastructure in the financial sector. Had they engaged in activities never done before their profitabilty was likely to have been adversely affected. Project financing is something tested and tried and allows them to remain inside their 'comfort zone'.

iii. Client demands have been responsible, to a large extent, for the institution offering a particular set of similar products/services. For instance if an existing large PICIC client wanted working capital financing for a new project, PICIC did not want to lose them to another institution. Nor did the clients want to go to another institution, having developed a track record and credit history with PICIC. So mandates and charters were adjusted to accomodate such client requests.

10.02 Most DFIs are not only performing similar functions but have also been sanctioning project financing loans largely concentrated in a particular area. The location of the head offices of virtually all of DFIs in Karachi has been cited as one of the main reasons for this state of affairs. Many of them have regional offices, but no sanctioning authority at that level. The IDBP was the only institution which reviewed loans and sanctioned them at the regional level.

10.03 The loan sanction-disbursement process cycle is full of unnecessary delays. In general the sanction process at any DFI usually involves the following steps;

Project Review
Legal documentation
Market survey/Feasability
Board approvals
Disbursement
Project Supervision

10.04 Over time DFIs have become a prey to bureaucratic delays. According to an estimate it takes almost two years for a project application to be processed and for the funds to be disbursed. During this period the applicant may be required, in extreme cases, to undertake 80-120 visits to the DFI headquarters. The legal documentation is usually lengthv and delays between loan approval and disbursements are long. The slow release of funds sometimes leads to abandonment of implementation schedule and project suspension till such time that funds become available. Delays sometimes necessitate re-appraisal and re-scheduling. As a result projects either go ahead with reduced scope on available finances or, anticipating delays, the sponsors look for alternative financing. Moreover, there is hardly any monitoring or supervision by DFI staff beyond disbursement.

10.05 The appraisal process gives too little importance to the choice of technology or the impact of the choice of technology. While evaluating financial viability and macro economic development effects it is also important to consider the appropriateness of technology to

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FUNCTIONAL MARTIX

INSTITUTION

FUNCTIONS

	Commercial Banking	Development Banking	Investment Banking	Co-operative Banking	Issuing Agent	Under-writing	Guarantee/ Counter Guarantee	Foreign Exchange Financing	Management Advice	Borrowing From SBP	Investemnt In Stock Exchange	Equity Support	Med-Long Term Financing	Bridge Financing	Leasing
Nationalized Commercial Banks	*				*	*	*	*		*			*		
Foriegn Commercial Banks	*				*	*	*	*		*			*		
A.D.B.P		*							*				*		
Federal Bank For Co-operatives		*		*											
I.D.B.P.		*				*		*				*	*	*	
B.E.L.		*	*			*	*	*				*	*	*	
E.P.F.		*										*	*		
I.C.P.		*	*			*					*				
N.D.F.C.		*	*			*	*	*				*	*		
N.D.L.C.		*													*
N.I.T.			*								*				
PICIC		*	*			*	*	*			*	*	*		
Pak Kuwait		*				*	*	*	*			*			
Pak Libya		*						*				*			
Saudi Pak		*						*	*			*			
S.B.F.C.		*													
R.D.F.C.		*													
H.B.F.C.		*													

the country's capabilities and problems.

10.06 There is a trend in DFIs to sanction bigger projects, thus eliminating those that are small but may seem complicated due to design. These are usually innovative from a social or technological viewpoint and may be new or very labor intensive. Such projects may deviate slightly from the institution's quantitative guidelines.

10.07 There are some dedicated lines available to DFIs to finance the purchase of locally manufactured machinery. However since the collateral quality is a major consideration and institutions are risk averse they like to finance foreign manufactured machinery. Machinery manufactured by reputable suppliers is bound to have a better re sale and subsequent salvage value. Thus by playing it safe DFIs are not contributing to the country's indigenous technological capability.

10.08 Management of DFIs is done through executive boards which consist of federal and provincial nominees. There is a very high turnover at the board level which is responsible for lack of continuity of policy. The management of these institutions, like most others in Pakistan is 'personality dependant'. The profitable operations of NDFC and BEL has repeatedly been attributed to the genius of its ex-chairmen's management style, and the length of stay in office Top management has a lot of power as regards who gets the loan. The strength of one person has often swayed the entire board in one direction or another. The decisions of the chief executive are rarely challenged by senior managers. If they wish to indulge in speculative ventures, it will be obvious only after the event. Senior management at DFIs has been known to rush towards undertakings that may not have been viable but were undertaken due to personal motives.

10.09 Initially all DFI sanctions used to go through a central agency which provided an objective assessment . The projects under consideration were evaluated on economic and technical grounds before the actual disbursement. In order to liberalize the process and remove unnecessary delays this agency was done away with. There were two outcomes of this action. Some decision makers became extremely conservative while others were swept up with all the power.

10.10 In the absence of clear cut objectives the cautious managers became overly conservative. They are still hesitant to make any decision, even if they know it to be right, for fear of retributon. Moreover politicaly inspired decisions have also become fairly common. The aggressive managers took bold measures some of which proved to be very successful. NDFC is a case in point. It was set up to provide financing exclusively to SOE so that there was no need to compete for resources of other institulons and NCBs. This changed in the late 1970s when new departments were subsequently added with innovative objectives in view and private sector ventures of all sizes and descriptions were undertaken. Many competent people were atttracted to this public sector DFI with a private sector profile. Its profitability performance has been well above other DFIs. However skepticism on whether such performance is sustainable abounds. The institution showed some slack when there was a change in management and lately shadows of doubt have been repeatedly cast over the performance of the innovative departments. To qoute an official of the Finance Ministry, the deparments "have smart names and are filled with smart people in smart clothes who can converse in good english but are not able to produce a worthwhile analyis of industrial policy, when asked."

10.11 Management at DFIs is expected to perform like entrepreneurs yet they are not looked upon with favor incase of mistakes. Everyone welcomes a success story but are reluctant to appreciate that in order to achieve the desired objectives even the most successful entrepreneurs'win some and lose some'. If management is provided with targets to be met there must be guidelines for the minimum acceptance of non performing undertakings. If not, narrowly defined financial viability will always remain the foremost consideration which may not necessarily be the most desirable.

10.12 There is a general lack of appropriate expertise in DFIs due to more desirable terms being offered by private banks and private enterprise. Exodus of bright qualified people to better prospects overseas is also taking place. This extreme shortage is further accentuated by the 'thinning out effect' due to expansion in the operations and rapid promotions.

10.13 There is no specialized cadre for commercial or development bankers. Similarly there are no special skill requirements for new employees. There is a lack of structured training programs for entrant. This results in fresh inductees going straight to the decision making position and then undergoing 'on-the-job-training'.

10.14 Hiring and firing decisions are also motivated by political considerations. As was mentioned by an official in the concerned ministry, 28 people from a particular region were hired as clerical staff during the previous elected government. These people were promoted to the official cadre due to pressure by the present government. There appears to be no justification for this, as these staff members were only matriculates whereas there were many graduates and experienced people who were superceded. In Pakistan today the problem of positive discriminatin in favor of various ethnic, geographical groups and women is a glaring reality. But such measures are diffi. An official of the Ministry labelled this as 'the cost of democracy.'

10.15 There are no special incentives or performance based rewards for DFI personnel. There are no performance criteria nor any well defined objectives. In general promotions within the organization are a factor of the time spent in a position and not any achievements such as quick decision making or good credit. All this results in staff following a path of least resistance so as to be safe and secure in their jobs.

10.16 Financial planning has been taken out of the hands of the borrower, with all of the assets of the business backing one loan and subsequent lenders having second and third charge on the same asset (subject to prior lender approval). These institutions used collateral guidelines as if it were a term loan instead of project financing.

10.17 In the absence of any credit information network there is not enough scrutiny at the appraisal level. It is difficult for institutions to evaluate the credibility of the individuals, their track record and repayment histories with other institutions. Further it is difficult to get an idea of the individual's total indebtedness or that of his group.

10.18 Borrowers also suffer from a reputation of being unprofessional. DFI personnel cite frequent examples of lack of proper paper work and delay in provision of audited financial statements as part of the application package. Further, any objections raised by DFI staff are looked upon as delays and means of extracting financial favors by sponsors.

Regulatory agencies have not played a very positive role in streamlining the working of the DFIs either. The NIT and ICP have repeatedly been denied membership of the stock exchanges, on grounds that they are direct competitors. The government and the relevant ministry have been discouraged from interference in this regard by international agencies. On the other hand if the government continues using the current pricing formula for public offerings and continues to stipulate what is to be offered to them they will never be viewed as playing a positive role in market making.

10.20 Since their inception subsidized credit lines have been made available on easy terms to

DFIs. This 'spoon feeding' has led to lack of creation of innovative means of resource mobilization. These instituion have relied on credit ceilings and have always sought expansion of ceilings. It is only recently that this request has been denied and they have been asked to mobilize their own resources. As can be seen in Annexure 6 there are advertisements of PICIC and IDBP in the various national dailies introducing new schemes. At this stage one cannot help but wish them luck as their track record has not been very good and it is ironical to see these advertisements appearing almost at the same time as repayment notices.(please refer to annexure 7).

