Exclusive
Interview

Mr. Ehsan Malik
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ICMA Pakistan: What is the official viewpoint of PBC on the current economic situation of the country in the backdrop of COVID-19 pandemic and what is its negative impact on the manufacturing sector.

EM: The COVID crisis is unprecedented in its depth, width, and in the uncertainty of its duration. No sector will escape impact; most will experience a significant reduction in sales and profit, with inevitable consequences on jobs and economic activity. So far as manufacturing is concerned,

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lock down of non-essential sectors obviously had a negative impact, but it is important to remember that even before the Covid crisis, manufacturing was in decline. Pakistan has been experiencing premature de-industrialization, outsourcing jobs to overseas suppliers through reliance on imports, even for essentials. In the last fifteen years, it has also lost share of world exports, whilst countries like Bangladesh and Vietnam grew theirs by 2 and 7-fold, respectively. A consequence of this is a recurring balance of trade crises and repeated IMF programs. The PBC's thrust is to promote "Make-in-Pakistan" in an effort to correct this imbalance and to generate jobs.

ICMA Pakistan: Which industry sectors have suffered the most due to the COVID-19? How they can sustain and re-build business?

EM: With all but essential sectors under lockdown starting from the last week of March to the end of April (and some well into May in Sindh), the impact on business was significant. Most of the larger businesses acted responsibly, by continuing to pay their employees, including the daily-paid, notwithstanding factory closures. Additionally, they had to meet fixed costs, including bank interest. Without output and sales but with costs to defray, the sectors impacted the most are textiles, autos, motorcycles, domestic appliances, cement, and steel. The March Quarter profit this year of listed companies was down 23% over the same quarter last year. PBC's own estimates for March and April showed between 50-100% decline in sales of cables, steel, cement, and autos over the prior year.

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Starting with ensuring that own employees remained, businesses reached out to value-chain partners to ensure their financial and operational continuity. In parallel, businesses started helping the communities in the proximity of their facilities and then widened their assistance beyond the neighborhood with rations and hygiene products. Businesses also conducted detailed risk and resource evaluations to ensure they remained prepared to respond swiftly and effectively to challenges and opportunities. Some relied on the State Bank's Payroll scheme, whilst others rescheduled loans to safeguard their liquidity. The reduction in borrowing costs helped. The more progressive businesses also reviewed and updated their IT and communication technology to improve the agility and speed of response. Regular and honest feedback remained a critical enabler and motivator, whilst a heightened sense of purpose and putting people before profit acted as a guiding beacon.

ICMA Pakistan: What would be the fall out of COVID-19 on our exports? Do you think Pakistan can take advantage of emerging international requirements for COVID-related products? What should be the role of TDAP in this regard?

EM: With a downturn in demand in the USA and Europe, which together represent over 50% of Pakistan's exports, our textiles sector saw cancellations and shipment deferral requests. Exports in April were down 54% and in May they declined by 34%. It is unlikely that the demand in the next few months would increase substantially as retail chains abroad have previous inventory to sell and employment levels will take time to bounce back to near previous normal. Besides, other supplier countries are also fighting for a share of a smaller export pie.

Pakistan has an opportunity to meet the demand of textile-based PPE. However, it has taken time for the government to allow exports. Textile companies report a heightened interest from the west as it opens up post-COVID. Suppliers have pricing power which may not last for long.

ICMA Pakistan: According to SBP, the private sector credit fell by 53.3% during 11 months i.e. July 2019 to May 2020. Do you think the high-interest rate is the only reason or other factors that restrict the private sector to take loans from banks?

EM: Interest rates are of course one reason for lower offtake of debt. Amongst others are lower demand for items such as domestic appliances, automobiles, motorcycles, cement, and steel. Banks also have little reason to pursue the more risky SME when they can lend risk-free to the Government. COVID will see higher borrowing from banks as businesses strive to meet their cash flow requirements. The SBP Payroll scheme should get some traction, albeit not from SMEs.

ICMA Pakistan: While tax revenue target is unmet every year, do you think FBR would be able to generate sufficient revenue from untaxed and under-taxed segments in the backdrop of COVID-19 aftershock on business and industry?

EM: It has been difficult to broaden the tax base in the best of times. In the foreseeable future, this will be virtually impossible. The informal sector has suffered the most during COVID, represents a sizeable part of the economy (and the vote bank) and the government will not have the political will to pursue them. The Construction initiative which includes the whitening of wealth in real estate may have some positive impact to grow the tax base. The 2020/2021 budget cannot be a tax revenue centered budget, either from an expansion of the tax base or from trying to extract more tax from those already taxed. Latitude

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will need to be negotiated with the IMF and space found to fund social development. The government will need to curtail its expenses and make it easier and cheaper for the private sector to do business and restore employment.

