



## Analysis of Islamic Capital Market-Products and Challenges- A Case Study of Pakistan

**Issue:** <http://www.al-idah.pk/index.php/al-idah/issue/view/38>

**URL:** <http://www.al-idah.pk/index.php/al-idah/article/view/834>

**Article DOI:** <https://doi.org/10.37556/al-idah.041.01.0834>

### Author(s): Imran Abdul Aziz

PhD Scholar, Shaikh Zayed Islamic Centre, University of Karachi, Pakistan Email: [Imran.shakir@hotmail.com](mailto:Imran.shakir@hotmail.com)

### Abida Parveen

Director Sheikh Zayed Islamic Centre, University of Karachi, Email: [dr\\_abidashams@yahoo.com](mailto:dr_abidashams@yahoo.com)

### Azam Ali

Shaikh Zayed Islamic Centre, University of Karachi, Pakistan Islamic Banking Department, State Bank of Pakistan, Email: [Azaminceif@gmail.com](mailto:Azaminceif@gmail.com)

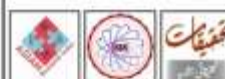
**Citation:** Imran Abdul Aziz, Abida Parveen and Azam Ali 2023. Analysis of Islamic Capital Market-Products and Challenges: A Case Study of Pakistan. Al-Idah . 41, - 1 (Jan. 2023), 1 - 16.

**Received on:** 13 – Sep - 2022

**Accepted on:** 10 – Dec - 2022

**Published on:** 15 – Jan - 2023

**Publisher:** Shaykh Zayed Islamic Centre, University of Peshawar, Al-Idah – Vol: 41 Issue: 1 / Jan – June 2023/ P. 1 - 16.



**Abstract:**

*Global financial meltdown-2008 brought attention of states and market participants towards asset based Islamic Financial System (IFS). Global financial crises-2008 was not only the debt crises but actually it was the collapse of conventional system that caused surge in Sharia complaint products demand by many folds from every corner of the world. Pakistan where Islamic banking started to come in limelight after 2001 when old Islamic banking procedures were announced NULL and VOID by sharia court and SBP set new road map for next 20 years for Islamic Banking in Pakistan. Islamic Capital market (ICM) also started its growth with rising Islamic bank (IBs) deposits and financing. This paper investigates the ICM products to maximize its growth and challenges. This study is based on review of previous papers and analysis of available data on ICM business from annual reports of PSX, NCCPL, CDC, SECP and PSX brokers. The study found that it is still needed to work for the sustainable growth of ICM in Pakistan as the sector has witnessed very low growth Specially equity market as compared to improvement of IBs during last 8 years.*

**Key Words:** *Islamic Capital Market, Products, Challenges GFC-2008, IFS, IBs, Pakistan*

**JEL:** *G01; G2; G21; G28*

**Disclaimer:** *This study represents the opinion of the authors, with responsibility of all errors and omissions and does not represent the opinion of their Institution & neither its faculty nor officials' position.*

## 1.0 Introduction

Capital Market is always a backbone of economy and barometer for any country to see its economic performance, political stability and confidence of its business community over policies. Capital market is a place where businesses/sponsors can fulfil their financial needs either in equity or debt form. It is also a place where investors can find investment opportunities either in ownership or debt-based form. Pakistani capital market has shown tremendous growth during last 20 years where it has passed the journey from KSE-100 1273 Index level (December-2001) to 53127 index level during 2017 (44596 till December 31, 2021) and market capitalization reached at its peak \$85bn (2017) from \$5bn (December-2001). Despite this remarkable performance, Capital market has not shown growth in terms of Account holders (UIN), Number of listed companies, FIIs portfolio investments and foreign brokerage houses and AMCs. Earlier, mostly people were avoiding to take exposure in stock market due to non-availability of any sharia products. But even introduction of sharia-based products based on decision of sharia scholars (Fatwa from all school of thoughts), failed to bring investors at large, mainly due to lack of awareness, confidence on capital market and attractive returns in property market due to easy parking option of black money (Still there is a much difference between documented property value and market value of property). This has restricted the growth of both conventional

and Islamic Capital market despite tremendous growth in Islamic Banking in Pakistan, since 2001 till now. During the same period, deposits of IBs touched 18.7% (June-21) and assets reached at 17% (June-21) of total deposits and assets of banking sector respectively but due to absence of “road map” in capital market (SBP came with proper road map for IBs during last 20 years to achieve IBs target), none of the major targets achieved either on conventional side or Islamic Capital market side specially in equity market

