

Budget 2023-24

Prioritizing Growth while Macro Challenges Linger

CAL's view on the budget and
impact on the listed entities

Executive Summary

- In this year's budget review, we will provide a broad overview of inflation, currency, growth, and interest rates, offering a general direction. The central bank's policy stance after the parliamentary approval of the national budget will play a critical role in shaping the outcomes of these crucial macroeconomic factors.
- Successfully navigating the complexities of participating in an IMF program, meeting the recommended policies for accessing the second tranche of funding, and managing the political pressures associated with an upcoming election year presents a significant challenge. Recognizing the magnitude of these macroeconomic challenges and the wide array of potential outcomes, **we will present a more in-depth analysis in our forthcoming macroeconomic outlook report.**
- The FY2023-24 budget places emphasis on fostering digital inclusion for individuals and businesses, aligning with the SMART Bangladesh plan to drive digitization across various activities. Additionally, a universal Pension Scheme was also introduced.
- Despite the prevailing macroeconomic challenges, the FY 2023-24 National Budget places a strong emphasis on stimulating growth.
- Expenditure allocation for pay & allowances, interest, and subsidies equals 77% of revenue, which inflates the operating expenditure limiting fiscal space for development spending. On the other hand, the government has raised the social safety net allocation by 11% from last year's budget while adding around 8 lac new direct beneficiaries under various programs aiming to provide relief during a high inflation environment.
- The revenue collection target including grants has been raised by 15.5% to BDT 5,039 bn, with a special focus on the expansion of the tax base and tax policy reforms. However, a 26.6% increased revenue target from direct taxes, may be difficult to achieve due to unchanged tax rates and the adverse impact of global and local challenges on business activities.
- The projected budget deficit is set to rise by 15.0%, accompanied by a 14.7% higher borrowing target from the banking system and a 22.3% increase in foreign sources. However, meeting these borrowing targets presents significant challenges.
- Challenges in meeting higher bank borrowing targets under the budget may prompt interest rate hikes or debt monetization by the central bank, exacerbating inflationary pressures.

Taka goes to...

A Focus on the Growth while Expenditures Rise

Total expenditure in the proposed budget increased by 15.3% over the last year's revised budget to BDT 7,618 bn.

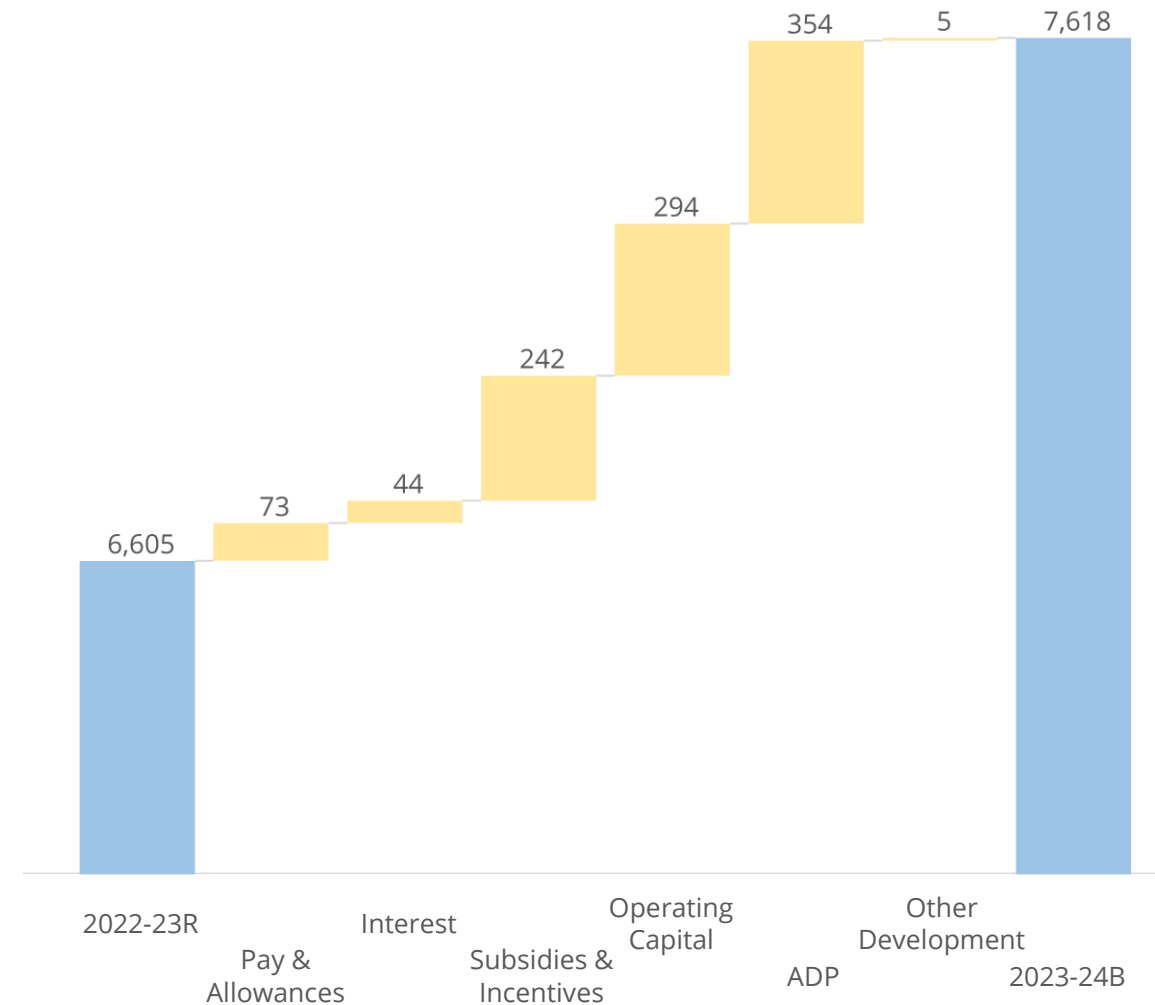
The government has raised the social safety net allocation by 11% to BDT 1,263 bn from last year's budget. Additionally, around 8 lac new beneficiaries are proposed to be included aiming to provide relief during a high inflation environment.

The allocation for interest expenditure has increased by 4.8%, while the deficit financing requirement has risen by 15%. Due to the need for higher incremental deficit financing in an environment of rising interest rates, it is likely that the allocation for interest payment will be revised upward.

In light of challenging economic circumstances, including dollar shortage and high inflation, the proposed budget allocates 36.4% of the total budget towards development expenditure compared to the actual expenditure of 38.6% in the pre-COVID period of 2018-19. These measures aim to address pressing needs within the available resources, considering the prevailing constraints.

