

REGULATORY SANDBOX

DRIVING BENEFICIAL REGULATION THROUGH INNOVATION



SECURITIES AND EXCHANGE COMMISSION OF PAKISTAN

Regulatory Sandbox (RSB) was introduced as a means to gain knowledge that can lead to pro-innovation regulation making. It provides space to test technological driven financial products and business models that falls within the regulatory domain of Securities and Exchange Commission of Pakistan (SECP/ Commission).

THIS PAPER AIMS TO GIVE:

Regulatory
Sandbox
Overview

01

Regulatory
Sandbox
Life-Cycle

02

Regulatory
Sandbox
Journey

03

Testing
Outcomes

04

Way
Forward

05

Annexures

06

GLOSSARY

COHORT

A cohort is an experimental cycle in which business models of applicants are evaluated and tested.

FRACTIONALIZATION OF REAL ESTATE

Involves creations of fractions of real asset in smaller denominations and selling the same to specified investors through electronic platform.

NBFC

Means a non-banking finance company that provides certain bank like financial services and are licensed by the Commission under NBFC framework.

FINTECH

Integration of technology with financial products to improve and automate the delivery and use of financial services and products.

DISTRIBUTED LEDGER

A distributed ledger is a database that exists across several locations or among multiple participants.

PEER-TO-PEER (P2P) LENDING

Enable individuals to obtain loans directly from other individuals through an online digital platform without involvement of financial institutions.

ROBO ADVISORY

Automated, algorithm-based investment advisory, involving no or little human involvement.

SYSTEMATIC INVESTMENT PLAN (SIP)

SIP is a method of investing a fixed sum, regularly, in a mutual fund scheme. SIP allows one to buy units on a given date each month, so that one can implement a saving plan for themselves.

EQUITY CROWDFUNDING (ECF)

A mechanism that enables broad groups of investors to fund startup companies and small businesses through electronic platform in return for equity stake.

INSURANCE BROKERAGE

Insurance brokerage is a business model that connect insurance sellers with buyers and get commission in return.

FINANCIAL INCLUSION

Availability of affordable financial products in sustainable way to individuals and businesses to meet their needs such as capital, payments, savings, investment, credit and insurance.

ASSET MANAGEMENT SERVICES

Involves pooling of funds from various individual and institutional investors and investing the same in various securities.

ASSET MANAGEMENT COMPANIES (AMC)

Means NBFCs licensed by the Commission to provide asset management services.

MICRO-INSURERS

Means insurers that provide micro insurance products and services.



The graphic features a 3D isometric design with various blue and green cubes and icons. Some cubes are labeled with terms like 'GLOBAL', 'SYNC', 'PAYMENT', 'FINANCIAL TECHNOLOGY', 'INVESTMENT', and 'SECURITIES'. A large green semi-transparent box is overlaid on the center, containing the title 'REGULATORY SANDBOX OVERVIEW' in white, bold, uppercase letters.

REGULATORY SANDBOX OVERVIEW

Financial inclusion and technological innovation(s) are crucial for growth of developing economies like Pakistan. Through the Regulatory sandbox SECP aims to learn about the regulatory impediments and likely risks arising from a proposed financial products/solution for test is conducted. Introduction of regulatory sandbox is an important step towards enhancing financial inclusion and introducing new financial products

Objective

Financial inclusion and technological innovation(s) are crucial for growth of developing economies like Pakistan. Through the Regulatory sandbox SECP aims to learn about the regulatory impediments and likely risks arising from a proposed financial products/solution for test is conducted.

Introduction of regulatory sandbox is an important step towards enhancing financial inclusion and introducing new financial products