10.21 The loan loss experiences and low recovery ratios have become an essential characteristic of DFI performance. These can be attributed to a number of factors;

1. Foreign currency denominated loans have been classified due to non payment because of the fast depreciating value of the rupee. In the absence of appropriate hedging mechanisms even the interest payments on loans sanctioned in the early 1960s are in default.

2. A number of industrial undertakings have been declared 'sick units'. This adverse classification is sometimes desired by the entrepreneurs. These people often make a considerable amount of money while setting up the venture and later wish to gain by getting preferential treatment. DFI management has no built in mechanism that would check this practice.

3. The actual intentions of the businessman are not evident to the DFI in the absence of post disbursement review or on going appraisal. In cases where the entrepreneur had a portfolio of businesses DFIs have been known never to question why one or two units should be declared sick when others are doing well.

4. Similarly when the industry is a clear winner due to its inherent supply-demand situation or other favorable factors there is little justification for poor performance. For instance cotton ginning, yarn and cement units have the advantage of competing in a seller's market, so there is no apparent reason for the declared unprofitable operations.

5. In Pakistan the legal framework for debt recovery is very weak and full of unnecessary delays which may take up to five or ten years. As a result the institutions have become very cautious with respect to collateral.

6. Many borrowers resort to wilfull default in the absence of any sound recovery mechanism. There is always some tension between the borrower who wants litigation so as to delay the recovery and the lender who invariably opts for a out-of-court settlement.

7. At the end of the day the only asset worth having as collataeral is land even though it forms a very small part of the assets of any heavy industry. It seems somewhat absurd for the rate of growth of industry to be constrained by its ability to provide land as collateral.

RECOMMENDATIONS FOR IMPROVING DFI PERFORMANCE

10.22 DFI performance has to be seen alongwith the infrastructural and other inherent weaknesses of the financial sector. DFIs may be performing similar functions but there is hardly any competition among them. Applicants have also felt free to approach more than one institution. The government must encourage competition within the DFIs. For this it may chose certain target performance measures such as rate of return on assets or rate of recovery. In fair competition it is necessary to reward performance just as it is necessary tc penalize poor re:.ults. However there must also be a miniimum acceptable level of adve:se performance.

10.23 All DFIs must be encouraged to mobilize their own resources and not depend on sul.sidized credit facilities of the SBP or internaticnal agencies. If their mandate does not allow resource mobilization, it should be amended accordingly. At this stage some DFIs may not be in a position to do so, owing to the adverse quality of their loan portfolios.

10.24 Concentration of DFI headquarters in one region has resulted in large projects becoming the prerogative of Karachi businessmen. To have an equitable disbursement of funds DFI headquarters must be moved up country. Initially the headquarters of two institutions should be moved to Lahore and one each to Islamabad, Peshawar and Quetta. This should be coupled with opening of regional offices (as recently announced by ADBP). This step might also lead to a natural division of sectoral lending, for instance DFIs based in Punjab may end up financing more agro based industry and/or cotton textiles. Similarly there might be a natural division on the basis of rural or urban concentration of the projects under consideration. Looking ahead, if the government wants to move towards (say) rural industrialization , DFIs can play an important role in developing infrastructural facilties for industries in selected rural areas.

10.25 Competition for DFIs is also emerging in the form of private sector Investment Finance Banks. These institutions will undertake project finance activities as well and claim to have turn around time of 10 to 15 days. In order to compete DFIs will be forced to atleast work within the stated 60 day approval cycle and push towards early disbursements.

10.26 It is recommended that DFIs should create a technical intelligence unit and hire inhouse technical consultants. In this age of rapidly changing technology, such a unit should have the ability to evaluate technological choices, its interaction with other technologies, its relationship with social and economic systems and its impact on the economic viability of the project.

10.27 DFIs must also consider the technological development objectives of the country while evaluating projects. Import substitution, deletion policies and utilization of indigenous capabiities could be a consideration while considering loans. Related certain quantitative measures and targets could be made prerequisites for disbursal. For instance, they could include graduated deletion of foreign technology import by (say) 5-10% per year.

10.28 DFI performance has been excessively top management dependant. As is the practice in many other areas of Pakistan society, individual personalities have dominated certain institutions. One way of avoiding this would be by giving more power to the Executive Boards who should have an equal number of internal and external members, thus increasing the chances of dissent. Decentralizing to regional or provincial levels will also decrease the dependence on Head Office and the decision making on one person. Regulatory agencies could keep a check on performance by monitoring the trend in the number of sanctions over time and doing the needful in case there is an extreme movement.

10.29 Terms and conditions of work and salary structure at DFIs need to be reviewed. Ideally these should be brought in line with private sector terms. Performance criteria and objectives should be decided in consultation with the employees and performance reviews should be carried out regularly. Moreover performance based rewards and promotion must be introduced, as is the case in private banks.

10.30 New employees should go through intensive training modules along with on-the-job training. This should be similar to the training programs being offered by private sector financial institutions. DFIs could also institute the Account Officer system. (see detail in commercial banking section).

10.31 DFIs must also have ready or on-line access to the credit information network for NCBs. This will enable them to have up to date information regarding group accounts and total liabilities outstanding of corporate individuals and groups, and delinquencies ,if any.

10.32 Disbursing institutions must ensure that the recipients of funds are the initial sponsors of the projects. In many cases sanctions have been sold to other non deserving parties or original sponsors are no longer associated with the project when it finally takes off.

10.33 Certain preconditions must be imposed on borrowers, such as the provision of audited financial statements in a timely fashion. The integrity and sophistication of reporting standards depends on the sophistication of its users. In developed systems it is analysts and institutional stake holders who ensure high quality reporting. Laws regarding timely preparation of accounts are in place in Pakistan, as in other countries, but the implementation is too slow or is non existent.

10.34 In order to play their due role in capital market development in Pakistan, DFIs could make it a precondition for borrowers to have a public offering. DFIs could provide an all-in-one package to clients. This would also result in better reporting practices.

10.35 Internationally employed loan clssification criteria must be adopted by DFIs. The importance of post disbursal evaluation and project monitoring must be recognized in this regard. Having an account officer sytem in place will aid this process greatly.

10.36 Over the long term it is recommended that the DFIs be restructured finanacially and administratively. Some measures regarding administrative restructuring have been mentioned earlier. Measures for financial restructuring should include a thorough portfolio audit in each institution as a first step.

10.37 Secondly the formation of a central management service company or smaller companies is recommended. These should be along the lines of "work-out groups" in some Western countries. The company consists of an independent group of professionals including accountants, financial managers. lawyers, tax advisors which may be hired by the institution(s). This group usually takes over the management of problem companies which would be similar to our 'sick units'. It carries out a management audit and puts measures in place that may aid in turning it around. In case of a situation beyond redemption, it aids in the filing of bankruptcy proceedings and the final disposal of assets of all creditors. DFIs could have inhouse work out groups if outside consultants are not available.

10.38 Institutional retructuring along the lines of commercial banks could also be undertaken. Here each instituion would be divided to form two separate ones. One would retain all the 'good loans' and the other all the classified or sub standard ones. The purpose of the latter would be restricted to that of a collection agency - collecting interest payments and pursuing loan recovery with the aid of the legal sytem. A combined collection agency for all the DFIs could also be set up.

ANNEXURE 1

REGISTERED No. S-1033 / L-7646

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PART II

Statutory Notifications (S. R. O.)

GOVERNMENT OF PAKISTAN

FINANCE DIVISION

(Investment and Capital Issues Wing)

NOTIFICATION

Islamabad, the 13th July, 1987

S.R.O. 585 (I)/87.—In exercise of the powers conferred by sub-section (4) and (4A) of ~~section 3 of the~~ Capital Issues (Continuance of Control) Act, 1947 (XXIX of 1947), the Federal Government is pleased to stipulate that all consents and recognitions in respect of investment finance companies, for issue of capital, for making a public offer or taking any other action under sub-section (2) or sub-section (3) of the said section shall be subject to the following conditions :—

(1) *Definitions.*—In this notification, unless there is any thing repugnant in the subject or context,—

(a) " Act " means the Capital Issues (Continuance of Control) Act, 1947 (Act XXIX of 1947) ;

(b) " associated companies " or " associated issuer " or " associated client " includes companies and associated undertakings as defined in sub-section (2) of section 2 of the Ordinance ;

(c) " bankers acceptance " means a draft drawn on a commercial bank or investment finance company by an individual or firm ordering the drawee bank or investment finance company to pay to the order of third person a specified sum of money, either on demand or at some future specified date, and accepted by the drawee ;

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(d) " Controller " means the Controller of Capital Issues appointed under the Act ;

(e) " close relative " includes spouse and minor children :

(f) " company " means a company incorporated under a law for the time being in force ;

(g) " investment finance company " means a company registered and granted licence under this notification to undertake and carry on the business of an investment finance company ;

(h) " liquid net worth " means an investment finance company's book value (or net worth) reduced by its fixed assets and direct investment of more than 20 per cent in the paid up capital of a client enterprise or a lease or leases in respect of its assets aggregating more than 20 per cent of the total assets of the enterprise :

(i) " margin loan " means a loan made by an investment finance company to a client to partly finance investments by the client in marketable securities which shall be held by investment finance company as collateral, the amount invested by the client being the " margin " against the loan ;

(j) " marketable securities " means freely negotiable debt and equity instruments bearer or, otherwise, such as corporate stocks and shares and Modaraba certificates listed on Stock Exchanges, Government or Government-guaranteed securities, corporate financial paper, short-term commercial paper, bankers' acceptances, certificates of deposit and investment, Participation Term Certificates and Term Finance Certificates :

(k) " Ordinance " means the Companies Ordinance, 1984 (XLVII of 1984) ;

(l) " risk assets " means marketable securities and other assets held by an investment finance company in the ordinary course of its business:

(m) words and expressions which have been used in this notification but not defined and have been defined in the Act or the Ordinance shall have the same meaning as in the Act or the Ordinance.

