Alfalah Securities

Broader Market Measures To Outweigh The Negatives

BUDGET FY19

28-Apr-2018

Research Entity Notification Number: REP-088

http://www.JamaPunji.pk

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Executive summary

The government has envisaged a PKR5.9trn budgetary outlay for FY19, up 10.7% from FY18 revised estimate. Total national PSDP has been cut by 21.9% compared to budget FY18, however it is up 6.5% from FY18 revised estimate.

The government has set an ambitious GDP growth target of 6.2% for FY19, which we believe would be challenging since we see high likelihood that external vulnerabilities might force a reentry into the IMF program.

Government has upwards revised its fiscal deficit target for FY18 from 4.1% to 5.5%. In its medium term budgetary framework, government has forecasted fiscal deficit to reach 4.5% in FY21.

From corporate earnings standpoint the budget is negative in the short run because of imposition of Super tax, however since government would reduce corporate tax rate by 1% each year till FY23, long term implications of budget on earnings and valuations are positive.

That said, markets response to budget would be positive, due to abolishment of tax on bonus shares, reduction in corporate tax rate, extension of tax credits till FY21 and relaxation of mandatory payout rule.

Total national PSDP raised by 6.5% from FY18 revised estimate

Total National PSDP has been raised by 6.5% from FY18 revised estimate (cut by 21.9% compared to budget FY18): Budget FY19 envisages total outlay of PKR5,932bn, 10.7% higher than FY18 revised expenditure of PKR5,361bn. Government has allocated PKR1,152bn for development expenditure compared to PKR1,062bn for FY18 (revised target). Development expenditure under PSDP is expected to exceed PKR800bn, this is a cut of 20% from budget FY18 (up 6.7% from FY18 revised estimate). Total national PSDP has been cut by 21.9% compared to budget FY18 (increased by 6.5% from FY18 revised estimate).

Gross/net revenue receipts to increase by 13.4/14.7% YoY in FY18: On the collections side government expects gross/net revenue receipts to reach PKR5,660/3,070bn in FY19 (up 13.4/14.7% from FY18 revised estimates). Non tax revenue is targeted at PKR771bn in FY19 (down 8.8% from FY18 revised estimates), the decline mainly emanates from Extraordinary receipts, down 63.0% (PKR85bn). FBR tax collections are estimated at around PKR4,435bn, up 12.7% from FY18 revised estimates (direct/indirect taxes up 11.0/13.8% respectively).

Total subsidy for FY19 budgeted at PKR174.7bn: Total subsidies for FY19 are budgeted at PKR174.7bn, up 18.4% from FY18 revised target. The increase mainly emanates from subsidy to WAPDA/PEPCO which are budgeted at PKR134bn, up 64.4% from FY18 revised estimate. Subsidy to KESC is cut by 54.0% to PKR15.4bn in FY19.

Once again concessions to agriculture and exports oriented industries are extended in FY19: Finance Minister in his Budget speech announced GDP growth target of 6.2% for FY19 compared to 5.8% (revised projection) for FY18. Government targets fiscal deficit of 4.9% (as % of GDP) for FY19 compared to FY18 revised estimate of 5.5%. Other key highlights of the budget include; agriculture sector incentives announced in last year's budget to be continued in FY19, zero rating regime for five export oriented sectors to be maintained, sales tax on fertilizers to be reduced to 2%.

Federal PSDP up by a modest 6.7% YoY

PKR (bn)	Revised FY18	Budget FY19
Resources	4,774.5	4,917.1
Internal resources	3,544.8	3,799.1
External resources	1,229.7	1,118.0
Privatization proceeds	0.0	0.0
Expenditures	5,361.0	5,932.4
Current expenditure	4,298.2	4,780.3
Development expenditure	1,062.7	1,152.1
Bank borrowing	586.4	1,015.3

Details of subsidies

	FY18R	FY19BE
WAPDA/PEPCO	81.5	134.0
KESC	33.4	15.4
USC	4.0	6.0
PASSCO	17.5	19.0
FERTILZERS	10.7	0.0
OTHERS	0.3	0.3
TOTAL	147.6	174.7

Short and medium term Macro economic targets

Macro economic indicators	FY18R	FY19BE	FY20BE
Real GDP growth rate	5.8%	6.2%	6.5%
Inflation	4.5%	6.0%	6.0%
Total revenue	16.0%	16.3%	16.4%
Total expenditure	21.5%	21.2%	21.1%
Fiscal balance	-5.5%	-4.9%	-4.7%
Total public debt (Net)	64.9%	63.3%	61.1%

Source: Budget docs, Eco. Survey, Alfalah Research

Fiscal deficit revised up to 5.5%

Fiscal deficit revised up to 5.5% in FY18: Government has upwards revised its fiscal deficit target for FY18 from 4.1% to 5.5%. In its medium term budgetary framework government has forecasted fiscal deficit to reach 4.5% in FY21. Total revenue as a percentage of GDP is forecasted to reach 16.5% while expenditure is expected to clock in at around 21.0%.

