https://doi.org/10.52131/joe.2023.0502.0125

*i*RASD Journal of Economics

Volume 5, Number 2, 2023, Pages 253 – 259

Journal Home Page:
https://journals.internationalrasd.org/index.php/joe

# Mutual Funds in Pakistan: Origin and Development

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**ARTICLE INFO**

***Article History:***

| | | |
|---|---|---|
| Received: | April | 20, 2023 |
| Revised: | June | 08, 2023 |
| Accepted: | June | 09, 2023 |
| Available Online: | June | 12, 2023 |

***Keywords:***
Mutual funds
Trust
Exchange-traded funds
Net assets
Voluntary pension funds

***JEL Classification Codes:***
G19, H55

***Funding:***
This research received no specific grant from any funding agency in the public, commercial, or not-for-profit sectors.

**ABSTRACT**

Mutual funds were born due to the financial crisis in Europe in the early 1770s. The first modern mutual fund emerged in the Netherlands in the second half of the 20th century. The apparent motivation for organizing the mutual funds was to provide diversification for small investors. The paper traces the history of mutual funds in Pakistan, from establishing a national investment trust in 1962 to developing exchange-traded funds in 2020. The findings of this research are based on a comprehensive review of existing literature and statistical data. The results indicate that the mutual fund industry in Pakistan has shown promising growth in recent year. The formation of mutual fund association of Pakistan in 2001, and development of non-banking finance companies rules 2003, brings a revolutionary change in the mutual industry of Pakistan. The industry is continuously growing as there were only 0.31 billion net assets in 2001, which was 662 billion in 2020.

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**Citation:** Khan, S. N.., Alim, W.., Sohail, M.., & Waince, A. G. (2023). Mutual Funds in Pakistan: Origin and Development. *IRASD Journal of Economics*, *5*(2), 253–259.
https://doi.org/10.52131/joe.2023.0502.0125

## 1. Introduction

A mutual fund is an investment vehicle that pools money from different investors to invest in securities such as stocks, bonds, and money market instruments (Hayes, 2020). Mutual funds are operated by fund managers, who invest funds to provide better returns to the unit holders. Mutual funds offer broad investment opportunities, i.e., equity, bonds, and cash funds (Fant & O'Neal, 2000; Neal, 1993). Another benefit of mutual funds is that low-income individuals can enjoy the returns of stocks and bonds, which is otherwise impossible (Palmer-Rubin, 2019). Also, investors are not burdened with the responsibility of management and the safekeeping of investments. The history of mutual funds is ancient as the history of modern trade itself (Bullock, 1959). In the late 1500s, the Spanish and Portuguese dominated the sailing routes to the East.

But after the destruction of the Spanish Armada in 1588, the British and Dutch became more active in trade with the East (Barbour, 1950). Dutch initially took the lead in business with the East. In 1600, Queen Elizabeth-I granted the right to 200 merchants to trade with East Indies. This small group of merchants later became the famous East India Company. During the boom years, this company borrowed money excessively to support its ambitious colonial interest. In 1772, the East India Company was about to go bankrupt because of its higher expenditures with lower revenues. They demanded a bailout package from the already depressed British government. It was initially too big to fail a corporation, and the repercussions were felt worldwide. Meanwhile, the condition of the Dutch was similar to that of the British, and this all occurred similarly to the subprime crisis, which occurred in 2008.

After this downfall, investors were terrified and were less involved in trading activities. In those circumstances, a Dutch merchant named Adrian Van Ketwich generated an idea to form an investment trust (Bullock, 1959). The idea was to share the financial risk by diversifying across several European countries and American colonies where investment was backed by income from plantations (Riley, 1980). In this way, the first mutual fund came into being in 1774, similar to today's mortgage-backed securities (Hendricks, Patel, & Zeckhauser, 1993). He named it "Eendragt Maakt Magt," which means unity creates strength. Initially, 2000 shares were made public and traded in the open market. Fund published their prospectus annually, which was also provided to investors on their request. After that, two more funds were established in the Netherlands with a primary focus on diversification. In 1822, diversification became an integral part of mutual fund investments. After that, the concept of mutual funds became popular across the globe, and it traveled to Switzerland, Scotland, Britain, France, and the USA in the 1890s. The rest of the article is structured as follows: Section 1 presents the history of the first modern mutual fund. Section 2 presents the historical development of mutual industry in Pakistan. Section 3 presents the conclusion of the study.