2. *Commencement of operation.*—(1) An investment finance company shall commence business and its operations as such company only after it has been registered and issued a licence under this notification by the Controller.

(2) A company proposing to commence the business of investment finance company shall make an application to the Controller, in the manner notified by the Controller in the official Gazette, with a declaration that it complies with all the terms, conditions and requirements of this notification and shall comply with all that is required of investment finance companies in the conduct of such business.

(3) At the time of making the applications under sub-paragraph (2), the applicant—company shall have fulfilled and complied with the following conditions, namely :—

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(a) it shall be registered as a public limited company under the Ordinance or any other law for the time being in force with objects and functions specified in paragraph 4 of this notification ;

(b) it shall have a minimum paid-up capital of one hundred million rupees and shall be listed on Stock Exchanges in Pakistan ;

(c) its investment policy shall be clearly and concisely stated in its Memorandum and Articles of Association and the prospectus published for public offer of its securities. The prospectus shall, so far as may be, conform to and comply with all applicable provisions of the Ordinance and the Act ;

(d) no person who has been convicted of fraud or breach of trust or of an offence involving moral turpitude shall be its director, officer or employee : and

(e) no person who has been adjudged as insolvent or has suspended payment or has compounded with his creditors shall be its director, officer or employee.

(4) The Controller shall, if he is satisfied that the company has fulfilled the conditions specified in sub-paragraphs (2) and (3) and in his opinion the promoters thereof are persons of means and intergrity, have knowledge of matters which the company may have to deal with as an investment finance company and have engaged adequate qualified staff, register the company as an investment finance company.

3. *Bar on interest bearing transactions.*—An investment finance company will not transact any business on the basis of interest, except for the time being that relating to foreign loans and credits. All financial transactions will be in accordance with the Islamic modes of financing.

4. *Bar on purchase or sale by beneficial owners.*—An investment finance company shall not, without the prior approval in writing of the Controller, purchase anything from, or sell anything to, any director, officer, employee or a person who either individually or in concert with close relatives beneficially owns ten per cent or more either of the equity or other securities with voting rights, if any, issued by the investment finance company.

5. *Objects and functions.*—The objects and functions of investment finance companies shall be as follows, namely :

(a) *Money market activities* :

(i) Issuing short-term paper of its own or certificate of deposits or investments of not less than 30 days maturity.

(ii) Trading in commercial paper issued by its clients, Government securities, promissory notes, bankers' acceptances and other money market instruments, acting either as a broker or acting on its own account.

(iii) Assisting in the issue of commercial paper, including introduction of companies to the money market, preparation of documentation, distribution and market making.

(iv) Acting as broker or on its own account in the Call Money Market.

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(b) *Capital market activities* :

(v) Trading in listed securities, both equity and non-equity instruments. acting either as broker or acting on its own account.

(vi) Providing professional analysis of securities to both institutional and individaul investors.

(vii) Issuing of long-term certificates of deposit or investment and underwriting of stocks and shares. short and long term Participation Term Certificates and other negotiable term obligations of corporations and financial institutions. acting singly or jointly as manager. underwirter and distributor of such issues and taking an active part in all stages of preparation for such issues either public issues or private placement.

(viii) Floating and managing both open-end and closed-end mutual funds and managing portfolios of stocks and shares, pension and provident funds, Participation Term Certificates and other negotiable and debt instruments for both individual and institutional clients, on a discretionary as well as non-discretionary basis.

(ix) Providing margia loans to individual and institutional investors.

(x) Offering of cash management accounts to enable clients to shift at their discretion among various investment alternatives.

(c) *Project financing activities* :

(xi) Making investments in projects through underwriting of public issue of stocks and shares and securities. short-term and long-term Participation Term Certificates and Term Finance Certificates of varyingfeatures.

(xii) Guaranteeing and counter-guaranteeing loans and obligations.

(d) *Corporate financial services* :

(xiii) Acting as adviser and financial agent for companies in obtaining direct bank loans, syndicated loans. export credits, leases and project finances, both domestically and internationally.

(xiv) Assisting companis in private placement of debt and equity. domestically and abroad.

(xv) Acting as adviser to companies in corporate or financial restructuring as well as in the preparation of resource mobilisation plans.

(xvi) Acting as adviser to companies in mergers, acquisition and divestitures.

(xvii) Assisting companies with cash management systems.

(xviii) Preparing feasibility, market or industry studies for companies, both domestic and foreign.

(xix) Raising equity, such as through venture capital. for new and existing companies, by acting as a financial intermediary.

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(*e*) *General*

(xx) Carrying on any other investment finance business specifically allowed by the Controller with the exception of banking business and insurance business as defined in the Banking Companies Ordinance, 1962 (LVII of 1962), and the Insurance Act, 1938 (IV of 1938), respectively, and in this connection they will neither issue cheque-books nor accept deposits.

(xxi) Raising funds through equity, foreign debentures, both short and long term, commercial paper issued abroad, sale of short and long term Participation Term Certificates and Term Finance Certificates, deposit and investment certificate, floating and managing of Modarabas and through other methods and instruments :

Provided that the period of term finance certificates and other instruments shall not be less than 30 days.

6. *Ratio of equity to liabilities.*—An investment finance company shall maintain for the first two years of its operation a ratio of equity to liabilities of not less than one is to seven and thereafter this ratio may be increased up to a maximum of one is to ten.

7. *Submission of reports, etc.*—(1) An investment finance company shall submit quarterly reports to the Controller in the manner and form to be prescribed by him from time to time or in any specific case or on any particular occasion and shall comply with such orders, directions or advice as the Controller may give in writing.

(2) The Controller shall monitor the general financial health of the company, and, at his discretion, may order special audit and appoint an auditor to carry out detailed scrutiny of the affairs of the company, or appoint both an auditor and an Inspector, provided that the Controller, may, during the pendency of the scrutiny, pass such interim orders and directions for the due completion of the scrutiny as may be deemed appropriate by him.

(3) On receipt of the special audit report or report from the Inspector, the Controller may direct the investment finance company to do or to abstain from doing certain th... and issue directives for immediate compliance which shall forthwith be complied.

(4) All orders, directions, advice under the foregoing sub-paragraphs and all that may be required to be done thereunder shall be done, acted upon and carried out. In case an investment finance company fails to comply with or carry out the said orders, directions, or advice, the Controller may take action under section 13 of the Act or any other law by making a complaint.

(5) The Controller, in case of gross mismanagement of the investment finance comoany, may also cancel the registration and licence granted to the investment finance company.

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8. *Total investment in equities.*—Without the approval of Controller,—

(a) the total assets in equities shall not exceed an investment finance company's liquid net worth, except equities taken up as a consequence of underwriting commitment in which case this limit may be exceeded by the amount of equities taken up for a period of six months; and

(b) risk assets shall not exceed ten times an investment finance company's liquid net worth.

9. *Maximum exposure to a single issuer or associated issuer of risk assets.*—Unless otherwise specified by the Controller, the maximum exposure of an investment finance company to any single issuer, associated companies or associated issuer of risk assets, shall not exceed the following limits :—

Risk Assets	Maximum exposure to single issuer/ associated-issuer expressed as percent of investment finance company's liquid net worth
Equity investment	10%
Margin Loan	10%
Corporate financial paper and short-term commercial paper ..	35%
Underwriting of shares and corporate financial paper ..	50%

10. *Underwriting commitments.*—All underwriting commitments shall be fully backed by either available funds or firm stand by lines of credit or other funding arrangements.

11. *Principles for margin loans.*—The grant of margin loans to clients shall be governed by the following principles :—

(a) The aggregate of margin loans granted by an investment finance company shall not exceed 50% of its liquid net worth.

