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Budget Update

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BUDGET ISN'T GROWTH ORIENTED

The federal budget for the fiscal year 2009-10, was an effort to halt dwindling economic situation of the country. With limited resources and IMF constraints, we would call it an average budget. And we would not favor the claims that the next fiscal year would be the year of industrial revival.

For industrial revival, we need to put many things in place altogether. And a coherent approach is needed to get back on the feet. We need political harmony, improvement in law & order situation, restoration of investors' confidence. Control over inflation in such a way that does not hurt the economy. What would the decline in CPI do if people are out of their jobs? Besides the policy tools, administrative measures should also be employed to control inflation. Unless the Central bank reduces the discount rate to single digit, hopes of industrial revival couldn't become reality.

Due to relief given to Telecom, Auto and Cement sectors, a temporary activity can be seen in these sectors. However Banking & Insurance sectors may witness some lackluster performance.

FISCAL BUDGET 2009-10

- Total Outlay for the next fiscal year will be Rs 2.482 trillion, which is 23.5% higher than the budget estimates of 2008-09.

- Consolidated budget of Federal & Provincial Governments estimated at Rs 2.897 trn, whereas total Resources estimated at Rs 2.174trn.
- The gap or overall budget deficit of Rs 722.7bn (4.9% of GDP) will be financed through Foreign Loan of Rs 264.9bn & domestic borrowing of Rs 457.6bn.
- Of the deficit 1.5% is planned to be met from external resources. Pakistan is likely to receive external resources equivalent to 1.2% of GDP (Rs 178bn) from pledges made at the Donor's Conference in Tokyo. Further external resources equivalent of 0.3% of GDP (Rs 48bn) expected for IDPs. So real deficit will be 3.4% of GDP, according to State Minister.

ANNUAL PLAN

According to Annual Plan as a component of 2009-10 budget, GDP growth rate is targeted at 3.3% with major contributions from agriculture (3.8%), manufacturing (1.8%) & services sector (3.9%).

- Large Scale Manufacturing (LSM) is targeted to grow by 1% as compared to negative growth of 7.7% in 2008-09.
- CPI base inflation is targeted at 9.5% for 2009-10 as compared to expected 20% in 2008-09.
- Total investment is projected at 20% of GDP while National Savings as a ratio of GDP is projected at 14.7%.
- Exports are projected at \$18.3bn as compared to \$18.6bn estimated for 2008-09. Downward revision in target is due to global economic slow down, domestic energy problems and law & order situation.
- Imports are projected at \$ 28.9bn as compared to \$30.7bn estimated for 2008-09. As a results of this trade deficit is projected at \$10.69bn for 2009-10.
- Govt. estimates that foreign investment in Financial & pharmaceutical sectors would continue, however the annual plan 2009-10 said that the persistent fluctuations in the exchange

rate are the main obstacle for the smooth inflow of foreign capital. (Please recall that in previous 8-9 years, we had almost stable exchange rate & during that period foreign investment also flourished)

- Workers remittances are the main foreign exchange that we receive after exports. The Govt. projects remittances at \$6.7bn in 2009-10 as compared to \$7.45bn in 2008-09.

FMCG SECTOR

Govt. has announced the relief measures for the salaried class which would help them to increase their disposable income which would eventually benefit the FMCG sector. For example, UniLever, Nestle and Engro foods etc. These measures are as follows:

- Ad-hoc relief allowance of 15% of pay of serving government employees from July 1, 2009.
- Increase in allowances of armed forces.
- 15% increase in net pension of retired government and armed forces personnel from July 1, 2009;
- Limit for exemption on income tax for salaried male is being enhanced from Rs 180,000 to Rs 200,000
- Limit for exemption on income tax for salaried female is being enhanced from Rs 240,000 to Rs 260,000

But the drastic cut in power sector subsidies by more than 40% would result in increase in the electricity tariffs. And this would have adverse impact on disposable income & eventually on FMCG sector.

CEMENT SECTOR

In the fiscal budget 2009-10, excise duty on cement has been cut to Rs 700 per ton from Rs 900 per ton. This reduction in duty if fully passed on to end users would bring down 50kg bag price by Rs 8 – Rs

10. The reduction in price may increase demand & hence good for cement companies.

Increase in PSDP has always been positive for Cement sector and vice versa. Govt. has allocated Rs 646bn for Public sector development program (PSDP) while for other, development expenditures of Rs 157bn has been allocated. PSDP shows an increase of 54% over the revised estimates of 2008-09, which were slashed during the current year to meet the budget deficit target with IMF.

That is why we think in the 2nd half of 2009-10 the Govt. may slash PSDP expenditures in order to meet IMF conditions. Because in the budget Govt. targets fiscal deficit of 4.9% of GDP which is 1.5% higher than what was agreed with IMF in a Letter of Intent (LoI) signed in March 2009.

REAL ESTATE SECTOR

Cheaper cement may reduce the construction cost but the increase in capital value tax (CVT) on property transactions to 4% from 2% would further stifle the investment. Pace Pak and AKD capital are the companies in this sector.

POL, CNG SECTOR

The Govt. decided to replace petroleum development levy (PDL) with "Carbon Surcharge". And its collection has been targeted at Rs 122bn in 2009-10. The Govt. will charge Rs 8/litre, carbon surcharge on HSDO, Rs 10/litre on MS, Rs 6/litre on kerosene Oil, Rs 3/litre on LDO and Rs 14/litre on HOBC.

The Govt. also decided to levy "Carbon Surcharge" on CNG. The estimated collection is targeted at Rs 12bn (Rs 6/kg on CNG)

TELECOM SECTOR

Govt. has given the following relief measures to the sector.

- Regulatory duty of Rs 250 per set of cellular phone eliminated.
- Customs duty reduced from Rs 500 to Rs 250 per set on cell phone.

The Govt. has levied 20 paisa per SMS in addition to the rate specified for telecom sector. On the whole these steps (except sms tax) would benefit PTCL (stake in Ufone) and Bank alfalah (stake in warid).

TOBACCO SECTOR

In order to discourage the consumption of cigarettes, FBR proposed FED at the rate of Rs4.75/ten cigarettes on retail price of packet upto Rs 10. The FED @ Rs 4.75/ten cigarettes plus 70% over every incremental rupee and on retail price of over Rs 19 per packet, 64% FED will be levied.

This step will hurt companies in the tobacco sector.

AUTO SECTOR

In order to give a breather to auto sector, Govt. has proposed 5% reduction in Excise duty on automobiles. This would reduce the prices of auto units. The FED used to be charged at the retail level and was mentioned when the sale invoice was cut on the purchase of cars.

So there will be reduction of Rs 50,000 if the retail price of car is Rs 1mn. But at the same time the Govt. has also made it mandatory for all persons owning a motor vehicle having a capacity of 1000CC or more to file return of income.

Govt. has also announced subsidy of Rs 4bn for farmers for purchasing tractors under Benazir Tractor Scheme would boost the sale of local manufacturers.

BROKERAGE SECTOR

The excise duty on brokerage services was levied at 16%. This is still confusion in the budget that whether this new excise duty will replace the existing CVT or not.

Research Analyst: Kamran

www.mahasecurities.com

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