Pakistan Economy

IMF seems to be back in the mix as the government makes some tough calls

Wednesday, June 22, 2022

Pakistan seems to have finally taken the IMF on board to unlock the 7th tranche of the Extended Fund Facility (EFF) and we opine Staff Level Agreement will be reached soon as the Amended Budget is passed through Parliament. However, it has come at some cost as tax collection targets have been increased by PKR 422Bn to PKR 7.4Trn which include increase in poverty alleviation tax, revision in petroleum development collection, upwards adjustment in customs duty collection and alteration in personal income tax slabs to name a few. Similarly, total budget outlay has ben increased to PKR 9.9Trn from PKR 9.5Trn while primary surplus target has been revised down slightly to PKR 152Bn. We opine this to be a positive development from the economic perspective as the green signal from IMF would help in bringing other multilateral/ bilateral sources and friendly countries into the mix thus easing concerns about the USD 35Bn external funding gap for the next fiscal year. Similarly, this should ease the consistent pressure building on the PKR. From the equity market's perspective, we believe the amendments to be negative for the stock market in the wake of higher incidence of tax, higher inflation and possibly further monetary tightening.

Some major amendments to be made: Following IMF's disapproval of the initial budget announcement, the government is expected to make some major changes to the taxation measures highlighted earlier. Broadly speaking, tax collection target has been revised up from PKR 7.0Trn to PKR 7.4Trn with new taxes of PKR 422Bn to be imposed. Key changes in the collection targets are attributable to:

i) Relief of PKR 47Bn provided to the salaried class is proposed to be rolled back. Tax exemptions are only available to people earnings up to PKR 600k/annum which was initially proposed to be scaled up to PKR 1.2Mn/annum. People earning between PKR 600k-1.2Mn per annum will be liable to a 2.5% income tax against 5% earlier. There is a progressive taxation rate for income classes of over PKR 1.2Mn per annum.

ii) Income slabs have been proposed for the imposition of poverty alleviation tax compared to the blanket 2% for AoP's/corporates earning over PKR 300Mn annually. Here on, 1% tax will be applied on annual earnings between PKR150Mn-200Mn; 2% if earnings are between PKR 200-250Mn; 3% if earnings range between PKR 250-300Mn and 4% if annual earnings exceed PKR 300Mn.

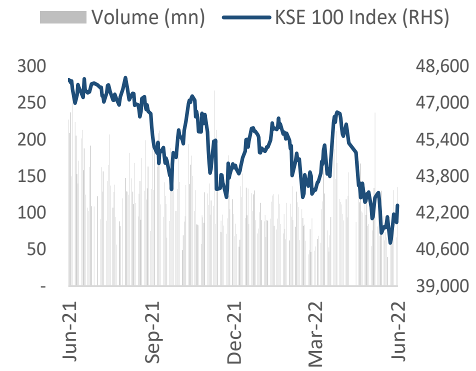
iii) Petroleum Development Levy (PDL) target revised down from PKR 750Bn to PKR 550Bn. PDL will be imposed @PKR 5/ltr per month incrementally up to 10 months cumulating to PKR 50/ltr.

iv) GIDC collection target which was set at PKR 200Bn has been abolished as the matter is in court and the affected companies have taken a stay order against paying the same.

Iii) Custom duty collection target has been revised upwards to PKR 1005Bn from PKR 953Bn earlier.

Market vantage point: From the stock market's perspective, we opine positive talks between IMF and Pakistan to ease nerves particularly with regards to the external funding gap as bridging the yawning USD 35Bn seemed to be an uphill task for the government without having the IMF on board. We also expect this to be key in taking the heat off PKR which has consistently weakened against the USD on the back of panic buying and economic woes. From an earnings standpoint, we believe the said development is negative due to higher taxes and lower profitability. Inflation readings are also expected to create some pressure as they are expected to remain in high-teens in the next few months. However, we believe the situation can change drastically if international commodity super-cycle starts to cool down as it will likely take some pressure off the external account and strengthen our footing on the economic front.

KSE 100 Index Performance



Source: PSX, BMA Research

Brent Crude Oil (USD per barrel)

Source: Bloomberg, BMA Research

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Buy	>15% expected total return
Hold	10%-15% expected total return
Underperform	<10% expected total return
*Total stock return = capital gain + dividend yield	

Old rating system

Overweight	Total sector return > expected market return
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Underweight	Total stock return < expected market return

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