Table-01-Islamic Banking at a Glance								
							CAGR %	CAGR %
	Dec-03	Dec-06	Jun-10	Jun-14	Jun-17	Jun-21	FY17-21	FY14-21
Deposits (in PkR bn)	8.3	83	330	932	1720	3822	22.1%	22.3%
% of Banking Industry	0.4	2.8	6.4	10.6	13.7	18.7		
Total Assets (inPkR bn)	12.9	118	411	1089	2035	4797	23.9%	23.6%
No of Branches	17	150	667	1335	2320	3583	11.5%	15.1%
No. of Islamic Banking Institutions	1	6	19	22	21	22		
Source: SBP-Islamic Banking Bulletin								

Though not much work has been done on development of Islamic Capital Market in Pakistan, the rising interest from local investors in ICM requires much attention of the government, regulator and scholars. ICM can not only give sharia-based opportunities to investors but can also play vital role in economic development and reduce dependence on conventional financing (Riba based Economy). This research helps all stakeholders to bring development and growth not only in ICM but also for the overall capital market.

This study on Islamic Capital Market in Pakistan, needs a lot of aspects to cover specially, rules and regulations, product innovation and development, taxation matters and integration between market players and regulator. However, activity/volumes remained the major concern at PSX since long time especially after 2008 crises. For detailed analysis, we need to consider lessons from regional markets and research by other scholars on international markets.

### 1.6 Problem Statement:

GFC-2008 imposed negative impact on strength and growth of financial markets specially Riba Based financial Sector. The researchers and market players identified the drawback of non-Islamic business and appreciated asset backed financial system in light of their less effected growth as compared to their counterpart. This is the problem to identify the reasons of good performance of Islamic Financial System as compared to conventional system. Despite the justification of Islamic System, ICM in Pakistan do not depict the growth in their business as IBs do

### 1.7 Objectives of the study:

- To provide overall idea about ICM
- To draw attention to the current position of ICM in Pakistan
- To identify the problems related with operation of ICM in Pakistan

- d) To provide suggestion and make recommendations to take up-to the level of IBs in Pakistan

### **1.8 Research Questions:**

Q-01: Why ICM specially equity Market has not posted growth as IBs in Pakistan mainly during last 8 years?

Q-02 Why there is no full fledged sharia-based brokerage house operational in PSX?

Q-03 Why number of investors are not rising in Pakistan despite introduction of sharia-based products?

### **1.9 Hypothesis:**

H1: ICM growth specially in equity market in Pakistan is not in line with IBs growth during last 8 years.

H0: ICM growth in Pakistan is in line with IBs growth specially in equity market during last 8 years.

H1: Full fledged sharia-based brokerage house operation is not possible in Pakistan in current scenario

H0: Full fledged sharia-based brokerage house operation is possible in Pakistan in current Scenario

### **2.0 Literature Review:**

Bekaert and Harvey (2018) explained the relationship the importance of capital market that in a country that restricts its capital markets will not only keep away foreign investors but it will negatively impact on local companies that will reduce the growth. He further added that it would make difficult for local companies to compete in global markets. However, Abduh and Sukmana (2013) revealed that there is no evidence found of co-integration between conventional market and economic growth in Malaysia. But they found co-integration between ICMs and economic growth. Moreover, they added that there is bidirectional relationship between Islamic Stock Market and economic growth. (Geert Bekaert, 1998)

Alhabshi (1994) suggested that there should be equitable distribution of Income and wealth in business and economics, so that no one suffers from any form of injustice and loss. He also mentioned about ICM that it must be without interest-based transactions, absence of gharar and not dealing with companies who are involved in unlawful activities. Nienhaus (2014) explained that expectations are that Islamic finance is superior to conventional finance because it is based on a comprehensive worldview and tied to religious norms and values. He further added that as a consequence, it is expected that Islamic finance promotes economic development better than the profit-driven conventional finance. Herzi (2010) defined that ICM represents an assertion of law in capital market where Riba (Interest), Maisir (gambling) and Gharar (ambiguity) must be avoided and prohibited.

