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**FUND'S INFORMATION**

## MISSION STATEMENT

*The Pakistan Capital Market Fund's mission is to provide investors the benefit from an investment portfolio of high quality shares, debt securities and money market transactions, which optimises return with an emphasis on minimising risk.*



**PAKISTAN CAPITAL MARKET FUND**

S. No.	Name	Designation	Meetings		
			Total	Attended	Leave Granted
1.	Mr. John W. Kirkham	Chairman	6	2	4
2.	Mr. Salim Chamdia	Vice Chairman	6	5	1
3.	Mr. Nasim Beg	Chief Executive	6	6	-
4.	Mr. Muhammad Akmal Jameel	Director	6	4	2
5.	Mr. Muhammad Shafi Malik	Director	1	1	-
6.	Mr. Muhammad Kashif	Director	1	1	-
7.	Mr. Sirajudin Cassim	Director	6	-	6
8.	Mr. Arif Habib	Former Chairman	6	5	1
9.	Mr. Samad A. Habib	Former Director	5	4	1
10.	Mr. Mohammad Yousuf	Former Director	5	5	-

S. No.	Trades by	Designation	<i>Investment</i>	<i>Redemption</i>
			<i>(No. of Units)</i>	
1.	Mr. Nasim Beg	Chief Executive	105,040	147,899
2.	Syed Ajaz Ahmed	Company Secretary & CFO	807	-









## Future outlook

### *Attractive relative valuations compared to regional peers*

In our view, equities should remain a favoured asset class in 2008. Capital markets globally are on an unprecedented run and Pakistan equities market is no exception. There are some real fundamentals working that are pushing equity markets higher. The Pakistan equity market historically has been trading at very low multiples offering deeply discounted prices in respect to valuations and also compared to its regional peers. With a sound economic growth story and global fund managers seeking bargains, Pakistan has been the beneficiary recipient of foreign portfolio and direct investments. The Price-Earnings Ratio of stocks in Pakistan now averages around 13 times on last reported earnings, which is not excessively high or expensive relative to its own historic averages or regional comparison.

### *Tight monetary policy likely to continue*

Monetary policy is likely to remain tight as inflationary pressures have not yet subsided. While, the SBP is expected to keep interest rates tilted at the higher end, liquidity in the banking system and slowing credit demand should not cause a major increase in overall interest rates.

### *Uncertainty in the run-up to the elections*

For the equity market, the biggest challenge in FY2008 will be domestic political instability and worsening of security situation in the run-up to elections in coming winter. The cautionary note here is the real (or perceived) political instability which may curb some of the inflows especially from foreign portfolio investors in the short term.

### *High trade deficit to be a challenge*

Key challenges for the economy are worsening trade deficit (at \$13.5 billion) and higher current account deficit (\$7.0 billion or 4.8% of GDP during 2007). The weakness in exports resulting in higher trade deficit will need to be cushioned with more foreign investment or privatization / disinvestment proceeds.

### *Fundamentals conducive to long-term investment*

Pakistani economy has grown at an average rate of 7% during the past five years, and we expect that this growth will be sustained in FY2008. We are confident that the broader fundamentals of the stock market are conducive to long-term investment. Rising per capita income is expected to drive aggregate demand in major sectors: Autos, Fertilizer, consumer goods, Banks, infrastructure and Energy. We thus anticipate that these sectors are well-poised to leverage off the overall growth of the economy.

## PAKISTAN CAPITAL MARKET FUND

### Associated Companies

Arif Habib Investment Management Limited	1,018,626
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### Directors and CEO

Chief Executive

Nasim Beg	6,453
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Director:

Akmal Jameel	-
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<b>Public Limited Companies</b>	8,527,440
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<b>Banks and Financial Institutions</b>	14,020,366
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<b>Individuals</b>	43,742,759
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<b>Retirement Funds</b>	3,554,944
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<b>Other Corporate Sector Entities</b>	2,593,856
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<b>Non Profit Organizatons</b>	823,752
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<b>TOTAL</b>	<b>74,288,196</b>
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**REPORT OF THE TRUSTEE**

**Report of the Trustee Pursuant to Rule 76(h) of the Non- Banking Finance Companies (Establishment and Regulation) Rules, 2003.**

The Pakistan Capital Market Fund (PCMF), a closed-end fund was established under a trust deed executed between Arif Habib Investment Management Limited as the Investment Adviser and Central Depository Company of Pakistan Limited as the Trustee on October 27, 2003. The Scheme was authorized by the Securities and Exchange Commission of Pakistan (SECP) on November 5, 2003.

Pakistan Capital Market Fund was converted from a closed end fund to an open end fund on November 21, 2005 under a supplemental trust deed executed between Arif Habib Investment Management Limited as the Asset Management Company and Central Depository Company of Pakistan Limited as the Trustee on October 5, 2005. The conversion was authorized by SECP on June 24, 2005.

In our opinion, Arif Habib Investment Management Limited, the Asset Management Company of Pakistan Capital Market Fund has in all material respects managed Pakistan Capital Market Fund during the year ended June 30, 2007 in accordance with the provisions of the Trust Deed (and the modifications authorized by SECP from time to time) and Non- Banking Finance Companies (Establishment and Regulation) Rules, 2003.

For the purpose of information, the attention of the Unit Holders is drawn towards the Auditors' report where in they have specified that Term Finance Certificates have not been valued on the basis of Non-Banking Finance Companies (Establishment and Regulation) Rules, 2003.

