PAKOMAN ASSET MANAGEMENT

Dated May 28, 2012

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Budget Highlights

- The total budget outlay is expected to be PKR 3.62tn
- Proposed PSDP outlay is PKR 873bn
- The size of GDP is estimated at PKR 20.7tn
- No new taxes are expected in upcoming budget
- KSE has proposed 5% tax relief for listed companies

Sector Impact	
Sector	**Impact**
Fertilizer	Negative
Cement	Positive
Banks	Negative
Power	Neutral
Auto	Neutral
Textile	Negative

Budget Preview FY2012-13

Budget at a Glance:

Budget Snapshot		
PKR Bn	**FY12B***	**FY13F****
Tax Revenue	1,331	1,469
FBR Collections	744	791
Total Tax Revenue	**2,075**	**2,260**
Non tax revenue	658	616
Total revenue	2,733	2,876
Transfer to provinces	1,203	1,266
Net Federal Revenue	1,530	1,610
Net Capital Receipts	394	490
Net External Receipts	344	350
Total Resources	**2,268**	**2,450**
Current Expenditure	2,314	2,744
PSDP	521	873
Total Federal Expenditure	**2,835**	**3,617**
Federal budget deficit	(567)	(1,167)
as % of GDP	-3%	-5.64%
Provincial budget surplus	125.00	100.00
Consolidated budget deficit	(442)	(1,067)
as % of GDP	-2.10%	-5.15%
GDP (PKR Bn)	**21,041**	**20,700**

****B=Budgeted***

***** F=Forecasted***

Salient Features:

- As year 2013 is election year, the government is expected to come up with a higher overall budget outlay.
- The total outlay of budget 2012-13 is expected to be PKR 3.62tn.
- The availability of resources has been estimated at PKR 2,450bn during 2012-13.
- Net federal revenue receipts for 2012-13 have been estimated at PKR 1,610bn indicating an increase of 5.23% over the budget estimates of fiscal year 2011-12.
- The provincial share in federal revenue receipts is estimated at PKR 1,266bn during 2012-13 which is 5.24% higher than the budget estimates of 2011-12.
- Proposed Public sector development program (PSDP) outlay is PKR 873bn, including federal PSDP of PKR 360bn and provincial PSDP of PKR 513bn.
- The size of GDP is estimated at PKR 20.7 trillion (USD 232bn).
- The overall expenditure during 2012-13 has been estimated at PKR 3.62bn of which the current expenditure is PKR 2,744bn and development expenditure at PKR 873bn.
- Consolidated Budget deficit is estimated at PKR 1,067bn which is 5.15% of GDP
- General Sales Tax (GST) will remain the same at 16%.
- FED on cement is further expected to decline by PKR200/ton to PKR300/ton from PKR500/ton.
- Minimum taxable salary level is being considered to increase from PKR 350,000 to PKR 400,000.
- No new taxes are expected in the upcoming budget.
- Gas Infrastructure Development Cess (GIDC) is further expected to increase on certain sectors including fertilizers, cement and IPPs to generate the funds for Iran-Pakistan pipeline project.
- Government is considering increase in subsidy on imported urea to support agriculture sector.
- To promote the usage of scrap rubber as an alternate fuel to coal in the cement industry, government is considering removing custom duty on shredded rubber scrap.
- Power tariffs are expected to increase in order to reduce the burden of subsidy on government.

- Government may remove 50% regulatory duty on luxury items, applicable on cars above 1800cc engine size.
- Proposals under discussion for the budget also include implication of 50% tax on T-bill income or 5% higher corporate tax for banks, which is less likely to be implemented as government relies heavily on bank borrowing for deficit financing.
- KSE management has proposed 5% cut in corporate tax for listed companies.

Budgetary Measures & Impact on Sectors		
Sector	**Budgetary Measure Expected**	**Estimated Budgetary Impact**
Equity Market	Implementation of CGT	Positive
Telecom	Issuance of 3G license by the government	Negative
	Ending sales tax exemption to broad band users	Neutral to negative
Automobile Assemblers	Removal of 50% regulatory duty on imported luxury items	Negative
	Cut in CKD duty from 32.5% to 20%	Neutral to Positive
	Cut in CBU import duties by 5-15%	Negative
Fertilizers/Chemical	Increase in subsidy for urea imports	Negative
	Increase in presumptive tax for importers	Negative
	Increase in custom duty o PTA, PVC & hydrogen peroxide	Positive
	Increase in GIDC	Negative
Cement	PSDP allocation PKR 825bn	Positive
	Reduction in FED by PKR 200/ton	Positive
	Application of 16% GST on retail price	Neutral to negative
	Withdrawal of custom duty o rubber scrap	Positive
	Rise in presumptive tax for exporters	Negative
Power	Increase in Power tariff	Positive
	Increase in GIDC & PL	Negative
	Continuation of power subsidy	Neutral
Textile	Increase in GIDC	Negative
Commercial Banks	Tax rate on interest earned from T-bills to 50%	Negative
	5% increase in corporate tax rate	Negative
	Increase in tax free cash withdrawal limit	Neutral

Equity Market:

Karachi Stock Exchange has proposed some measure for the upcoming budget, which are mentioned below with their respective impacts on the performance of market:

- 5% cut in corporate tax rate for listed companies: Companies may opt for listing if they are offered tax incentive. It will bring more capital in the market.
- Mandatory requirement to pay 40% profits as dividends: As compulsory 40% payout ratio has some drawbacks, so the KSE management has proposed that companies with payout ratio of less than 40% be taxed at 3% higher than the companies having payout ratio of 40% or higher.
- Removal of tax on dividends received by companies: To eliminate the dual taxation for shareholders, KSE has proposed the removal of tax o dividends received by the companies.
- Calculation of CGT for foreigners in foreign currency: KSE has recommended that capital gain tax should be calculated in foreign currency for foreign investors to apply tax on real income only instead of notional income which occurs due to exchange rate.