Current expenditure as % of GDP is forecasted to decline from 16.6% to 16.0% over FY18-21. Development expenditure on the other hand is expected to increase from 4.9% of GDP to 5.0%.

FY18 revised net public debt to GDP ratio stands at 64.9% compared to 59.2% in budget FY18. Over the medium (FY18-21) term total public debt (net) is forecasted to decrease from 64.9% to 58.6%.

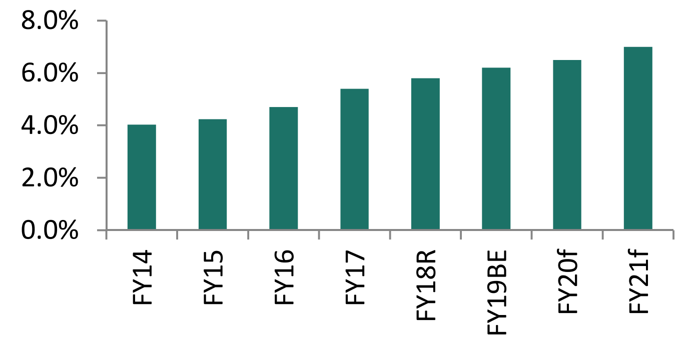
Pakistan posts a 13 year high GDP growth rate in FY18: Pakistan's provisional GDP growth rate for FY18 has clocked in at 5.8% vs revised estimated of 5.4% for the previous year. Though Pakistan has missed the targeted 6.0% growth rate it has managed to post a 13 year high number.

Strong performance show by services (up 6.4% YoY), agriculture (up 3.8% YoY) and industrial sector (up 5.8%) enabled Pakistan to achieve this growth rate.

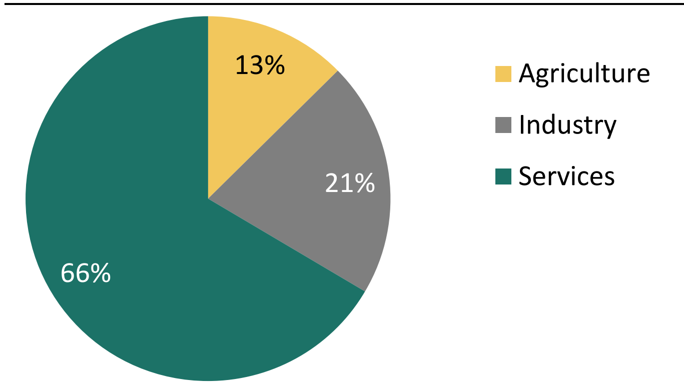
Govt. incentives, improved crop yields and better commodity prices helped agriculture sector post a 3.8% increase in FY18.

Where as growth in large scale manufacturing segment provided the impetus to the industrial sector. Overall improved performance can be attributable to better energy availability, historically low interest rates and CPEC/infrastructure led demand growth.

Real GDP growth gradually gaining pace



GDP composition of FY18



Source: Budget docs, Eco. Survey, Alfalah Research

Reduction in corporate tax rate to 25% a major positive for listed space

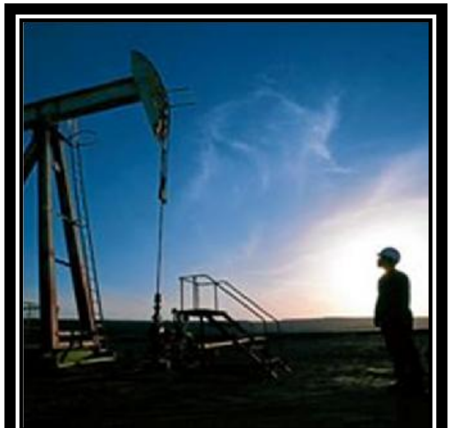
Budget FY19 mildly positive for the broader stock market: We see budget FY19 to improve the overall market sentiment, our view is premised on the following positive developments, (1) Corporate tax rate to be reduced by 1% each year by 2023 to 25%, (2) Tax on bonus shares has been abolished, (3) Tax on dividends for REITs reduced from 12.5% to 5%, (4) Tax credit allowed under 65B, 65C, 65D and 65E extended till FY21, (5) Companies will now be required to give a minimum payout of 20% (previously 40%) of PAT or pay additional tax of 5% (previously 7.5%) of PAT in case of non-compliance. On the negative side, Super tax will be continued at the same rate for FY18 but will be phased out at the rate of 1% each year for financials/non-financials.