(b) The margin to be maintained by the client shall not be less than 33-1/3% of the loan amount outstanding calculated as the residual value obtained after deducting from the portfolio's market value the loan amount outstanding.

(c) Margin loans to a single client or associated clients (being the same, in the case of corporate bodies, as associated companies or associated issuers) shall not exceed 10% of an investment finance company's liquid net worth.

(d) Margin loans shall be approved by a minimum two-thirds majority of the Board of an investment finance company and shall not be granted to any employee, officer, director, or a shareholder having a beneficial ownership including that of close relatives of more than 10% in the paid-up capital of the investment finance company whether directly or indirectly (through their close relatives, companies controlled by them, affiliates, subsidiaries, or by way of acting in concert with others).

12. *Insurance coverage.*—An investment finance company shall obtain sufficient insurance coverage on its own or on its clients' benefit against any losses that may be incurred as a result of employee's fraud or gross negligence :

Provided that the Controller may, from time to time, specify the nature and extent of insurance coverage to be obtained by an investment finance company.

13. *Exchange fluctuation risk.*—An investment finance company shall make satisfactory arrangement to insulate itself from exchange fluctuation risks associated with foreign currency obligations and transactions.

14. *Ban on acquiring controlling interest.*—Except where it is necessary to protect its investment, an investment finance company shall not seek to acquire a controlling interest in any enterprise in which it has invested or has any other interest which would give it primary responsibility for management.

15. *Managing mutual funds and discretionary client accounts.*—In managing mutual funds and discretionary client accounts, an investment finance company shall—

(a) exercise due diligence and prudence to achieve the investment objective of the mutual fund holders and discretionary clients :

(b) so organise its affairs that mutual fund and discretionary client accounts are managed separately from other activities, each investment or disinvestment decision being taken independently on its own merit without consideration of any other potential or actual involvement of the investment finance company ; and

(c) secure no remuneration directly or indirectly resulting from or otherwise related to transactions.

Explanation

In the event of any dispute, the onus of proof shall be on the investment finance company to show that it complied with the principles stated at cluses (a), (b) and (c).

16. *Audit of accounts.*—(1) The accounts of an investment finance company shall be audited by an auditor who is a chartered accountant within the meaning of the Chartered Accountants Ordinance, 1961 (X of 1961), appointed by the investment finance company with the approval in writing of the Controller (which shall be obtained prior to proposing the name of the auditor at the Annual General Meeting) and such auditor shall have the same powers, duties and liabilities as an auditor of a company has under the Ordinance.

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(2) A casual vacancy of an auditor shall be filled with the prior approval in writing of the Controller.

17. *Opening of branches.*—(1) An investment finance company may be authorised by the Controller to open one branch to begin with.

(2) For opening more branches, the investment finance company shall obtain prior permission in writing from the Controller.

18. *Penalties.*—(1) Any contravention of and an attempt to contravene these conditions shall be punishable under section 13 of the Act.

(2) Without prejudice to an action and punishment under section 13 of the Act, in case of contravention of any provision of this notification the Controller may cancel the registration licence of the investment finance company after issuing a show cause notice and giving such company an opportunity of being heard or passe an order deemed appropriate by the Controller which shall be complied with as ordered.

(3) Upon cancellation of the registration and licence, the functions and carrying on the business of investment finance company shall cease and the Controller may move the Court for a winding up order in respect of the company.

(4) Every director, chief executive, manager and other officer of a defaulting investment finance company shall be liable as provided under sub-section (2) of section 13 of the Act.

19. *Miscellaneous.*—(1) An investment finance company shall not offer any of its own or other securities for any consideration other than cash, nor make any loan or advance against these securities.

Liquidity

(2) No investment finance company shall—

(a) transfer ownership of controlling shares, merge with, acquire or take-over any other investment finance company unless it has obtained the prior approval of the Controller in writing to the scheme of such merger, acquisition or take-over;

(b) make a loan or advan[illegible]ey to any person except in connection with the ordinary course of business of the investment finance company ; and

(c) employ as a broker, directly or indirectly, any of its directors, officers or employees, or a person who beneficially owns whether individually or in association with close relatives ten per cent or more either of the equity or other securities with voting rights, if any, issued by the investment finance company.

[F. No. 14 (1) RO (INV)/85.]

SHAMIM AHMAD KHAN,
Controller of Capital Issues.

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PART II

Statutory Notifications (S. R. O.)

GOVERNMENT OF PAKISTAN

FINANCE DIVISION

(Investment and Capital Issues Wing)

NOTIFICATION

Islamabad, the 31st August, 1987

S. R. O. 752 (I)/87.—Pursuant to sub paragraph (2) of paragraph (2) of Finance Division's S.R.O. No. 585 (I)/87 dated the 13th July, 1987 following procedure for applying to the Controller of Capital Issues for registration as Investment Finance Company is notified for the public information :

(i) In the first instance, those desirous of registration as Investment Finance Company should apply to the Controller of Capital Issues (CCI), providing information (as given at Annex. I) for obtaining permission to form an Investment Finance Company.

(ii) On receipt of the permission from the Federal Government, the sponsors should apply to CCI on Form I.

(iii) The specimen of licence to be issued by CCI, permitting the companies to carry on the business of an Investment Finance Company is also published for public information (Form II).

[F. No. 14(1)-RO (INV)/85.]

SHAMIM AHMAD KHAN,
Controller of Capital Issues

Price : Ps. 60

[4292 Ex. Gaz.]

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Annex I

INFORMATION TO BE SUPPLIED FOR OBTAINING PERMISSION TO FORM AN INVESTMENT FINANCE COMPANY IN TERMS OF S.R.O. 585 (I)/87 DATED 13TH JULY 1987

1. Full names, any former names, Father's/Husband's name, nationality, full residential and business addresses and details of other director ships and occupations of the proposed directors and officers including Chief Executive and Chairman of the Board indicating their respective designation and name of firms in which any one is a partner

2. Name of companies, firms or organisations of which the aforesaid directors and officers have been directors, managers, officers, employees or partners in the past.

3. Financial standing, professional qualifications and experience of persons mentioned in (1) above, supported by documentary evidence

4. Whether any aforesaid person has ever been convicted of fraud or breach of trust or of an offence involving moral turpitude or removed from serivice. If so, full particulars thereof.

5. Whether any person referred to in (1) above or any company or firm in which he has been associated in the past has been adjudicated an insolvent or has suspended payment or defaulted in making payments or has compounded with his or their creditor or gone into liquidation. If so, full particulars thereof.

6. Shareholdings of each of the person referred to in (1) above in the proposed company.

7. Names of professionals to be engaged for management.

8. Description of business operations to be undertaken and organizational set up and plans along with feasibility report, if prepared.

9. Bank references.

FORM I

[*See* paragraph 2(2)]

S.R.O. 585 (I)/87, dated 13th July 1987.

APPLICATION FORM FOR REGISTRATION OF INVESTMENT FINANCE COMPANY

Dated , 198 .

To

The Controller of Capital Issues,

....

DEAR SIR

We hereby apply for registration of—————————— under paragraph 2 of S.R.O. 585 (I)/87, dated 13th July, 1987, as an investment finance company.

2. We hereby confirm—

(a) that it is registered under the Companies Ordinance 1984 as a public limited company with the paid up capital of Rs. one hundred million :

(b) that none of its directors, officers or employees has been convicted of fraud or breach of trust or of an offence involving moral turpitude :

(c) that none of its directors, officer or employees has been adjudged an insolvent or has suspended payment or has compounded with his creditors ;

(d) that it has engaged adequate qualified staff.

the details of which are as follows :

3. Three copies of the following documents pertaining to the company are also enclosed :

(a) Memorandum and Articles of Association duly certified and signed by all directors.

(b) Certificate of incorporation (one copy of which should be certified by the Registrart, Joint Stock Companies).

(c) Prospectus published for public offer of securities.

(d) Latest audited Balance Sheet and Profit and Loss Account together with related documents.

4. Information and documents as required in the Annexure to this form duly verified and signed by all directors alongwith three spare copies of this application and an affidavit as to the correctness of the details by the Chief Executive and two directors are furnished herewith. We undertake to keep th . information up to date by communicating changes modifications therein within fourteen days of such changes/modifications.

5. We further undertake that no change in the emorandum and Articles of Association nor any change in the majority share-hoiders and directors shall be made without prior written authorisation of the Controller of Capital Issues and that we shall comply with all requirements of law and conditions of registration.

6. We being authorised by the directors of the company hereby solemnly declare and affirm that to the best of our knowledge and belief the information contained in this application (Form-I), annex to Form-I and the documents accompanying thereto are true and correct and that all terms, conditions and requirements of *S.R.O. 585 (I)/87 dated 13th July*, 1987 in respect of all matters precedent to the registration of the said------------------as an investment finance company or incidental thereto have been duly complied with and the said company shall also comply with all that is required of an investment finance company in the conduct of such business.

Yours faithfully

Verified by
Oath Commissioner.