Estimated Impact: Positive

- The approval of proposed measures will boost investors' confidence and hence the performance of the market.

Sector Wise impact of Budget expectations

Fertilizer/ Chemicals: (Negative)

Key Budgetary Measures expected

- Increase in subsidy for urea imports: To support the agriculture sector, government may increase the subsidy on imported urea.
- Increase in presumptive tax for importers: The government has proposed increase in presumptive tax rate for importers from 5% to 6%.
- Increase in Gas Infrastructure Development Cess: To fund the IP project, government may increase the GIDC on fertilizer sector as a revenue generating measure.
- Increase in custom duty on PTA, PVC & hydrogen peroxide: Chemical producers may propose the government to increase custom duty on PTA, PVC & hydrogen peroxide (H_2O_2) to prevent the local industry from potential cheaper imports.

Estimated Impact: Negative

- Increase in imported urea will cast a negative impact on bottom lines of local fertilizers as local producers will have to reduce the prices to match the subsidized urea.
- Increase in presumptive tax from 5% to 6% on importers is negative news for fertilizer imports.
- Increase in GIDC for fertilizers to PKR 103/mmbtu on feedstock. It will lead to increase in urea prices. However, if the surcharge is not transferred to the customers, it will hit the bottom line of the sector.
- As international prices of PVC & hydrogen peroxide are on a lower side compared to local prices, the local producers may favor the increase in import duty on PVC & H2O2. If approved, the increase will show a positive impact on the sector.
- Increase in custom duty on imported PTA will be beneficial for the local producers as imported PTA is cheaper the locally produced PTA.

Cement: (Positive)

Key Budgetary Measures Expected

- Increase in PSDP allocation: For FY13, the PSDP allocation has been announced to PKR 825bn as compared to PKR 730bn in FY12 depicting an increase of 13%YoY. Utilization of funds is expected to be better in the face of elections ahead.
- Cut in FED: APCMA has proposed to cut Federal Excise Duty (FED) by PKR200/ton to PKR300/ton that will result in decrease in cost by PKR 10/bag.
- Application of GST on retail price: Application of GST on retail price instead of ex-factory price: Imposition of 16% GST o retail price instead of ex-factory price will lead to increase in cement prices by PKR 10/bag.
- Withdrawal of custom duty on rubber scrap: To promote usage of shredded rubber as alternative of coal for the energy production in cement sector, government may consider the withdrawal of 20% custom duty on scrap rubber, as proposed by APCMA.

Estimated Impact on the Sector: Positive

- PSDP increment is positive for the sector. The utilization of PSDP for the coming year is expected to be 65%, much higher than the previous trends, as this is election year.
- Reduction of FED will save the cost of cement by PKR 10/bag, a positive point for the sector.
- Application of 16% GST on retail price instead of ex-factory price will increase the cement price by PKR 10/bag. If the price is transferred to the consumers, it will have neutral impact on the sector.
- Cement companies using scrap rubber for the energy production will benefit from the withdrawal of 20% custom duty on import of scrap rubber.

Banks: (Negative)

Key Budgetary Measures Expected

- 50% tax rate o T-bill income: The increase in tax rate on interest earned on T-bills or 5% increase in corporate tax for banks may be considered by the government in order to increase the tax base.
- Increase in tax free cash withdrawal limit: Tax on Cash withdrawal is expected to be same in the next budget. However, the daily withdrawal limit may be increased to PKR 30,000 per day.

Estimated Impact: Negative

- Increase in tax on T-bill income to 50% for banks is unlikely, as it may discourage banks from investing in government papers, which will be unfavorable for government because government funds its budget deficit through bank borrowings. However, if imposed, it will spell negative impact on the sector.
- Increase of 5% in corporate tax for banks would bring negative impact on the sector's earnings.
- Increase in tax free withdrawal limits per day will lead the banks to increase their liquidity position which will impact their lending limits & thus earnings to some extent.

Power: (Neutral)

Key Budgetary Measures Expected:

- Increase in power tariff: To reduce the subsidy burden, government is considering increasing the power tariffs gradually to pass on the cost to consumers.
- Increase in GIDC for IPPS: To fund the IP project, government is considering imposition of higher GIDC on some sectors including IPPs.

Estimated Impact: Neutral

- Subsidy reduction will lead to higher revenue collection for the power distribution companies and that will lead to better cash flow situation and hence better performance.
- Imposition of GIDC on IPPs will increase the cost of producing energy, if the cost is not transferred to consumers, it may further add to circular debt issues.

Automobile Assemblers: (Negative)

Key Budgetary Measures Expected

- Removal of 50% regulatory duty on cars including above 1800cc engine size:
- Decline in CBU import duties by 5-15% across all segments
- Cut in CKD duty from 32.5% to 20%:

Estimated Impact: Negative

- Removal of 50% regulatory duty on cars including above 1800cc engine size will increase the demand for imported cars which may hamper sale of locally assembled cars.
- Decline in CBU import duties by 5-15% across all segments will also lead to increased demand for imported cars and hamper local companies
- Cut in CKD duty from 32.5% to 20%: Local companies would benefit from the cut as they will be able to compete with the cheaper imported cars by passing on the cut to the customers.

Textile: (Negative)

Key Budgetary Measures Expected

- Increase in GIDC for textile sector

Estimated Impact: Negative

- Increase in GIDC for the sector will lead to increase in the cost of energy and would cast a negative impact on financial performance of the sector.