## 2. Literature Review

### 2.1. The First Modern Mutual Fund

The first modern mutual fund was established in 1924 as a Massachusetts investor trust (Rouwenhorst, 2004). It was the first open-ended fund that continuously allowed the issuance and redemption of shares. Its assets grew from $50000 to $392,000 in a single year, and went public in 1928 (Bosch, 1948). It later became MFS investment management. After the 1930s, the mutual fund idea was at a glance, and several regulations were made for the well-functioning of the mutual fund (Neal, 1993). By 1951, only 100 mutual funds were operating across the globe, and this figure doubled in the next 20 years. In the 1960s, the first aggressive growth funds were created, mainly comprised of technology stocks. While the 1980s brought the most significant contributions in the history of mutual funds, index fund creation is one of them. Evolutions in mutual funds are still ongoing with the creation of different products. One of the evolutions of this era is an exchange-traded fund, commonly called ETF (Fink, 2011). Because of their popularity, mutual funds are growing tremendously across the globe. Table 2.1 presents the region-wise summary of mutual funds across the globe.

At the start of the 21$^{st}$ century, mutual funds witnessed supernormal growth worldwide. One of the reasons behind this was globalization and technological advancement. In 2007 the financial assets of mutual funds were around $26 trillion, and half of their investments were in stocks (factsheet, 2019). And at that time, the total numbers of funds operated worldwide were 66000, which increased to 122,528 at the end of 2019 (factsheet, 2019). Fifty percent of funds belong to the equity category, around 42000. The next largest categories are bond funds and balanced (see table 2.1). In the last quarter of 2019, the net sales in mutual funds were around 836,034 million dollars (factsheet, 2019). In Asia and pacific countries, it's approximately 215,317 million dollars (factsheet, 2019).

**Table 1**
***Regional summary (ICI, 2019)***

| REGION | TOTAL | Equity | Bond | Balanced | Money Market | Real Estate | Others Funds | Institutional Funds |
|---|---|---|---|---|---|---|---|---|
| **TOTAL NET ASSETS (Millions of US dollars, end of quarter)** | | | | | | | | |
| World | 54,882,571 | 24,511,954 | 11,795,557 | 6,844,491 | 6,936,926 | 11,131,703 | 3,612,237 | 5,071,721 |
| Americas | 28,640,793 | 15,504,101 | 6,441,305 | 2,590,609 | 3,845,099 | 29,559 | 229,642 | 555,131 |
| Europe | 18,808,011 | 5,709,681 | 4,599,600 | 3,764,633 | 1,489,699 | 767,424 | 2,428,170 | 3,586,471 |
| Asia and Pacific | 7,256,321 | 3,257,866 | 748,467 | 403,613 | 1,577,100 | 329,821 | 939,033 | 930,119 |
| Africa | 177,446 | 40,306 | 6,185 | 85,636 | 25,028 | 4,899 | 15,392 | |
| **TOTAL NET SALES (Millions of US dollars, quarterly)** | | | | | | | | |
| World | 836,034 | 142,934 | 256,845 | 87,016 | 287,099 | 16,359 | 48,834 | 79,182 |
| Americas | 430,943 | 54,724 | 154,572 | 19,058 | 199,870 | | 2,741 | -789 |
| Europe | 189,978 | 60,368 | 40,613 | 55,547 | -5546 | 10,811 | 31,235 | 58,791 |
| Asia and Pacific | 215,317 | 28,360 | 61,394 | 11,933 | 93,852 | 5,642 | 14,116 | 21,180 |
| Africa | -204 | -518 | 266 | 478 | -1077 | -94 | 742 | |
| **TOTAL NUMBERS OF FUNDS (end of quarter)** | | | | | | | | |
| World | 122,528 | 42,017 | 21,971 | 28,898 | 2,484 | 4,375 | 21,887 | 21,697 |
| Americas | 28,734 | 10,593 | 6,235 | 8,069 | 1,012 | 429 | 2,374 | 3,630 |
| Europe | 56,924 | 15,489 | 10,562 | 15,185 | 682 | 1,887 | 12,358 | 11,238 |
| Asia and Pacific | 35,260 | 15,518 | 5,107 | 4,788 | 739 | 1,981 | 7,105 | 6,829 |
| Africa | 1,610 | 417 | 67 | 947 | 51 | 78 | 50 | |