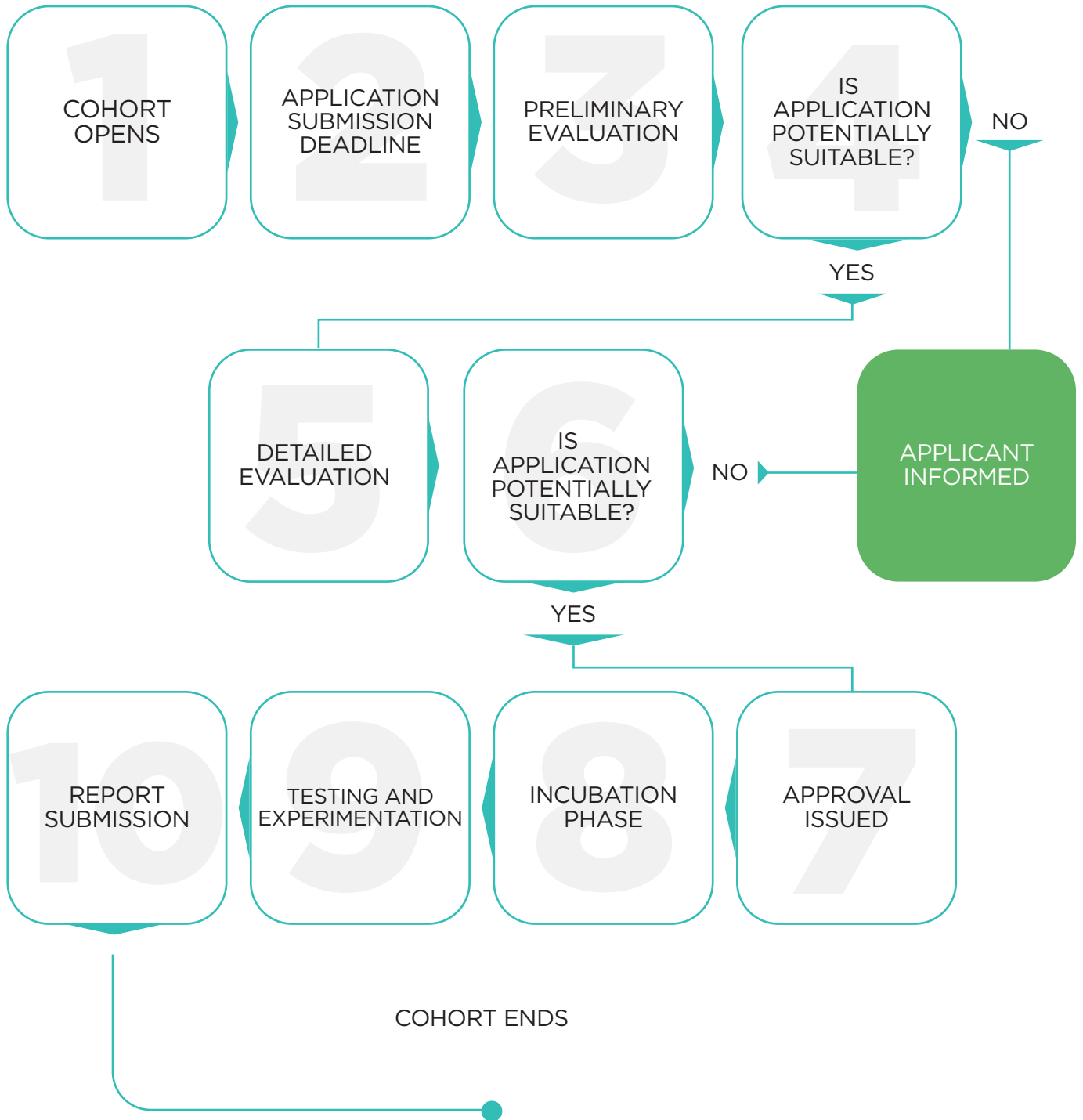
Regulatory Framework:

Regulatory sandbox guidelines were introduced in 2019 to provide a detailed and comprehensive framework under which business models are tested in controlled environment with approval of the Commission. Regulatory framework can be accessed through following link

“

<https://www.secp.gov.pk/document/secp-regulatory-sandbox-guidelines-2019-reissued-under-section-458-a-of-the-companies-act-2017/?wpdmdl=44219&refresh=6218a27fefe741645781631>

REGULATORY SANDBOX LIFE-CYCLE














REGULATORY SANDBOX JOURNEY

SECP has launched three cohorts under regulatory sandbox allowing testing and experimentation of new business models/financial products.

- Amongst thirty three applicants in first cohort, six participated in testing and experimentations. Life-cycle of first cohort has been completed and results have been shared with the Commission.
- Amongst thirty eight applicants in second cohort, six participated in testing and experimentation. Testing phase of second cohort is on-going.
- Application window for third cohort is open till May 31st, 2022.