The allocation for pay & allowances, interest, and subsidies comprises about 77% of the revenue, adding pressure to the widening budget deficit. Subsidies and incentives have witnessed a 13% increase, which may offer some relief in the inflationary environment. However, Operating Capital Expenditure posted a 61.3% increase, inflating the overall operating expenditure and limiting fiscal space for development spending.

Incremental Government Expenditure (BDT bn) 2023E



Taka comes from...

Ambitious revenue targets amidst a challenging macroeconomic landscape

On the revenue front, direct tax and VAT will make up 63% of total revenue and are expected to contribute 74% of the incremental revenue compared to last year's revised budget.

The government has introduced some measures in the area of direct taxation to enhance tax compliance and broaden the tax base. Instead of raising tax rates, initiatives have been aimed at bringing more taxpayers into the tax net, reforming tax policies, and encouraging e-TIN holders to file returns voluntarily.

The proposed budget aims to raise the tax-to-GDP ratio by an additional 0.5% of GDP in FY-24 as per IMF guidelines, resulting in a rise to 8.99% from 7.54% in FY 2021-22 (Actual).

Meeting the ambitious 26.6% revenue growth target from direct tax sources might pose a challenge as corporate tax rates remain unchanged. Furthermore, the adverse impact of global and local challenges on business activities is likely to exert downward pressure on profit margins, thereby adding to the difficulties of meeting the set targets.

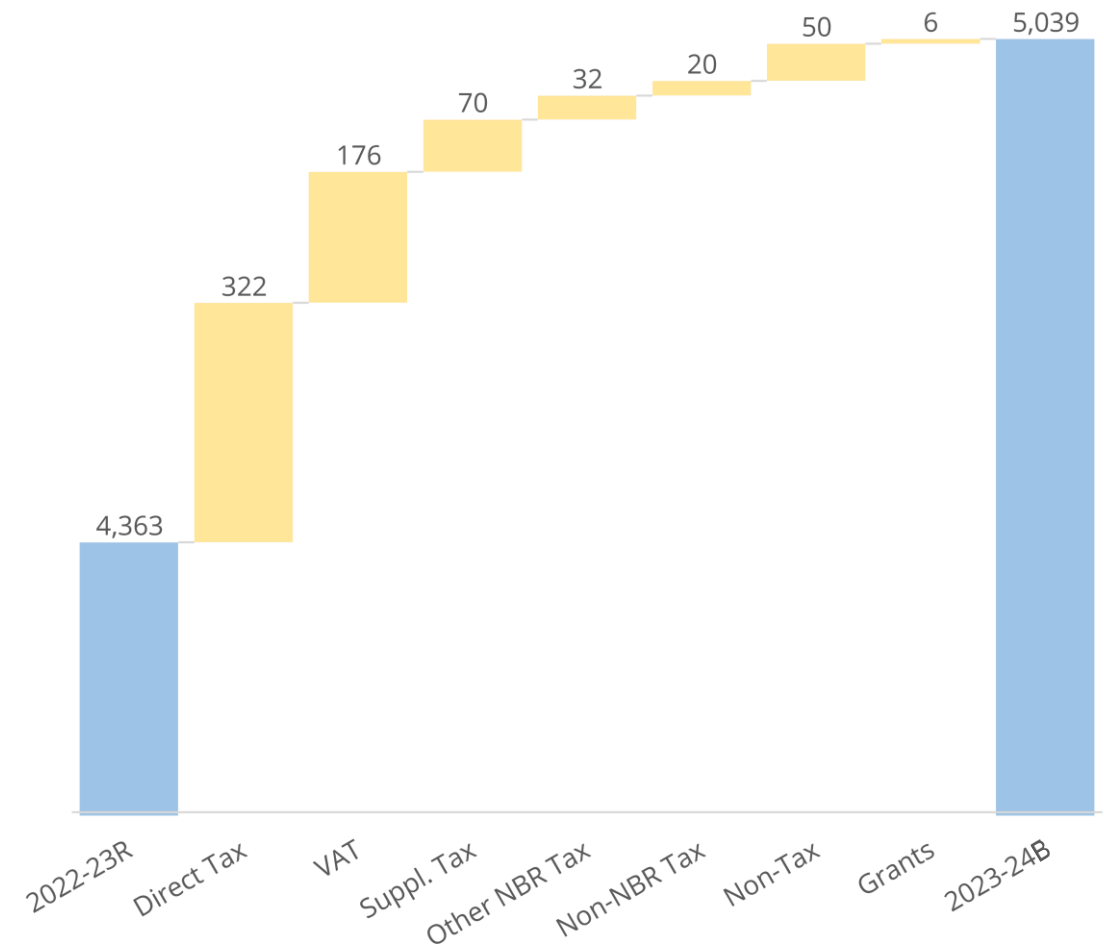
The implementation of a minimum tax of two thousand taka for individuals below the taxable limit may impose a tax burden on low-income earners while it is a step towards expanding the tax base.

Increasing import duties to promote import substitution will incentivize the local industry and boost revenue collection.

Selected sources that will drive higher revenue collection :

- Price increase on cigarettes: Premium 5.6%, High 1.8%, Medium 3.1% and Low 12.5%
- Increase import duty of cement clinker from 500 taka to 700 taka per m.ton.
- Withdrawal of concessionary rate for importing materials of the hotel industry.
- Imposition of 25% customs duty and 15% VAT on the import of software.
- Increase in Customs Duty on lift and skip hoists to 15% from 5% and for escalators to 15% from 1%.

Incremental Government Revenue and Grants (BDT bn) 2023E



Deficit to be financed from...

