

EVOLUTION STUDY OF ISLAMIC MUTUAL FUNDS IN PAKISTAN

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Abstract

The Investors' perceptions and the perceived characteristics and behavioral intentions towards investment through Islamic Mutual Funds in Pakistan are assessed. The impacts of critical working conditions and traditional demographic structure in Pakistan are not mainly covered in previous research. This paper examines the significance of cultural and demographic aspects in view of the Mutual Funds operating in Pakistan to fill the gap. It is concluded that the drives that lead to choosing Islamic Mutual Funds as preferential institutions by the investors, respondent degree of awareness about the Islamic financial system, and knowledge about Islamic Mutual Funds stands out as being the primary reason, among other numerous reasons, based on individual faiths or investors beliefs. Whereas the evidence produced in this paper regarding impact factors of critical environmental and traditional demographic structure did not find a significant weightage in extending the use of services being provided by Islamic Mutual Funds, the level of information of investors assumes a significant part in choosing Islamic Mutual Funds as preferred organizations over Conventional Mutual Funds. There is a significant level of consciousness concerning investments regarding the benefit of good administrative services and the structure of Islamic Shari'ah Compliant Mutual Funds in the growth of social and nonbanking-financial services in Pakistan.

Keywords: Islamic Mutual Funds, Conventional Mutual Funds, Mutual Funds' Growth, Investors, Fund Managers, Pakistan.

INTRODUCTION

Mutual Fund (MF) is an aggregate investment scheme that collects money from numerous investors and pool of money that is managed by experts under an Asset Management Company (AMC) adequately authorized by government regulator "The Securities and Exchange Commission of Pakistan (SECP). AMC contributes the money to benefit for the unit holders in a portfolio of financial assets or the securities which are included in the respective portfolio; for the purpose of rewards and income as per proportion to their investments on a pro-rata basis. The income earned by the mutual fund's portfolio is rewarded to the investors/unit holders as per the agreement between Fund Manager and the Investors. The growth in YoY return from Shariah Compliant income funds in Pakistan was 12.38% by December 2022.

Table 1

Returns Growth (from 2013 to 2022) of Conventional and Sharia-Compliant Mutual Funds

Category	Open-End Fund Returns									
	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Money Market	9.05%	8.18%	8.80%	5.71%	6.96%	5.45%	8.85%	12.67%	6.89%	10.74%
Income	9.73%	9.32%	13.97%	7.67%	5.94%	5.15%	8.24%	14.16%	6.99%	11.03%
Equity	56.42%	47.34%	21.73%	9.05%	33.37%	-11.17%	-21.26%	3.06%	39.36%	-14.71%