Cohort - I

Cohort - II

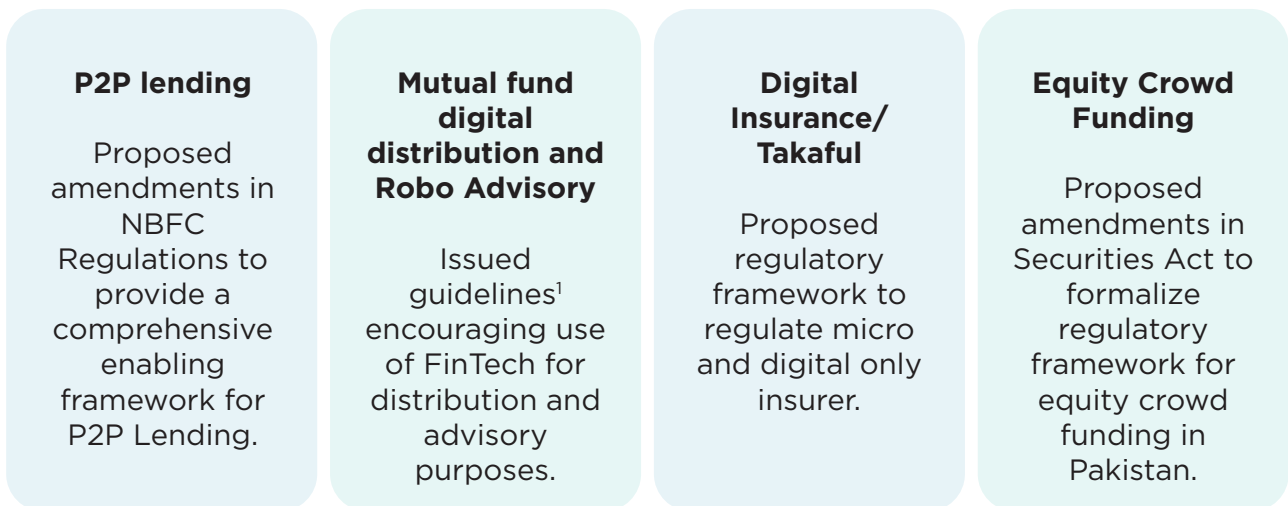
 <p>FINJA Lending Services Limited (Finja) Digital Peer-to-Peer (P2P) Lending Platform</p>	 <p>Salaam Takaful Limited Parametric Insurance</p>
 <p>YPay Financial Services (Ypay) Mutual Fund Digital Distribution</p>	 <p>MyQasaar Private Limited Fractionalization of Real Assets through Electronic Platform</p>
 <p>Finox Alpha (Finox) Robo Advisory</p>	 <p>FracEstate Private Limited Fractionalization of Real Assets through Electronic Platform</p>
 <p>Pakistan National Investor Portal (PNIP) Equity Crowdfunding Platform</p>	 <p>Innovest Tech Private Limited Unified Digital Distribution and Central KYC for Mutual Funds</p>
 <p>First Digital General Takaful (FDGT) Digital General Takaful Provider</p>	 <p>Sahal Software Solutions Private Limited Digital Identity/AML/KYC</p>
 <p>Waada Digital (Pvt) Limited (Waada)* Digital Insurance Brokerage Model</p>	 <p>Oraan Tech Private Limited Women Focused Mutual Funds Distribution Platform</p>

* Waada took exit from the sandbox prior to testing to seek licence for commercial operations.