Prioritizing Growth while Macro Challenges Linger

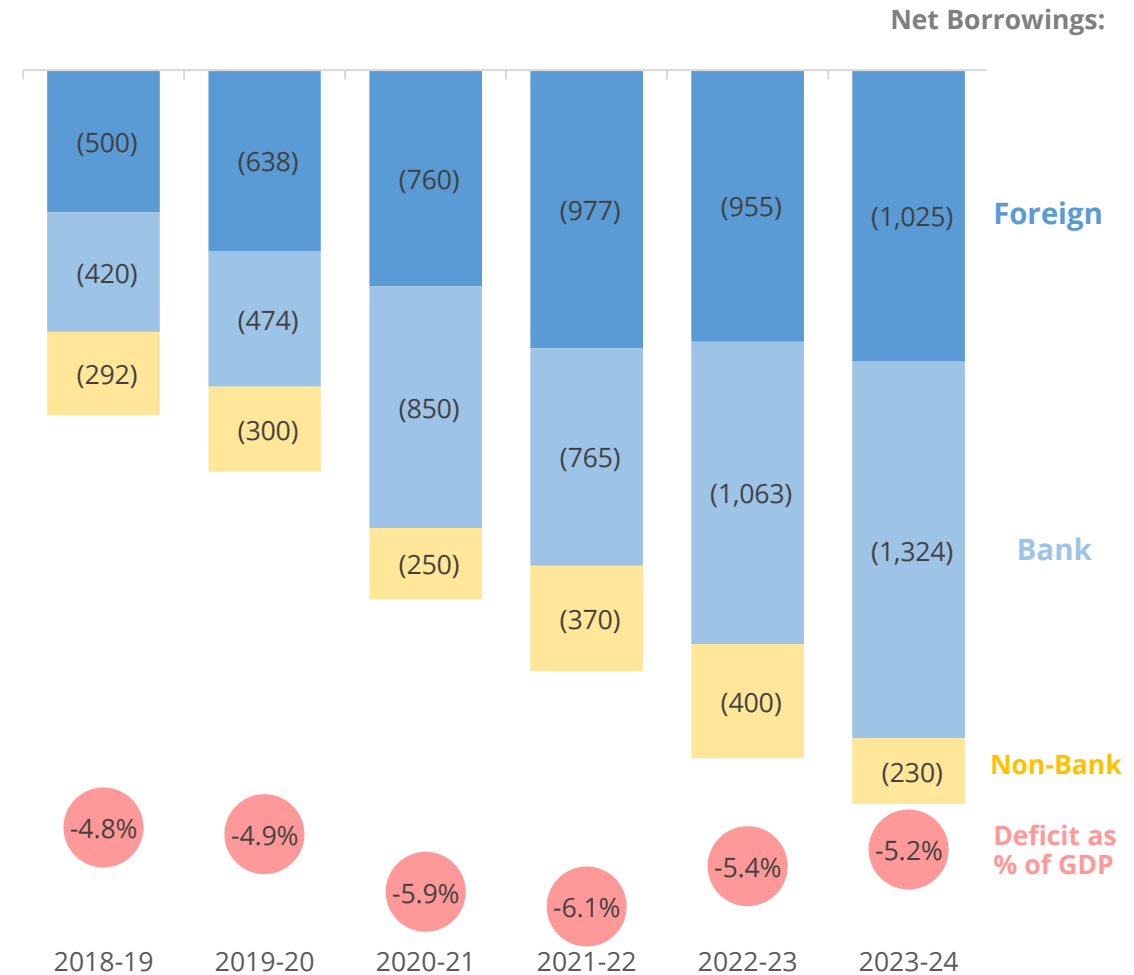
The national budget for FY2023-24 has been unveiled in the midst of pressing concerns regarding inflation control and currency stability. Despite these challenges, the budget maintains its focus on prioritizing growth, with a 7.5% GDP growth target.

The budget deficit is expected to expand by 15.0% YoY to BDT 2,578.9 bn which is expected to be funded by BDT 1,554.0 bn from domestic sources and BDT 1,024.9 bn from foreign sources.

The budget deficit's funding plan presents significant challenges due to various factors. Domestically, the borrowing target from the banking system in FY2023-24 has been increased by 24.5% compared to last year's budget, potentially pressuring the banking system and will lead to either excessive money printing or a steep rise in interest rates, which could crowd out the private sector.

The goal of acquiring BDT 1,025 billion (USD 9.5 billion) through foreign sources is ambitious, considering that historically on average 62% of the foreign financing target has been achieved in the past five years. Furthermore, the situation is compounded by the recent Moody's rating downgrade for Bangladesh and the global rise in interest rates, making the task even more daunting.

Budget Deficit & Deficit Financing (BDT bn)

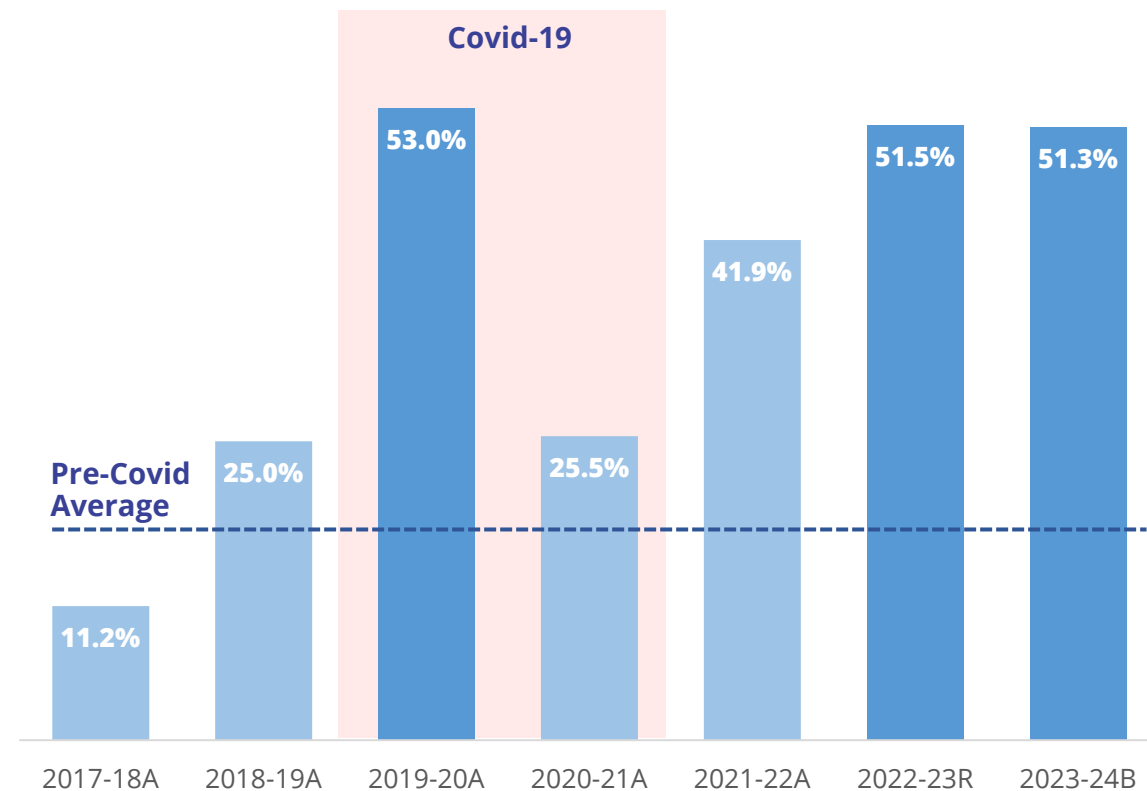


The Tug of War: Attaining higher bank borrowing targets will either push up the interest rates or lead to further debt monetization.