**Kamran Qazi**

Company Secretary

Central Depository Company of Pakistan Limited

Karachi: September 6, 2007

**STATEMENT OF COMPLIANCE  
WITH THE CODE OF CORPORATE GOVERNANCE  
FOR THE YEAR ENDED 30 JUNE 2007**

This statement is being presented by the Board of Directors of Arif Habib Investment Management Limited (Company), the Management Company of the Pakistan Capital Market Fund (Fund) to comply with the Code of Corporate Governance contained in Regulation No. 37, Chapter XIII and Chapter XI of listing regulations of Karachi, Lahore and Islamabad stock exchanges respectively for the purpose of establishing a framework of good governance, whereby a listed company is managed in compliance with the best practices of corporate governance.

The Management Company has applied the principles contained in the Code in the following manner:

1. The Management Company encourages representation of independent non-executive directors and directors representing minority interests on its Board of Directors. At present the Board includes six non-executive directors however, none of the directors on the Board represent minority shareholders.
2. The directors have confirmed that none of them is serving as a director in more than ten listed companies, including this Company.
3. All the resident directors of the Management Company are registered as taxpayers and none of them has defaulted in payment of any loan to a banking company, a DFI or an NBFIs or, being a member of a stock exchange, has been declared as a defaulter by that stock exchange.
4. Casual vacancies occurred thrice during the year in the Board. On 27 January 2007 Mr. Samad A. Habib and Mr. Mohammad Yousuf resigned and were replaced by Mr. Muhammad Kashif Habib and Mr. Shafi Malik respectively on the same day. On 14 June 2007 Mr. Arif Habib, the Chairman of the Board, resigned. Mr. John Kirkham was appointed as new Chairman of the Board on 04 July 2007.
5. The Management Company has prepared a 'Statement of Ethics and Business Practices', which has been approved by the Board of Directors and signed by all the directors, management and employees of the Company.
6. The Board has developed mission statement and significant policies of the Fund. A complete record of particulars of significant policies along with the dates on which they were approved or amended has been maintained.
7. All the powers of the Board have been duly exercised and decisions on material transactions, including appointment and determination of remuneration and terms and conditions of employment of the Chief Executive (CE) has been taken by the Board. There is no other executive director of the company besides the CE.
8. The meetings of the Board were presided over by the Chairman and, in his absence, by a director elected by the Board for this purpose and the Board met at least once in every quarter. Written notices of the Board meetings, along with agenda and working papers, were circulated at least seven days before the meeting. The minutes of the meetings were appropriately recorded and circulated and signed by the Chairman of the meeting of the Board of Directors.

## PAKISTAN CAPITAL MARKET FUND

9. The Board arranged an orientation course for new directors during the year to apprise them of their duties and responsibilities.
10. The Board has approved appointment, remuneration and term and conditions of the employment of Chief Financial Officer, Head of Internal Audit and the Company Secretary. During the year appointment of Head of Internal Audit was made by the Board.
11. The roles and responsibilities of the Chairman and Chief Executive have been approved by the Board of Directors.
12. The Directors' Report of the Fund for this year has been prepared in compliance with the requirements of the Code and fully describes the salient matters required to be disclosed.
13. The Directors, CE and executives of the Company do not hold any interest in the units of the Fund other than that disclosed in the pattern of unit holding.
14. The financial statements of the Fund were duly endorsed by CE and CFO of the Management Company before approval of the Board.
15. The Management Company has complied with all the significant corporate and financial reporting requirements of the Code relevant to the Fund.
16. The Board has formed an audit committee for the Fund. It comprises four members, all of whom are non-executive directors including the Chairman of the committee.
17. The meetings of the audit committee were held at least once every quarter prior to approval of the interim and final results of the Fund and as required by the Code. The terms of reference of the committee have been formed and advised to the committee for compliance.
18. There exists an effective internal audit function within the Company.
19. The statutory auditors of the Fund have confirmed that they have been given a satisfactory rating under the quality control review program of the Institute of Chartered Accountants of Pakistan, that they or any of the partners of the firm, their spouses and minor children do not hold units of the Fund and that the firm and all its partners are in compliance with International Federation of Accountants (IFAC) guidelines on code of ethics as adopted by Institute of Chartered Accountants of Pakistan.
20. The statutory auditors or the persons associated with them have not been appointed to provide other services except in accordance with the listing regulations and the auditors have confirmed that they have observed IFAC guidelines in this regard.
21. We confirm that all other material principles contained in the Code have been complied with.

For and on behalf of the Board

Karachi  
21 July 2007

Nasim Beg  
Chief Executive



## **INDEPENDENT AUDITORS' REPORT TO THE UNIT HOLDERS**

We have audited the accompanying financial statements of **Pakistan Capital Market Fund**, which comprise the statement of assets and liabilities as at 30 June 2007, and the income statement, distribution statement, cash flow statement and statement of movement in unit holders' funds for the year then ended, and a summary of significant accounting policies and other explanatory notes.

### *Management's responsibility for the financial statements*

Management Company of the Fund is responsible for the preparation and fair presentation of these financial statements in accordance with the requirements of the Trust Deed, the Non-Banking Finance Companies (Establishment and Regulation) Rules, 2003 (NBFC Rules) and approved accounting standards as applicable in Pakistan. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

### *Auditors' responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards as applicable in Pakistan. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### *Basis of qualified opinion*

As more fully explained in note 3.1 to the financial statements, the investment of the Fund in Term Finance Certificates (TFCs) was not marked to market on the basis of the rates quoted on the stock exchange as per the requirements of the Non-Banking Finance Companies (Establishment and Regulation) Rules, 2003. Instead, the investment of the Fund in TFCs was valued on the basis of the rates obtained from stock exchange website adjusted for the effect of partial redemption of the principal amount of these certificates, not been incorporated in these rates. Had the Term Finance Certificates been valued at last sale price quoted on the stock exchange, the carrying value of the investment as at 30 June 2007 would have been higher by Rs. 3.076 million with corresponding effect on income and unit holders' fund. In addition, as the Net Asset Value of the Fund was not determined strictly in accordance with NBFC Rules, it would have been different and consequently the number of units issued / redeemed as well as the element of accrued income / (loss) and capital gains / (losses) included in units issued less those in units redeemed recorded by the Fund were also affected. These effects have not been quantified, as it was not practical to do so.