Ali (2008) identified the rising interest of Islamic Economics and Finance in developed countries like North America and Europe, where universities are offering funding and support for researchers in both areas of subject, as the interest in Islamic finance is

growing rapidly due to large Muslim minorities in these areas. He further added that the number of prestigious institutions, such as Harvard, Rice, and Durham have thus come to house budding Islamic finance researchers. Ayaz et al (2019) explained that ICM is a part of the overall CM and they function as an equivalent market to the conventional CMs. ICMs work parallel to their conventional counterparts and need to be strengthened and developed quickly / widely in countries under study because of Muslim population in majority. They further said that ICMs work as a fundamental part of the Islamic banking system in growing and expanding the Islamic financial market in Pakistan

Masoud Ahmed et al (2019) emphasized that as a part of the Islamic financial system, ICM plays a significant role in offering different modes of financing and investment options to individuals as well as corporations. They further explained that it helps investors to find Shariah compliant investment opportunities and also works parallel to the Conventional Market. They highlighted that the important role of Islamic Capital Market in economic development has not really been exploited especially in developing countries. Anwar (1995) emphasized that market operations of ICM should be done in a way that public is convinced of their consistency with the Islamic norms of Adl.

## 2.1 Summary of Literature Review

Author(s) name	Title of the study	Variables of the analysis
Geert Bekaert, Campbell R. Harvey	Capital Markets: An Engine for Economic Growth	Variables: Stock Market Development and Economic Growth. <b>Stock Market Development Measures:</b> Market Capitalization, Value Traded, Turnover Ratio. <b>Market Openness Variables:</b> Investible % in country, % investible in global, Exchange Rate Regime
Muhamad Abduh, Raditya Sukmana	The Role of Stock Markets in Promoting Economic Growth in Malaysia: Islamic vis-à-vis Conventional	ARDL model regresses a dependent variable over its own past values, besides present and past values of a number of exogenous variables
Datuk Dr. Syed Othman Alhabshi	Development of capital market under Islamic	Literature Based

	principles	
Ahmed Abdirahman Herzi	An overview of Islamic capital market in Malaysia	Literature Based
Dr. Mohammad Ayaz Dr. Talat Hussain Dr. Hassan Shakeel Shah Majid IqbalMohammad	Islamic Capital Markets and Economic Growth: A Comparative Study of Pakistan, Malaysia and UAE	ARDL Test Variables: GDP Growth Islamic Market Capitalization, Total Newly issued Securities
Masoud Ahmad Md. Mahmudul Islam, Abdullah Mohammad Ahshanul, Mamun Mohammed HasnathZabed	Islamic Capital Market (ICM) in Bangladesh: Products, Regulations and Advancement	Literature and studies based
Volker Nienhaus	Islamic Finance and Economic Development	Book Chapter Book Name: Islamic Finance and Development
Sumaira Ghafoor, Irum Saba, Rehana Kouser	Sukuk Issuance in Malaysia: Lessons for Pakistan	Literature Based Paper
Muhammad Anwar, Syyid Tahir	An Islamic Perspective on Capital Marketsand "Islamic" Securities in Malaysia	Literature Based Paper

## 2.2 Methodology

Maximum data has been gathered from secondary sources. So the researcher's work is based on published information and data available in any form such as newspapers, journals, books, magazines etc. devoted to ICM sector. Secondary data has been taken out from the websites of Pakistan Stock Exchange (PSX), Securities and Exchange Commission of Pakistan (SECP), Central Depository Company Pakistan (CDC Pakistan), National Clearing Company Pakistan Ltd. (NCCPL), Mutual Funds Association of Pakistan (MUFAP) and State Bank of Pakistan (SBP). The present study is mainly qualitative in nature. It is based on a comprehensive review of articles focused on ICM; gathering and analysis of secondary data. The secondary data have critically reviewed and discussed by using statistical techniques like averages and by analyzing data.

### 3.0 Analysis and Findings

#### 3.1 ICM Products and Current Status

Islamic Capital market posted reasonable growth during last 20 years since re introduction of Islamic Banking in country. During the period under review, growth witnessed from all areas of ICM due to rising demand especially after 2008 financial crises where global and local market participants realized the weaknesses of conventional markets and almost collapse of financial markets due to absence of asset backing of financial contracts.