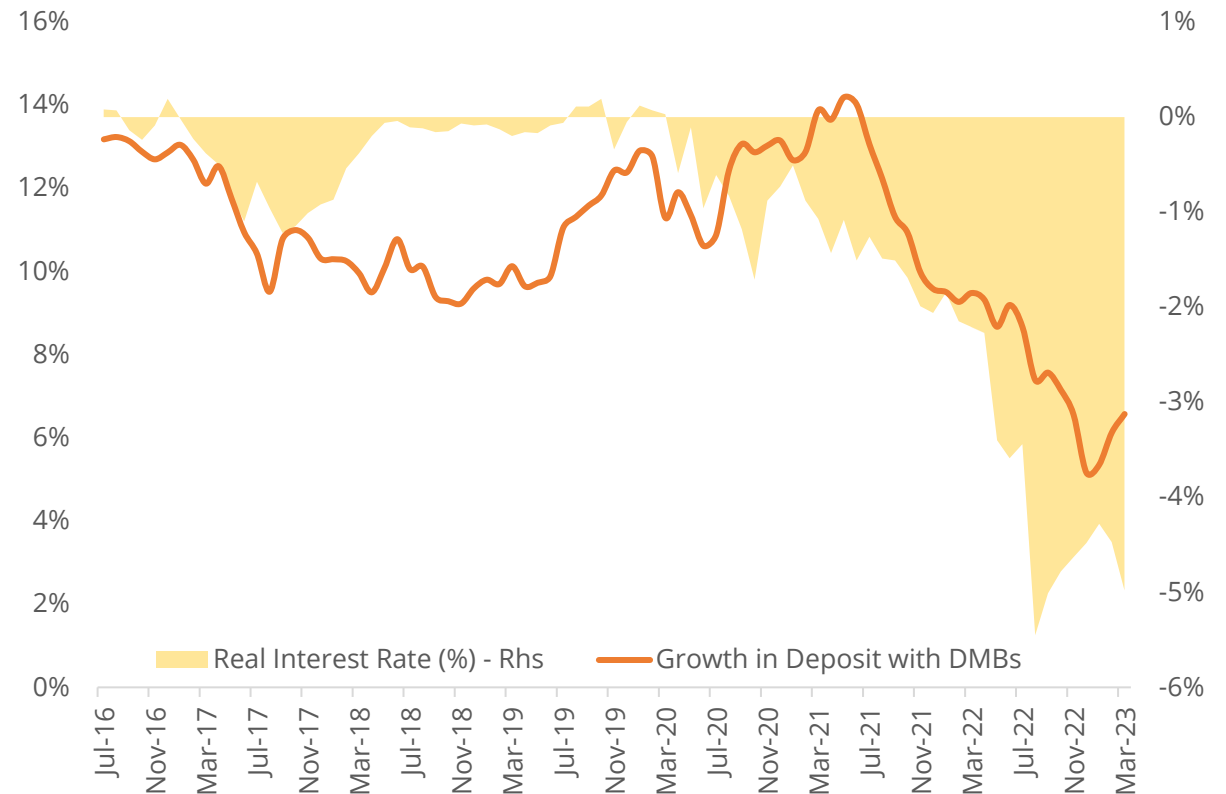
Global headwinds, high inflation, increased interest expenses, and rising operating expenditures of the government widened the budget deficit, leading to heightened government reliance on bank borrowing.

Due to negative real interest rates, deposit growth in the banking system has sharply declined, leading to a liquidity shortage in the banking system. To reach a 14.7% higher bank borrowing target in FY-2023-24E, there will be a need for a substantial increase in interest rates to attract deposits or lead to further debt monetization, which will fuel inflation.

Borrowing from the banking system as % of total deficit financing



Deposit growth vs Interest Rate



Post-budget Economic Outlook

Growth Outlook Under Strain

Dollar scarcity and import restrictions have had a detrimental impact on the overall economic activities, with LC opening for Capital Machinery experiencing a significant drop of 56.9%, while Industrial Raw Materials and Intermediate Goods declined by 31.9% and 31.4%, respectively, over the last ten months. Additionally, private sector credit growth has declined from 14.1% in August 2022 to 11.3% in April 2023. Achieving the ambitious 7.5% GDP growth target in such circumstances poses significant challenges. However, the expansionary stance of the national budget holds the potential to act as a counterforce.

Interest rates to trend higher

The target for a 14.7% increase in the government's borrowing from the banking sector carries the potential risk of a significant interest rate hike if funds are obtained from commercial banks at market-determined rates. However, the central bank's continued devolvement strategy aims to maintain rates at current levels. Since the IMF program for Bangladesh aims for a gradual transition towards interest rate targeting, CAL expects further policy rate hikes may be necessary to control inflation. However, the extent of these hikes might depend on the government's stance on prioritizing growth versus curbing inflation, considering the upcoming national election.

Inflation to remain elevated

In April 2023, inflation remained high at 9.24%. CAL expects inflation to remain at elevated levels above the government's target of 6% unless interest rates are raised sufficiently to restore positive real interest rate dynamics. Continuing the current debt monetization approach to finance the budget deficit in the upcoming fiscal year will exacerbate inflationary pressures. One silver lining, though, is the softening of global commodity prices, particularly petroleum products, which will offer some respite in managing inflation.

Exchange rate to remain under pressure

If the central bank adopts a market-based uniform exchange rate by the end of June, in line with IMF recommendations, there might be initial currency volatility. The imposition of import restrictions, coupled with declining commodity prices, has helped improve the current account balance and alleviate some currency pressure. However, as the current foreign exchange reserve is below the IMF target of USD 24.5 bn (June-23) under the new reserve calculation formula, BB's ability will be limited to provide support to currency against external shocks. Moreover, the already devolved amount of c. BDT 770 bn in the first eleven months of this fiscal year by BB will put additional pressure on the currency.

Tax Highlights

Personal Tax

The minimum tax-free income limit for individuals increased which will increase disposable income for the average person and provide some relief in a high inflationary environment

Tax Exemption Threshold (BDT)	Existing	Proposed	Changes
General	300,000	350,000	50,000
Women & Senior Citizen	350,000	400,000	50,000
Physically Challenged Persons	450,000	475,000	25,000
War-wounded Freedom Fighters	475,000	500,000	25,000
Third Gender Tax Payers	350,000	475,000	125,000

	Proposed rates
Up to BDT 4 crore	Nil
Net wealth from BDT 4 crore to BDT 10 crore or ownership of more than one motor car; or ownership of house property having an aggregate area of 8,000 sq. ft	10%
From BDT 10 crore to BDT 20 crore	20%
From BDT 20 crore to BDT 50 crore	30%
Above BDT 50 crore	35%

