

“We can work together on improving the corporate governance and financial reporting standards in Pakistan”

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Richard Morin

Chief Executive Officer, Pakistan Stock Exchange (PSX)

ICMA Pakistan: Please tell us about your professional career?

Richard Morin: Managing the Stock Exchanges has always remained my passion. I started my career at a young age in Montreal Stock Exchange where I ran the whole gamut of responsibilities including stocks, options, futures operations, regulations, marketing and listing companies. I had fantastic eleven years there, then I went to Mauritius where I became the Chief Executive of Mauritius Stock Exchange. Being a French Canadian, I then moved to the French speaking West Africa to set up a regional Stock Exchange and Central Depository. I spent twenty years in Canada dealing in brokerage and wealth management until I got a call from Pakistan in 2017 that they were looking for a CEO of Stock Exchange. I decided to take arm the challenge to develop this capital market.

ICMA Pakistan: When you took this challenge what vision you had in mind for the growth of Stock market in Pakistan and how long it would take for Pakistan to stand at par with developed stock markets of the world?

Richard Morin: This is an excellent question. I start with the vision. I think that there should be at least 4 million retail investors on Pakistan Stock exchange and I say this because I look at regional peers in Bangladesh, India, Sri Lanka and Vietnam whose stock markets have large proportion of retail investors as compared to their population size and level of economic development. Bangladesh has two and half million retail investors; India 25 million investors and Vietnam with a population of 90 million have 6 million investors. The

population of Srilanka is 1/10th the population of Pakistan yet they have 700,000 investors. So if you extrapolate that to Pakistan's population, it should be 7 million so I think the vision is to have few million retail investors on stock market in Pakistan but how we get there is the real challenge. First of all, they need to be realized that coming to PSX would create wealth for them. PSX has provided to investors an annual return of 20 percent with dividend and capital gain included during past ten years which means that if anyone had invested one million rupees in PSX ten years ago, he would have around eight million rupees today so it is a fantastic investment story. Now we need to get that story out to retail investors and convince them to come to PSX to invest because no one else in Pakistan can provide similar returns. Real estate and saving bonds do not provide such type of return on investments. As these retail investors come to PSX they will not only create wealth for themselves but will also participate in capital formation and provide capital for Pakistani companies for their financing, business growth and job creation. Finally, for an economy to grow, you need stock exchanges which plays vital role in capital formation, wealth creation and economic development.

ICMA Pakistan: As a financial expert what strengths and weaknesses you witness in capital market of Pakistan as you earlier told that return is the major strength so beside that how would be the next numbers?

Richard Morin: I think Pakistan has made a lot of progress during last six years in modernizing its capital market which include initiatives like demutualization of Stock Exchange in

2012; adoption of a new and modern Securities Act in 2015; integration of three exchanges in 2016 and arrival of foreign strategic partners and the IPO in 2017. All these steps have altogether transformed and modernized the Pakistani stock market and form a strong basis on which PSX can build upon and consolidate its future infrastructure development and governance structure.

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Today, PSX is independent and it is becoming a professionally managed organization with an independent board. In all markets around the world, it has been truly shown that demutualization of exchange is important to develop and unlock the potential of capital market. We have got a core group of stock brokers who are very supportive of capital development in Pakistan and we are working hand-in-hand with this core group of brokers to bring Pakistan to the next level of development.

We have also got over 500 listed companies. Some say that the number should be higher and I tend to agree with them that there is a potential to list more companies but let not be shame with these 500 companies as it is a significant number if you compare that to other markets that are far behind. We may have issues in terms of liquidity and we can work making these companies more liquid. There is always a room for improvement in corporate governance standards and we will work with the listed companies to achieve this goal.

Now, looking at weakness or areas which need improvement, I would have to put top of the list the negative perception of PSX and perhaps that negative perception is in great part result of a level of investors' protection that could be better than what it was in the past. We have already improved our ability to protect investors in future, however, in the past it has happen too often that broker go to bankrupt and investor lose money as a result of broker's bankruptcy. Now, we have already taken measures and we will continue to implement these measures to improve investors' protection in Pakistan. We are going to strength the brokers' regulation framework so that we reduce the risk that the broker goes bankrupt. We can never eliminate completely the risk of broker going bankrupt but we can reduce it considerably. We have covered a lot of ground in that area and in collaboration with SECP we will continue to improve the framework in 2018 so that is one area.