**Note:** Data excluding fund of funds

## 2.2. History of Pakistani Mutual Funds

In 1962 Government of Pakistan established the first mutual fund in the country with the name national investment trust. Initially, it was established as a trust, and the national bank was appointed as its trustee (Yearbook, 2012). Since then, the national investment trust has been the dominant player in the industry. The fund is the largest mutual fund in Pakistan, with investments in approximately 630 listed Pakistani companies. Mutual funds are operated in Pakistan under the non-banking finance company act 2003, and SECP is their regulatory body.

The second mutual fund was established in 1966, named Investment Corporation of Pakistan. The ICP was established through an ordinance passed by the national assembly. ICP came into being on the advice of Professor Louis Loss from Harvard University, who was engaged as a consultant by the government of Pakistan. Up to early 1990, ICP had established 26 close-ended funds in Pakistan (Yearbook, 2012). In 2000, the federal administration planned to restructure the ICP and winded up the corporation.

In **1971**, the federal government notified the asset management companies and advisory rules. Under these rules, the private sector was allowed to float closed-ended mutual funds. Under these rules, no investment company can commence business without registration. The eligibility criteria for registration as an Investment Company were as follows: The company should be registered as a public limited company under the security exchange commission act 1969 (Amended company ordinance 1984); The minimum capital outlay for a closed-ended investment company should not be less than 100 million; The court should not have convicted the investment company employees, directors or officers; The investment company cannot appoint any director or officer that has been declared insolvent by a court of law; The promoters should know the affairs of Investment Company and have integrity and person of means to deal with Investment Company.

In **1983,** the first closed-ended mutual fund in the private sector, Golden arrow stock fund, was launched. In 2012, the golden arrow stock fund ranked as the best-performing fund in Asia and Pakistan (THELIGHT). In 2018, Thomson Reuters ranked Golden arrow as number 5 in the list of top 100 funds. In **1995,** Asset management rules were notified, allowing the launch of open-ended mutual funds by the private sector. In this regard, the first closed-ended shariah complaint fund was launched (Al Meezan mutual fund) on July 13, 1995. In **1996** first meeting of the asset management companies was held to establish the mutual fund association of Pakistan. In **1997** Unit trust of Pakistan's first private sector open-ended fund was launched by JS investments. In **2001** an association was formed and officially registered with the name mutual fund association of Pakistan (Yearbook, 2012). It is representative of fund management companies in Pakistan. In **2002,** the Government of Pakistan decided to sell the management rights of closed-ended ICP mutual funds through open bidding to the private sector. For this purpose, all funds operated under the umbrella of the Investment Corporation of Pakistan were divided into two lots, mainly 'Lot A' and 'Lot B. 'Lot A was acquired by ABAMCO, which compromised 12 funds, whereas Lot B was acquired by PICIC, which comprised 13 funds. The first fixed-income security fund and the first open-ended shariah compliant fund were launched in the same year.