Budget is earnings negative in short term, positive in the long term: Overall we see budget to be earnings negative in the short run because of imposition of Super tax, however the reduction in corporate tax rate to 25% would improve valuations and long term earnings.

For cements increase in FED from PKR1,250 per ton to PKR1,500 per ton is a negative, which overshadows the positive of 2% reduction in custom duty on coal. For Autos the ban on new car purchases by non-filers is earnings negative. If fertilizers are able to pass on the impact of abolishment of subsidy, then budget is earnings Neutral, however, otherwise budget is earnings negative. For textiles, Finance Minister announced that government would announce another exports package which we believe could be earnings positive.


34.841M
8.842M
1.104M
82.022M
-1.26 -5.12%
+12.40 3.27%
+0.74 0.78%
+0.42 1.69%


KSE100 36683.03 +142.06
At 16:46 O 36549.96 H 36776.52 L 36531.41 Prev 36540.97
KSE100 Index
Page 1/2 Security Description: Index
1) Profile
2) Characteristics
Karachi Stock Exchange KSE100 Index
FIGI BBG000VJVVX4
The Pakistan Stock Exchange (fka Karachi Stock Exchange) KSE100 Index comprises the top company from each of the 34 sectors on the PSX, in terms of market capitalization. The rest of the companies are picked on market cap ranking, without any consideration for the sector to make a sample of 100 common stocks with base value 1,000.
3) Price Chart | GP »
Index Information
Volume 109.08M (05/26/16)
Index Market Cap 1.97T
Divisor 53.86328662
Trading Hours 09:00 - 16:30
Currency PKR
Composite Volume N.A.
6) Members | MEMB » 100 54 38 8
No Industry Groups
8) Movers | MOV »
Leaders % Chg Laggers % Chg
9) PSEL PA +5.00 13) BNWM PA -4.24
10) FML PA +5.00 14) KEL PA -2.52
11) HPL PA +5.00 15) NCL PA -2.05
12) ASRL PA +4.97 16) MUREB PA -1.88
Period Level % Change Net Change
Year to Date 32816.31 +11.78 +3866.72
52 Week Ago 32842.59 +11.69 +3840.44
52 Week High 36848.02 (05/20/16)
52 Week Low 29784.60 (01/18/16)
4) Financial Analysis | FA »
Price/Earnings 10.09 Ex-Dividend -1.749
Dividend Yield 5.60 Ex-Date 05/23/16
Australia 61 2 9777 8600 Brazil 5511 2395 9000 Europe 44 20 7330 7500 Germany 49 69 9204 1210 Hong Kong 852 2977 6000
Japan 81 3 3201 8900 Singapore 65 6212 1000 U.S. 1 212 318 2000 Copyright 2016 Bloomberg Finance L.P.
SN 344068 H452-5013-1 27-May-16 16:47:00 PKT GMT+5:00



Stock Market

Reduction in corporate tax rate to improve sentiment

Positive

	Key Stock Market Measures	Positive	Slightly positive	Neutral	Slightly negative	Negative
		Intensity				
1	Corporate tax rate to be reduced by 1% each year to 25% by 2023					
2	Tax on bonus shares has been abolished.					
3	Tax on dividends for REITs reduced from 12.5% to 5%.					
4	0.02% withholding tax on transactions of stock brokers made adjustable instead of full and final.					
5	Tax credit allowed under 65B, 65D and 65E for new industrial undertakings to be extended till FY21					
6	Companies will now be required to give a minimum payout of 20% of PAT or pay additional tax of 5% of PAT in case of non-compliance					
7	Super tax will be continued at the same rate for FY18 but will be phased out at the rate of 1% each year for financials/non-financials.					

Sectoral Developments

- **Fertilizer:** Reduction in GST to replace subsidy of Fertilizers.
- **Textile :** All eyes on new textile package
- **Cement:** Declining PSDP and rising FED to compound problems.
- **Banks:** Continuation of super tax to erode medium term earnings.
- **Oil and Gas:** Various incentives to make budget positive
- **IPPs:** Nonevent for IPPs except KAPCO.
- **Autos:** Restriction on purchase by non-filers can hit local OEMs demand.
- **Steel:** Decline in PSDP offsets the positive of low corporate tax..