Since we cannot completely eliminate the risk of broker bankruptcy, we will also improve and reform the Investors Protection Fund in Pakistan. We will eliminate the limit of 25 million rupees for broker that the investor protection fund can use to reimburse the investor that has lost money to a broker bankruptcy. We will eliminate that limit and replace it with the limit per investor and that is very fundamental. We want to be in a position to tell the investors that if they lose money because

their broker has gone bankrupt, the investor protection fund would make them hope up to stated limit, probably around 1 to 2 million rupees. We will have to define the precise number but between 1 and 2 million rupees would offer guarantee to investors.

ICMA Pakistan: Who is the sponsor of that Investor Protection Fund?

Richard Morin: The fund is currently an independent trust with its own trustees and administered by the PSX. I think that structure is correct so we can continue with that structure. We need to reform the mechanics of the fund again by eliminating the limit per broker and replacing it by limit per investor. The fund has significant resources available which is around three billion rupees in assets and those assets can probably be leveraged to provide the fund with additional financial resources if we need some. So I think we got the financial resources to improve investor protection in case of broker bankruptcy. The investor will find that they will enjoy a level of asset protection when they invest through PSX dot broker which is far better than what they enjoyed in the past. I think that is one of the issues we need to resolve in order to attract more investors in the market.

Another thing we need to do is to introduce new products in PSX to attract the 4 million retail investors, contrary to investors currently trading on PSX, as these 4 million investors are part of middle class Pakistan and they are not on market side and also they do not spend hours every week to analyze companies. We need to introduce simple investment products to attract these investors to stock market. One very appropriate product for these investors is mutual funds as you have seen mutual funds are growing at reasonable rate in Pakistan. So our priority is to list exchange traded funds which is like a mutual fund but that's traded on stock exchange like KSE-30 exchange traded fund offering same return as if you bought 30 stocks of KSE 30. So our priority product of 2018 is exchange trade fund.

ICMA Pakistan: What are the important macro-economic indicators that influence the stock market?

Richard Morin: A number of indicators would affect the stock market and this question may be better directed towards asset manager rather than an exchange manager. For a retail investor, the profitability of a company is more important so that he can receive regular dividends from that company. On the other hand, the company will be willing to generate profit in future so that it continues to pay dividends to investors. So as a Pakistan retail investor, this is what you should be looking for and hence this would be driving return in market in the long term. In the short term, other factors would affect the price of securities in the market; some of them are local factors such as political situation, balance of payment position. There are factors outside of Pakistan which will also affect the stock market. For instance,



Interview session with CEO, PSX Mr. Richard Morin. Interview panel included Mr. Aamir Ijaz Khan, Executive Director, ICMA Pakistan and Mr. Shahid Anwar, Director Research & Publications

if the Federal Reserve in US starts tightening its monetary policy, the global investors tend to repatriate their assets and bring them back to US. So we tend to see outlooks from the emerging markets. These external factors do affect investment flows which ultimately impacts the price of securities listed on PSX.

Here I would like to submit that as a retail investor these factors shouldn't affect your decision. If any foreign investor pulls money out of PSX and its share price tends to go down, I think the local investor should see it as a buying opportunity. If the price of stocks go down its just mathematical. The dividend yield goes up and you as a retail investor should be even more interested in these companies. So to summarize, a number of macroeconomic factors will affect the market and when these factors tend to push down the values of shares listed on PSX, the retail investor should see out the buying opportunity more than anything else.

ICMA Pakistan: What was stock market performance in 2017-18 in terms of KSE 100 index and market capitalization?