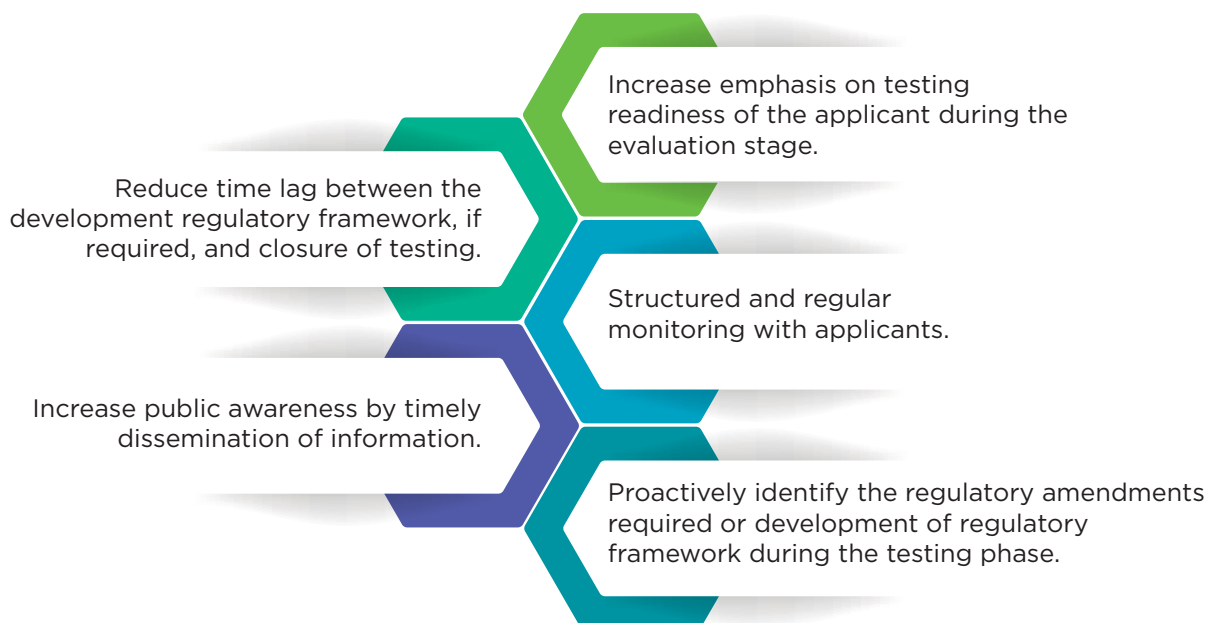
TESTING OUTCOMES

Sandbox initiative has been effective for assessing risk a new financial product poses and the likely impediments it can face. It has proved to be mutually beneficial for both regulator and the market participants. Results of first Cohort have provided a direction to SECP in terms of providing regulatory framework for introduction of tested financial products in the market. In fact this has led to SECP issuing guidelines and/or initiating the process for modifying/setting up regulatory framework.

Regulatory reforms in the following sectors within the domain of SECP are being introduced:



Way Forward



¹<https://www.secp.gov.pk/document/guidelines-for-mutual-fund-digital-distribution-platform/>



ANNEXURE



FINJA INVEST

Objective

Test P2P Digital Lending platform, understand its practical aspect, its potential for reaching out to the MSME market with the ultimate aim to develop/adapt the regulatory framework.

Methodology

FINJA opened P2P accounts of investors and borrowers digitally and verified by NADRA in real-time basis. The platform enabled that lenders could add funds to their account either via interbank funds transfer from any mobile banking application or via credit/debit card, for which 3D secure payment gateway is integrated with FINJA web platform.

Lenders then choose to disburse their capital to relevant borrowers available on the platform duly scrutinized based on their credit history, monthly turnover etc. The disbursed capital is credited to the digital account of the distributor of that particular borrower/karyana stores. The borrower repaid the loan using IBFT/mobile wallet/agent network and then the P2P account of the lender is credited with principal and profit amounts. The whole process is digitally enabled where lenders directly choose borrowers based on their credit scores.

Performance

FINJA INVEST- PAKISTAN'S FIRST P2P LENDING PLATFORM			
Investors		Borrowers	
No. of Investors	48	No. of Karyana Stores	623
Total lending Portfolio	20M; 4M from FINJA	Loans Funded	1132
Amount Returned	Rs 10M	Active Lenders Accounts	501
Accounts on Waitlist	500+	No. of Cities	12
Average Investment	Rs.14,000/Karyana	Outstanding Portfolio	7 M
Monthly Return	1.6-2.7%	Delinquency (>30)	1.60%
Loan Tenures offered	7, 15, 30 Days	Loans Sold	14 (6 recovered)

Learnings

While developing the framework to enable Non-banking finance companies with a lending license to operate a P2P Lending platform the following should be catered:

Risk due to involvement of public money

Exposure to illegal / malicious activities being a technology-based platform

Illegal deposit taking

Protection of participants



YPAY FINANCIAL SERVICES

Objective

A centralized digital mutual fund distribution platform acted as an intermediary between the Asset Management Companies and the Investors. Through such platform, the AMC's had access to individual customers in remote areas and cater needs of small savers.

Methodology

An online dashboard enables customers to onboard through an online sign up using their email account (Gmail/Yahoo/Outlook) and complete the process. Subsequent to KYC and linking of Banking a risk profile of customer is created based upon risk appetite related details provided to the platform. Customers can browse a list of investment opportunities (Conventional/ Islamic), read about their summaries and market profiles and make their investment decision.

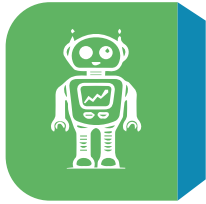
The Application Commissioner receives the request and confirm the status of investment once the background process has been completed. Redemption request can be made online as through the dashboard. YPay will forward their request to the concerned AMC, and upon successful redemption the funds will be transferred to the customer's linked bank account and they will be duly notified via Email notification.