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Corporate tax rate to be reduced	**Positive**
Corporate tax rate is prescribed to be reduced by 1% each to 25% by 2023	

Tax on bonus shares has been abolished	**Positive**
Withholding tax on bonus shares has been removed, currently bonus issuance is taxed at 5%	

0.02% withholding tax on transactions of stock brokers made adjustable instead of full and final	**Positive**
Tax deducted on purchase and sale of shares has been made adjustable, currently is was full and final. This can improve investor participation (volumes) in the stock market	

Tax credit for new undertakings	**Positive**
Tax credit allowed under 65B, 65D and 65E for new industrial undertakings to be extended till FY21.	

Relaxation in mandatory payout rule	**Positive**
Companies will now be required to give a minimum payout of 20% of PAT or pay additional tax of 5% of PAT in case of non-compliance	

Super tax has been imposed on financials/non-financials	**Negative**
Super tax will be continued at the same rate for FY18 but will be phased out at the rate of 1% each year for financials/non-financials.	

GST reduced by 3% to 2% (PKR66/bag to PKR40/bag) on all fertilizer products. — Positive

Fertilizer products (except urea) were subjected to fixed tax regime which has been proposed to change to flat tax of 2%. Reduction in GST from 5% per bag to 2% per bag on urea has been proposed in Budget FY19 while it has also proposed to remove subsidy of PKR100/bag. This will have a positive impact on the fertilizers products which were subjected to fixed tax regime but will be negative for urea if the price ceiling remains intact. Assuming a price cap of PKR1,400/bag, the combined impact of 2% sales tax on all fertilizer products will have a negative CY18E earnings impact of PKR1.55/0.95 per share on FFC/EFERT's bottom-line. While for FATIMA, it will have a positive CY18 earnings impact of PKR0.4/sh due to higher portion of CAN/NP in sales mix and no impact on FFBL (negative impact on urea will be off-set by positive impact on DAP).

If the fertilizer manufacturers are able to pass on the impact of flat 2% sales tax on all fertilizer products. — Neutral

If the fertilizer manufacturers are able to pass on the impact, this will have a neutral impact on fertilizer sector's profitability.

Sales tax on feed stock is reduced to 5%; Sales tax on LNG withdrawn. — Positive

Presently, sales tax on feed stock is 10%. The government has proposed to reduce the sales tax on feed stock from 10% to 5% to improve cash-flow position of the fertilizer manufacturers. Similarly, sales tax on LNG consumed by fertilizer manufacturers for use as feed stock is also proposed to be reduced from 5% to 0%.

Agriculture tube well tariff maintained. — Positive

The government will continue to provide subsidized tariff on agri-tube wells. In addition, reduction in GST has been proposed on agriculture machinery to 5% from previous 7%. This will improve crop yield resulting in improved farm economics.

Fertilizer | Reduction in sales tax to replace subsidy | Positive

Other measures to support farmers — Positive

Agriculture credit has also been enhanced to PKR1,100bn from PKR1,001bn. This will improve farm economics and agriculture output, translating into better off-take of the fertilizer sector.

Measures to improve crop yield — Positive

Plant Breeders Rights Act has been established which will help to produce higher yield varieties of cotton and other crops locally through availability of better quality seed.

Fund for the support of agriculture technology — Positive

The government has also proposed to establish an agriculture research support fund and agriculture technology fund of PKR5bn each. Agriculture research support fund shall finance research and development of modern plant and seed varieties, while Agriculture technology fund will promote indigenization of agriculture technology.

Super Tax to scrape profitability — Positive

Budget FY19 has witnessed the continuation of the dreaded 3% super tax but will be phased out at the rate of 1% each year while corporate tax rate will follow the same trend and will be reduced by 1% each year till 2023 to 25%. This will marginally affect our fertilizer manufacturer's earnings in the short term but will increase valuations due to lower effective tax going forward. As per our calculations, CY18 earnings for FFC, EFERT, FFBL and FATIMA are likely to face an attrition of PKR0.27,0.28,0.04 and 0.12 per share respectively.

All eyes on new textile package

Positive

New Export Package to focus on value added exports — Positive

The GoP is looking to shift from quick fixes to more robust and sustainable long term policy making in order to promote exports. Hence, a new export package is on the cards which will focus on value added exports and non-traditional markets. Details of the package are expected to be announced soon.

New timeline to clear long standing refund claims — Positive

The existing refund claims are proposed to be cleared in 12 months starting 1st Jul-18. And all new refund claims after the said day will be cleared on a monthly basis.

Zero-rating of Export Oriented Sectors continued — Positive

The zero rated scheme for five main export oriented sectors, which was re-instated in FY17 budget, is continued. This addresses the long standing issue of textile exporters whereby refund of input sales tax for exports used to remain stuck which resulted in significant liquidity crunch. The zero-rating facility is available on purchase of raw materials, intermediate goods and the purchase of energy. In our textile universe; we expect improved operational efficiencies and resultant lower borrowing to support the bottom-line of NML and NCL

Export refinance/long term finance facility to remain subdued — Positive

Export refinance facility, and long term financing facility will continue to be at reduced mark up rates as per SBP policy.