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Capital Protected	11.38%	0.00%	4.29%	3.81%	3.26%	0.74%	3.62%	10.64%	9.75%	9.46%
Capital Protected – Income	-	-	-	-	-	-	4.26%	17.59%	4.81%	10.00%
Fixed Rate / Return	-	-	-	-	-	-	-	-	-	15.00%
Fund of Funds – CPPI	-	-	11.47%	8.68%	-	0.72%	2.11%	4.83%	18.39%	-
Aggressive Fixed Income	8.14%	5.88%	12.40%	9.06%	5.98%	5.01%	7.39%	11.66%	7.87%	9.75%
Balanced	36.65%	23.70%	19.86%	7.05%	25.26%	-7.67%	-10.89%	5.40%	21.84%	-10.32%
Asset Allocation	23.42%	14.78%	20.04%	5.96%	17.26%	-5.12%	-6.06%	3.27%	19.46%	-0.70%
Fund of Funds	35.93%	9.93%	20.44%	6.17%	11.70%	-3.74%	-2.72%	4.21%	21.81%	-5.54%
Index Tracker	44.78%	35.37%	12.57%	4.73%	20.77%	-11.55%	-20.01%	-0.19%	34.58%	-12.18%
Commodities	-17.14%	9.19%	-5.01%	13.27%	-3.28%	-	-	-	-	-
Shariah Compliant Money	8.06%	8.70%	7.06%	4.63%	5.13%	4.49%	9.06%	11.33%	6.56%	9.90%
Market										
Shariah Compliant Income	9.37%	8.74%	7.27%	5.28%	5.58%	4.48%	8.41%	11.29%	6.58%	9.49%
Shariah Compliant Equity	47.94%	28.72%	21.02%	14.08%	25.16%	-14.87%	-22.61%	3.24%	34.57%	-13.46%
Shariah Compliant Capital	10.45%	3.68%	21.21%	3.64%	23.83%	0.80%	-1.32%	11.97%	-	-
Protected										
Shariah Compliant Capital	-	-	-	-	-	-	-	-1.15%	5.25%	6.29%
Protected – Income										
Shariah Compliant Fixed Rate /	-	-	-	-	-	-	-	-	-	13.84%
Return										
Shariah Compliant Fund of Funds	-	-	9.31%	7.15%	15.06%	0.15%	2.75%	0.82%	10.57%	-3.12%
– CPPI										
Shariah Compliant Aggressive	7.81%	12.96%	8.39%	7.34%	4.81%	3.49%	6.52%	11.30%	7.78%	8.01%
Fixed Income										
Shariah Compliant Balanced	25.00%	28.25%	15.56%	11.82%	14.86%	-8.93%	-12.80%	8.12%	18.13%	-3.61%
Shariah Compliant Asset	30.80%	16.01%	29.26%	9.46%	17.98%	-6.18%	-9.81%	6.80%	16.13%	0.45%
Allocation										
Shariah Compliant Fund of Funds	6.26%	6.08%	3.99%	7.47%	8.05%	-5.95%	-7.84%	7.35%	24.26%	-2.98%
Shariah Compliant Fund of Funds	-	-	-	-	-	-	-	7.28%	5.58%	9.01%
– Income										
Shariah Compliant Index Tracker	49.64%	26.49%	17.06%	13.32%	15.89%	-11.19%	-25.07%	0.88%	36.43%	-10.69%
Shariah Compliant Commodities	-	-	-	10.59%	-7.21%	11.99%	30.43%	23.54%	-0.65%	24.83%

(Source: <https://mufap.com.pk/pdf/yearbook/2022/Yearbook/Industrystats.pdf>).

Pakistan is one of the major emerging Muslim Countries. The Security and Exchange Commission of Pakistan (as regulator) has been supporting and regulating the setup for developing the Islamic Mutual Funds System in Pakistan. However, Islamic Mutual Funds are still relatively one step ahead of the initial stage compared to Pakistan's more established Conventional Mutual Funds sector. After reviewing some prior studies on Islamic Mutual Funds, the investigation determines that stand-alone Islamic Mutual Fund outperforms Pakistan's overall Mutual Funds sector. Returns of conventional and Islamic MFs of the last decade from 2013 to 2022 are mentioned in Table 1.

Many leading conventional Asset Management Companies & Mutual Funds have developed Islamic Mutual Funds in Pakistan to fulfill the Sharia Compliant regulatory requirements under the guidelines of the Security and Exchange Commission of Pakistan (SECP) (Akhtar, 2007). Islamic Mutual Funds must implement other international and locally developed governance to improve trust levels and reinforce risk management under the Islamic Shariah principles to strengthen the framework of mutual funds (Abdullah et al., 2012). Especially the Muslims from rural parts now comprise above half of some Islamic Mutual Funds' investors (Hasbullah and Rahman, 2023). Islamic Mutual Funds, such as Equity Funds and Money Market Funds based on the Islamic mode of finance, Murabaha and Mudarabah or other permissible Islamic modes of finance, have drawn considerable interest from Pakistani investors based on their faith. Globally, Murabaha and Sharia-compliant participatory modes (such as Mudarabah

and Musharakah) are some of the fastest-growing instruments of Islamic mode of finance, with the research work's conclusion of many studies based on investor's satisfaction and understanding towards the role of Islamic Mutual Funds. Global Islamic Finance Report (GIFR) states that the assets of 3.14 trillion are also being accomplished under Islamic investment laws and regulations, whereas 29% of Mutual Funds investors have now progressed towards services of Islamic finance (Dar et al., 2016).

