

Recently, Sirajul Haq, senior minister of NWFP, during his visit to Karachi, announced that the MMA government in the province was considering establishing a stock exchange in Peshawar. The announcement is a welcome development for the Frontier, as it has a very narrow capital base and almost non-existent manufacturing sector. Whereas, corporate culture is nowhere found in the province.

The decision has also come no less than a surprise, as the MMA being a conglomerate of ultra-religious parties is widely considered being averse to Western-styled economic institutions.

In NWFP, the dominant form of investment is in real estate or bank deposits. Investment in stocks has not taken root because of absence of a financial market. People have started shying away from investing in the real estate business, as the meager savings they accumulate are no more lucrative being invested in real estate. Therefore, investment in stock equities could be very compatible with the trivial savings of the NWFP inhabitants.

Entrepreneurs of the province would get maximum advantage if a stock exchange is established in Peshawar, as it would raise equity in the local market that would provide succour to at least medium-sized industries. Besides, investors from the whole province, the adjoining FATA, and of course, Afghanistan, where there is no such market, would have an easy access to locally incorporated companies. Moreover, they will be in a better position to link corporate efficiency with share prices.

Portfolio investment is more suitable for residents of the Frontier, as it would not only divert savings from real estate business but would also help reduce prices of the latter. Afrasiab Khattak, chairman Human Rights Commission of Pakistan and an observer of Pukhtoon society comments, "Investment in real estate enhances the social status in a Pukhtoon society." This status is a source of numerous acrimonious disputes, especially protracted land disputes usually claiming precious

A case for bourse in Peshawar

NWFP government's plan to set up a stock exchange in Peshawar is a welcome move that will boost provincial economy

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lives. So, with attention diverting to portfolio investment interest in real estate business would also dwindle, and hence, may result in lessening of bloody animosities. This menace has been a great hurdle in the development of the region, and underlies the economic woes of people.

With a consequent fall in land prices, entrepreneurs would buy more land for setting up vast industrial units. Besides, cheaper land would be available for agro-based industries like tobacco, orchards and vegetables—lifecycle of provincial economy.

As local joint stock companies would have major stakes in the stock exchange, they would be extra-cautious and efficient for obvious reasons. Likewise, they would be more interested in improving socio-economic milieu in the province for their own benefit. That would be beneficial for every one in the final analysis. The formation of local companies will significantly improve human resource and would create new openings for employment. Presently, due to paucity of skilled labour, most industries in the Frontier are based in sectors that do not require skilled labour. Resultantly, profits are meager and wages minimum. There are no incentives for workers to improve technical skills. By floating shares on the stock market, the local companies would have more funds to dedicate to research and development (R&D)—a concept unknown to the corporate sector in the

Frontier.

Both sole proprietorship and partnership in the Frontier have limited finances for long-time investments; therefore, there is very little vertical integration of different sectors. Consequently, there is very nominal production of value-added goods as well as specialisation that at times becomes counterproductive due to cost overruns, for instance, carpet industry, gemstones and agricultural commodities.

The detrimental affect is that the industries of the province cannot meet significant export orders. With capital formation through share selling, companies would be adequately equipped to vertically integrate their enterprises even opening outlets abroad.

Currently, bank loans are the only source of financing for NWFP businessmen and industrialists. With the rate of mark-up on bank loans as high as 17-22%, it is not pragmatic to borrow for long term. According to a high official of Bank of Khyber (BoK), the account holders in the province deposit for short term, therefore, it is extremely difficult for banks to extend long-term financing available to the entrepreneurs. Long-term investors usually invest in federal government securities such as defense bonds having 17% return. Therefore, banking sector is bereft of necessary funds to loan out to industrialists.

As bank loans form usually 70% of the initial capital for a new enterprise due to which

risk factor is quite high. The production stage usually takes considerably long for an industry amidst which it already accumulates interest in the range of 30-50% of loan amount. In the Frontier, only companies of cigarettes and certain pharmaceutical industries that produce counterfeit items could pay such high interest rate, while most other industries financing their operations with 70% bank loan have failed. This is the underlying reason for the closure of more than half of the NWFP's industrial units. In this scenario, shares capital is going to reduce companies' reliance on heavy debt financing, thus, curtailing the risk.

In the Frontier, family-based businesses dominate the corporate scene in which there is no concept of distinction between ownership and management. With joint stock companies created through shared capital, a professional and vibrant management would be a must for each company that would definitely enhance its business prospects. Moreover, with more capital available, economies of scale could be created that would produce high quality but competitively priced products. These can especially be created in tobacco and fruit farming sectors.

Frontier's investors confidence in banks has eroded tremendously with the ever reducing rate of return, unstable private sector banks, and above all, due to freeze of (FCAs) in 1998. Stock investments may bring back

the investor because the lure of sustainable return is there when dividend is paid from the net profits of a company.

Other investments of people include grocery stores, auto spare parts shops etc. The reasons behind it is rampant unemployment and these petty businesses have in-built mechanism of passing on impact of inflation to consumers. Investing in stocks may provide this in-built mechanism to offset inflation and also put an end to the mushroom growth of petty shops that have numerous socio-economic disadvantages.

When investment would get diverted from petty businesses to corporations, government would be in better stead to tax them due to their smaller number and easily calculable transactions. Many people do not invest in banks, as they considered mark-up unIslamic. Stock investment offer opportunities of investing for profits not pre-determined, besides having the risk of loss making; therefore, stock is a form of Islamic investment.

The above is enough justification for establishment of a stock exchange in the NWFP. However, certain quarantine measures have to be taken to protect the said entity from ill effects. For instance, capital markets often become volatile when speculation is unchecked. Therefore, initially all corporations listed on the Peshawar bourse should be owned by the shareholders from the province. In this manner people of the province would feel a sense of ownership and would consider big corporate entities as their own, instead of outsiders exploiting provincial resources.

A stock exchange can function best if it is given financial autonomy. At the moment Corporate Law Authority (CLA) has the monopoly to award any company the right to establish a stock market, and CLA is a federal organisation. This right needs to be transferred to the provinces.

A capital market can really boost industrialisation and corporate culture if it is accompanied with a full fledged economic package including reduction in both taxes and electricity prices in order to off set the locational disadvantage and giving Frontier's companies competitive edge.