Corporate Tax

Description	Existing FY 2022-23	Proposed FY 2023-24	*Applicable tax rate if fails to meet the condition
Publicly traded company- free float equal to or above 10%	20.0%	No change	22.5%
Publicly traded company -less than 10% free float	22.5%		25.0%
Non-publicly traded company	27.5%		30.0%
One person company	22.5%		25.0%
Publicly traded bank, insurance and FI	37.5%		*
Non-publicly traded bank, insurance and FI	40.0%		*
Merchant bank	37.5%		*
All sorts of tobacco manufacturing company including cigarette, bidi, chewing tobacco, gul etc.	45% + 2.5% (surcharge)		*
Publicly traded mobile operator company	40.0%		*
Non-publicly traded mobile operator company	45.0%		*
Association of persons	27.5%		30.0%
Artificial juridical person and other taxable entities	27.5%		30.0%
Private university, medical, dental and engineering college or private college solely dedicated to imparting education on ICT	15.0%		*

* Condition not applicable

LISTED EQUITIES

Impact on CAL's coverage universe

Tobacco

Engineering

Textile

Constructions

Pharmaceuticals

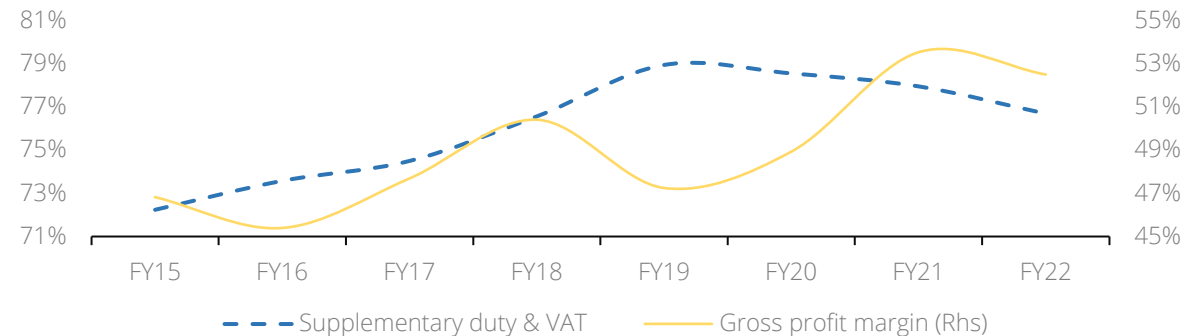
Others

Tobacco

BATBC: Positive Impact

In the low segment, the price has been increased by 12.5% to BDT 45 per 10 sticks and supplementary duty raise from 57% to 58%. For BATBC, the low segment contributes 75% of total volume sales. **Revenue and margin for BATBC are likely to expand as an upward revision in retail prices of low segments cigarettes will offset for 100 bps increase in Supplementary duty and possible volume contraction.** In FY22, a significant portion of consumers switched from higher segments of cigarettes to lower segments. And we expect a similar trend to continue in FY23-24 on the back of inflationary pressure. However, compared to the Top-3 segment consumers, lower segment cigarette consumers might shift to other cheaper alternatives offsetting some of the margin benefits as there has been no price change proposed for Homemade Filter and Non-Filter Bidi.

In the proposed budget for FY2023-24, the Price of 10-stick premium segment cigarettes has been increased to BDT 150, High segment cigarettes to BDT 113, and Medium segment to 67, implying an average price increase of 3.5% in the top 3 segments with no change in Supplementary duty (SD). Considering the top 3 segments contribute 25% of total volume sales, a 3.5% price increase is likely to bring revenue and gross margin expansion to BATBC.



Proposed Changes in Tobacco Tariffs & SD					
Cigarette	Existing price per 10 stick	Proposed price per 10 stick	Change (%)	Existing SD	Proposed SD
Premium	142	150	5.6%	65%	65%
High	111	113	1.8%	65%	65%
Medium	65	67	3.1%	65%	65%
Low	40	45	12.5%	57%	58%

Homemade Filter Bidi	Existing price	Proposed price	Change (%)	Existing SD	Proposed SD
20 stick	19	19	0%	40%	40%
10 stick	10	10	0%	40%	40%

Homemade Non-Filter Bidi	Existing price	Proposed price	Change (%)	Existing SD	Proposed SD
25 Stick	18	18	0%	30%	30%
12 Stick	9	9	0%	30%	30%
8 Stick	6	6	0%	30%	30%

Engineering

PROPOSAL	COMPANY	IMPACT
In case of supply of Extra High Voltage Power Cable 33KV to 500KV by local manufacturers having own Vertical Continuous Vulcanization line	BBSCABLES	Positive: A flat 3% source tax instead of a 2-7% varying source tax
Extension of existing VAT exemption facility for production of refrigerator and freezers till June 30, 2024	WALTON, SINGERBD	Positive: Refrigerator sale contributes 92% of WALTON's sales and 40% of SINGERBD's, extension of VAT exemption facilities will help to keep product prices lower.
Extension of existing VAT exemption facility for production of Washing Machine, Microwave Oven, and Electric Oven till June 30, 2025	WALTON, SINGERBD	Positive
Exemption from Advance Tax on import of Rice transplanters, dryers, all types of sprayer machines, potato planters used in agriculture	ACI	Positive: ACI Motors provide a wide range of agriculture machinery from land preparation and cultivation to crop preservation

Fuel and Power

PROPOSAL	COMPANY	IMPACT
Imposition of 7.5% VAT instead of the existing 5% VAT at the local manufacturing stage on iron or steel (LPG Cylinder)	MJLBD	Negative: Gross margin will decline if the company fails to pass the price to the consumer
Imposition of BDT 1,117 specific duty per barrel instead of the 5% existing rate on import of Petroleum oils and oils obtained from bituminous minerals, crude.	JAMUNAOIL, PADMAOIL, MPETROLEUM	Positive: An increase in fixed price per liter of petroleum oil price will increase the float balance for oil distributions companies creating scope for increased interest income
Imposition of BDT 13.75 specific duty per liter instead of the 10% existing rate on import of Motor spirit, Naphtha, Furnace oil	CVOPRL	Positive
Exemption from VAT (from 15% to 0%) for Petroleum oils and oils obtained from bituminous minerals, Motor spirit, Naphtha, Furnace oil	Fuel and fuel distribution companies	Neutral Reduction in VAT will reduce the fuel price without impacting the float balance of the company

Pharmaceuticals

PROPOSAL	COMPANY	IMPACT
Exemption of VAT at the production stage on anti-malarial and anti-tuberculosis drugs	BXPHARMA, SQURPHARMA, ACMELAB, IBN SINA, BEACONPHARMA, NAVANAPHARMA	Positive
Inclusion of one hundred more raw materials of cancer medicines in the concession rate list of pharmaceutical productions.	BEACONPHARMA, BXPHARMA, SQURPHARMA, ACMELAB, IBN SINA, NAVANAPHARMA	Positive
Inclusion of 3 more diabetic management-related drugs in the concession rate list of pharmaceutical productions.	SQURPHARMA, BXPHARMA, ACMELAB, IBN SINA, BEACONPHARMA, NAVANAPHARMA	Positive
Allowing import of Silicon tubes for the production of IV Cannula at a concessionary rate.	JHRML	Positive