Performance

YPAY FINANCIAL SERVICES - MUTUAL FUND DIGITAL DISTRIBUTION PLATFORM	
No of Customers	100+
Customer on waitlist	3000+
Total Investment	Rs. 1.7M
Investments per customer	3
Investment ticket size	Rs. 9,000
Investor Demographics	
Early graduate male	63.8%
Early graduate female	25.5%
Housewives	10.5%

Learnings

Testing of this model enabled better understanding of the operations of digital distribution of mutual funds, as a result of which the Commission issued guidelines for mutual fund digital distribution platforms



FINOX ALPHA

Objective

Feasibility of robo-advisory solution under a controlled environment. Investment advice to be given based algorithms run on the information provided by the investor.

Methodology

Robo-Advisory products are for long-term, therefore, “back-testing approach” was adapted to simulate returns of Robo-Advisory product.

Performance

The response was positive as the Systematic Investment Plan (SIP) under the Robo Advisory Product outperformed KSE 100 and MCB Asset Allocation Fund, but underperformed Pakistan Stock Market Fund. Robo-Advisor with SIP increase the expected annual return of investor by at least 1.5% to 2% as compared to the benchmarks.

Learnings

Customized investment solutions for investors can be formulated through Robo-Advisory with the following advantages:

Several biases including human bias can be controlled through Robo-Advisory

Good quality and affordable investment advisory services can be made available to investors to improve long-term risk-adjusted returns

As the product of robo-advisory is scaled, it may add to a new type of systemic risk in the market as automated services may recommend certain asset classes to investors on a similar pattern. This may result in risk of large-scale parallel behavior ultimately resulting in increase of systemic risk



PAKISTAN NATIONAL INVESTOR PORTAL

Objective

- To identify the risks involved in equity crowdfunding, so that regulatory framework addressing the concerned risks can be introduced
- To identify optimal approach for regulating equity crowdfunding

Methodology

PNIP called applications from potential companies that wanted to raise funds through crowdfunding. Companies were further shortlisted based on due diligence criteria of PNIP. After shortlisting, companies went through investment readiness program, where they were prepared for pitching the issue to eligible investors. Subsequent to the investment readiness program, platform was opened for registration of eligible investors. The platform could then match potential investors with companies seeking funds. All subscriptions were to be made through banking channels and parked in an escrow account.

Performance

PNIP identified/shortlisted potential companies for crowdfunding, however said companies could not be showcased before the investors due to time constraint, difficulty faced in marketing of crowdfunding platform and identification/registration of eligible investors.

Learnings

Success of crowdfunding requires:

Liberal and disclosure-based regime

Stringent requirements make difficult for startups to raise funds

Offer customized investment opportunities to accommodate variety of investors based on their risk appetite



FIRST DIGITAL GENERAL TAKAFUL

Objective

To test digital only insurer/ takaful model whereby, complete process, for a small size insurance entity, from policy issuance, policy servicing and claims settlement is to be carried out digitally, with an aim of development of a regulatory framework for introduction of dedicated digital only insurers and micro-insurers.

Methodology

The applicant deployed web platform for end to end sale, delivery and settlement of takaful products. Customers can buy suitable product on the First Digital web platform. They are requested to fill details on application forms, and make payment either online or cash on delivery. The policy is then issued digitally and documents are shared with the customer through SMS and email. In case of claims, customers can digitally file claim through online claim portal available on the website. The claims are settled within 2 days of the completion of all the requirements and claims payments are disbursed to the customer as per payment instrument selected.

The products offered by the applicant includes health insurance, personal accident, home insurance and travel insurance. The participant has also obtained 100% risk transfer arrangement with existing insurer for allowed sum cover limits.

Performance

FIRST DIGITAL GENERAL TAKAFUL – DIGITAL ONLY TAKAFUL OPERATOR	
No of policies sold	1700+
Average contribution	Rs. 880
Gross contribution	Rs. 1.5 million+
Amount of Claims	Rs. 169,000
No. of Claims	15
Claim settlement period	2 Days

Learnings

Testing of this model enabled better understanding of:

Operations of digital only insurer model for micro insurance

Identification of suitable products that can be offered through digital only models

Appropriate limits/ or caps that are needed to be placed on sum insured under various products

Identification of possible issues that may arise in the products and processes



Securities and Exchange Commission of Pakistan

WWW.SECP.GOV.PK