## PAKISTAN CAPITAL MARKET FUND

### *Qualified Opinion*

In our opinion, except for the effect on the financial statements of the matter described in the preceding paragraph the financial statements give a true and fair view of the state of the Fund's affairs as at 30 June 2007, and of its financial performance, cash flows and transactions for the year then ended in accordance with approved accounting standards as applicable in Pakistan.

### *Other matters*

In our opinion, the financial statements have been prepared in accordance with the relevant provisions of the Trust Deed and NBFC Rules.

The financial statements of the Fund for the year ended 30 June 2006 were audited by another firm of Chartered Accountants who vide their report dated 16 September 2006 issued a qualified report thereon.

Dated: 21 July 2007  
Karachi

**KPMG Taseer Hadi & Co.**  
Chartered Accountants



**STATEMENT OF ASSETS AND LIABILITIES  
AS AT 30 JUNE 2007**

	<i>Note</i>	2007 (Rupees in '000)	2006
<b>Assets</b>			
Bank balances	4	180,573	55,240
Investments	5	917,419	1,362,174
Dividend and profit receivable	6	3,454	6,671
Advances, deposits, prepayments and other receivables	7	2,133	8,990
Preliminary expenses and floatation costs	8	4,592	7,492
Conversion cost	9	4,981	6,449
<b>Total Assets</b>		<b>1,113,152</b>	<b>1,447,016</b>
<b>Liabilities</b>			
Payable on redemption of units		2,519	1,428
Payable to Arif Habib Investment Management Limited - Management Company	10	2,674	3,171
Payable to Central Depository Company of Pakistan Limited - Trustee	11	174	195
Payable to Securities and Exchange Commission of Pakistan - Annual fee	12	1,253	1,670
Accrued expenses and other liabilities	13	19,193	1,837
Advance against issue of certificates	14	200	200
Dividend payable		2,942	2,864
<b>Total Liabilities</b>		<b>28,955</b>	<b>11,365</b>
<b>Net Assets</b>		<b>1,084,197</b>	<b>1,435,651</b>
<b>Unit holders' funds (as per statement attached)</b>		<b>1,084,197</b>	<b>1,435,651</b>
		<b>(Number of Units)</b>	
<b>Number of units in issue</b>		<b>74,288,196</b>	<b>98,832,091</b>
		<b>(Rupees)</b>	
<b>Net asset value per unit</b>		<b>14.59</b>	<b>14.53</b>

The annexed notes 1 to 25 form an integral part of these financial statements.

**For Arif Habib Investment Management Limited  
(Management Company)**

**Chief Executive**

**Director**

**PAKISTAN CAPITAL MARKET FUND**


**For Arif Habib Investment Management Limited  
(Management Company)**

**Chief Executive**

**Director**



**DISTRIBUTION STATEMENT  
FOR THE YEAR ENDED 30 JUNE 2007**

	2007 (Rupees in '000)	2006
Undistributed income brought forward	346,580	341,163
Net income for the year	108,929	392,053
Element of income and capital gains included in prices of units sold less those in units repurchased - amount representing unrealized capital (losses)	(5,812)	(124,383)
Cash distribution @ 30% for the year ended 30 June 2006 (2005 :17.5%)	(24,854)	(262,253)
Final distribution for the year ended 30 June 2006 @ 30 % (2005 : Nil) - transfer to reserve for issue of bonus units	(271,642)	-
	(193,379)	5,417
Undistributed income carried forward	<u>153,201</u>	<u>346,580</u>

The annexed notes 1 to 25 form an integral part of these financial statements.

**For Arif Habib Investment Management Limited  
(Management Company)**

**Chief Executive**

**Director**

**STATEMENT OF MOVEMENT IN UNIT HOLDERS' FUND  
FOR THE YEAR ENDED 30 JUNE 2007**

	<i>Note</i>	2007 (Rupees in '000)	2006
Net assets at the beginning of the year		1,435,651	1,960,420
Issue of 149,859,000 units at the time of conversion		-	1,498,590
Cancellation of 149,859,000 certificates at the time of conversion		-	(1,498,590)
		-	-
Issue of 49,148,960 units (2006: 65,970,061 units)		581,472	973,379
Redemption of 97,252,448 units (2006: 116,996,971 units)		(1,183,280)	(1,775,167)
		(601,808)	(801,788)
Element of (income) and capital (gains) included in prices of units issued less those in units repurchased			
- amount representing accrued (income) and realised capital (gains) - transferred to the income statement		78,915	167,135
- amount representing unrealised capital losses / (gains) transferred directly to the Distribution Statement		5,812	124,383
		84,727	291,518
Net unrealised appreciation / (diminution) during the year in market value of investments classified as 'available for sale'	5.4	87,364	(19,916)
Issue of 23,559,593 bonus units for the year ended 30 June 2006 (2005 : Nil)		271,642	-
Net income for the year less distribution		(193,379)	5,417
Net Assets as at the end of the year		<u>1,084,197</u>	<u>1,435,651</u>

The annexed notes 1 to 25 form an integral part of these financial statements.