All eyes on new textile package

Positive

Incentives under Textile Policy 2014-19 continued — Positive

Various incentive schemes under Textile Policy 2014-19 shall be continued in FY19. In addition to this, Ministry of Commerce is also working on Strategic Trade Policy Framework 2018-23 and an amount of PKR10bn is being allocated for various schemes under these policies.

Clarity on super tax; corporate tax to reduce by 1% every year — Negative

Super tax has been set at 3% for FY18, and will be reduced by 1% each year. In our AFS universe, the negative impact of super tax is likely to trim NML's FY18/19/20 EPS by 3.6/2.3/1.2% respectively to PKR11.5/12.9/14.4 and decrease our Dec-18 TP by 0.8%. Similarly, NCL's earnings will witness a decline of 3.6/2.5/1.2% respectively to PKR6.2/6.1/8.4 per share while its valuation will witness an attrition by 0.6%.

ST on import and supply of leather and textile sector to be increased — Neutral

The rate of sales tax on import and supply of finished articles of leather and textile sector is being increased to 9%. However, all those branded outlets which will be integrated through electronic fiscal devices with FBR online system shall be charged sales tax at 6%.

Declining PSDP and rising FED to compound problem

Negative

Budgeted PSDP to decrease by 11% to PKR1.88trn — Negative

It has been proposed to decrease national budgeted PSDP by 11% YoY to PKR1.88trn for FY19 (4.9% of GDP as against 5.9% for last year's budgeted estimates). This is the first time in the last 15 years that budgeted PSDP allocation has been reduced. Additionally, the federal PSDP includes PKR230bn as self-financing by corporation/authorities, in the absence of this amount national budgeted PSDP would decline by 22% YoY.

Federal Excise Duty (FED) on cement increased by PKR12.5/bag — Negative

FED on cement has been increased by PKR12.5/bag to PKR75/bag. In the wake of pressure on cement prices in the North region coupled with upcoming 2.84mn tons DGKC capacity in South, it would be difficult for cement players to pass on the impact of hike in FED. In our AFS cement universe the impact of PKR12.5/bag increase in FED on FY19 EPS of CHCC/MLCF/KOHC/PIOC/DGKC/FCCL/LUCK is negative 25/19/16/15/11/11/9% respectively, assuming FED is not passed on.

Super tax & Corporate tax — Positive

While it has been proposed to apply 3% super tax on FY18 and gradually reduce it to 0% by FY21, the government has also recommended gradually reducing corporate tax rates to 25% by FY23. The net impact of these two measure is decline in near-term earnings but a rise in valuations and long-term earnings. Hence, in our AFS cement universe, valuation impact of this measure on PIOC/KOHC/CHCC/MLCF/DGKC/LUCK/FCCL is positive 8/7/6/6/5/2/0% respectively. Additionally, the net impact of these two measures on FY19 EPS for FCCL/KOHC/LUCK/MLCF&PIOC is -4% while for DGKC & CHCC is -3% respectively.

Customs Duty (CD) on coal reduced to 3% — Positive

It has been proposed to reduce CD on coal from 5% to 3%. In our AFS cement universe the impact of this measure on FY19 EPS of CHCC/MLCF/KOHC/DGKC/FCCL/LUCK/PIOC is positive 3/3/2/1/1/1/1% respectively.

Extension of tax credits upto Jun-21 — Positive

Tax credit available under 65B, 65D, 65E has been extended from Jun-19 to Jun-21. This measure is expected to be beneficial for CHCC, LUCK, PIOC, KOHC, MLCF, BWCL and POWER.

Reduction in minimum payout to 20% — Positive

It has been proposed to reduce the minimum payout from 40% to 20%. This measure would allow the cement companies undergoing expansion to conserve internally generated cash and hence limit their financial leverage.

Sales tax on steel sector increased from PKR10.5/unit to PKR13/unit — Neutral

It has been proposed to increase sales tax on steel sector from PKR10.5/unit to PKR13/unit, which would raise cost by ~PKR1600/ton. We believe that given the price differential of ~PKR38,000 to 45,000 per tons between landed price of imported rebar and local rebar prices, local rebar manufacturers should be able to pass on the impact of increase in sales tax.

