

### Box 5: Brief History of DFIs in Pakistan

In developing economies, the DFIs have played a beneficial role by boosting the industrialization process in the early stages of their economic development.<sup>179</sup> Besides, DFIs also bring international experience in the domestic market, which adds to the diversity of the existing range of financial services.

Over the period, the DFIs have stepped into financing activities like corporate financing, leasing, trade financing, refinancing, SME financing and house financing directly competing with banks. Instead of being a driver for economic development, the performance of DFIs in Pakistan has remained on lower side.

#### *History of DFIs...*

DFIs, around the globe, were established in 50s and 60s, as an initiative of the World Bank Group.<sup>180</sup> The purpose of the DFIs was to support the developing countries in industrialization process by making available long-term funding through public sector entities. In Pakistan, pre-nationalization, DFIs had played pioneering role in establishing the industrial base. Few of them are PICIC, PIDC and PIFC.

However, post nationalization, the DFIs incurred losses due to their financing to loss-making public sector enterprises.

The shift in philosophy of World Bank, globally, from project based lending to program based lending pared down the credit lines, which further worsened the financial health of DFIs.

The reasons for the failure of DFIs have also been identified as strong public sector orientation, political interference, compromised credit standards, non-performing loans and inability to raise funds from the market.<sup>181</sup> The DFIs, in the region, which

survived were those who had adjusted to market dynamics, diversified their financial activities to strengthen their income stream, implemented corporate governance framework and raised their own long term funding through secondary market.

#### *Post reforms...*

The experiment of nationalization was unsuccessful to obtain the desired results of ensuring flow of financial services to the grass root level (ibid). The government opted for financial reforms, structural adjustment, and privatization. During reforms, few DFIs were closed down and few suffered heavy losses and were on the brink of shut down but rescued by government through considerable financial support. However, post privatization, private sector banks were incorporated with universal banking model that contributed positively in the enhancement of financial services. At the same time, DFIs kept struggling with their financial losses and in the absence of long-term credit lines, could not keep up with the pace of growing banking sector.

#### *Structure of DFIs, at present...*

There are 9 DFIs, out of which 7 DFIs have been established in cooperation with bilateral, one DFI is wholly owned by the Government and one DFI is established as a private-public partnership. The purpose for their establishment was to support economic development through financing the industrial sector, extend project financing and facilitate the trade between bilateral. However, their participation in the desired areas is limited due to various reasons including funding constrain

<sup>179</sup>Yaseen Anwar, 2011, "Role of Financial Institutions and Capital markets in Pakistan's Economy", Speech, PAF Air War College, Karachi, delivered on 21 December 2011.

<sup>180</sup>MARTÍNEZ, J. (2017). The role of development financial institutions in the new millennium. [Blog] World Bank Group. Available at: <http://blogs.worldbank.org/eastasiapacific/the->

[role-of-development-financial-institutions-in-the-new-millennium](#) [Accessed 5 Mar. 2019].

<sup>181</sup>Faruqi, S. (2015). The Role of DFIs in Industrial Growth and Transformation: Why the East Asian Countries Succeeded and Pakistan Did Not. The Lahore Journal of Economics, (20), pp.13-33.