**For Arif Habib Investment Management Limited  
(Management Company)**

**Chief Executive**

**Director**

**NOTES TO THE FINANCIAL STATEMENTS  
FOR THE YEAR ENDED 30 JUNE 2007**

**1. LEGAL STATUS AND NATURE OF BUSINESS**

Pakistan Capital Market Fund (PCMF) was established under a Trust Deed executed between Arif Habib Investment Management Limited (AHIML) as Investment Adviser and Central Depository Company of Pakistan Limited (CDC) as Trustee on 27 October 2003. The Investment Adviser of PCMF has obtained the requisite license from the Securities and Exchange Commission of Pakistan (SECP) to undertake investment advisory services under the Non-Banking Finance Companies (Establishment and Regulation) Rules, 2003 (NBFC Rules). Formation of PCMF as a closed-end scheme was authorised by SECP on 5 November 2003. PCMF is listed on all three stock exchanges in Pakistan. The certificates of PCMF were offered for public subscription from 22 January 2004 to 24 January 2004. PCMF started investing activities from 26 January 2004.

AHIML entered into a Supplemental Trust Deed with the CDC (Trustee) on 5 October 2005 in order to initiate the conversion of the Fund from a closed-end scheme to an open-end scheme pursuant to the resolution passed at a meeting of the Certificate Holders' held on 21 May 2005, approving the same. The conversion of the Fund from a closed-end scheme to an open-end scheme was authorised by SECP vide its letter no. NBFC-II/JD(R)/AHIM/481 dated 24 June 2005. The post conversion Trust Deed and post conversion Offering Document were approved by SECP vide letter no. NBFC/MF-AD-II(R)/683/2005 dated 20 September 2005 and letter no. NBFC-II/JD(R)/AHIM-PCMF/744 dated 17 October 2005 respectively. The Fund was converted into an open-end scheme with effect from 21 November 2005. Each certificate holder was allotted units according to their respective holdings as at that date on the basis of a ratio of 1 certificate : 1 unit. Accordingly, 149,859,000 units were issued at the rate of 14.61 per unit, thus constituting Rs. 2.189 billion i.e. the Net Asset Value of the Fund on the date of conversion.

AHIML also holds the requisite licence from the SECP to undertake asset management service under the Non-Banking Finance Companies (Established and Regulation) Rules 2003. The registered office of the management company is situated at 2/1, R.Y.16, Old Queens Road, Karachi, Pakistan.

The policy of the Fund is to invest in a mix of listed equity and debt securities, unlisted government securities and secured debt securities, money market transactions and reverse repurchase transactions.

Title to the assets of the Fund are held in the name of Central Depository Company Limited as a trustee of the Fund.

**2. BASIS OF PREPARATION**

**2.1 Statement of Compliance**

These financial statements have been prepared in accordance with approved accounting standards as applicable in Pakistan and the requirements of the Trust Deed, NBFC Rules and directives issued by the Securities and Exchange Commission of Pakistan (SECP). Approved accounting standards comprise of such International Accounting Standards (IASs) / International Financial Reporting Standards (IFRSs) as notified under the provisions of the Companies Ordinance 1984. Wherever the requirements of the Trust Deed, NBFC Rules or directives issued by SECP differ with the requirements of these standards, the requirements of the Trust Deed, NBFC Rules and the said directives take precedence.

**2.2 Basis of measurement**

These financial statements have been prepared under the historical cost convention, except that certain financial assets have been included at fair value in accordance with the recognition criteria specified in the relevant IAS applicable to these assets and the requirements of NBFC Rules.

**2.3 Functional and presentation currency**

These financial statements are presented in Pak Rupees, which is the functional and presentation currency of the Fund and rounded to the nearest thousand rupees.

**2.4 Use of estimates and judgements**

The preparation of financial statements in conformity with approved accounting standards as applicable in Pakistan requires management to make judgments, estimates and assumptions that affect the application of policies and reported amount of assets and liabilities, income and expenses. The estimate and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making judgments about carrying value of assets and liabilities which are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revision to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of its revision and future periods if the revision affects both current and future periods.

Information about significant areas of estimation, uncertainty and critical judgements in applying accounting policies that have the most significant effect on amounts recognised in the financial statements are described in note 20 and 21.

**3. SIGNIFICANT ACCOUNTING POLICIES**

The accounting policies set out below have been applied consistently to all periods presented in these financial statement.

**3.1 Investments**

All investments are initially recognised at fair value, being the cost of the consideration given including transaction cost associated with the investment, except in case of held for trading investments, in which case the transaction costs are charged off to the income statement.

All purchases and sales of securities that require delivery within the time frame established by regulation or market convention such as 'T+3' purchases and sales are recognised at the trade date. Trade date is the date on which the Fund commits to purchase or sale of assets.

The management determines the appropriate classification of the investment made by the Fund in accordance with the requirements of International Accounting Standards (IAS) 39: 'Financial Instruments: Recognition and Measurement', at the time of purchase.

The fund classifies its investments in the following categories:

### *Available for sale*

Investments intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in market prices, are classified as 'available for sale'. Subsequent to initial measurement, 'available for sale' investments are re-measured to fair value. Net gains and losses arising on changes in fair values of these investments are taken to equity as part of Unit Holders' Funds. However, any premium or discount on acquisition is amortised and taken to the Income Statement over the life of the investment using the effective interest rate method. When securities are disposed off or impaired, the related fair value adjustments previously taken to equity are transferred to the Income Statement.