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1. Name of the Company .. .. ..

2. Registered office of the company .. ..

3. Date of incorporation as a public limited company.

4. Authorised, subscribed and paid up capital of the company .. ..

5. Management.

   (a) Names, business and addresses of directors, amount of shares held by each and name(s) of the banker(s) of each of them .. ..

   (b) Director's interest, direct or indirect in any other company(ies) giving details of such interest. .. ..

   (c) Details of persons or group controlling the company including of those persons who own 10% or more shares given number and value of shares held .. .. ..

   (d) Name(s) of holding, subsidiary and associated undertaking(s), if any .. ..

   (e) Whether any director, officer or employee of the company has been convicted of any fraud or breach of trust or committed any offence involving moral turpitude or has been adjudicated as insolvent or suspended payment or compounded with his creditors.

   (f) Name of the proposed chief executive officer of the company, his qualifications, experience and proposed remuneration ..

6. Reasons for selecting the proposed place of business giving statistical data, if any ..

7. Whether the company fulfils all the conditions laid down in paragraph 2(3) of S.R.O. 585 (I)/87, and whether it is agreeable to permit the Controller of Capital Issues or any officer authorised on his behalf to satisfy himself by inspection of the books of the company or otherwise that the prescribed conditions are being fulfilled by the company .. ..

8. Any additional facts which the company may wish to add in support of its application ..

---

1. Date of receipt of application .. ..

2. Date of Registration .. .. ..

3. Registration No. .. ..

4. Date of Issue of Licence .. .. ..

Signature of Controller
of Capital Issues

FORM II

[*See* paragraph 2(4)]

LICENCE TO CARRY ON THE BUSINESS OF AN INVESTMENT FINANCE COMPANY

OFFICE OF THE CONTROLLER OF CAPITAL ISSUES

Islamabad, the————————,198 .

Registration No.——————

Certified that having considered the application for registration under paragraph 2(4) of S.R.O. 585 (I)/87 and being satisfied that the company, whose particulars are specified below, is eligible for registration, I, in exercise of the powers conferred under paragraph 2(4) of S.R.O. 585 (I)/87 do hereby grant licence to the company subject to the conditions laid down in the said S.R.O. or imposed thereafter :

1. Name .. ..

2. Address .. ..

3. Date of Registration .. .. ..

4. Other particulars, if any .. ..

Issued under my signature and seal.

Signature of the Controller
of Capital Issues.

ANNEXURE 2

GRESBANK'S DEPOSIT SCHEMES

INTRODUCTION:

Crescent Investment Bank Limited(CresBank) is the first investment bank in the private sector. CresBank has been incorporated under the Companies Ordinance 1984 as a public limited company with the paid-up capital of Rs. 100 million. The Bank is a joint venture of the Crescent Group and National Development Finance Corporation (NDFC). They have participated in the equity contribution of CresBank to the extent of 50 percent and 20 percent respectively. Balance thirty percent of the capital has been raised from the general public.

Crescent Group, a reputable and well established group, has for years been involved in converting ideas into reality by repeatedly bringing varied industrial ventures to fruitatio . Crescent Group has successful track record of developing a profitably operating several industrial, commercial ventu es (including fiftenn public companies) with a wide range of product and services. The industrial ventures include seven textile units, two sugar mills distilleries, jute, particle board, urea formaldehyde, steel and engineering works, construction, insurance and leasing. The Group is also developing its expertise in the field of power generation, including technical and financial feasibilities, engineering and arranging financial packages, etc. The Group has also been dominent in the field of cotton trade and is backed by seven modern ginning factories in the cotton growing arease of Punjab and Sind. Crescent Group has a substantial resource pool of project, engineering and financial services. These resources are regularly supplemented by a close association with the leading financial, engineering and supply organizations, within Pakistan and Overseas.

National Development Finance Corporation is the largest financial institution in Pakistan in the public sector. NDFC's resource base consists of funds raised through its own deposit schemes and credit lines from the State Bank of Pakistan and lines provided by multinational lending agencies such as World Bank, Asian Development Bank, Islamic Development Bank and other sources.

CresBank has been placed under the administrative control of the Ministry of Finance through the office of the Controller of Capital Issues.

SERVICES:

CresBank's primary objective is to provide a wide range of financial products and services to individuals and enterprises in the country. The broad and flexible framework for the investment companies allows CresBank to undertake a wide range of functions and provide a variety of financial product and services.

The activities in which CresBank can engage in is as follows:

- Provide project finance
- Make equity investment and trade in listed securities
- Underwriting of issue of corporate equity and debt securities
- Guaranteeing loans and other obligations
- Loan syndication
- Financing trade
- Financing securities purchases (Margin Finance)
- Issuing certificates of deposits on its own behalf and on behalf of customers
- Discounting of Debt Securities
- Mobilization and management of Mutual Funds
- Investment and financial advisory services
- Provide fee based services like fund managment, portfolio management, preparation of feasibility studies/reports etc.

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DEPOSIT CERTIFICATES:

CresBank has developed Deposit Certificates keeping in view the requirements of varied group of depositors like individuals and organizations in respect of liquidity, high return and simple formalities. The certificates are both registered and bearer in nature.

The important feature of each type of scheme are given hereunder:

<u>Deposit Certificates - Registered</u>

Under this scheme deposits can be placed for a fixed period varying from 30 days to 5 years.

Profit under this scheme is paid at the time of maturity or in case of certificates of longer maturity i.e. more than six months the profit is paid on half yearly basis.

The expected profit rates applicable to deposit certificates for the first half of the year 1990 are as follows:

period	rates
30 days	8.0%
3 months	10.0%
6 months	11.0%
1 year	12.0%
2 years	12.5%
3 years	13.0%
4 years	13.5%
5 years	14.0%

The certificates are non negotiable and non transferable. The encashment can only be made at the place of issue.

In case, the certificate(s) are lost, stolen or destroyed, duplicate certificate(s) can be issued against indemnity.

The Certificates are undenominated and issued according to the requirement of the customer.

Identification of the Depositor is required at the time of deposit and encashment.

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Deposit Certificates - Bearer

This is a bearer instrument and ownership is transferred by mere delivery. The scheme is simplest form of placing deposits and no formalities in respect of account opening forms, signatures, etc. are required. The scheme is developed for investors who want to maintain liquidity with maximum return.

The deposit is accepted for a 5 year period. However, certificates can be encashed at any time during the maturity period along with applicable profit.

No claim in respect of stolen, lost or destroyed certificates is entertained and no duplicate certificate is issued.

The holder is deemed and treated as absolute owner of the certificates for the purposes of payment of proceeds and for all other purposes (notwithstanding any notice of ownership or writing thereon or notice of any previous loss or theft or confiscation or any other similar act thereof).

The Deposit Certificates are available in the following denominations.

Rs. 10,000/=
Rs. 25,000/=
Rs. 50,000/=
Rs. 100,000/=
Rs. 250,000/=

The expected profit rates applicable to deposit certificates for the first half of the year 1990 are as follows:

Period	Rates
a) At maturity (i.e. 5 years from the date of issue)	14.0%
b) On premature encashment after:	
4 years	13.5%
3 years	13.0%
2 years	12.5%
1 year	12.0%
6 months	11.0%
3 months	10.0%
1 month	8.0%

Profit is payable at the time of encashment/maturity.

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Deposit Accounts:

This is a unique deposit scheme which allows multiple withdrawals and deposits without any limit. The salient features of the account are as follows:

Multiple withdrawals can be made through Withdrawal

Request slips which may be obtained from the Bank branch.

Minimum balance acceptable is Rs. 10,000/=.

Deposit to be kept with the Bank for a minimum period of 30 days.

Deposits below the minimum limit in any single day during the month will not attract any profit for the month.

Profit is calculated on the minimum monthly balance and credited to the account on half yearly basis.

Rate of profit is 8% per annum which is subject to change from time to time.

Deposit Account facility is available to the following:

- indiviuals
- sole traders
- private limited company
- public limited company
- trusts, funds, societies, etc.

Identification of the account holder is necessary.

The account is liable to compulsory deduction of Zakat subject to the exemption provided in the Zakat and Usher Ordinance.

GENERAL INFORMATION:

(point no. 1 to 4 below do not apply to our Bearer Deposit Certificates)

1. Clients desirous of placing funds with CresBank may do so by cash or cheques, demand drafts/pay orders drawn to the order of Crescent Investment Bank Ltd., crossed "ACCOUNT PAYEE", supported by completed Account Opening form, specimen signatures card and a copy of National Identity Card.

2. On maturity, Deposit Certificate will be repaid in accordance with the depositor's written instructions after a proper discharge on the reverse of the certificate.

3. CresBank may, at its sole discretion, authorise withdrawal of a deposit even before maturity subject to appropriate adjustment in (a) the profit paid before encashment and (b) the relative profit rate applicable thereon.

4. In the event of depositor's death, the deposit and profit accrued thereon will be paid on request of the legal heirs after the completion of prescribed legal formalities.