In **2003**, a significant development occurred when the federal government notified the Non-banking Finance company rules 2003 and terminated the investment advisor rules 1971 and asset management companies' rule 1995. NBFC rules enabled open-ended and closed-ended funds to be administered under the same regulations and resolved many irregularities. In **2004,** the Mutual fund association of Pakistan secured the international investment fund association (IIFA) membership. From 1997 to 2004, the mutual fund industry in Pakistan had tremendous growth. The total net asset increased from 29 billion to 112 billion. In the last quarter of **2005**, thirty-three funds were operating in Pakistan. Out of which, the public sector operated one fund, and others were operated by the private sector. In the same year, Voluntary pension system rules were notified.

In **2007,** the Security exchange commission of Pakistan (SECP) allowed mutual funds to launch pension schemes. In the same year, the federal government amended the NBFC regulation in 2003. Subsequently, the Mutual Fund Association of Pakistan hosted the 12th Asia Oceania Regional Meeting of IIFA, attended by the heads of respective associations of Australia, Japan, Taiwan, China, Philippines, Hong Kong, India, and Bangladesh. In **2009**, after the approval of SECP, the mutual fund association of Pakistan (MUFAP) introduced the model for TFC pricing based on transactions. In the same year, SECP, in consultation with MUFAP, properly categorized the mutual funds according to their investment avenues and risk profiles. Subsequently, a Money market fund was introduced to overcome the liquidity problem faced by investors; the other aim was to provide the least risky investment opportunities.

In **2010,** MUFAP, in collaboration with the Karachi stock exchange (KSE), launched an automated bond trading system for trading corporate debt securities. MUFAP also upgraded its website and added daily returns and net asset values daily. MUFAP also started printing yearbooks and quarterly newsletters, compromising ten years of data and industry issues. In **2011,** SECP made it compulsory for the distributors of Mutual funds to register with MUFAP as a registered service provider. From 2002 to 2011, the mutual fund industry in Pakistan gained significant growth in terms of the number of funds and assets under management, which is supported by the following data.

**Table 2**
***Mutual fund growth (2002 TO 2011)***

| Years | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 | 2011 |
|---|---|---|---|---|---|---|---|---|---|---|
| Open-ended funds | 4 | 13 | 17 | 19 | 29 | 49 | 67 | 81 | 105 | 119 |
| Closed-ended funds | 35 | 35 | 15 | 19 | 19 | 23 | 23 | 21 | 21 | 16 |
| Pension funds | 0 | 0 | 0 | 0 | 0 | 4 | 7 | 7 | 9 | 9 |
| Number of AMC | 12 | 12 | 16 | 16 | 20 | 29 | 26 | 27 | 28 | 26 |
| Number of Funds | 39 | 48 | 32 | 38 | 48 | 76 | 97 | 109 | 135 | 144 |

**Source**: Mutual year-end fund fact sheet 2011

In **2012**, SECP set the criteria for management fees and approved regulation for exchange-traded funds for KSE. During the financial year, mutual funds showed a growth of 52%. MUFAP issued a code of conduct and qualification for registered service providers. In **2013,** the Board of Investment (BOI) gave the evolutionary investment policy 2013. It was the logical enhancement of the investment policy in 1997. The goal of the new investment policy was to uplift the country's economy by facilitating foreign investors and reducing the cost of doing business in Pakistan (Shah, Hijazi, & Hamdani, 2005). Subsequently, SECP amended the 2009 merger policy of open-ended funds. In this regard, it was clarified that unitholders of an open-ended fund scheme might vote on the resolution of mergers of open-ended schemes by physically appearing in the meeting, through a proxy, or by post. SECP also determined the criteria for valuing net assets of the Collective investment scheme (CIF). In **2014,** SECP, in consultation with the Mutual fund association of Pakistan (MUAFP) and its members, determined the requirements for AMC to advertise open-ended investment schemes. In **2015,** SECP made various amendments to NBFC rules 2003 and 2008. In this regard, it was mandatory for asset management companies to open a certain minimum number of branches across the country to enhance the limited retail investor base. The SECP also allowed for charging marketing and selling expenses to strengthen their retail network.