Modifications in the financial system of Pakistan's environment and the elevation of Islamic Mutual Funds have produced new features and predictions in the Mutual Funds sector. Such evidence also contributed to the investor's selection and demand for natural and highly effective Mutual Funds facilities. Since the progress of more asset management companies in the last few years, conventional and Islamic investors of different income categories have been presented with giant potential products, services and facilities to choose from regarding their fulfillment and demand. In conclusion, investors now do not have ample options to select the desired ones to fulfill their requirements and needs (Thambiah et al., 2010). This state of affairs applies to the offered options and services presented by Islamic Mutual Funds and conventional Mutual Funds. These funds developed various challenges for funds/ units presented by the conventional Mutual Funds but also amongst the funds controlled by the Islamic Mutual Funds. Islamic Mutual Funds are increasing and developing close relations with local Muslims in Pakistan, but then again, still, not as much as it is supposed to be, 95% of the population are Muslims, according to the Survey of Pakistan.

Does it due to not having as much understood and information about the controlling issues of Islamic funds and facilities, demand for high profit, or any other motives? For hypothesis, we assume that the impacts of the Islamic mutual funds' framework in Pakistan are intervened by investors' knowledge level and by the level under which demographic factors are causation.

More precisely, the research intended to attain the following definite study goals:

1. To find out whether investors with different backgrounds act to develop and uplift the outlook towards the improvement of Islamic MFs in Pakistan.
2. To examine and compare the perception of Pakistani investors towards the development of the Islamic Mutual Funds system.

The result of investment in Sharia Compliant manner in the Islamic world is well recognized. Funds and facilities offered by Islamic Mutual Funds have methodologies that are differentiated from those of conventional Mutual Funds (Chapra, 2016). The growth of Islamic Mutual Funds in the global market has been very positive in meeting ethical and spiritual principles (Bukhari et al., 2014). Religious principles and various financial factors govern the evidence of the development of Islamic Mutual Funds. From the Islamic Mutual Funds viewpoint, many researchers linked the idea of justice to Islamic Mutual Funds and highlighted two essential aspects of Islamic finance: the religious element and the income element (Haron, 1996; Nawaz et al., 2017). Islamic Mutual Funds, as a vehicle of Islamic finance providers, is a business entity that collects funds and facilities for income generation through savings (Hassan et al., 2022).

Mutual Funds in Pakistan as Islamic Mutual Funds are given Islamic laws and regulations (Manzoor et al., 2010), and the more significant part of the investors of Islamic Mutual Funds have taken on both Mutual Funds frameworks, as around 67% of the investors have invested in conventional Mutual Funds (Khattak, 2010). This highlights that Islamic Mutual Funds are required to focus on many aspects and requirements that investors need. Muslims need their investment security and growth without Riba (Rashid et al., 2009). Because of fierce opposition among the type of funds of Mutual Funds, Islamic Mutual Funds in this manner need to consider better methodologies and strategies, for example, Mutual

Fund's outlook and performance, the execution time of transactions, alternative digital delivery channel system, and Products variety to draw in conventional and Islamic investors to continue Mutual Funds business (Abdullah et al., 2012) without hassle. Erol and El_Bdour (1989) research is viewed as the managers; investigation of individual purchasers' mentalities connection with Mutual Funds governing practices. Investors' mentalities, behaviour, and support factors were discovered by a self-directed questionnaire survey (both Islamic and traditional) with a concentration in Jordan (Naser et al., 1999).