### *Financial assets 'at fair value through profit or loss - held for trading'*

Investments that are acquired principally for the purpose of generating a profit from short-term fluctuations in prices are classified as financial assets 'at fair value through profit and loss - held for trading'. Subsequent to initial recognition these investments are marked to market and are carried on the Statement of Assets and Liabilities at fair value. Net gains and losses arising on changes in fair values of these investments are taken to the Income Statement.

### *Basis of valuation of Term Finance Certificates*

The Fund values its investment in listed Term Finance Certificates (TFCs) on the basis of rates obtained from stock exchange website which are adjusted for the purpose of marking to market the investment of the Fund in TFCs on the basis that the effect of partial redemption of the principal amount of these certificates has not been incorporated in these rates. NBFC Rules require securities which are quoted on the stock exchange should be valued at its last sale price on such exchange on the date on which it is valued. However, the management believes that the policy adopted by the Fund is fair to all investors and protects their interests. Had the TFCs been valued at last sale price quoted on stock exchange, the carrying value of the investments would have been higher by Rs. 3.076 million. Further, the Net Asset Value (NAV) of the Fund during the year would have been different and consequently the number of units issued / redeemed during the year as well as the element of income / (loss) and capital gains / (losses) included in the prices of units issued less those in units redeemed recorded by the Fund would also have been different. These effects have not been quantified as it was not practical to do so.

## **3.2 Derivatives**

Derivative instruments held by the Fund generally comprise of future contracts, forward contracts and options in the capital market. These are initially recognised at fair value on the date a derivative contract is entered into and are subsequently remeasured at their fair value which is their quoted price. Derivatives with positive market values (unrealised gains) are included in assets and derivatives with negative market values (unrealised losses) are included in liabilities in the statement of assets and liabilities. The resultant gains and losses are included in the income statement.

Derivative financial instruments entered into by the Fund do not meet the hedging criteria as defined by International Accounting Standard - 39, Recognition and Measurement of Financial Instruments (IAS - 39), consequently hedge accounting is not used by the Fund.



**3.3 Securities under repurchase / resale agreements**

Transactions of purchase under resale (reverse-repo) of marketable and government securities, including the securities purchased under continuous funding system, are entered into at contracted rates for specified periods of time. Securities purchased with a corresponding commitment to resell at a specified futures date (reverse-repo) are not recognised in the statement of assets and liabilities. Amount paid under these agreements are included in receivable in respect of reverse repurchase transactions / against continuous funding system. The difference between purchase and resale price is treated as income from reverse repurchase transactions / continuous funding system and accrued over the life of the reverse-repo agreement.

All reverse repo / continuous funding system transactions are accounted for on settlement date.

**3.4 Issue and redemption of units**

Units issued are recorded at the offer price, determined by the Management Company for the applications received by the distributors during business hours on that date. The offer price represents the net asset value per unit as of the close of the business day plus the allowable sales load, provision for transaction costs and any provision for duties and charges, if applicable. The sales load is payable to the investment facilitators, distributors and the Management Company. Transaction costs are recorded as the income of the Fund.

Units redeemed are recorded at the redemption price, applicable to units for which the distributors receive redemption requests during business hours of that day. The redemption price represents the net asset value per unit as of the close of the business day less any back-end load, any duties, taxes, charges on redemption and any provision for transaction costs, if applicable.

**3.5 Element of income / (loss) and capital gains / (losses) included in prices of units sold less those in units repurchased**

An equalisation account called the 'element of income / (loss) and capital gains / (losses) included in prices of units sold less those in units repurchased' is created, in order to prevent the dilution of per unit income and distribution of income already paid out on redemption.

The Fund records the net element of accrued income/ (loss) and realised capital gains/ (losses) relating to units issued and redeemed during an accounting period in the Income Statement while the portion of the element of income/ (loss) and capital gains/ (losses) that relates to unrealised gains/ (losses) held by the Fund in equity is recorded in a separate reserve account and any amount remaining in this reserve account at the end of an accounting period (whether gain or loss) is included in the amount available for distribution to Unit holders.

**3.6 Net asset value per unit**

The net asset value per unit as disclosed on the Statement of Assets and Liabilities is calculated by dividing the net assets of the Fund by the number of units in issue at the year end.

**3.7 Cash and cash equivalents**

Cash and cash equivalents comprise of bank balances.

### 3.8 Taxation

Provision for current taxation is based on taxable income at the current rates of taxation after taking into account tax credits and rebates available, if any.

The income of the Fund is exempt from income tax under clause 99 of Part I of the Second Schedule to the Income Tax Ordinance, 2001 subject to the condition that not less than ninety percent of its accounting income of that year, as reduced by capital gains, whether realised or unrealised, is distributed amongst the unit holders. Accordingly, no tax liability has been recorded for the current year.

The Fund provides for deferred taxation using the balance sheet liability method on all major temporary differences between the amounts used for financial reporting purposes and amounts used for taxation purposes. In addition, the Fund also records deferred tax asset on unutilised tax losses to the extent that it is no longer probable that the related tax benefit will be realised. However, the Fund has not recognised any amount in respect of deferred tax in these financial statements as the Fund intends to continue availing the tax exemption in future years by distributing at least ninety percent of its accounting income for the year as reduced by capital gains, whether realised or unrealised, to its unit holders every year.