Richard Morin: I would prefer to talk in terms of calendar year rather than financial year because the world talks in calendar years. As I said before, past ten years, PSX has provided 20 percent annualized returns, however, some years were up and some years down. 2015 was about 2 percent; 2016 was an excellent year at 46 percent and PSX was one of the best emerging stock market in the world; 2017 was a down year with 15 percent whereas so far this year 2018 we are the best performing regional stock market and PSX is up by 5.6 percent on close of market yesterday while the average emerging market is slightly down by 1 or 2% in 2018. So you see variability; some years are average; some years are excellent and some years are negative and this happens in every country including the developed markets. So the retail investors should focus on long term return. The 20% return provided by PSX was unmatched by any other asset class such as savings and real estate.

As far a market capitalization of PSX is concerned, the current market capital stands at around Rupees 8.8 trillion.

ICMA Pakistan: What is your comment on measures announced for stock market in Federal budget 2018-19?

Richard Morin: The budgetary measures were generally quite positive. I think elimination of tax on bonus shares is a positive measure. Further, the proposed restrictions on the ability to buy real estate by non-tax filers would certainly help level the playing field between real estate and the stock market. Presently, the playing field is not level as you can invest in real estate without having to pay too much tax on your gains in real estate but on the stock market which is a formal economy, you have to pay withholding capital gains tax and dividend tax. By restricting the ability to invest in real estate by non tax filers, you re-establish the balance. I think that's a very positive measure in long term because one of the challenges we have in Pakistan is that such a large portion of the economy is informal. It is a

challenge for us to bring the money from the informal economy into the stock market.

We really look forward to working with the government to make them realize that capital market development is a long term project that requires that PSX, regulators, tax authorities and stock brokers should have a common vision on what need to be done to develop the capital market in long term. What we expect from the government is to provide a stable, predictable and conducive tax environment for stock market instead of taking adhoc measures. We must develop vision on the type of tax environment in terms of investment savings vehicles and their long term tax treatment. If we are able to put in place such as system that stays for next 20 to 40 years, that would attract money into our capital market and provide incentives for money that's seeping into the informal sector. I think more can be done to provide a conducive, stable and predictable tax environment for stock market.

ICMA Pakistan: What are the reasons for recent outflow of portfolio investment from PSX and do you think withdrawal of tax on bonus shares in recent budget would provide a boost to portfolio investment?

Richard Morin: Well, any economist or a broker or a portfolio manager would be the right person to answer this question.

Anyway, I think it is hard to make a connection between the performances of stock market with one or all of the tax measures that have been announced in the budget as the stock market is influenced by a innumerable factors including, as I mentioned earlier, the monetary policy in USA. All the emerging markets around the world are suffering from the fact that the Federal Reserve in USA is tightening its monetary

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policy and Pakistan cannot remain immune to these changes. You need to look outside Pakistan for what's happening. I think you also need to know about what's happening within Pakistan. The current political transition and the level of uncertainties surrounding that is probably a factor affecting our market and only when this uncertainty clears up and there is more clarity as to direction, I think that would have a positive effect on the stock market.

ICMA Pakistan: What initiatives are required for PSX to become one of leading stock markets in the world?

Richard Morin: Improved investors' protection and product development is our major area. After introducing exchange-traded funds, in 2019 we will be looking at launching the 'Index options' and 'stock options' products. We will also review our 'future products' to make them more in line with the best international practices.

We will look to offer more value-added services for listed companies on PSX such as advice on investor relations; corporate governance and compliance with financial reporting standards. These initiatives will be supported by major re-investments in organizational capacity at PSX. We are currently hiring a 'Head of Marketing and Business Development' which position did not exist at PSX before. We are also hiring a 'Head of Product Management and Research' specifically to focus and

dedicate resources to new products launchings. We will be investing in technology. By the end of 2018 or early 2019 PSX will have a new trading platform which would be best in class trading platform that would support current list of products listed on PSX as well as new products as I mentioned earlier. It would also provide best-in-class market 'surveillance platform' as well as best-in-class data platform. PSX produces a lot of data that is broadcast by Bloomberg so we would have better data vending platform for PSX.