Super tax & Corporate tax — Positive

While it has been proposed to apply 3% super tax on FY18 and gradually reduce it to 0% by FY21, the government has also recommended gradually reducing corporate tax rates to 25% by FY23. The net impact of these two measure is decline in near-term earnings but a rise in valuations and long-term earnings. Hence in our AFS steel universe, valuation impact of this measure on ASTL/ISL/ASL is positive 8/7/6% respectively. Additionally, the net impact of these two measures on FY19 EPS for ASTL/ISL/ASL is negative 2/1/1% respectively.

Extension of tax credits upto Jun-21 — Positive

Tax credit available under 65B, 65D, 65E has been extended from Jun-19 to Jun-21. This measure is expected to be beneficial for ASL and ASTL.

Reduction in minimum payout to 20% — Positive

It has been proposed to reduce the minimum payout from 40% to 20%. This measure would allow the steel companies undergoing expansion to conserve internally generated cash and hence limit their financial leverage.

Budgeted PSDP to decrease by 11% to PKR1.88trn	Negative

It has been proposed to decrease national budgeted PSDP by 11% YoY to PKR1.88trn for FY19 (4.9% of GDP as against 5.9% for last year's budgeted estimates). This is the first time in the last 15 years that budgeted PSDP allocation has been reduced. Additionally, the federal PSDP includes PKR230bn as self-financing by corporation/authorities, in the absence of this amount national budgeted PSDP would decline by 22% YoY.

Continuation of super tax to erode earnings — Negative

Super tax @ 4% has been continued for another year, however 1% will be phased out each year (i.e. no super tax in CY21). The imposition is negative for banks, as we had not incorporated it in our earnings estimates. The worst hit would be ABL/BAHL/UBL with negative earnings impact of 8.7/8.2/8.2% for CY18 respectively.

Cuts in WHT to facilitate the number of banking transactions — Positive

Reduction in withholding tax on banking transactions for non-filers from 0.6% to 0.4% is positive for banks as it is expected to increase the quantum of banking transactions.

Agriculture based credit continues to be high on the govt.'s agenda — Positive

To facilitate the agriculture sector, the Govt. has proposed a 10% YoY accretion in agri based credit. The total outlay for agriculture would be PKR1,100bn compared to PKR1,001bn in the previous budget.

WHT to be collected on payments remitted overseas via credit/debit/prepaid cards — Negative

Banks that have issued credit/debit cards shall be obligated to collect 1/3% advance tax from filers/non-filers in case of transactions that result in outflow of remittances from Pakistan.

Losses from foreign operations can no more be offset against income from the local end	Negative

Losses from foreign operations of a bank can only be offset against foreign income. Previously, banks could adjust their foreign losses against income from Pakistani operations, they are now barred from doing so. Banks with greater foreign exposures are thus at a risk namely HBL, UBL & NBP.

Gradual reduction in corporate tax rate from 30% to 25%; Diminishing Supertax	Neutral

Any change in income tax has no impact on listed power companies as they are exempt from income tax apart from KAPCO. It has been proposed to trim corporate tax rate by 1% each year for the next 5 years, reducing from 30% to 25%. Additionally 3% super-tax has also been imposed, which will also be reduced by 1% each year. If approved, KAPCO's earnings are expected to surge in FY18/19 by 4.3/1.5% respectively. However, from FY20 onwards we see positive impact of 1.4/4.3/5.8% in the bottom-line for FY20/21/22 respectively. Moreover, this would increase our Dec'18 valuation by 4.0% to PKR90.6.

Subsidies to power sector increased	Positive

Supporting the ailing energy infrastructure of the country, subsidies allocated for the power sector have been increased to PKR149.4bn to meet T&D losses and tariff differential.

Burgeoning circular debt remains unanswered	Negative

No respite for the ballooning circular debt, which currently stands at ~PKR530bn (after PKR53bn payment to IPPs and OMCs), was announced in Budget 2018-19. Ministry of Energy has requested the government to dole out PKR150-200bn to keep the turbines running, we foresee IPPs dividends to remain subdued until full or partial payment's are made to IPPs.

Restriction on car purchase by non-filers to hit OEMs

Negative

Reduction in corporate tax rate from 30% to 25% over 5 years; Declining Supertax — Positive

As per the new corporate tax and super tax proposal, initially INDU/HCAR/MTL are expected to witness attrition in the bottom-line by 4.3/4.2/3.1% respectively in FY18 (MY19 for HCAR). However, corporate taxes are expected to positively impact the bottom-line from FY20 (MY21 for HCAR) onwards. As a result, our Dec'18 TP for INDU/HCAR/MTL are expected to improve by 4.3/4.8/4.7% to PKR1,825/614/1,650/sh respectively.