In **2017,** SECP introduced a new and technologically advanced online service desk management system (SDMS), and a toll-free number facility was integrated with the SDMS. SECP also directed all asset management companies to place queries and online complaint portals on their websites. In March **2020**, the Pakistan stock exchange (PSX) launched exchanged traded funds for the very first time in the history of Pakistan. Initially, two asset management companies, a national investment trust and UBL funds, were permitted to offer ETFs. Later on, two more asset management companies, Meezan Pakistan ETF and NBP Pakistan growth ETFs, launched their ETFs. The mutual fund industry in Pakistan has grown remarkably in the last decade. Up to **2020,** seventeen asset management companies were working in Pakistan that was operating 262 funds. The industry is continuously growing as there were only 0.31 billion net assets in 2001, which was 662 billion in 2020 (Yearbook, 2020).

**Table 3**
***Total net assets growth in Pakistan (US Million Dollars)***

| **Years** | **2012** | **2013** | **2014** | **2015** | **2016** | **2017** | **2018** | **2019** |
|---|---|---|---|---|---|---|---|---|
| TNA | 3159 | 3464 | 4156 | 4164 | 5360 | 4591 | 4348 | 4018 |

**Source:** ICI statistic worldwide public tables. (Dec 2019)

## 3. Conclusion

A mutual fund is an investment vehicle that pools money from many investors and invests them into different financial instruments such as stocks, bonds, and T-bills. The history of mutual funds is as old as the history of modern trade itself. Mutual funds were born due to the financial crisis in Europe in the early 1770s. The first modern mutual fund was established in 1924 under the name of Massachusetts investor trust. It was the first open-ended fund that continuously allowed the issuance and redemption of shares. Its assets grew from $50000 to $392,000 in a year, and it went public in 1928. It later became MFS investment management. After the 1930s, the mutual fund idea was at a glance, and several regulations were made for the well-functioning of the mutual fund. By 1951, only 100 mutual funds were operating across the globe, and this figure doubled in the next 20 years. In the 1960s, the first aggressive growth funds were created that mainly compromised technology stocks. The 1980s brought the biggest contributions in the history of mutual funds, and index fund creation is one of them. Evolutions in mutual funds are still ongoing, as it is still happening with the creation of different products. One of the evolutions of this era is an exchange-traded fund, commonly called ETF.

The first mutual fund was established in Pakistan in 1962. The Government of Pakistan established the first mutual fund in the country with the name national investment trust. Initially, it was established as a trust, and the national bank was appointed as its trustee. Since then, the National investment trust has been the dominant player in the industry. The fund is the largest mutual fund in Pakistan, with investments in approximately 630 listed Pakistani companies. Mutual funds operate in Pakistan under the non-banking finance company act 2003, and SECP is their regulatory body. The second mutual fund was established in 1966, named Investment Corporation of Pakistan. The ICP was established through an ordinance passed by the national assembly. ICP came into being on the advice of Professor Louis Loss from Harvard University, who was engaged as a consultant by the government of Pakistan. In early 1990, ICP established 26 close-ended funds in Pakistan. In **2001,** an association was formed and officially registered with the name mutual fund association of Pakistan. It is representative of fund management companies in Pakistan. In **2013,** the Board of Investment (BOI) gave the evolutionary investment policy 2013. It was the logical enhancement of the investment policy in 1997. The goal of the new investment policy was to uplift the country's economy by facilitating foreign investors and reducing the cost of doing business in Pakistan. The industry is continuously growing as there were only 0.31 billion net assets in 2001, which was 662 billion in 2020.

**Authors Contribution**

Saleh Nawaz Khan: Envisaged the idea of Historical research on mutual funds, and supervised the whole research process, develop a study design.
Wajid Alim: Contribute to the study design, and writing introduction
Muhammad Sohail: Literature review
Abdul Ghaffar Waince: Referencing and Proofread

**Conflict of Interests/Disclosures**

The authors declared no potential conflicts of interest w.r.t the research, authorship and/or publication of this article.

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