5. The profit is linked with the pretax profit of the CresBank and distributed on the basis of profit and loss sharing. The rate of the profit are subject to change from time to time according to the profitablity of the Bank.

6. Profit is calculated on the basis of 365 days a year.

7. No profit is payable if encashed if encashed within one month from the date of issue.

8. No profit is payable on Deposit Certificates after the maturity date.

9. Minimum deposit limit is Rs. 10,000/-.

10. The certificates are only to be encashed at the place of issue.

11. Zakat shall be charged and collected on a compulsory basis in accordance with the Zakat and Ushr Ordinance, 1980, and rules made thereunder. Deposit Certificates on which return is paid periodically, the Zakat will be deducted from the first payment made after the valuation date or on encashment whichever is earlier.

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12. Deposit Certificates on which return is paid on encashment or maturity, the Zakat will be collected on maturity or encashment if falling after at least one Valuation Date.

13. Persons exempted from the provisions of the Zakat ordinance are required to file necessary declaration with the concerned office/branch of CresBank with in a period of three months prior to Valuation Date.

14. It should be noted that Zakat is charged/ collected on the basis of hijra calendar year. Hence, incstance may arise when two Zakat Valuation Dates may fall in one Gregorian year and in that event Zakat will be collected twice in the same Gregorian year.

15. This brochure is for the general guidance of prospective depositors. The profit rates, specific features of the schemes are subject to change without any notice.

16. For further information, please contact our office / branch or one of the following officers:

Lahore:	Mr. Ali Sameer	Tel. 324110
	Mr. Mohsin Mehdi	" "
Karachi:	Mr. Mahmood Ahmed	Tel. 524677, 526094

ADDRESS:

Crescent Investment Bank Ltd.
45, Shahrah-e-Quaid-e-Azam,
Lahore.
Tel: 324110, 324733
Telex: 44445 CBS PK.

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ANNEXURE 3

MARGIN FINANCE

One of the main area of activities of the CresBank is providing Margin Finance against the security of listed shares. The main objective for the financing is to contribute in the development of the capital markets in the country by increasing the liquidity of interested investors.

WHAT IS MARGIN FINANC

The financing against the leveraged purchases of securities is called Margin Finance. Margin Finance collateralised by share purchases are made to individuals /firms /companies who wants to buy shares but do not have enough liquidity to the finance full cost of the purchases or wants to leverage themselves with the expectation of future rise in prices resulting in Capital gain. The expected Capital gain combined with dividend yield is expected to more than offset the financing cost. The total cost shares purchased is met proportionately from financing from the CresBank called Margin Finance and from the client's own sources called Margins.

HOW MARGINS ARE CALCULATED

Margins are normally calculated on the basis of maximum debt equity ratio of 60:40 as illustrated hereunder:

If 100 shares are bought by a client at Rs. 20 per share, the total cost disregarding commission will be Rs. 2000/-. Assuming that the client invests 40 percent, the margin finance will be Rs. 1200 and margin on purchase date will be Rs. 800. The shares purchased would be retained by CresBank as collateral. In the case of fall in price of shares, the Bank will call for additional margin to maintain the 60:40 ratio.

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WHO CAN APPLY

The target customers for Margin Finance are the individuals with a track record of dealing in capital markets and having good repute in meeting their commitments against purchase of shares.

The firms and companies engaged in the trading of securities at stock exchanges can also apply for margin financing facility.

COLLATERAL

Shares Purchased against the margins and margin finance are taken as collateral. CresBank at its sole discretion can call for additional security against any margin finance facility.

Not all the securities listed at the Stock Exchanges qualify for the margin finance. For a margin finance facility from CresBank, a list of acceptable shares with respective margin requirements is given in the Annexure 1.

RATE OF RETURN

The rate of return payable by the client on margin finance shall be arrived at, on case to case basis, with mutual consent.

GENERAL INFORMATION

1. Clients desirous of obtaining Margin Finance from Cres Bank may do so by applying for an allocation of a Margin Finance line on a standard form supported by references of stock brokers / bank managers and a copy of National Identity Card.
2. On approval of the facility the client is required to open a Margin Deposit Account with CresBank.
3. CresBank may, at its sole discretion, debit the deposit account for any margin against any authorised purchases or for any additional margin required to maintain the margin ratio against a particular collateral.

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4. CresBank may, at its sole discretion, at the time of falling share prices call for additional margin to maintain required ratio for a particular security or to sell the collateral without informing the client and adjust its financing and any other dues outstanding.
5. Withdrawal from a Margin Deposit Account is subject to prior clearance from the bank.
6. In the event of client's death, balance of the Deposit Account and profit accrued thereon after adjustment of all the outstanding contracts of margin finance, will be paid on request of the legal heirs after completion of the prescribed legal formalities.
7. The profit on Deposit Account is linked with the pretax profit of CresBank and distributed on the basis of profit and loss sharing on minimum balance during a calendar month. The rate of profit are subject to change from time to time according to the profitability of the Bank.
8. Profit is calculated on the basis of 365 days a year payable biannualy.
9. Minimum deposit limit is Rs. 10,000/-
10. Deposit Account is subject to Zakat which shall be charged and collected on a compulsory basis in accordance with the Zakat and Ushr Ordinance, 1980, and rules made thereunder. The Zakat will be deducted on the outstanding balance on the valuation date.

11. Persons exempted from the provisions of the Zakat Ordinance are required to file necessary declaration with the concerned office/branch of CresBank with in a period of three months prior to Valuation Date.

12. It should be noted that Zakat is charges collection on the basis of hijra calendar year. Hence, instance may arise when two Zakat Valuation Dates may fall in one Gregorian year and in that event Zakat will be collected twice in the same Gregorian yearr.

13. This Brochure is for the general guidance of the prospective Margin Finance clients. The specific features of the scheme are subject to change without any notice.

14. For further information, please contact our office/branch or one of the following officers:

Lahore:	Mr. Ali Sameer	Tel. 324110 / 323882
	Mr. Mohsin Mehdi	Tel. 324110 / 62217
Karachi:	Mr. Mahmood Ahmad	Tel. 525677 / 526094

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LIST OF ACCEPTABLE SHARES

FOR MARGIN FINANCE

Name Of The Companies	Margin %	Name Of The Companies	Margin %
A. Finance Cos., Mutual Fund & Banks		C. Cotton Textiles	
1) Bankers Equity	40	1) Allawasaya	40
2) Atlas BOT Lease	50	2) Alhamd	40
3) B.R.R Capital Modaraba	40	3) Ayesha	40
4) Crescent Investment Bank Ltd.	40	4) Bhanero	40
5) 1st Grindlays Modaraba	40	5) Burewala	40
6) 1st ICP	40	6) Crescent	40
7) 2nd ICP	40	7) Crescot	50
8) 3rd ICP	40	8) Dawood Cotton	40
9) 4th ICP	40	9) Dewan	40
10) 5th ICP	40	10) Gul Ahmed	40
11) 6th ICP	40	11) Gulistan	40
12) 7th ICP	40	12) Gulshan Spinning	40
13) 8th ICP	40	13) Hussain Industries	40
14) 9th ICP	40	14) Ittefaq	40
15) 10th ICP	40	15) Jubilee Spinning	40
16) 11th ICP	40	16) Kohinoor Industries	40
17) 12th ICP	40	17) Kohinoor Spinning	40
18) 13th ICP	40	18) Mohammad Farooq	40
19) 14th ICP	40	19) Mushtaq	40
20) 15th ICP	40	20) Nagina Cotton	40
21) 16th ICP	40	21) Nafees Cotton	40
32) 17th ICP	40	22) Nishat Mills	40
23) 18th ICP	40	23) Quetta	40
24) ICP S.E.M.F	40	24) Sana	40
25) LTV Capital Modaraba	40	25) Sapphire	40
26) Mod. Ali Mali	40	26) Service (Tex)	40
27) NDLC	40	27) Shadab	40
28) Orix Leasing	40	28) Shams	40
29) PICIC	40	29) Shaheen Cotton	40
30) PIL Corp	40	30) Star	40
31) 1st National	55	31) Sunshine	40
		32) Suraj Cotton	40
		33) Zaman	40

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H. Cement

1)	Asbestos	40
2)	Cherat	40
3)	Gharibwal	40
4)	Zeal Pak	40

I. Tobacco

1)	Pakistan Tobacco	40

J. Fuel & Energy

1)	Attock Ref.	40
2)	Burshane Pak	40
3)	Haroon Oils	50
4)	Karachi Electric	40
5)	National Refinery	40
6)	P.O.S.	40
7)	Pak Oilfields	40
8)	Pak Refinery	40
9)	Pak. State Oil	40
10)	Sui Suothern Gas	40
11)	Sui Northern Gas	40