#### 3.2 Types of ICM Investment Products

##### 3.2.1 Islamic Mutual Funds

Assets Management companies' business have grown tremendously since last 20 years. AMCs backed by banks brought huge assets under management from both sides i.e. corporate and individuals. Surge in AUMs was mainly behind due to a) technical and professionals' team at AMCs b) marketing and awareness at large scale specially for retail investors c) Relaxation in CGT during past years for long time d) tax rebate for individuals e) offering sharia based products under supervision of certified sharia advisors f) availability of different type products (equity based, index based and fixed income based).

AUMs touched almost PkR1,018bn in 2021 from PkR354bn in 2012. However, major growth witnessed in sharia based funds ( up 9x Vs 2x of conventional Funds) during last 10 years as earlier most of investors were reluctant to invest in stock market due to non-availability and lack of understanding of sharia based funds.

**Table-02 : Mutual Funds in Pakistan**

PkR bn		2021	2012	Times (X)
Sharia		420	48	9
Conventional		598	306	2
<b>Total</b>		<b>1018</b>	<b>354</b>	3

Source: MUFAP Annual Report, 2021

Islamic Funds invest same as conventional funds do except a) only invest in sharia complaint stocks b) avoid intraday trade as it is not permissible by sharia advisors on sharia grounds. AMCs are not offering only pure equity-based sharia complaint funds but also asset allocation funds, cash funds, index funds, income funds and sector-based Funds that attracted investors from masses.

##### 3.1.2 Sharia Complaint Securities

Sharia complaint securities have not shown satisfactory growth in terms of number during last 6 years since the launch of KMI All share index. Listed companies are not incentivized to keep themselves sharia complaint except they can attract more investors when they are raising money from equity market either at the time of IPO or via right issue. More investors in capital market also means higher valuations in both cases either IPO or secondary offering. With the passage of time, Al-Meezan group with the help of Al-Meezan Investment Management

Limited created more awareness among investors about fulfilling requirements of sharia Complaint Company. Sharia complaint securities reached to 256 till mid of 2021, since the issuance of 225 eligible securities listing November 2015 (sharia complaint ratio to eligible securities reached at 63% from 54%)

**Table-03: Percentage of Sharia Complaint Securities**

	2015	2021	Increase/(Decrease)
<b>Sharia Complaint Securities</b>	225	256	<b>31</b>
<b>Total Eligible Securities</b>	431	402	<b>-29</b>
<b>% of Sharia Complaint Securities</b>	<b>52%</b>	<b>64%</b>	

**Source: Meezan Bank Website**

**: PSX Website**

### **3.1.3 Islamic ETFs:**

First ETF was introduced in 2020 in capital market as PSX was missing this demanding product which gave timely investments at lower cost to investors than Mutual Funds as MFs charged little higher front end and back-end load than ETF (First two ETFs namely UBL Pakistan Enterprise and NIT Pakistan Gateway on March, 2020). Another major benefit in ETF for investors, its timely investment in asset class than MF, which invest as per cut off timing rules. So far four (till June-21) ETFs have been introduced, only 1 is sharia based i.e. Meezan Pakistan Exchange Traded Fund.

### **3.1.4 Murabaha Share Financing-MSF:**

Long time demanding product from investors side, SECP Sharia Advisory Board (SAB) finally with the consultation of stakeholders approved sharia-based financing product for share financing in its meeting held on August, 2018 with certain amendments. The SAB approved the final product with the conditions that NCCPL will appoint a full time Shariah Advisor who will ensure ongoing Shariah compliance of the transactions and will issue its Shariah review report periodically. However, after putting great efforts by CDC and NCCPL, product implemented on September, 2019. Though, it is still not much in practice due to lack of awareness and lesser marketing about product from brokers. However, availability of sharia-based financing product will bring more retail investors interest. Till June 2022, one or two financiers are active in MSF with negligible amount, that shows the level of acceptance of product by participants. Even conventional leverage products are not catching investors, not only because of its non-sharia nature but due to falling interest of retail investors in equity market.

### **3.1.5 Sharia complaint indices:**

PSX introduced sharia complaint indices not only for using as benchmark or selection of sharia complaint stocks, but also for purchase of index-based companies (investment in index in one go by using basket order option). These

indices are KMI-30 and KMI All share index. KMI-30 was introduced in 2009, taking base year as 2008 while KMI All was introduced in 2015. Earlier only conventional indices options were available for investors. At the time of introduction almost 225 companies were the part of KMI All share index but now 256 companies are the part of KMI All share index. Most of Islamic mutual funds are using KMI-30 index as their benchmark performance.