We will invest considerable resources on investor awareness. We need to talk to 40 million middle-class Pakistanis that do not currently invest in PSX. It is important that not only PSX but also stock brokers and financial institutions must reach out to these prospective investors and encourage them to invest in PSX. The mutual funds companies and asset management companies are already doing that and we will do it with exchange trade funds.

ICMA Pakistan: How you foresee the stock market in next five years? This is relevant to your long term planning especially in context of coming general elections?

Richard Morin: I will not make any future prediction of stock market. However, as I already emphasized earlier, the investors focus should be on the long term investment in diversified portfolio of 15 to 20 stocks listed on PSX. They must keep the mutual fund and exchange traded funds on PSX for a long term that would do great for them. I have no idea what will the market do in one month, six months or in a year. A five-year investment would, however, be quite positive; ten years very confident and next ten years should be any less positive than the past ten years with 20 percent return. Companies listed on PSX are affordable in terms of price earnings ratio and dividend yield. I think the investment case for next ten years is very strong and we would all be surprised in next ten years for the same type of returns as in the past ten years.

ICMA Pakistan: Do you think CPEC will have any far reaching impact on stock market performance?

Richard Morin: I think PSX is an investment vehicle or mechanism for CPEC. We hope that in next few years we would see many CPEC projects being financed through PSX either through share offerings or through bond offers. We intend to play a role in CPEC initiatives as I believe that CPEC would have a role to help develop our capital market. We will grow along with that. CPEC will find financing on PSX which will help PSX to grow. In terms of performances what impact they will have I don't know but CPEC will help grow the market and provide investment opportunities for Pakistanis through PSX.

ICMA Pakistan: How management accountant can facilitate companies in IPOs process and enlistment at PSX?

Richard Morin: I think your role as management accountants is to help companies continue to improve their corporate governance standards and make sure that companies give their best standards. You can also play a role in making CFOs and CEOs aware of the many benefits of listing on PSX and financing through PSX. We look forward to working with ICMA Pakistan in putting forward the argument for listing on PSX.

ICMA Pakistan: What are the areas where ICMA Pakistan and PSX can collaborate for developing capital market?

Richard Morin: We can work together on improving the corporate governance and financial reporting standards in Pakistan. Let me say here that PSX will soon be dedicating a



team of people to work with the listed companies to improve their abilities and investors' relations, corporate governance and financial reporting. We like to work with groups like ICMA Pakistan in bringing about those improvements so you can collaborate with PSX as we roll up these initiatives towards the listed companies.

ICMA Pakistan: A number of study tours of our students and members tours were arranged in the past which helped in knowing about the mechanism of working at Stock Exchange. Can we enter into any collaboration wot continue with such study tours for our students and members?

Richard Morin: Yes, I encourage you to stay in touch with our new Head of Marketing and Business Development who will be taking charge in next two months or so after end of recruitment process with whom you can keep contact for mutual collaboration in this regard.

ICMA Pakistan: Lastly we need your kind advice for our members to make careers in capital market?

Richard Morin: I think accounting is a good background for capital market, however it may not be sufficient to make career in financial market. If I were a young lad with accounting designation, my next move would probably have been to get my CFA [Chartered Financial Analyst] designation. I think both internationally and within Pakistan, CFA is an important designation to get for making career in capital market. This degree broadly covers overview and training in capital market equities; capital market structure; financial analysis and portfolio management. If your members want to pursue their careers in capital market they should go for this CFA designation.

I believe in future in terms of employment opportunity. I think future lies if we see the opportunity in bringing those 40 million middle-class Pakistanis to the stock market. If you are looking in long term employment opportunities, you must ask yourself what these 40 million people need. My humble opinion is that what they need is investment and wealth management advice. Their question is how do I finance my purchase of next house; how do I finance my kids' education; how do I insure and how I accumulate sufficient wealth to have comfortable retirement. They need advice and consultancy in wealth management so I think your members should be looking into that. On the corporate side as well, they would be looking for advice on investments. So these are two areas where I see opportunities for your members to move forward in future in capital market front.

The Editorial Board thanks Mr. Richard Morin, CEO, PSX for giving his exclusive interview for Management Accountant Journal.