N. Chemicals & Pharmaceuticals

1)	Abbot Labs	40
2)	Berger Paints	40
3)	Boots Company	40
4)	Ciba Geigy	40
5)	Cynamid	40
6)	Dawood Hercules	40
7)	Exxon Chemical	40
8)	Ferozsons Lab	40
9)	Glaxo Labs.	40
10)	Hoechst	40
11)	ICI Pak	40
12)	Otsuka	50
13)	Pak Gum & Chem.	40
14)	Parke Davis	40
15)	Pak Oxygen	40
16)	Reckitt & Colman	40
17)	Sandoz	40
18)	Sind Alkalis	40
19)	Sitara Chemical	40
20)	Smith Kline & French	40
21)	Wah Nobel CHem.	40
22)	Wellcome	40
23)	Wyeth Labs.	40

O. <u>Paper & Board</u>

1) Orient Straw Board	40
2) Packages	40
3) Pak. Paper Product	40
4) Pak. Papersack	40
5) Security Paper	40

P. <u>Vanaspati & Allied</u>

1) Associated Ind.	40
2) Fatima Ent.	40
3) Fazal Veg.	40
4) Kakakhel	40
5) Wazir Ali	40

Q. Construction

R. <u>Leather & Tanneries</u>

1) Bata Shoes	40
2) Hilal Tannery	50
3) National Tannery	40
4) Service (Shoes)	40
5) Universal Leather	40

S. <u>Food & Allied</u>

1) Brooke Bond	40
2) Lever Brothers	40
3) Milkpak	40
4) Rafan Maize	40
5) Shezan International	40
6) National Foods	50

T. <u>Glass & Ceramics</u>

1) Emco Ind.	50
2) Prince Glass	40

U. <u>Miscellaneous</u>

1) Grays of Cambridge	40
2) Haji Dosa	40
3) United Distributors Pakistan	40

ANNEXURE 4

ISSUES FACING INVESTMENT BANKS REGARDING DELAYS IN OBTAINING PERMISSIONS FOR ACTIVITIES THAT ARE PERMITTED UNDER THE GOVERNING STATUTORY REGULATIONS- SRO # 585 (I) / 87.

Investment Banking activities have been permitted under the Statutory Notification - S.R.O #585 (1)/87 issued by the Investment and Capital Issues Wing of the Finance Division of the Government of Pakistan (GOP).

These activities are classified into five major categories:-

a) Money Market Activities
b) Capital Market Activities
c) Project Financing
d) Corporate Financial Services &

These categories cover a very wide range of Investment Banking activities. Most of these activities are explicitly stated and permitted under the said SRO. Infact, the SRO is not a sealed regulation and is open to accommodate other Investment Banking activities which are listed in the SRO but can be discussed with the Controller of Capital Issues and may be permitted if found conducive.

As Investment Banking is new in Pakistan, the market as well as the bureaucracy do not understand it completely. Uptil now the only experience that the market has had with Investment Banking has been with the fraudulent Investment Finance Companies which brewed up in the past decade, offering tremendous returns and finally taking-off with the investors money. Therefore, the market is cautious and so are the regulatory bodies.

As CresBank - Crescent Investment Bank is the first Investment Bank to start operations in Pakistan, it is in a position to specify such areas of business and activities where Investment Bankswill counter problems. These problems if not removed will undermin the role of Investment Banks.

Investment Banks are expected to play a major role in the restructuring of the financial system in Pakistan.. They have to mobilise new sources of funds and tap into those niches where Commercial Banks and Development Finance Institutions- DFI's have not ventured. Investment Banks are expected to develop the Capital market and Money Market Operations, by first introducing instruments of varied nature and then increasing their marketability by encouraging their discounting and trading on the stock exchanges and over the counters of financial institutions. Other responsibilities include sharing the burden of DFI's in providing financial assistance to projects and providing advisory services to investors.

Following is a list of the problems faced in various activities which are limit the scope of Investment Banking.

A) MONEY MARKET ACTIVITIES:

i) Trading in Government Securities:

The Section 5. (a) (ii) of the SRO permits Investment Banks to purchase and sell Government Securities on its own account and as a broker. Commercial Banks are the approved agents for the sale of WAPDA Bearer Bonds, National Saving Schemes and other such government securities. FCDC has approved CresBank as its brokers only for the sale of the third issue of WAPDA Bearer Bonds. However, it is desirable that sale and purchase of all government securities should also be allowed to Investment Banks, as is to commercial Banks.

ii) Acting as a Broker or on its Own Account in the Call Money Market:
As per Section 5. (a)(iv) of the SRO, Investment Banks are allowed to borrow and lend in the Call Money Market. As this is the cheapest form of funding available to meet the current liquidity requirements it is a very essential source of funds available to all commercial banks and financial institutions. Investment Banks will require to lend and borrow in the Call Money Market to manage their liquidity position in the same manner as CBs and DFIs.

CAPITAL MARKET ACTIVITIES:

i) Trading in Listed Securities, both Equity and Non-Equity Instruments, Acting either as a Broker or Acting on its Own Account:
This activity has been allowed under Section 5.(b)(v) of the SRO. Investment Banks have been allowed to act as a broker on the stock exchange but they will not be issued new membership cards. The stock exchange does not want to increase the number of its members, therefore, Investment Banks will have ~~have~~ to purchase a card from an existing member. This situation has lead to a monopoly situation for the existing card holders. They have started quoting unrealistic prices for their membership cards. There is also an accounting problem involved under which the seller of the card wants to sell at an exorbitant price but bill the buyer of the card for a minimal amount, in order to avoid tax problems.

When Investment Banking is a government approved activity ans is expected to improve the economic environment of the country the stock exchange should allow fresh membership to all Investment Banks. Investment Banks have not allowed to act as a broker on the stock exchange. ~~This issue is under discussion with the Corporate Law Authority- CLA and the MOF.~~

/ MWC

C) PROJECT FINANCING ACTIVITIES:

i) Issue of Short and Long-Term Participation Term Certificates-PTC's and Term Finance Certificates-TFC's:

This activity has been allowed under Section 5. (b) (vii) and 5. (c)(xi) of the SRO. As per the definition of redeemable capital in Clause 30-A of Section 2. of the Companies Ordinance 1984, redeemable capital includes TFC's.

The problem facing Investment Banks in this respect is that under Section. 120 of the Companies Ordinance, a company can issue any instrument in the nature of redeemable capital in favour of Schedule Banks, Financial Institutions or other persons as may be specified for the purpose by the Federal Government by notification in the Official Gazette.

The term 'Financial Institution' has been defined in Clause 15-A of Section. 2 of the Companies Ordinance . This term means "a Financial Institution set-up and controlled by the Federal Government or a Provincial Government or a corporation set-up or controlled by such government" and includes such other institutions or companies as the Federal Government by notification in the Official Gazette specifies for the purpose.

As an Investment Bank is neither a Schedule Bank nor a Financial Institution, companies governed by the Companies Ordinance cannot issue a TFC in favour of an Investment Bank. Therefore, an appropriate notification to this effect is required under Section 2. (15-A) and Section 120. of the Companies Ordinance 1984.

ii) Guaranteeing and Counter-Guaranteeing Loans and Obligations:

The Section 5. (c) (xii) allows Investment Banks to undertake guaranteeing business. The problem faced in this activity is that, the large public sector corporate institutions, which are a major component of our target market resist the acceptance of guarantees issued by an Investment Bank. This follows from the absence of Investment Banks in the definitions of the Companies Ordinance 1984. Financial Institutions according to the Ordinance are only Schedule Banks and DFI's. Therefore, it is required that Investment Banks should be defined in the Companies Ordinance 1984.

Other Problems.

1) Unregulated Competition:

The Investment Banks are working in an extremely regulated environment. The activities of Investment Banks are specifically defined in the SRO No. 585 (I)/87 and each activity is restricted in terms of percentages of the liquid net worth or such other ratios. Whereas, on the other hand, the activities of Leasing and Modaraba Companies are not defined under any government regulation. Due to this they are doing all Investment Banking activities without any control limits. They are investing in shares, discounting bills, giving margin loans, accepting large deposits & lending them out without any government control.

As a result of this lack of control and their high earning rates, Modaraba and Leasing Companies are easily able to undercut Investment Banks in rates and limits of assistance that can be offered to clients.

Therefore, Modarabas should be either disallowed Investment Banking Activities or if Modarabas are to be allowed to do all Investment Banking Activities, they should be governed by specific regulations that should define their activities and similar limits in each activity should be applied to them as are applicable to Investment Banks. This will atleast bring Investment Banks, Modarabas and Leasing Companies on the same footing.

Dealing in Foreign Exchange Through Letter of Credit Business:
Leasing Companies along with CBs are involved in the Letter of credit business. As this activity has a lot of potential in term of development of a customer base, and profitability, Investment Banks should also be given the opportunity to operate in this business.

Definition of Investment Banks should be Incuded in all Government Notifications, Regulations, Acts and Laws:
As Investment Bank is a new terminology, all previous government laws, acts and notifications need to be updated. At every place where the words Schedule Banks (Commercial Banks) and Development Finance Institution are used, the word Investment Banks should be added. This addition will solve many problems that Investment Banks might face in the future while dealing its clients (individuals, Public sector and Private sector Companies, Ministries and all other Government offices).