### 3.9 Revenue recognition

- Gains / (losses) arising on sale of investments are included in the Income Statement in the period in which they arise.
- Unrealised capital gains / (losses) arising on marking to market of investments classified as 'financial assets at fair value through profit or loss - held for trading' are included in the Income Statement in the period in which they arise.
- Dividend income is recognised on the date of book closure of the investee company / institution declaring the dividend.
- Income on debt securities is recognised on an accrual basis.
- "Gains / (losses) arising on the revaluation of the derivatives to the fair value are taken to the Income Statement as discussed in note 3.2 to these financial statements."
- Income on reverse repurchase transactions, continuous funding system transactions and profit on bank deposits is recognised on a time proportionate basis.
- Transaction costs are recognized as income as and when the units are issued/converted/redeemed.

### 3.10 Expenses

All expenses including management fee and trustee fee are recognised in the income statement on an accrual basis.

**3.11 Impairment**

The carrying value of the Fund's assets are reviewed at each balance sheet date to determine whether there is any indication of impairment. If such an indication exists, the assets recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset exceed its recoverable amount. Impairment losses are recognised in the Income Statement.

**3.12 Provisions**

Provisions are recognised when the Fund has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the obligation can be made. Provisions are regularly reviewed and adjusted to reflect the current best estimate.

**3.13 Preliminary expenses and floatation costs**

Preliminary expenses and floatation costs represent expenditure incurred prior to the commencement of operations of the Fund and include underwriting commission, commission to the bankers to the issue, brokerage paid to the members of the stock exchanges and other expenses. These costs are being amortised over a period of five years.

**3.14 Conversion cost**

Conversion costs represent expenditure incurred in connection with the conversion of the Fund into an open end scheme and include fees paid to the Securities and Exchange Commission of Pakistan (SECP) and other expenses. These costs are being amortised over a period of five years as per clause 7.4 of the Post Conversion Offering Document of the scheme which has been approved by the Securities and Exchange Commission of Pakistan.

**3.15 Financial instruments**

All the financial assets and financial liabilities are recognised at the time when the Fund becomes a party to the contractual provisions of the instrument. At the time of initial recognition, except for those classified as "fair value through profit or loss", all financial assets and financial liabilities are measured at cost, which is the fair value of the consideration given or received for it. Transaction costs are included in the initial measurement of all financial assets and liabilities except for those classified as "fair value through profit or loss" and transaction costs that may be incurred on disposal. Any gain or loss on derecognition of the financial assets and financial liabilities is taken to income statement.

**3.16 Offsetting financial instruments**

Financial assets and liabilities are offset and the net amount is reported in the Statement of Assets and Liabilities when there is a legally enforceable right to set off the recognised amounts and there is an intention to settle on a net basis, or realise the assets and settle the liabilities simultaneously.

**3.17 Other assets**

Other assets other than derivatives are stated at cost less impairment losses, if any.

**3.18 Dividend distributions and appropriations**

Dividend distributions and appropriations are recorded in the period in which the distributions and appropriations are approved.

**3.19 New accounting standards and IFRIC interpretations that are not yet effective**

The following standards, amendments and interpretations of approved accounting standards are only effective for accounting periods beginning on or after 1 July 2007 and are not relevant to the Fund's operations or are not expected to have significant impact on the Fund's financial statements other than certain increased disclosures in the certain cases:

- IAS 1 - Presentation of Financial Statements - Amendments Relating to Capital Disclosures
- IAS 23 - Borrowing Costs - Amendments relating to mandatory capitalisation of borrowing costs relating to qualifying assets
- IAS 41 - Agriculture
- IFRS 2 - Share-based Payments;
- IFRS 3 - Business Combinations;
- IFRS 5 - Non-current Assets Held for Sale and Discontinued Operations;
- IFRS 6 - Exploration for and Evaluation of Mineral Resources;
- IFRIC 10 Interim Financial Reporting and Impairment;
- IFRIC 11 Group and Treasury Share Transactions;
- IFRIC 12 Service Concession Arrangements.
- IFRIC 13 Customer Loyalty Programmes.

		2007	2006
		(Rupees in '000)	
<b>4. BANK BALANCES</b>			
In current accounts		3,501	2,873
In deposit accounts		177,072	52,367
		<u>180,573</u>	<u>55,240</u>
<b>5. INVESTMENTS</b>			
Investment in marketable securities			
At fair value through profit or loss - held for trading	5.1	457,291	838,367
Available for sale	5.2	460,128	523,807
		<u>917,419</u>	<u>1,362,174</u>











## PAKISTAN CAPITAL MARKET FUND

	2007 (Rupees in '000)	2006
<b>16. AUDITOR'S REMUNERATION</b>		
Audit fee	225	225
Other certifications and services	365	315
Out of pocket expenses	40	27
	630	567

### 17. TRANSACTIONS WITH CONNECTED PERSONS

Connected persons include Arif Habib Investment Management Limited being the Management Company, Arif Habib Securities Limited and Arif Habib Limited being companies under common management, Central Depository Company Limited being the trustee of the Fund.

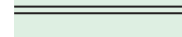
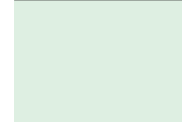
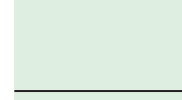
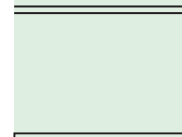
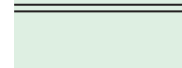
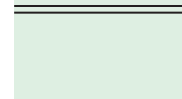
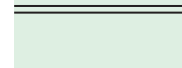
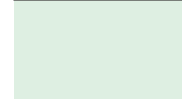
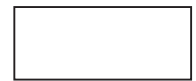
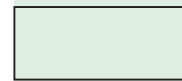
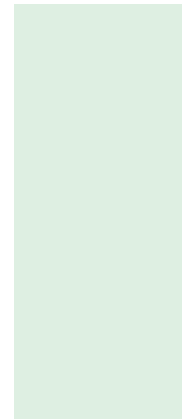
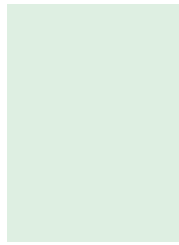
The transactions with connected persons are in the normal course of business, at contracted rates and terms determined in accordance with market rates.