### 3.1.6 Sharia complaint brokerage house:

Despite having more than 200 active TREC-Holders (Brokers) in Pakistan, almost no single broker is full fledged sharia complaint brokerage house. However, few of them are providing limited window-based operation. Almost all areas of conventional financial markets are offering full fledged separate company based (or product based) Islamic services either banks (via Islamic banks), insurance (via Takaful), Mutual Funds (Islamic Mutual Funds), Asset Management companies (Islamic AMCs), Stocks (Sharia complaint stocks) or Bonds (Sukuk) and their sharia based products are giving them higher growth/returns than conventional products. But there is no single full fledged brokerage house who can claim itself a sharia based brokerage house at PSX as feasibility/existence of conventional brokerage house is at stake specially during last 5 years since 2017 mainly due to low volumes. This can also be visible in ROEs of selected leading brokerage houses since 2014.

**Table-04: Selected Conventional Brokerage Houses (10 Brokers)- Average ROEs:**

										FY14-21	FY17-21
		FY14	FY15	FY16	FY17*	FY18	FY19	FY20	FY21	Average	Average
<b>Average ROEs</b>		16.3 %	6.7 %	6.6 %	23.5 %	4.9 %	13.9 %	11.2 %	30.1 %	<b>9.5%</b>	<b>9.2%</b>

\* During FY17, Chinese Consortium bought PSX shares which gave one time gain to each TREC Holder that enhanced all brokers ROE.

Above data is showing that average ROE earned by broker is less than 10% even in conventional business which includes brokerage from all stocks (Conventional and Sharia stocks both), income from conventional leverage sources i.e. Margin Trading System (MTS) and Margin Financing System (MFS), Brokerage on Futures trading, Portfolio gains either sharia based or non-sharia based and Interest income earned on bank deposit. It is necessary to mention here that PSX introduced minimum brokerage structure and implementation started from October 14<sup>th</sup>, 2019 that helped brokers to earn the above ROEs. Otherwise, low trading volumes would have been resulting in massive losses except in FY21 where volumes rose massively during COVID period. So one can easily understand and expect the ROEs in the absence of some said non sharia sources of income in case of fully sharia based brokerage. Traded volumes and values are self-explanatory during the same period that how conventional business survival is difficult due to low activity at bourse.

**Table-05: Volumes and Value Traded at PSX**

	<b>FY13-17</b>	<b>FY18-22</b>	<b>Change %</b>
<b>Avg Value Traded (in bn)</b>	12,814	14,625	14.1%
<b>Avg Volume (in mn)</b>	294	362	23.1%

FY21 was exceptional year when highest ever volumes witnessed during Covid in last 10 years

Source: Zakheera

Low growth in volumes and traded value is also due to low penetration of stock market among the general public as mostly people believe about stock market is a place of gambling and it is the place where people lost their wealth. However, government also failed to attract general public in the stock market due to over-regulation at capital market compared with property market, where source of income/Funds is not asked for full price of asset. It means if investor is buying PkR100k shares in stock market, here he has to show the sources of funds for full amount. However, in property market, asset market value is PkR100k but sources of funds will be asked not more than 20% to 30% of the asset value (Due to difference between documented value and market value of asset). Even CGT rates are much low for property market than PSX despite much documented sector than property. Most of property players trade in property during the development phase where files moved (buy and sell) from one to another without any record to government, that saved their CGT as government doesn't have any record of that property. In all these circumstances, why one investor would take entry into PSX?

**Table-06: Status of brokers and investor at PSX**

<b>Brokers and Investors Status</b>			
	<b>FY14</b>	<b>FY21</b>	<b>8 Year CAGR %</b>
<b>*No. of CM Brokers</b>	490	203	-287
<b>**IAS Clients</b>	51000	64758	3.5%
<b>Sub Accounts</b>	241000	282637	2.3%
<b>***UIN Active (Total)</b>	210451	257714	2.9%
<b>UIN Active (Individuals)</b>	202775	236801	2.2%
<b>Source: NCCPL/CDC Annual Reports and News Letters</b>			
<b>* No of brokers (Clearing Members -CM) have reduced by 287 during last 8 years</b>			
<b>** Investor Account Services</b>			
<b>*** Unique Identification Number which is assigned to every client to track its trade and transaction record</b>			

Survival of any business at below 10% ROE where inflation and Currency depreciation remained major concern (During last five years till June-2022 PkR depreciated against green back (USD) more than 13%) . Other businesses are making more than 10% ROE in the same period and even banking and insurance sector remained in the same range, so brokerage business would remain less attractive.

