

## **Would PM's Package for Construction Industry Deliver?**

**Syed Hussain Haider, Arsalan Ahmed, Ali H. Zaidi**

PM Imran Khan on April 3, 2020 finally unveiled the long-promised, long-awaited package to stimulate the construction industry that he believes is vital for economic growth. The package was much sought after by both the real estate sector and the government, but the crisis management required to overcome the twin deficit and the FATF challenge kept pushing it further down the to-do list. The package would on the face of it benefit the economy.

- ❖ Given the numerous economic challenges faced over the past 2 years (the twin deficits, FATF and border tensions), announcement of the construction package at this point in time appears predetermined.
- ❖ With the world heading towards an economic meltdown, Pakistan will find the package great news indeed; There would hardly be any critique given that its beneficiaries can be found across the income distribution.
- ❖ An amnesty scheme with such generous tax breaks and incentives is, quite frankly, unheard of. However, even though the supply side has been generously catered for, demand remains elusive in these uncertain times.
- ❖ The government wants to re-open industries by the 14th of April, but it seemingly contrary to PM's statement that the extent of the spread of Covid-19 going forward is a big unknown.
- ❖ Unlike developed nations that can afford a complete lockdown, Pakistan is torn between health and economy. At least based on the government's narrative, the two are mutually exclusive.
- ❖ The package could undoubtedly bring tremendous benefits in the long term, but it is near impossible to determine its success in the immediate term given the ongoing pandemic.

The approval of the package by the federal cabinet is expected soon. Nevertheless, with the different tiers of government and countless departments and bodies involved, transitioning from approval to implementation may take some time. Salient features of the scheme are as below:

- In what is being termed as an amnesty scheme, the government has decided that source of income will be exempted from enquiries until 30th June 2022 if the amount is invested in purchase of land and construction thereon, construction on land already owned and first purchase of newly constructed property. Such amounts may be declared in wealth statements.
- A fixed rate regime has been proposed that would effectively lower the tax rate applicable to the construction sector. Income arising from the construction industry will now be treated separately and tax will be levied on per square yard basis (for developers) and per square feet basis (for builders).
- Withholding tax shall not be applicable to construction services and purchase of raw materials except for cement and steel.

- All taxes, levies, fees and charges on transfer of property by provincial and local governments are proposed to be clubbed together at the rate of 2%.
- Construction of, and transactions relating to ‘first house’ shall be exempted from all taxes, including Capital Gains Tax (CGT). Furthermore, the holding periods for the CGT have been revised: it will be now be applicable to property held for up to 3 years (previously 4 years).
- With the aim of reducing construction costs, sales tax and excise duties on raw materials are to be reduced/ removed, as required.
- The real estate sector has finally been given industry status. This naturally implies that a registered, better documented and more regulated real estate sector would make for a more coherent approval system which will be more convenient for all stakeholders. Furthermore, the establishment of a Construction Industry Development Board (CIDB) has also been proposed. Just a few months ago, the government had decided on establishing Real Estate Regulatory Authority (RERA) and had even finalised a bill, as per media reports. As the name suggests, RERA would be responsible for regulating the real estate sector. Only time will tell how this developing structure of the industry will shape out.

The package is certainly a positive development, which has already been reflected in the phenomenal performance of the cement & steel sectors during the last week.

The demand for cement can be broadly segregated by public and private sector which constitute roughly 70% and 30% respectively. Further bifurcating the latter, we find that builders & developers make up roughly 40-50% of private sector demand. The scheme holds the potential to add nearly 2-3mn tons of incremental demand (approx. 8% YoY) in FY21.

As a rule of thumb, every 7 tons of cement sold translates to a ton in rebar sales. Considering this, it is expected that FY21 should see an incremental demand of nearly 0.3-0.5mn tons (approx. 8% YoY).

The above estimates do not incorporate demand arising out of activity in Naya Pakistan Housing Scheme. Tax for projects under this scheme will be reduced by 90%. Moreover, it has been proposed that such projects be completely exempted from provincial sales tax. In addition to this, the government has also earmarked Rs30bn in subsidies to promote low cost housing. To further catalyse economic activity, a lower interest rate (6%) has been proposed for house mortgages of 100,000 units. Currently 7% is applicable to greenfield projects.

Having mentioned the key highlights, the following aspects require greater clarity:

- a) With regards to the dates announced to avail exemptions (amnesty), the PM had mentioned investments made during the ‘*current year*’. However, the draft document mentions a period ending ‘*June, 2022*’. This is giving the impression to some that the projects are to be completed in this short time span.

- b) It is still unclear what the Rs30bn subsidy is meant for and whether it will be enough.
- c) The draft and the PM's speech both imply 'fresh investments'. Will ongoing projects be able to avail the same benefits?
- d) Will the incentives only be available to builders/developers? Will final buyers be able to get the same benefits?

With the world heading towards an economic meltdown, Pakistan will find the package good news indeed; there would hardly be any critique given that its beneficiaries can be found across the income distribution. There is no doubt that in the long term the package would bring tremendous benefits. At the same time, it is near impossible to determine its success in the immediate term given the ongoing pandemic.

Courtesy: JS Global