Remuneration payable to management company and trustee is determined in accordance with the provisions of NBFC Rules and the Trust Deed respectively.

Details of the transactions with connected persons and balances with them at year end are as follows:

	2007 (Units)	2006	2007 (Rupees in '000)	2006
<b><u>Units sold to:</u></b>				
<i>Management Company</i>				
Arif Habib Investment Management Limited	11,447,327	13,858,497	132,155	190,000
<i>Associated Companies</i>				
Arif Habib Securities Limited- Brokerage house	-	38,909,900	-	568,474
<b>Other related parties</b>				
- Directors and executives of the management company	93,016	183,375	1,060	2,741
<b><u>Units redeemed by:</u></b>				
<i>Management Company</i>				
Arif Habib Investment Management Limited	27,893,052	-	340,332	-
<i>Associated Companies</i>				
Arif Habib Securities Limited- Brokerage house	-	38,909,900	-	581,071
<b>Other related parties</b>				
- Directors and executives of the management company	147,899	102,037	1,750	1,585
<b><u>Bonus units distributed to:</u></b>				
<i>Management Company</i>				
Arif Habib Investment Management Limited	3,605,853	-	41,575	-
<b>Other related parties</b>				
- Directors and executives of the management company	12,831	-	148	-

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## PAKISTAN CAPITAL MARKET FUND

- 17.1** The amount disclosed represents the amount of brokerage paid to connected person and not the purchase or sale values of securities transacted through them. The purchase or sale values have not been treated as transactions with connected persons as ultimate counter-parties are not connected persons.
- 17.2** During the year, as a result of certain risk management measures, the limit prescribed by NBFC Rules relating to the maximum transactions to be carried out through a connected broker was breached. The management is of the opinion that this limit has been imposed by NBFC Rules to ensure that brokerage expense in relation to the transactions entered into through a connected broker does not exceed 10 percent of the total brokerage expense of the Fund. Therefore, the management company, as a gesture of goodwill shall reimburse Rs. 0.328 million to the Fund representing the amount of brokerage in excess of the 10 percent limit. This amount is not repayable by the Fund at any later date.

Had the above arrangement not been made, the net income and cash flow for the year, equity and the total assets of the Fund as at 30 June 2006 would have been lower by Rs. 0.328 million.

### 18. FINANCIAL INSTRUMENTS AND RELATED DISCLOSURES

- 18.1** The Fund's MROR sensitivity related to financial assets and financial liabilities as at 30 June 2007 can be determined from the following:

	30 June 2007					Total
	Effective rate of mark-up / return (%)	Exposed to MROR risk			Not exposed to MROR risk	
		Upto three months	More than three months and upto one year	More than one year		
------(Rupees in '000)-----						
<b>On-balance sheet financial instruments</b>						
<b>Financial Assets</b>						
Bank balances	4.00 - 12.20	177,072	-	-	3,501	180,573
Investments	9.50 - 13.34	21,211	-	-	896,208	917,419
Dividend and profit receivable		-	-	-	3,454	3,454
Deposits and other receivables		-	-	-	1,728	1,728
		198,283	-	-	904,891	1,103,174
<b>Financial Liabilities</b>						
Payable on redemption of units		-	-	-	2,519	2,519
Payable to Arif Habib Investment Management Limited - Management Company		-	-	-	2,674	2,674
Payable to Central Depository Company of Pakistan Limited - Trustee		-	-	-	174	174
Payable to Securities and Exchange Commission of Pakistan - Annual fee		-	-	-	1,253	1,253
Accrued expenses and other liabilities		-	-	-	19,193	19,193
Dividend payable		-	-	-	2,942	2,942
		-	-	-	28,755	28,755
<b>On-balance sheet gap - 2007</b>		<b>198,283</b>	<b>-</b>	<b>-</b>	<b>876,136</b>	<b>1,074,419</b>
------(Rupees in '000)-----						
30 June 2006						
Exposed to MROR risk						
	Effective rate of mark-up / return (%)	Exposed to MROR risk			Not exposed to MROR risk	Total
		Upto three months	More than three months and upto one year	More than one year		
------(Rupees in '000)-----						
<b>On-balance sheet financial instruments</b>						
<b>Financial Assets</b>						
Bank balances	1.75 - 11.00	52,367	-	-	2,873	55,240
Investments	9.50 - 12.67	124,578	-	-	1,237,596	1,362,174
Dividend and profit receivable		-	-	-	6,671	6,671
Deposits and other receivable		-	-	-	8,585	8,585
		176,945	-	-	1,255,725	1,432,670
<b>Financial Liabilities</b>						
Payable on redemption of units		-	-	-	1,428	1,428
Payable to Arif Habib Investment Management Limited - Management Company		-	-	-	3,171	3,171
Payable to Central Depository Company of Pakistan Limited - Trustee		-	-	-	195	195
Payable to Securities and Exchange Commission of Pakistan - Annual fee		-	-	-	1,670	1,670
Accrued expenses and other liabilities		-	-	-	1,837	1,837
Dividend payable		-	-	-	2,864	2,864
		-	-	-	11,165	11,165
<b>On-balance sheet gap - 2006</b>		<b>176,945</b>	<b>-</b>	<b>-</b>	<b>1,244,560</b>	<b>1,421,505</b>

## **19. RISK MANAGEMENT**

The Fund primarily invests in shares of listed companies and debt securities, unlisted government securities, reverse repurchase transactions in government securities, secured debt securities and enters into Continuous Funding System transactions in listed securities. Such investments are subject to varying degrees of risk. These risks emanate from various factors that include, but are not limited to:

### **19.1 Market risk**

Market risk is the risk that the value of the financial instrument may fluctuate as a result of changes in market interest rates or the market price of securities due to a change in credit rating of the issuer or the instrument, change in market sentiments, speculative activities, supply and demand of securities and liquidity in the market.