ANNEXURE 5

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STRICTLY CONFIDENTIAL

FOR EPRU AND US AID ONLY

QUESTIONNAIRE

Interbank will commence business only after floatation of its shares on the Stock Exchanges. The ideas below will be subject to the test of the market and the regulatory environment, and therefore susceptible to substantial change and development.

How do you view the role of your Investment Bank (IFB) in the Financial Sector ?

As a private sector force we will exploit existing opportunities and seek to establish profitable new areas of business. Given liberalisation of the market and the setting of a regulatory framework conducive to capital market activities, we hope to be a leader in new areas and in the introduction of new products in Pakistan, thereby providing a substantial broadening of the financing options available to the corporate sector.

Please list the Products and Services your IFB proposes to offer.

Assistance in floatation of companies including underwriting of issues.
Arrangement and provision of short and long term finance through paper issues, musharias and mark-up arrangements.
Market making in corporate and government paper.
Money market, treasury and foreign exchange activities.
Corporate and project advisory work.
Floatation of modarabas and mutual funds.
Introduction of investors and capital to Pakistani investment opportunities.
Loan and equity syndication. Leasing.

What other Products and/or services would you ideally like to offer ?

Do You see competition from other institutions such as Nationalized Commercial Banks, Private Foreign Banks, Development Finance Institutions and Leasing Companies or Modarabas etc ? How ?

If conditions permit our securities issues to develop well, the nationalised and foreign commercial banks will under present interest rate conditions be capable of competing through rate reductions. Modarabas would be competition if a sufficient number were established, given their advantageous tax status.

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Do you see any Policy constraints in the present charter that the IFBs have been granted ? (e.g needless overlap with functions of DFIs, NCBs etc.)

The present charter is a brief guideline (as per SRO of 13 July 1987). The regulatory and legal framework presently constrains at every step as the SRO has no effect in terms of changing this environment, e.g. the approval process of capital issues, ability of investors to hold issues, stamp duty considerations, etc.

Could the above mentioned issues be streamlined by Ministry of Finance and/or State Bank of Pakistan ? Please suggest how ?

Yes. General approvals should be granted to the Investment Finance Companies to undertake issues on behalf of clients on their own books or by placement in the market. In those areas where the regulator wishes to retain specific control, there should be a "one window" swift approval process, which allows a transaction to proceed before market conditions change.

Have you been able to carve out a niche within the present guidelines ? If so, what do you see as your competitive advantage ?

We have not yet commenced business. Our advantage will be that we are a streamlined professional body with access to and knowledge of other markets and products, capable of introduction in Pakistan.

How can IFBs be encouraged to compete with NCBs and other Financial Institutions on a level playing field ?

1. IFB's must have access to the money markets as any financial institution (currently denied by the State Bank).
2. IFB's must have authorisation as FX dealers.
3. IFB's must be eligible for the remedies available to banks in cases of default.
4. IFB's must be able to take, hold and make markets in all kinds of paper without restriction or impediment.
5. IFB's should be permitted to raise funds for periods of less than 30 days.

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What Financial Incentives could promote the above mentioned without disturbing the competitive environment of the private sector ?

Companies could be encouraged to raise funds by way of paper e.g. "Form 1" limits short term borrowings. If paper were excluded from this limit or incorporated as a sub-limit, this would encourage entry by companies, help develop markets and create liquidity. Liquidity of paper will allow companies to productively invest short term funds (less than 70 days) representing a real boost to the emerging capital markets.

Elimination of stamp duty on IFB paper products.

What procedure did you follow in obtaining a license to operate an IFB ?

Submission of application through appropriate channels, supported by substantial written and verbal exhortation.

What was the time lapse between application and approval for the setting up of the IFB ? Could you suggest ways to reduce the time involved.

Approximately 2 years. One window apolitical approval process.

Were there any other constraints ? Please elaborate.

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What is the ownership structure of your IFB ?

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How did you go about selecting appropriate partner(s) ?

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Do you have a Private Foreign Bank as a partner ? Please also indicate if the Bank already had a representation in Pakistan.

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What rules and regulations govern IFB equity holders with respect to repatriation of profits ?

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Please feel free to use this space for any additional comments.

Thank You for your time and consideration!

ANNEXURE 6

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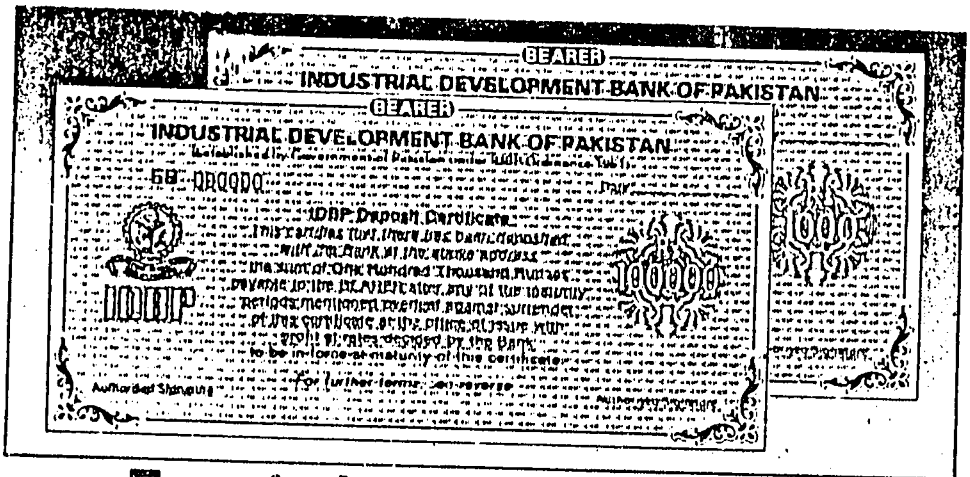
IDBP
Deposit Certificates (IDC)



Easy to buy - Easy to cash With Highest Profit Rates.

A prosperous future is in your hands when you're a holder of an IDBP Bearer or Registered Certificate. Irrespective of denomination, Rs 1000/- or Rs. 100,000/- I.D.B.P. Deposit Certificates offer you the following benefits which really make your investment worthwhile.

- **Highest profit** – Maximum expected yield of 14.25% per annum
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- **Ease of transfer** – Bearer certificates are transferable to others as cash
- **Acceptable as collateral** – By banks and financial institutions for short-term financing
- **Convenience** – Simple procedure for purchase and encashment

Maturity from date of issue	Expected Profit rate
5 years	14.25% per annum
4 years	13.75% "
3 years	12.75% "
2 years	12.25% "
1 year	11.75% "
6 months	10.75% "
3 months	9.25% "
1 month	7.00% "

So, why settle for anything less, when you can get so much more with IDBP Certificates.

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Invest in IDBP Deposit Certificates.

IDBP.7-90 PIO Islamabad

R-LINTAS

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ANNEXURE 7

ATTENTION

IDBP DEFAULTERS

ALL IDBP clients whose accounts are in arrears are well advised in their own interest to clear IDBP dues by June 30, 1990, failing which their credit facilities may be frozen by the nationalised banks under the instructions of PBC. The defaulters will not only become liable to be black-listed by the IDBP for any future credit facilities but may also be deprived of support and facilities from the Federal/Provincial Governments and their allied agencies.

IDBP.6-90 R-LINTAS

ANNEXURE 8

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QUESTIONNAIRE

How do you view the role of your Investment Bank (IFB) in the Financial Sector ?

Please list the Products and Services your IFB proposes to offer.

What other Products and/or services would you ideally like to offer ?

Do You see competition from other institutions such as Nationalized Commercial Banks, Private Foreign Banks, Development Finance Institutions and Leasing Companies or Modarabas etc ? How ?

Do you see any Policy constraints in the present charter that the IFBs have been granted ? (e.g needless overlap with functions of DFIs, NCBs etc.)

Could the above mentioned issues be streamlined by Ministry of Finance and/or State Bank of Pakistan ? Please suggest how ?

Have you been able to carve out a niche within the present guidelines ? If so, what do you see as your competitive advantage ?

How can IFBs be encouraged to compete with NCBs and other Financial Institutions on a level playing field ?

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What Financial Incentives could promote the above mentioned without disturbing the competitive environment of the private sector ?

What procedure did you follow in obtaining a license to operate an IFB ?

What was the time lapse between application and approval for the setting up of the IFB ? Could you suggest ways to reduce the time involved.

Were there any other constraints ? Please elaborate.

What is the ownership structure of your IFB ?

How did you go about selecting appropriate partner(s) ?

Do you have a Private Foreign Bank as a partner ? Please also indicate if the Bank already had a representation in Pakistan.

What rules and regulations govern IFB equity holders with respect to repatriation of profits ?

Please feel free to use this space for any additional comments.

Thank You for your time and consideration!