



Federal Budget FY23:

Initial Impressions

Date: 10th June, 2022

Initial Impressions

- **First Impressions:** While we continue to go over the details, Federal Budget FY23 does not seem to have the bite of an IMF mandated budget. However, there are certain measures that may have significant consequences for the stock market, with the balance substantially tilted to the positive side. Though the government has done away with several exemptions and concessions, tax incidence for salaried class has been reduced (IMF demanded otherwise). There is an additional 2% tax on individuals, AOPs and companies earning more than PKR 300mn and 3% additional tax on banks.
- **Real estate's loss is stock market's gain:** Government has imposed a 1% annual tax on fair market value of Real Estate (worth PKR 2.5mn and above) in the form of 20% tax on deemed rental income (assumed at 5% of fair market value of property). However, one property for one's own residence will be exempt. Additionally, gains from property will be subject to CGT up to 6 years with 15% in year 1 and 2.5% in year 6 (a decline of 2.5% annually). Advance tax on property purchase is also up from 1.0% to 2.0% (for filers) & 5.0% (for non filers).
- **Key negative for stock market:** Through abolition of section 62, 62A and 63, the government has ended the tax credit on Investment in Shares (IPOs, Mutual Funds), Health Insurance, Life Insurance and Contribution to Approved Pension Funds
- **The budget in numbers:** Total outlay of the federal budget FY23 stands at PKR 9.5 trillion (+13% YoY). FBR tax collection target is set at PKR 7.0tn, up from revised PKR 6.0tn while overall tax revenue is targeted at 8.9% of GDP. Overall budget deficit is expected at 4.9% of the GDP versus 8.6% in FY22E.

Key Relief Measures

- Custom duty on more than 30 APIs removed.
- Industrial undertaking will now be able to adjust 100% initial depreciation in first year.
- Rationalization of 400 headings of CD, ACD and RD to support manufacturing sector.
- Immediate release of PKR 40bn DTL for textile exporters.

Key Revenue Measures

- 3% Windfall levy imposed on banks and their tax rate has been increased from 39% to 42%.
- Individuals/AOPs earning PKR 300mn and above annually will pay additional tax of 2%.
- Higher advance tax on new automobiles greater than 1600cc.

Impact on Stock Market

- **Incentives for industrial undertakings:** Budget is also positive for the industrial undertakings as government is now allowing adjustment of initial depreciation at 100% in first year (previously 50%), resulting in lower tax liability. Additionally, advance tax collected at import stage from industrial undertaking will now be adjustable (previously no adjustment allowed) resulting in better management of working capital.
- **Higher taxes for banks and large taxpayers:** Banking sector will be negatively impacted due to 3% additional tax eroding the sectors earnings. Individuals/AOPs earning PKR 300mn and above annually will pay additional tax of 2%.
- **A circular debt payment may be in the offing:** The government has projected fiscal deficit of PKR 2.94tn in 4QFY22 up by PKR 1.2tn YoY. While some increase in 4QFY22 fiscal deficit would likely be driven by higher debt servicing amid higher interest rates, and petroleum subsidy, we believe such a large quantum of the increase in fiscal deficit may be hinting towards GoPs intension to payoff some portion of the circular debt before June 30th 2022. Oil & gas sector and power sector will be the major beneficiaries.
- **Other sectors:** Custom duty reduced on APIs to benefit Pharma sector. Reduction in PSDP to 0.9% of GDP in FY23 (PKR 727bn) as compared to 1.1% of GDP disbursed in FY21 is negative for cement sector.

Stock Market/ Sectors	Impact
PSX	Positive
Banks	Negative
Engineering	Neutral
Oil & Gas	Positive
Cements	Negative
Chemical	Neutral
Fertilizer	Neutral
Food & Personal Care Products	Neutral
Autos	Negative
Paper & Board	Neutral
Pharmaceutical	Positive
IPPs	Positive
Refinery	Neutral
Technology & Communication	Positive
Leather & Tanneries	Neutral
Textiles	Positive

Sector	Measures	Impact
Banks	<ul style="list-style-type: none"> • Windfall levy imposed on banks. Tax rate increased from 39% to 42%. 	Negative
Textile	<ul style="list-style-type: none"> • Immediate release of PKR 40bn DLT for exporters. • Tariff rationalization on thread. 	Positive
Pharmaceuticals	<ul style="list-style-type: none"> • Custom duty on more than 30 APIs removed. 	Positive
Technology and communication	<ul style="list-style-type: none"> • Tax holiday for film makers. • 5 year income tax holiday for new cinema halls, production houses, film museums. • Tax rebate for 10 years on export of films & dramas. • Income tax exemption for cinemas and producers' earnings. • 8% WHT on distributors and producers to be abolished. • Machines for Films and dramas to be exempted from CD for 5 years. • Entertainment duty to be abolished. • Abolishment of sales tax on Import of machinery for film and drama making. 	Positive
Auto	<ul style="list-style-type: none"> • Higher advance tax new automobiles above 1600cc. Further advance tax on Electric engine cars to be charged at 2% (for filers). Non filers advance tax increased from 100% to 200%. 	Negative
Real Estate	<ul style="list-style-type: none"> • 1% annual tax on fair market value of Real Estate in the form of 20% tax on deemed rental income assumed at 5% of fair market value of property. One property for one's own residence will be exempt. • 15% CGT on immovable property with holding period of 1 year and 2.5% in year 6 (a decline of 2.5% annually). • Advance tax on sale/purchase of property increased from 1% to 2% (filers) and 5% (non filers). 	Negative

Sector	Measures	Impact
General Industry	<ul style="list-style-type: none"> Industrial undertaking will now be able to adjust 100% initial depreciation instead of 50% during the first year Advance tax collected at import stage from industrial undertaking is proposed to be adjustable (previously no adjustment allowed) 	Positive
Miscellaneous	<ul style="list-style-type: none"> Taxable annual income increased from 600,000 to 1,200,000. Behbud saving certificate, pensioners benefit account and shauhda family welfare profit tax reduced from 10% to 5%. Introduction of fixed income sales tax for small retailers which will be collected in electricity bills in the range of 3,000 to 10,000. This will be a final settlement. Tax exemption on import of solar panels. Easy installment loans to be provided to people using less than 200 units electricity for solar panels. Tractors, Agriculture machinery and seeds of wheat, maze, canola, sunflower, rice will be tax exempt. Rationalization of 400 headings of CD, ACD and RD to support manufacturing sector. 	Positive

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Hold	Between -5% and +15%
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