ROE Averages of all non financial companies									FY15-20	FY17-20
	FY14	FY15	FY16	FY17	FY18	FY19	FY20	FY21	Average	Average
Average ROEs	*NA	16.28%	13.77%	15.03%	13.72%	12.46%	8.52%	NA	13.3%	12.4%

**Table-07: Return on Equity of NFCs**

Source: SBP, Analysis of Non-Financial Sector\*Not Available

**Table-08: Return on Equity of average banks and Insurance Companies**

ROE Averages of Banks and Insurance Companies									CY14-21	CY17-21
	CY14	CY15	CY16	CY17	CY18	CY19	CY20	CY21	Average	Average
Banks	16.62%	17.62%	15.99%	13.21%	12.09%	12.84%	15.91%	15.86%	15.02%	13.98%
Insurance	15.08%	18.30%	12.64%	12.51%	10.87%	12.02%	13.74%	16.35%	13.94%	13.10%

Source: SBP Analysis of Financial Sector

Though, it has been observed that some of investors tried to work on sharia-based brokerage house but failed to continue or implement it. Following are the reasons

- Listed companies are declining by way of delisting and merger. To remain listed, companies do not feel any benefit to keep posting and sharing everything with investors and public
- Intraday trade is not allowed as per Islamic principles and most of the PSX business is more than 60% to 70% business is intraday trade at PSX and investors/brokers missed that opportunity who wants to earn sharia-based income.
- Volumes at PSX are very much volatile and dependent upon economic and political situation. And Pakistan remained under turmoil after every one or two years that affect volume and business activity. In this situation, most of conventional brokerage businesses are not making reasonable ROEs (as mentioned above) so one cannot expect to commence full-fledged sharia-based brokerage business.
- Investor base is too low, only 65k IAS accounts (Both Individual and Corporate) and 237k UIN for individuals till June 30, 2021, which is very low in terms of total population (less than 0.15%) where as in India it has reached now almost 8% (100mn accounts till Mid-September, 2022 after introduction of DEMAT Accounts as per CDSL (Central Depository Services Ltd., India)
- Pakistani Financial market is over regulated where investors are asked at each and every stage of participation. Since account opening to operation, individuals/Corporate clients both felt that it is like we are under investigation and sharing our personal information without any justification as these information and documentation is not required in any other market specially Property and buying Gold. Even most of the time brokers and Exchange companies lost their businesses due to over-regulation.

### 3.1.7 Islamic Sukuk :

Sukuk market has grown more than anticipation of anyone during last 20 years. Sukuk can be defined as “Sukuk, in Islamic finance parlance, refer to the ownership of claims against certain assets or a pool of assets. Technically, Sukuk are certificates of equal value that represent units (undivided shares) in ownership of tangible assets, usufructs (manfa'ah), and services.” (Sumaira, Irum and Rehana, 2018) Sukuk has brought much attention from IBIs, Islamic Funds and sharia based retail investors. Most of Islamic institutions IDRs remained at much lower level due to non-availability of sharia based fixed return investments product as conventional institutions have more options to invest in like PIBs and T-bills e.t.c. Pakistan issued first of its sovereign sukuk in international market worth \$600m during 2005. However, in 2006, issued first of its local Sukuk. ICM in Pakistan witnessed major breakthrough when country issued 31 Sukuk valuing PkR821bn, this is the highest ever yearly sukuk issuance in a single year both in terms of numbers and value. However, out of PkR821bn, major chunk was contributed by Government of Pakistan (GoP) Ijarah Sukuk amounting PkR736bn. The year 2020 remained at second highest in term of value when PkR806.4bn was raised in a single year.