Restriction on purchase of new vehicle by non-filers — Negative

It is proposed that non-filers shall not be allowed to purchase new motor vehicles manufactured in Pakistan or any new imported vehicles. Given the low quantum of tax-filers in Pakistan, this will lead to higher demand for used car imports, negatively impacting the local OEMs (INDU/HCAR/PSMC).

Local OEMs to enjoy reduced CD/RD on HEVs and HEV's CKD kits — Neutral

The local OEMs are now being allowed concessionary rates of custom duty (25% from 50%) and regulatory duty (0% from 15%) on Hybrid Electric Vehicles (HEVs). Moreover, import of CKD kits for local assembly of hybrid vehicle is proposed at 10% custom duty. The policy is positive for INDU as it imports Toyota Prius/Camry, while it will encourage other players to add imported hybrid cars to their current product offering.

CD on Carbon Black rubber reduced; CD on Rickshaw tyres enhanced — Positive

Custom duty on Carbon Black rubber grade input for tyres manufacturers has been proposed to be reduced by 4% to 16%. Moreover, an increase in CD on rickshaw tyres, from 11% to 20%, has been put forward to protect the domestic industry. In our view, this will be positive for GTYR & SRVI.

Various incentives to make budget positive

Positive

Incentives offered to set up deep conversion refinery — Positive

Deep conversion refineries, being set up anywhere in Pakistan, with a capacity of minimum 100k bpd may be exempted from income tax for a period of 10 years. This incentive may be extended to existing refineries if they expand by installing deep conversion refinery of aforementioned capacity.

Gas distribution companies to benefit from tax rationalization — Positive

Sales tax may be reduced from 17% to 12% on import of LNG and supply of RLNG improving cash flow situation of gas distribution companies.

Despite super tax, reduction in corporate tax to increase valuations for OMCs — Positive

Application of 3% super tax will shave earnings for PSO/APL/ HASCOL by PKR2.0/2.3/0.4 per share to PKR 45.8/51.4/16.0 respectively. The said companies valuation are likely to increase by 7.9/6.5/5.2% to PKR409.4/716.5/388.0 per share respectively due to reduction in corporate tax by 1% each year to 25% by 2023.

Super tax continuation to slightly impact (non core) earnings of E&Ps — Slightly Negative

Super tax, as introduced in Finance Act 2016, has been extended for another year. As E&P companies are taxed under the 5th schedule of income tax ordinance, the core earnings of the oil and gas companies will remain insulated from any impact of super tax. However, non-core earnings such as dividend income, income on bank deposits/PIBs/TFCs would attract higher tax rate as seen in the previous year. We estimate PPL /OGDC EPS for FY18 to shrink by PKR0.2/0.1 to PKR21.3/17.0 respectively owing to incidence of super tax.

Various incentives to make budget positive

Neutral

Increase in maximum Petroleum levy rate

Slightly Negative

The GoP has increased maximum Petroleum Levy (PL) rate on various petroleum products including HSD/Mogas to PKR30/ltr. This will provide room to GoP to raise their collection from petroleum levy but will be negative for POL demand when petroleum levy is increased. Currently, PL on HSD/Mogas is PKR8.0/10.0 respectively.

Sales tax on FO to be reduced from 20% to 17%

Neutral

The government has proposed to rescind SRO 962(I)/2015 which would lead to reduction in sales tax from 20% to 17% on furnace oil import and supplies.

Change in mechanism for collection of tax from pumps on HSD

Slightly Positive

The government seems to taken a step forward with regards to HSD de-regulation. Tax on dealer margin shall now be collected on ex-depot price at rate of 0.5% from filers and 1% from non-filers.