Constructions

PROPOSAL	COMPANY	IMPACT
Proposal made to increase the existing specific rate of duty of cement clinker is from BDT 500 to BDT 700 per M.Ton	HEIDELCEM, LHBL, CROWNCEMNT, PREMIERCEM	The price of per bag cement will increase, which will have a negative impact on volume. However, LHBL will enjoy margin expansion if the cement price is increased.
Increase in the tax rate at source rationally during land registration in areas under and outside the jurisdiction of Rajuk and CDA	EHL	Negative
To reduce the VAT from 15% to 5% on Terephthalic acid, Ethylene glycol, hot rolled stainless steel	BSRMLTD, BSRMSTEEL	Positive
Total tax incidence for calcium carbonate at 43%	HEIDELCEM, LHBL, CROWNCEMNT, PREMIERCEM	Negative

Miscellaneous

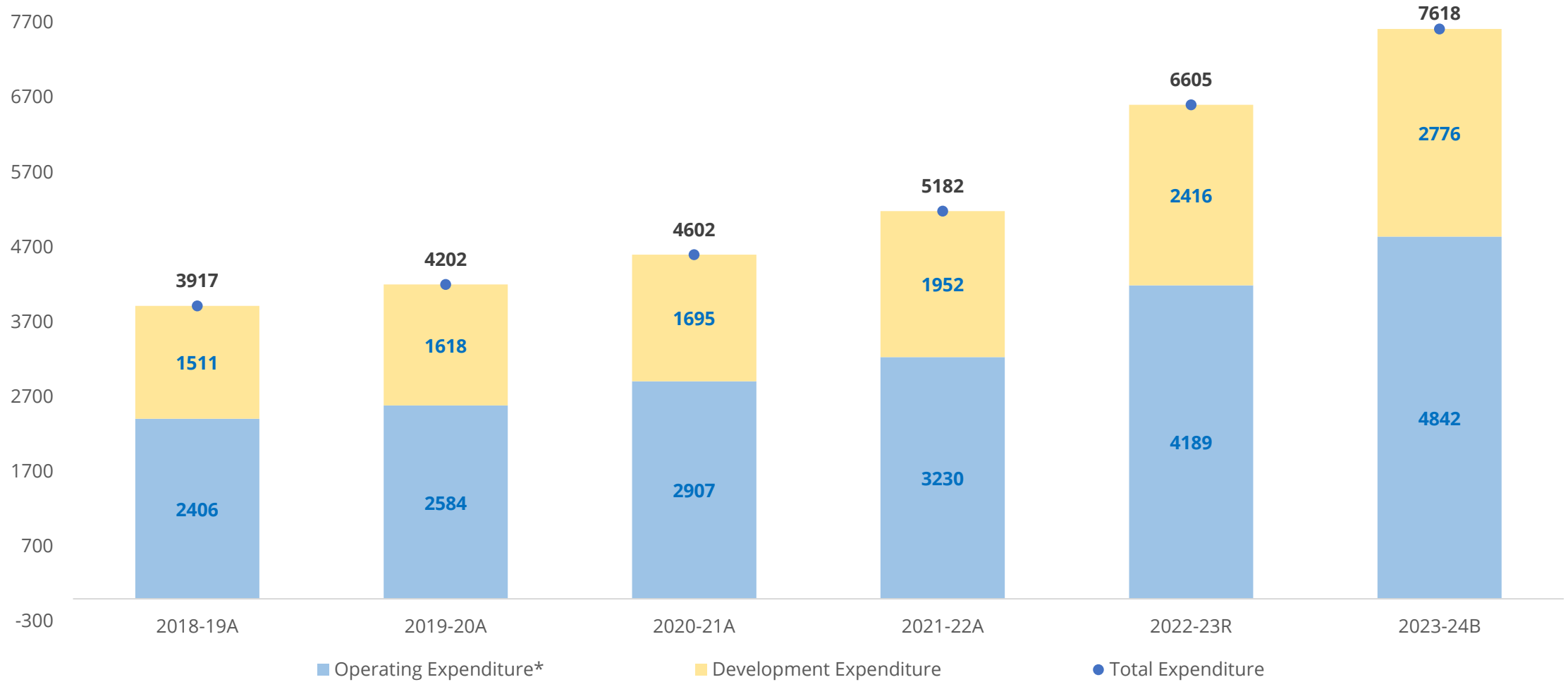
PROPOSAL	COMPANY	IMPACT
Imposition 25% customs duty and 15% VAT on the import of software	EGEN, AAMRATECH, DAFODILCOM	Negative
Exemption of VAT in excess of 5% at the production stage on optical fiber cable till June 30, 2024	BDCOM, AAMRANET, ADNTEL	Positive: Due to the reduction in VAT, cost will reduce for interest services providers
SD increased from 0% to 20% for the import of Fruit, nuts, and other edible parts of plants, otherwise prepared or preserved, whether or not containing added sugar.	OLYMPIC, LOVELLO, GHAIL	Negative: Input costs will increase slightly for the companies
Withdrawal of full exemption and imposition of 5% VAT at the local manufacturing stage on poly propylene staple fiber	Textile companies	Negative