**Table-09: Status of sukuk in Pakistan-2021**

Listing Status	Number of Issue	Rs. in billion
Privately Placed	153	2851
Listed	19	311
<b>Total</b>	<b>172</b>	<b>3162</b>

**Source: IIFM-2022**

**Table-10: Sukuk Structures in Pakistan**

Sale Based	Lease based	Partnership Based	Agency Based
a) Bai' Bithaman Ajil b) Murabha c) Salam d) Istisna	a) Ijarah b) Ijarah Bittamlik c) Ijarah Mawsafah-fi-Dimmah	a) Mudarbah b) Musayarakah	Wakalah bi Istithmar

**Source; Sukuk Issuance in Malaysia: Lessons for Pakistan. Sumaira Ghaffor. 2018**

### 4.0 Challenges and issues with ICM

- Acceptance of sharia compliant products at masses as pure interest free halal products
- Lack of awareness of capital market among general public. Most of rural areas have no access to capital market easily.
- Listings of companies is still a major challenge as most of businesses still do not want to share or declare wealth and profits with general public. So investors didn't get opportunity to invest in attractive businesses like superstores, restaurants, theme parks e.t.c

- d) Investors confusion remained there over sharia compliant stocks as KATS (Trading system of PSX) not giving direct indication that particular stock is either sharia complaint or not. Investors kept asking to their brokers about sharia complaint stocks
- e) Different opinions of sharia advisors over sharia complaint stocks, whether some stocks are sharia or not.
- f) As highlighted by Sumaira et al (2018) that the presence of an active secondary trading market plays a pivotal role in the success of any securities market. So, Pakistan needs to encourage the issuance of Sukuk with varied maturities, credit qualities, currencies and risk profiles as a result, the investors would have different choices in the Sukuk market

#### 4.1 Discussion on Findings

S.NO	Questions	Findings/Answers
1	Q.1- Why ICM specially equity Market has not posted growth as IBsin Pakistan during last 8 years?	IBs Deposits have grown by CAGR 22.3% during last 8 years till FY21 (Table-01) but Sharia complaint securities (Table-03) and number of investors in ICM specially in equity market has grown by meager % during the same period (Table-05)
2	Q.2- Why there is no full fledge sharia-based brokerage house operational in PSX?	Following reasons, we found for non-existence of full fledge sharia-based brokerage house: <ul style="list-style-type: none"> <li>a) Existing conventional brokerage houses ROEs (Table-04) are lower than IBs and other business ROEs (Table-07 and Table-08).</li> <li>b) Lower activity at PSX specially during last 8 years (Table-05)</li> </ul>
3	Q.3-Why number of investors in equity market are not rising in Pakistan despite introduction of sharia-based products?	Mainly due to over-regulation. lack of awareness of PSX and absence of any incentives and under regulation of property market, caused lower growth in investor base

<b>4.2 Acceptance or Rejection of Hypothesis</b>		
Hypothesis	Decision	Reasons
H <sub>1</sub> : ICM growth specially in equity market in Pakistan is not in line with IBs growth during last 8 years.	Accept	As we have seen from the data that growth in IBs is much higher than ICM specially in equity market.
H <sub>1</sub> : Full fledge sharia-based brokerage house operation is not possible in Pakistan in current scenario	Accept	Lower ROEs of conventional brokerage house due to low volumes, over regulations and low investor base made it almost not possible to run sharia-based brokerage house by any investor. Even, sharia-based brokerage house has to leave some activities which conventional do. So with limited number of activities, their ROEs would be much lower than conventional brokerage houses

### 4.3 Conclusion

ICM in Pakistan has grown much more than anyone's anticipation during last 20 years but still a lot needs to be done on regulation, development and awareness front. Growth in ICM specially in equity market is much lower (specially in equity market) than the Islamic banking due to several reasons as we highlighted in paper. We have also found after looking at numbers of brokerage houses and lower growth in stock market volumes that full fledge sharia based brokerage house is not possible without bringing some products and improvements as brokers are already working at very low ROEs. Government with support of private sector should work to resolve these issues to achieve the desired growth in ICM. Last but not the least Removal of Riba from every aspect of business, should be the first priority of government and growth in ICM can play major role to achieve the target of Riba free Economy

### 4.4 Recommendations

- CGT rate should be lowered in sharia complaint stocks vs conventional stocks as incentive will improve interest towards ICM.
- SECP Islamic Capital market division should issue the list of sharia complaint stocks on its website on quarterly basis that will bring uniformity in practice for all participants and will give timely information to all of them.
- Awareness sessions must be arranged for both capital market and Islamic Capital Market for students, investors and general public.