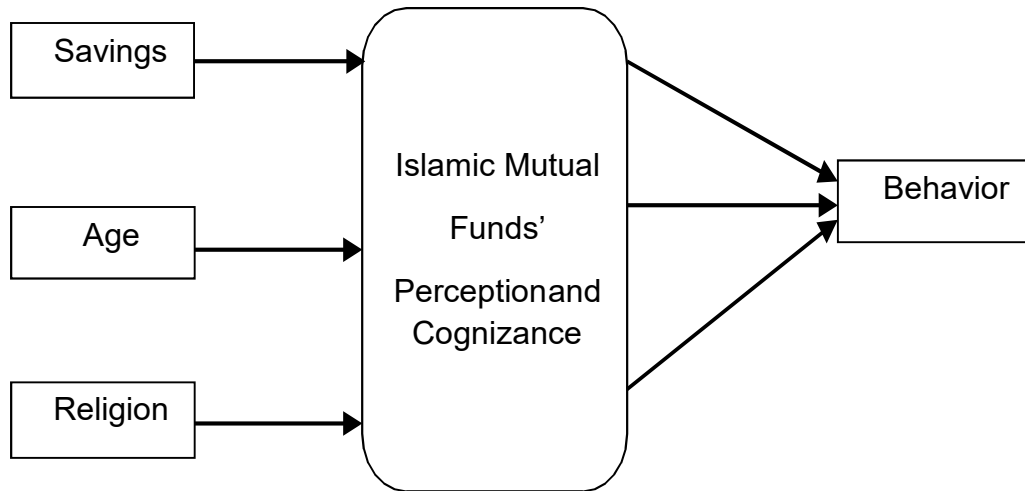


Figure 1: Proposed Conceptual Framework

Research Framework

The study depends on the research outcomes (Haroon et al., 1994; Metawa and Almassawi, 1998; Omer, 1992). Stanikzai et al. (2022) directed a review concerted on the discernments and mentalities of the investors toward Islamic Mutual Funds based on the Islamic mode of finance. A more significant art of investors' overview represented the significance of religion, mutual funds operations, and monetary factors. Gerrard et al. (2003); Haron (1996); Metawa and Almassawi (1998) expressed the financial matters of Islamic investments through analysis given conventional and Islamic investors in Malaysia, Bahrain and Singapore individually. They found that 53% of conventional investors proclaimed Islamic banking as considerable as per the understanding of its operational activities. Past studies also revealed numerous determinants of Islamic investment growth in Turkey in light of choosing the mutual fund based on its features as per sex, ageing bracket, academic background and financial market knowledge of investors.

It is articulated that the primary endeavor to lay out Islamic mutual funds was in Pakistan at the end of 2002. The initial fixed-income securities mutual fund (Pakistan Income Fund) was introduced in March 2002 and the first Shariah Compliant Fund (open-end UTP-Islamic Fund, now JSIL (Sharia-Compliant Fund) was started on December 27, 2002 (<https://www.mufap.com.pk/>) The significant growth in the Islamic mutual fund industry demonstrates that a more significant transformation of the components that impact various decisions can help the growth and improvement of suitable techniques to address the developing requirements for investment-related services (Bley and Kuehn, 2005; Nawaz et al., 2017, Lin and Park, 2023; Hassan et al., 2023). This study enhances this paper by more cautiously investigating the attributes and information on Islamic investment concepts, inclinations for Islamic

investment services, and respective investor dispositions or ratings of the local Pakistani market. The multi-dimensional research tools have been utilized in papers. As Rulindo & Mardhatillah (2011) indicated, ageing brackets, investors' beliefs, and savings do not associate with investors' revenue in the Islamic financial market of Malaysia. Moreover, the study is surrounded with detailed investigating tools by using variables, for example, investor's perception and behavior towards the selection of Islamic method of investment (Nawaz, 2017) because Islamic modes of investment are rapidly arising in the international financial market, which is further to be explored through focused research. As indicated by Alqadhib, (2023), knowledge of investor inspirations for selecting the Sharia Compliant mutual funds in comparison with the conventional mutual funds' services is suitably correct and sufficient, and the limited research is currently accounted for.

METHODOLOGY

In earlier research, as recognized in the literature-review segment of this paper, Islamic investment approaches were utilized to realize the insights, approaches, and conduct of investors towards the growth of Islamic Mutual Funds and products derived from services provided by mutual funds, resulting in a limited scope. This study defines investors' perceptions of Islamic MFs compared to Conventional MFs. Based on the reviews above and the target of this paper, we have to analyze the hypotheses as given below:

H_0 : The effects/ impact of Islamic mutual funds are mediated through investors having a certain degree of background investment cognizance.

H_1 : The effects/ impact of Islamic mutual funds institutions are not mediated through investors having a certain degree of background investment cognizance.