ICMA Pakistan: Do you think the reforms package announced for the construction and others would stimulate economic growth?

EM: For the package to stimulate growth, both the supply and demand sides of the equation need to be addressed. Cement, Steel, and building materials need to be cheaper to make housing affordable.

Surprisingly cement is subject to excise duty which is normally reserved for items such as cigarettes and soft drinks, where there may be a case to discourage consumption. Long term mortgages need to be made available and the foreclosure laws need to be reformed to give lenders the confidence to take long term exposure to the housing sector.

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ICMA Pakistan: Do you foresee any foreign investment coming into Pakistan in the next one or two years amid the COVID-19 scenario? What should be the top priority sector for investments in present circumstances?

EM: Pakistan needs to focus FDI primarily on export-led industries or those sectors in which local investors lack capital, technology, or risk appetite. Vietnam and others offer export-based models for us to emulate. In Pakistan, however, most of the current FDI leverage on domestic consumption. Example of capital, technology, and risk intensive sector is oil and gas exploration. Pakistan has a significant opportunity in agriculture, tourism, fisheries, and mining for foreign investment. Whilst tourism will take a back seat, post-Covid, food security will become even more important than hitherto, hence an opportunity for Pakistan.

ICMA Pakistan: Can you share with us a few major recommendations of PBC for the Federal Budget 2020-21?

EM: With export demand likely to remain subdued, the Corona Budget for FY21 will need to leverage Pakistan's large domestic market to revive the economy and restore employment. Measures should focus on making the daily lives of the common people of Pakistan easier. This can be accomplished by reducing/zero-rating GST and other levies on essentials: food, milk, clothes, transportation, construction, and building materials such as cement and steel, domestic appliances, motorcycles, and cars. Fuel prices have already been reduced but utility tariffs do not yet reflect the decline in the global cost of oil and gas. Fortunately, there is unutilized capacity in our textiles industry as well as in most of the other aforementioned sectors. However, these measures would need to include reforms in the tax system to make it cheaper and easier to do business and incentives to invest. These would include:

- Exemption from turnover based minimum tax for listed companies
- Reduction in minimum tax to a third of the current rate for other businesses
- Reduction in number of Withholding Taxes and reduction in some WHT in line with the reduction in the minimum tax
- Withdrawal of advance income tax and the sales tax on import of plant and machinery for manufacturing
- Restoration of group taxation to the pre-Finance Act 2016 basis to promote scale through consolidation
- Income tax credit at 10% for investment in balancing modernization and replacement in plant, machinery, and industrial buildings
- Reduction in tax on lower-paid employees

ICMA Pakistan: What is the viewpoint of PBC on the changes made in the Companies Act 2017 through the Companies (Amendment) Ordinance 2020?

EM: PBC supports the government and the SECP on the direction of the changes made but feels that they don't go far enough with respect to Section 452 (Global Registry of Shares) and Section 208 (Related Party Disclosure). It also disagrees with the deletion of Section 181 (independent and Non-Executive Directors).

On Section 452, which PBC advocates the complete withdrawal of, our position is based on the stance that there is no global precedence for reporting interests other than those that create potential conflicts of interests (which is adequately covered elsewhere in the Act); that reporting of foreign interests should be the subject of taxation and exchange control laws, not of Companies Law; that the Foreign Assets Declaration and Reporting Act has superseded the Companies Act; that no investor interest is served by this information which is merely passed on by the SECP to the FBR; and finally, that SECP's time and attention are best utilized on more value-adding activities than acting as a post office. Section 452 discriminates against those in the formal corporate sector which generates jobs, taxes, and exports. It is an unnecessary intrusion that will discourage corporatization.

ICMA Pakistan: How ICMA and PBC can work together to help out the industry and business to combat COVID-19 implications?

EM: PBC works with several professional organizations including ICAP and ACCA to jointly advocate for policies that promote the formal sector and looks forward to doing the same with ICMA. Specifically, on COVID, given the management accounting expertise of ICMA Pakistan members and their well-entrenched position in the industry, we will explore ways to promote "Make-in-Pakistan." One proposal we have been working on with the government is to set standard duty drawback rates to promote exports by SMEs that are unable to utilize the more complex DTRE scheme.

*The Editorial Board thanks **Mr. Ehsan Malik, CEO, Pakistan Business Council (PBC)** for giving his exclusive interview for Management Accountant Journal.*