Miscellaneous

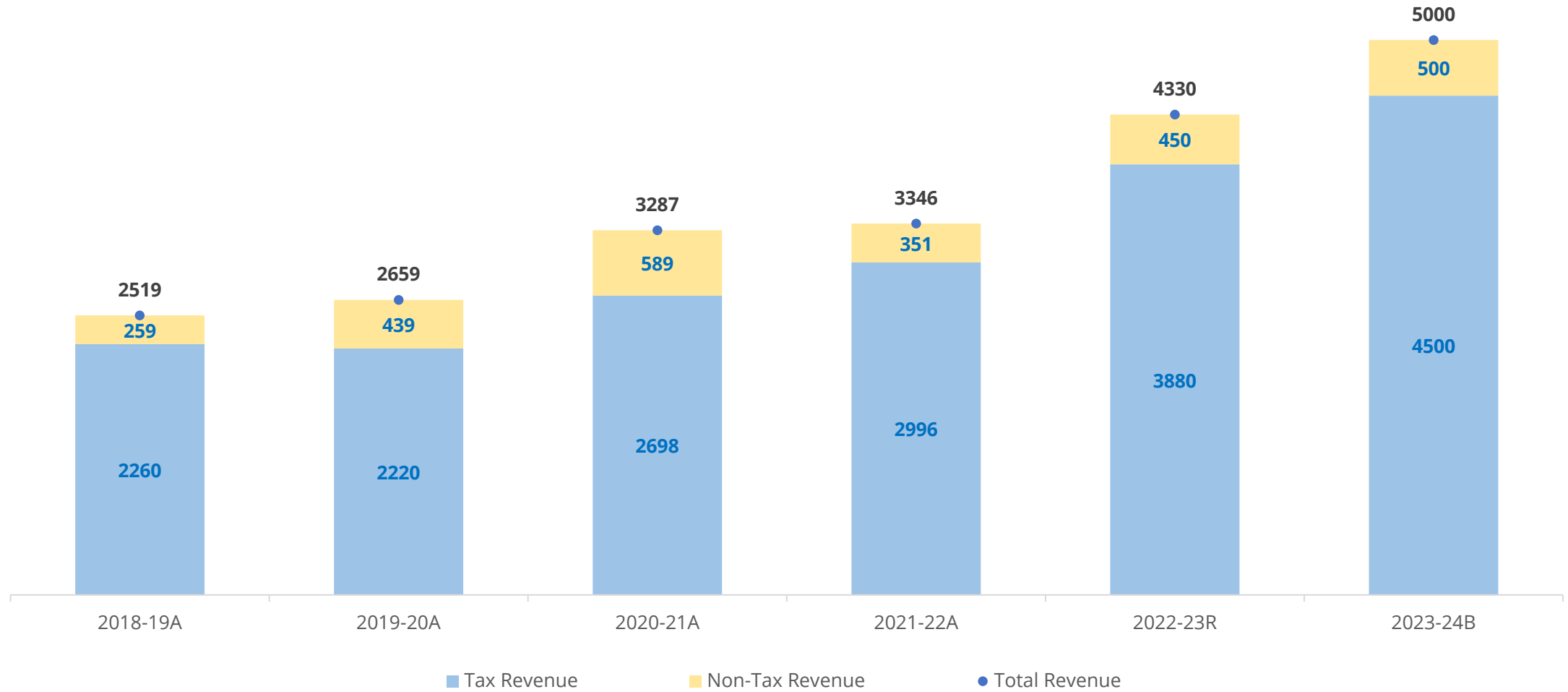
PROPOSAL	COMPANY	IMPACT
Imposition 7.5% VAT instead of 5% on kitchen towel, Toilet tissue, Napkin tissue, Facial tissue/pocket tissue, Hand towel/Paper towel/clinical bed	BPML	Negative: A significant portion of revenue for BPML comes from the tissues segment, a increase in VAT will reduce demand of tissue papers
Withdrawal of concessionary rate facilities to import materials for large-scale and high-quality hotels	UNIQUEHRL, SEAPEARL, BDSEVICE	Negative
Imposition 15% VAT on ballpoint pens at the manufacturing stage	GQBALLPEN	Negative

Appendix

Government Expenditure (BDT Bn)



Government Revenue Collection (BDT Bn)

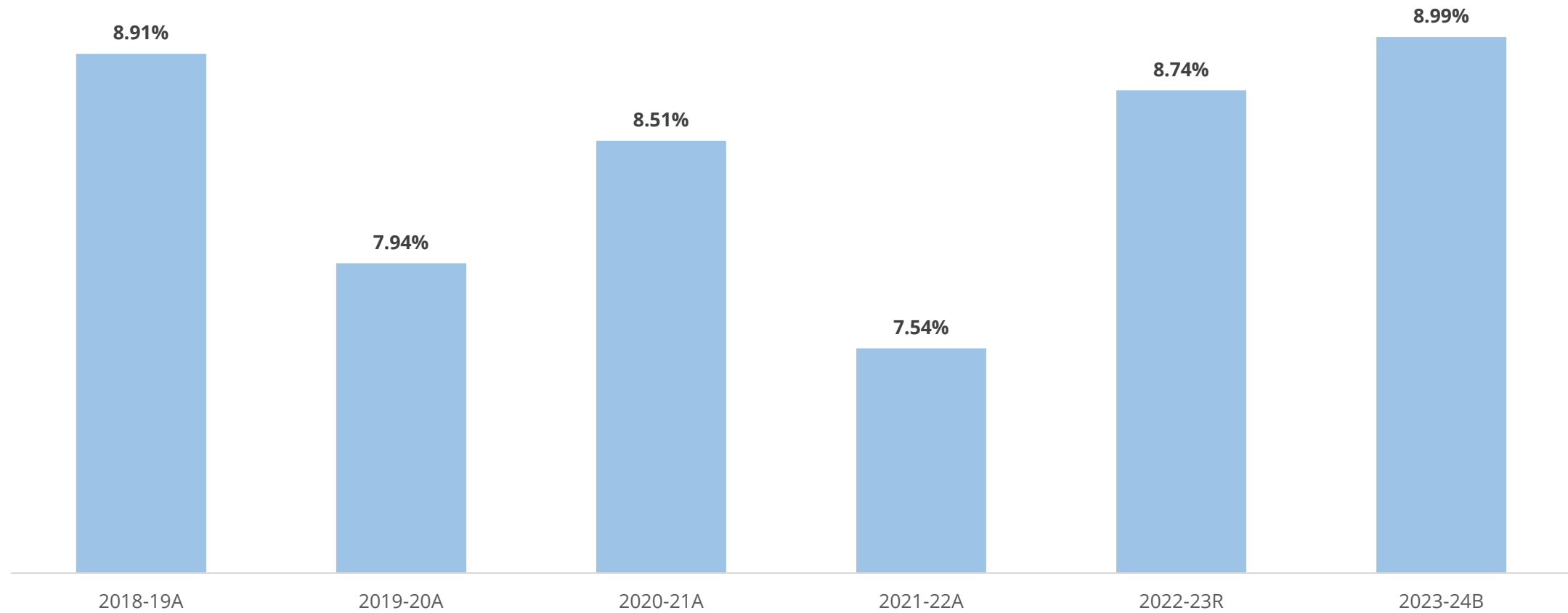


Primary Balance _ including grants (BDT Bn)