The structure model of this paper in Figure 1, mainly concentrates on predicting the variables of mediating, i.e. First response to investment through Islamic Mutual Funds in Pakistan; investors' perception towards Islamic Mutual Funds; Regulations for Islamic Mutual Funds in the country influence the connection between variables (independent: religion, savings and age on the variable dependent: behavior). The target population of this research comprised professional Investors of Asset Management Companies operating in Pakistan who had an experience of 3 years or more in funds investment services (Sharif et al., 2020). For the sample collection structure, a list of Asset Management Companies generated of 20 top companies professionals, collected for study purposes by the MUFAP (Mutual Funds Association of Pakistan), which provides the official platform as a trade body for the asset management industry operating in Pakistan and deals in different types of investment vehicles covering the bonds, Sukuks, stock market, money-market tools, government securities and investments/ deposits with local and international IFIs. The ultimate comprehended samples represent an 80% response rate which is considered suitable to attain the aim of this study. The research (quantitative approach) of the well-structured questionnaire survey was conducted for the paper. Multiple-choice questions of different levels were included in the survey and interview to gather responses from the respondents. Moreover, the analyst applied the "psychometric" technique too, one of the effective approaches (Likert, 1932) toward achieving the research goal. Psychometric appraisals are fastidiously estimation devices that quantify an individual's character qualities, mental capacities, and behavioral inclinations. The study implemented the five-point approach (Codes from 1 to 5), depends on Likert scale (Strongly Agree; Agree; Neutral, Disagree, and Strongly Disagree) for the reaction of respondents towards performance growth of Mutual

Funds in Pakistan.

Survey Results

The survey was influenced and dominated by experienced respondents (62%), and mainstream (51%) respondents stated periodic savings between Rupees 35,000/- and 75,000/-. The expressive statistical Table-1 showed that the significant uniformity in assessments is related to religion (Mean is 1.007, Standard Deviation is 0.091). The distinction in our test result tracked down on Governance/ Ruling the view of the growth of Islamic Mutual Funds (Mean=2.90, Standard Deviation is 1.28). The results of all variables other than the ageing factor have a slight variation with normal kurtosis ranging to 3.9 because of the slight variation from the mean. The result shows that 36% of investors/ respondents reflect a solid favorable inclination toward Pakistan's Islamic Mutual Funds system. Though, 22% of respondents/ investors were displeasure with the Islamic Mutual Funds system in Pakistan at an average medium degree. Besides, 23% of respondents/ investors appraise Islamic Mutual Funds for investment in Pakistan, as per the Shariah rulings, whereas 15% strongly believe in the perfect application of Islamic Shariah governance in Islamic Mutual Funds in Pakistan. Closely 30% of respondents/ investors utilize the facilities of Conventional Mutual Funds. Whereas 16% of respondents/ investors opt for Islamic Mutual Funds, and 23% of respondents/ investors proclaimed they are utilizing the facilities of both conventional and Islamic Mutual Funds while 70% of respondents/ investors are because of the significance of the need and improvement of the proper Islamic system in the Mutual Funds structure in Pakistan.

Table 1
Statistics (descriptive)

Factors	Mean	variance	St. Dev.	Kurtosis	Skewness
Governance	2.9	1.62	1.28	0.065	1.93
Perception	2.05	0.969	0.983	0.68	3.1
Religion	1.007	0.008	0.091	1.16	10.72
Response to MF	2.12	1.02	1.02	0.478	2.47
Savings	2.25	1.46	1.212	0.9717	3.1
Age	1.67	0.514	0.716	6.73	1.43
Behaviour	2.3	1.3	1.13	0.515	2.67

Table 2
Correlations

Factors		Governan ce	Perceptio n	Religio n	Respons e to MF	Saving s	Age	Behaviou r
Governan ce	Correlatio n Pearson Sig(2- tailed)	1	0.400**	0.004	0.476**	0.05	0.057	0.199*
Perception	Correlatio n Pearson	0.400**	1	-0.109	0.612**	0.111	0.021	0.180*

	Sig(2-tailed)	0		0.241	0	0.181	0.825	0.028
Religion	Correlation Pearson	0.004	-0.109	1	-0.015	-0.101	.a	0.05
	Sig(2-tailed)	0.969	0.241		0.874	0.283	0	0.592
Response to MF	Correlation Pearson	0.476**	0.612**	-0.015	1	0.058	0.012	0.239**
	Sig(2-tailed)	0	0	0.873		0.485	0.9	0.003
Savings	Correlation Pearson	0.05	0.111	-0.101	0.058	1	0.279*	-0.014
	Sig.(2-tailed)	0.546	0.181	0.283	0.486		0.004	0.871
Age	Correlation Pearson	0.057	0.021	.a	0.012	0.279*	1	0.059
	Sig.(2-tailed)	0.545	0.825	0	0.9	0.004		0.537
Behaviour	Correlation Pearson	0.199*	0.180*	0.05	0.240**	-0.014	0.059	1
	Sig.(2-tailed)	0.015	0.028	0.592	0.003	0.871	0.537	

A- computing is impossible due to the constant nature of at least one variable.