- d) Banks and insurance companies should be incentivized to keep equity portfolio at a certain percentage in sharia compliant stocks like lower CGT rates or lower corporate tax.
- e) Intraday settlement or one hour settlement-based system should be introduced to start sharia based intraday trade which is not possible in normal settlement process due to rule of possession as buyer didn't get possession without settlement (Normal Settlement process is T+2days)
- f) Minimum commission rates have been introduced by PSX from 2019 that is applicable on all market participants. Introduction of tax rebates on commission expenses made on investment in sharia compliant stocks will bring more interest towards Islamic Capital Market
- g) Higher tax rebates should be introduced by investing in Islamic Mutual Funds than conventional Funds.
- h) Property market should be brought under same regulation mainly regarding requirement of white (taxed money) as property market required less white money than 50% of asset class but financial market needs 100% taxed money for investments

### References / Bibliography:

- Alhabshi, D. D. (1994). Development of Capital Market Under Islamic Principales. *Managing and Implementing Interest Free Banking/Islamic Financial System*. Kuala Lumpur, Malaysia.
- Ali Waris, H. A. (May, 2018). Sharia Screening Process: A Comparison of Pakistan and Malaysia. *Asian Journal of Multidisciplinary Studies*, 13-21.
- CDC Pakistan. (2021,2020,2015). *Annual Report*.
- Dr. Mohammad Ayaz, D. H. (2019). Islamic Capital Markets and Economic Growth: A Comparative Study of Pakistan, Malaysia and UAE. *Islamic Banking and Finance Review*, 40-58.
- Editorial. (2017). *Journal of Islamic and Business Managment*, 7.
- Geert Bekaert, C. R. (1998). Capital Markets: An engine for Economic Growth. *The Brown Journal of World Affairs*, Vol.5, No. 1, 33-53.
- Herzi, A. A. (2010). An Overview of Islamic Capital Market in Malaysia.
- Hussain, T. (2019). Shari'ah Issues in Islamic Capital Markets of Pakistan:A Case Study of Sukūk. *Journal of Islamic Thought and Civilization (JITC)*, 16.
- IIFM. (2022). *Sukuk Report*. International Islamic Financial Market.
- Management, P. S. (2021,2020,2019,2005). *PSX Annual Report*. PSX.
- Masoud Ahmad, M. M. (May, 2019). Islamic Capital Market (ICM) in Bangladesh: Products, Regulations and Advancement. *IOSR Journal of Business and Management (IOSR-JBM)*, 1-10.
- Md. Mukitul Hoque, M. M. (2014, December ). Islamic Banks' Stepping into Securities Business of Bangladesh: A Case of Islamic Bank Bangladesh Ltd. (IBBL). *International Journal of Ethics in Social Sciences Vol.2 No. 2*.
- MUFAP. (2021). *MUFAP Annual Report*. MUFAP.

- Muhamad Abduh, R. S. (2013). The Role of Stock Market in Promoting Economic Growth in Malaysia: Islamic vis-a-vis Conventional. *Global Reveiw of Islamic Economics and Business*. Vol. I No. 1.
- Muhammad Anwar, S. T. (1995). An Islamic Perspective on Capital Market and "Islamic " Securities in Malaysia. *Pakistan Institute of Development Economics, Islamabad*. Vol.34, No.4 , 865-878.
- Muhammad Ejaz Rana, D. W. (April, 2015). *Performance of Islamic and Conventional Stock Indices: Empirical Evidence from an Emerging Economy*. Lahore: COMSATS Institue of Information and Technology.
- Muhammad Zeeshan<sup>1\*</sup>, J. H. (2020). Conventional Mutual Funds Out Perform Islamic Mutual Funds. *International Journal of Economics and Financial*.
- NCCPL. (2021,2020,2015). *NCCPL Annual Report*. NCCPL.
- Nienhaus, V. (2014). *Islamic Finance and Economic Development*. Harvard Law School.
- SECP. (2021,2020). *SECP Annual Report*. SECP.
- Sumaira Ghafoor, 2. I. (Dec, 2018). Sukuk Issuance in Malaysia: Lessons for Pakistan. *Journal of Accounting and Finance in Emerging Economies*, 159-176.



**This work is licensed under a Creative Commons Attribution 4.0 International Licence.**