The Management Company manages market risk by monitoring exposure on marketable securities by following the internal risk management policies and investment guidelines approved by the Investment Committee of Management Company and regulations laid down by the Securities and Exchange Commission of Pakistan (SECP).

### **19.2 Credit risk**

#### *Credit risk management*

Credit risk arises from the inability of the issuers of the instruments, the relevant financial institutions or counter parties in case of reverse re-purchase transactions or other arrangements to fulfil their obligations. There is a possibility of default by participants and of failure of the financial markets / stock exchanges, the depositories, the settlements or the clearing system etc.

The Fund's policy is to enter into financial contracts in accordance with the internal risk management policies and investment guidelines approved by the Investment Committee. In addition, the risk is managed through assignment of credit limits, obtaining adequate collaterals and by following strict credit evaluation criteria laid down by the Management Company. The Fund does not expect to incur material credit losses on its financial assets.

#### *Concentration of credit risk*

Concentration of credit risk exists when changes in economic or industry factors similarly affect groups of counterparties whose aggregate credit exposure is significant in relation to the Fund's total credit exposure. Financial assets subject to credit risk amount to Rs.1,103.641 million (2006: Rs.1,432.67 million). The Fund's portfolio of financial instruments is broadly diversified and transactions are entered into with diverse credit-worthy counterparties thereby mitigating any significant concentration of credit risk.

### **19.3 Liquidity risk**

Liquidity risk is the risk that the Fund may encounter difficulty in raising funds to meet its obligations and commitments. The Management Company manages the liquidity risk by maintaining maturities of financial assets and financial liabilities and investing a major portion of the Fund's assets in highly liquid financial assets.

**19.4 Market Rate of Return (MROR) Risk**

MROR risk is the risk that the value of a financial instrument will fluctuate due to changes in the market interest rates. The Fund manages its investments portfolio in order to reduce the risk of loss in market value of investments as a result of changes in market interest rates. In case the Management Company expects economic uncertainty the portfolio will be restructured so as to comprise of short-term debt securities, money market instruments, short maturity repurchase transactions, Continuous Funding System and reverse repurchase transactions.

**20. FAIR VALUE OF FINANCIAL INSTRUMENTS**

Investments on the Statement of Assets and Liabilities are carried at fair value. The Management Company is of the view that the fair value of the remaining financial assets and liabilities are not significantly different from their carrying values since assets and liabilities are essentially short term in nature.

**21. ACCOUNTING ESTIMATES AND JUDGEMENTS**

The management company makes estimates and assumptions that effect the reported amount of assets and liabilities. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

*Investments stated at fair value*

The management company has determined fair value of certain investments by using quotations from active market. Fair value estimates are made at a specific point in time, based on market conditions and information about the financial instruments. These estimates are subjective in nature and involve uncertainties and matter of judgements (e.g. valuation, interest rates, etc.) and therefore, can not be determined with precision.

*Other assets*

Judgement is also involved in assessing the realisability of the assets balances.

**22. NON-ADJUSTING EVENT AFTER THE BALANCE SHEET DATE**

The Board of Directors of the Management Company have approved bonus of Rs. 3 per unit (2006: Rs. 3 per unit) for the year ended 30 June 2007, amounting to Rs. 222.86 million (2006: 296.46 million) in total in their meeting held on 04 July 2007. Out of this, Rs. 24.85 million (2006: 24.85 million) will be distributed as cash dividend and Rs. 198.01 million (2006: Rs. 271.64 million) as bonus units.

## PAKISTAN CAPITAL MARKET FUND

	2007	2006	2005	2004
	----- <b>(Rupees in '000)</b> -----			
<b>23. PERFORMANCE TABLE</b>				
Net assets	<b>1,084,197</b>	1,435,651	1,698,167	1,618,903
Net income for the year	<b>108,929</b>	392,053	525,758	126,354
	----- <b>(Rupees)</b> -----			
Net assets value per unit	<b>14.59</b>	14.53	13.08	9.97
	----- <b>(Percentage)</b> -----			
Dividend distribution - Interim (%)	-	-	12.50	-
Dividend distribution - Final (%)	<b>30.00</b>	30.00	17.50	8.25
	----- <b>(Rupees)</b> -----			
Highest offer price per unit	<b>14.98</b>	16.92	17.84	11.27
Lowest offer price per unit	<b>11.31</b>	12.44	9.98	10.19
Highest repurchase price per unit	<b>14.61</b>	16.50	17.39	10.99
Lowest repurchase price per unit	<b>11.03</b>	12.13	9.73	9.94

## 24. CORRESPONDING FIGURES

Corresponding figures have been rearranged and reclassified for the purposes of comparison and better presentation as follows:

Reclassification from component	Reclassification to component	Amount (Rupees in '000)
Receivable against sale of units	Bank balance	3,299

## 25. DATE OF AUTHORISATION FOR ISSUE

These financial statements were authorised for issue on 21 July 2007 by the Board of Directors of the Management Company.

**For Arif Habib Investment Management Limited  
(Management Company)**

Chief Executive

Director