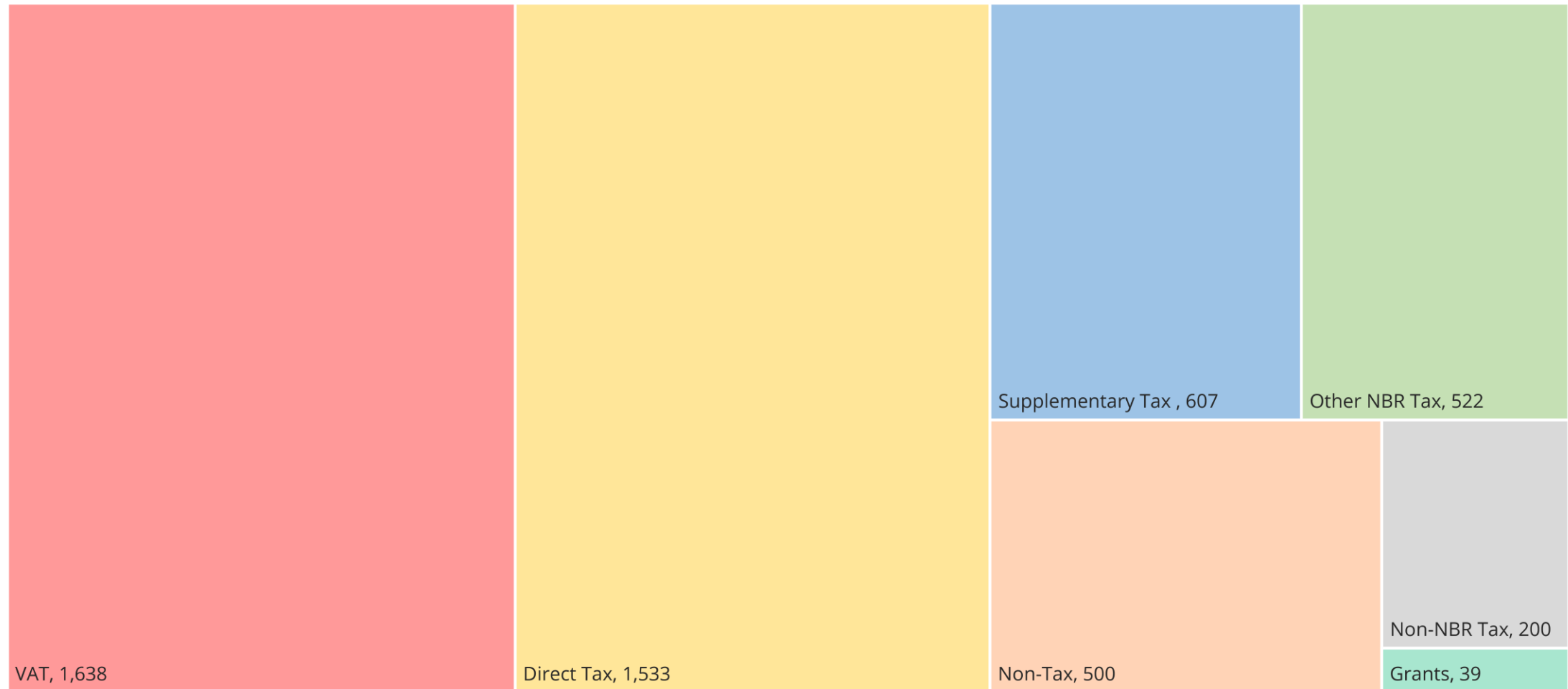


* The calculation is as per IMF definition

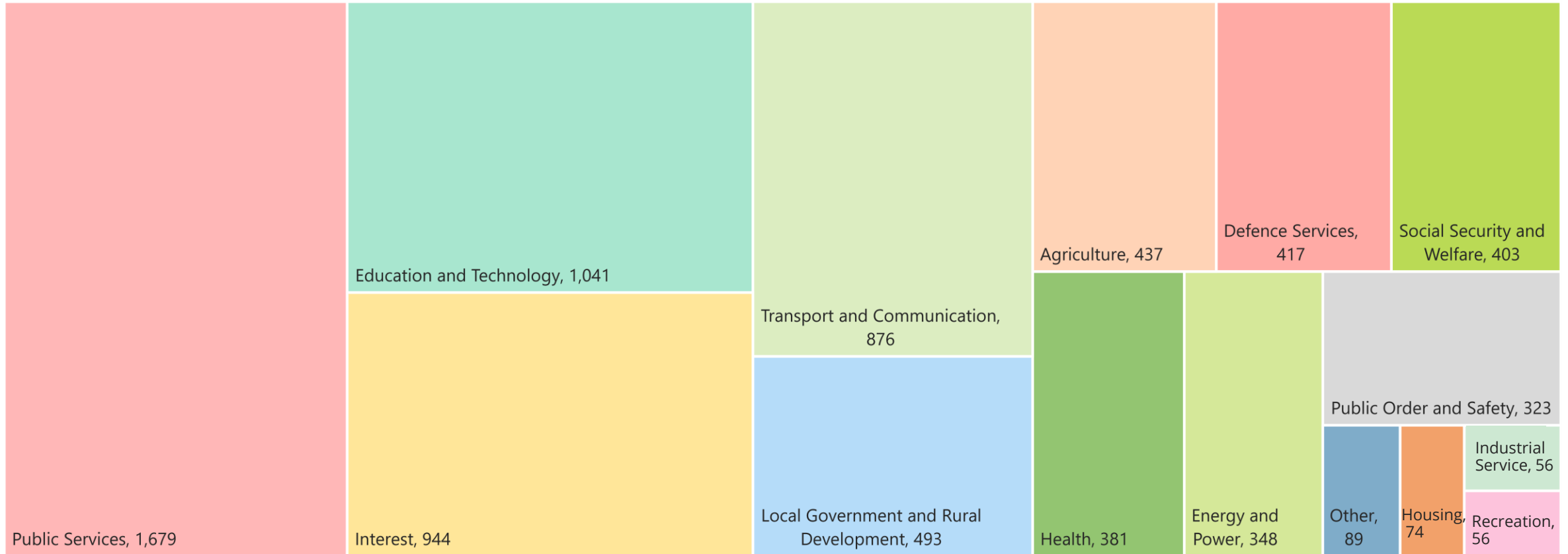
Tax Revenue to GDP (%)



Revenue and Grants (BDT Bn)



Operating and Development Expenditure (BDT Bn)



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Research

Ahmed Omar Siddique, CFA
Head of Investment Strategy
Tel: +8801709658760
Email: omars@calbd.com.bd

Nicholas Dipta Gomes
Senior Associate - Research
Email: nicholasg@calbd.com.bd

Ruhul Amin Raad
Associate - Research
Email: ruhula@calbd.com.bd

Stock Brokerage & Investment Banking

Rajesh Saha
Chief Executive Officer
CAL Securities Limited
Tel: +880-1994000999
Email: rajeshs@calbd.com.bd

Zobayer Mohsin Kabir
Chief Operating Officer
CAL Securities Limited
Tel: +8801715818608
Email: zobayerm@calbd.com.bd

S.M. Arafat Hossain
Head of Investment Banking
CAL Investments Ltd.
Tel: +8801730714171
Email: arafath@calbd.com.bd