Appendix

- RD on import of optical fiber cable is proposed to be changed to 10% from 20%. Moreover, duty on fibre optic cable and other raw material to be reduced to 5%.
- CD for silicon electrical steel sheets, used for manufacturing of transformers, may be reduced to 5% (currently 10%).
- RD of 10% is being proposed for CKD/SKD kits of specified Home Appliance.
- Fix duty/taxes of US$ 5,000 on vintage or classic cars and jeeps imports. Moreover, CD on import of firefighting vehicles has also been reduced from 30% to 10%.
- Increase in CD by 5% on aluminum auto parts scrap has been proposed.
- Reduction of CD on Lithium iron phosphate battery (LiFePO4) from 11% to 8% is proposed. Moreover, reduction of sales tax from 17% to 12% has also been proposed on Lithium iron phosphate battery (LiFePO4).
- Continuation of duty free import and sales tax exemption of combined harvesters has been put forward.
- It is being proposed that 3% CD on import of the microfeeder equipment be withdrawn in order to ensure appropriate quantities of micronutrients present in the flour.
- CD on eyesight glasses to be reduced to 3% and sales tax on hearing aid to be made 0%.
- Following proposals have been made for Film & Drama industry:
  - reduction in CD/ST of film and drama production equipment to 5%,
  - 5-year rebate of 50% income tax to companies investing in film projects, and
  - 50% tax rebate to income derived by foreign film makers from films made in Pakistan.
- 21 types of computer parts may be granted exemption from sales tax in order to promote local assembly of computers.
- It is proposed to restore stationery items under zero-rating to promote stationery sector and reduce prices of stationery items.
- FED on locally produced cigarettes is to be enhanced in respect of Tier-1/Tier-2/Tier-3 to PKR3,964/1,770/848 per thousand cigarettes respectively.
- It is being proposed that customs duty on import of tanned hides (including wet blue) would be withdrawn (for registered leather tanning sector).
- Proposal for reduction in duties on finished products and raw materials of liquid packaging industry. Currently the duty is 20%.
- To provide exemption from sales tax on import of paper weighing 60 g/m^2 by Federal or Provincial Governments and Nashiran-e-Quran registered with the Government for printing of Holy Quran as per quota determined by IOCO.
- Custom duties on filament tow of acrylic or modacrylic (PCT 5501.3000) which are currently at 11% are being withdrawn as they are now being categorized under the Prime Minister Export Package.
- In order to promote fish farming, sales tax of 10% on fish feed has been removed. Similarly, sales tax has been exempted for preparation of fans and animal feed of dairy farms.
- Custom duties on items defined under 28 PCT codes have been proposed to be reduced however, current custom duties on raw materials categorized under 104 PCT codes are to be abolished.
- In respect to the poultry sector, the concessionary rate of customs duty on import of growth promoters premix, vitamin premix, vitamin B12 (Feed grade) and vitamin H2 (Feed grade) is proposed to be further reduced from 10% to 5% for registered manufacturers of poultry feed.
- Import of solar panels were exempted from the condition of 'local manufacturing' till 30th June 2018 which is extended till 30th June, 2019.

- The government has proposed to remove 3% custom duty on import of bulls.
- Custom duty on import of plasters has been reduced from 16% to 11%.
- 5% Custom duty exemption on LED components used in the manufacture of LED lights and the imposition of 2% RD on LED tubes and bulbs.
- CD on coils of aluminum alloys for the manufacture of beverage cans to be reduced to 8% from 16%
- CD on Di-octyl terephthalate (DOTP) to surge to 20% to 3%.
- CD on medium density fiber to be reduced from 16% to 11% while RD of 5% to be imposed.
- RD on non-essential and luxury items to be reviewed.
- CD on corrective glasses to be slashed from 11% to 3%.
- Zero-rated regime to be applied retrospectively (from 5th May, 2014 to 31st July, 2014) on the import of potato.
- Sales tax exemptions to be granted to companies that import plant and machinery for the purpose of setting up of a Special Economic Zone.
- Limit for tax credit for investment in shares/sukuks by an resident has been increased from PKR1.5mn to PKR2.0mn.
- Depreciation losses to be limit to the extent of fifty per cent of the business income for a Tax Year except where the taxable income is upto Rs. 10 million. Hence taxpayers will still be entitled to carry forward unabsorbed depreciation losses indefinitely; however, such carry forward will be staggered over a greater number of years.
- Change in Tax collected from commercial importers at the import stage to minimum tax instead of final tax. Therefore, commercial importers will be required to file their returns of income depicting their taxable income. This measure is also a step towards gradual phasing out of the final tax regime.
- Presently, OMC's selling petroleum products to a petrol pump operator deduct tax (12%) from filers and (17.5%) from non-filers on commission or discount allowed to a petrol pump operator. As the prices of high speed diesel are to be deregulated, tax on dealer's margin shall now be collected on ex-depot sale price of HSD (excluding dealer's margin) at the rate of 0.5% from a filer and 1% from a non-filer.
- Pakistan Tobacco Board or its contractors will collect Health Levy at the rate of ten rupees per kilogram of tobacco from every person purchasing tobacco including manufacturers of cigarettes. This will have a negative impact on tobacco demand.
- It is proposed that value addition tax of 3% on import of RLNG may be removed. This measure is taken to address the cash flow issues of Gas Distribution Companies. In addition, it is also proposed to reduce sales tax from 17% to 12% on import of LNG and supply of RLNG.
- Custom duty on Acetic Acid to be reduced from 20% to 16% and to be withdrawn on Hydrogen Bromide/ Palladium-on-carbon on catalysts used by PTA industry. This will be slightly positive for LOTCHEM as para-xylene remains the major raw material cost.

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