* Correlation at a level of 0.05 (2 tailed) is significant

** Level of Correlations Significance at values 0.01 (2 tailed)

Table 2 portrays the Correlation Matrix of variables for this study. There is robust evidence of narrow correlations between background factors and behavior variables of the study (including Response to MF, Governance and Perception) explicit for the paper. Notwithstanding, bivariate correlation neglected to recommend the connection between demographic variable qualities [such as religion, Savings and religion] and the outcome of behavior variables. Moreover, the tool of testing was also applied for inward stability and combined reliability utilizing the coefficient alpha gauge of Cronbach (Tavakol & Dennick, 2011). Table-3 shows reliability inspection by Cronbach's coefficient of alpha reliability for variables under consideration. The Cronbach's alpha scale reliability coefficient (0.6), comparative to the value of minimum alpha as 0.59 (Chen & Tsai, 2007), in this manner, the established measures are considered authenticated.

Table 3
Test Results of Reliability (Cronbach's Alpha)

Scale Reliability Coefficient	Average Inter-Item Covariance
0.59	0.21

Regression investigation outcomes of the research indicate that cognizance and the perception regarding investment through Islamic Mutual Funds have a mediating impact in establishing the association between factors of socially demographic and respondents' decision to select Islamic mutual funds and facilities Table 4. This paper also suggests that awareness of Islamic investments can utilize the similar common corresponding concept for facilities presented when communicating with diverse degrees of variables, age, religion, and savings groups.

Table 4
Regression results

Variables/ Factors	Behaviour		
	Step 1	Step 2	Step 3
Social-demographic characteristics			
Religion		4.875**	-
Age		-0.3953	-0.220*
Savings		-0.2522*	-0.273*
Perception & cognizance regarding investment through Islamic Mutual Funds in Pakistan.	1.53**	-	0.172*
R2	0.07	0.112	0.177

Significance: $p^* < 0.05$ & $p^{**} < 0.001$

CONCLUSION

This research explored the prospective role of investing association endeavors in impacting investors' cognizance and behavior inclination towards Islamic Mutual Funds in Pakistan. The primary analysis likely exhibits investors' perceptions and the effect of superior treatment endeavors sent through Islamic Mutual Funds in Pakistan. For the samples, the result shows that the Islamic mode of investments in Pakistan can impact the reliance of the Pakistani Mutual Funds industry on certain market information or investors' knowledge about investment opportunities, irrespective of communal demographic variations. These results are in accordance with past examinations (Rashid et al., 2009). At large, the results made sense of the intervening result of perception and cognizance of Islamic Mutual Funds facilities for the improvement of Islamic investment opportunities in Pakistan. This clarifies that, aside from explicit investors' ageing bracing savings slabs and belief factors, the level of cognizance contributes to investors' trust. Our investigation shows that outreach and leading efforts of Islamic Investment through the Mutual Funds system are significant drivers of investment growth. Therefore, fund managers should coordinate a greater significance regarding creating and carrying out endeavors for equal endeavor sites. Our review proposes that facility administering systems can be worked around investors' trust and perceptions regarding religious beliefs.

Many researchers caution that investors' comprehension of service quality depends on beliefs and trust that shift from one investor to another (Mustafa et al., 2023). This study offers robust empirical help for the evolution of Islamic Mutual Funds in Pakistan resulting from the quality facilities in light of investors' perceptions and outreach of investment opportunities. A few limitations may be connected with gathering and interpreting effects. A primary limitation may be the lack of research on investors' perceptions in a structured and systematic approach, as the questionnaire was disseminated on an apparent and one-time basis. Another limitation is the small sample size and typical technique inclination as a simple questionnaire was utilized to develop measurement variables. A more excellent collection or sample size would have allowed additional better-quality outcomes.

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