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## Dejected textile sector needs cheering up

Investments in the industry to grow exports and substitute imports are a precondition for sustainable future economic growth. The economic stability the government expects to achieve on the back of fiscal, monetary and structural reforms it is executing under the 39-month, $6 billion bailout package from the International Monetary Fund is unlikely to last long unless it puts in place policies conducive for improving the business climate to attract new investments.

“Unfortunately the business and investment sentiments are at their lowest at present. The situation will worsen going forward if measures are not taken to correct the policies that have led us to this point where businessmen are forced to drop their investment plans,” asserts Khurram Mukhtar, a major exporter of home textiles and garments from Faisalabad, during an interview with this writer.

The chief executive of Sadaqat Limited, who also owns a large retail home textiles and clothing business in Pakistan and England, cites several factors that have depressed business and investment sentiments: massive exchange rate adjustments over the last one year, increased cost of credit, severe cash flow crunch facing most manufacturers owing to withdrawal of zero-rated regime for exporters, gas price subsidy issues and so on.

‘The withdrawal of zero-rating will tie up Rs424bn of working capital in the refund regime for a six-month cycle’

“The monetary policy adjustments, new tax measures announced in the budget and certain other policy changes have steeply raised the cost of investments in the industry and affected export competitiveness. The income tax credit of 10 per cent on new investments has been halved for the present fiscal year and the concession will be completely withdrawn from the next financial year.

“Many textile exporters, who planned to increase their production capacities to take advantage of foreign buyers’ renewed interest in Pakistan in the last one and a half years, have been forced to either put their plans on hold or scale down the size of their investments amid the new business environment prevailing in the country. The new business environment will work against the government’s two top economic policy objectives of creating jobs and increasing exports (to close the current account gap),” he argues.

Khurram, who himself had planned to substantially increase his denim and knitted garments production capacity to increase his company’s exports has significantly scaled down his planned investments from Rs3.5bn to Rs1.5bn. “We had worked out our investment feasibility in 2018 at an exchange rate of Rs124 a dollar to create 10,000 new jobs and raised our exports by $150 million a year. The 29pc depreciation in the value of the rupee since has hiked our capital expenditure to Rs4.5bn. Similarly, the spike of 750bps in the central bank’s policy rate to 13.25pc since early 2018 has made bank loans too expensive for us. The reduced size of investment will mean we will create only 4,000 new jobs with a potential of additional export revenues of just $50m”.

According to him, the share of subsidised loan under the EFS (export finance scheme to cover exporters’ needs for working capital) and LTF (long-term financing facility for purchase of machinery and equipment) as a ratio of the textile industry’s total exposure (to bank credit) has decreased from 41pc in 2017 to 27pc in 2018, which means the industry was compelled to borrow commercial loans at a very heavy price to meet their financing needs for working capital (for purchase of inputs, etc) that have increased by a fifth because of the massive exchange rate depreciation. "The cost of capital is much more than the profitability of the textile industry, which is a high volume and low margin sector. Majority of the textile and clothing exporters operate at a very thin margin of 3-5pc."

Khurram, who is also chairman of the Faisalabad-based Pakistan Textile Exporters Association (PTEA), points out that the cash flow crunch is squeezing the exporters' financial streams as a major part of their working capital is stuck in the refund regime and creating extreme financial stress for them.

"Before the withdrawal of the zero-rated regime, the average input sales tax paid (on packing/stitching material/certain chemicals and store items) was 1.75pc of the industry's foreign sales. After the withdrawal of zero-rating, it is feared to rise to 12.8pc of our total exports.

"If we add other refundable taxes to it, we will have 18-20pc of our total overseas shipments stuck in the refund regime for a minimum of 175 days (provided the government delivers on its promise of releasing the refund claims within the stipulated time framework). We estimate that the withdrawal of zero-rating of exporters will result in Rs424bn of their working capital stuck in the refund regime for a six-month cycle.

"I do not ask for a return to the zero-rated regime, but I want the government to release the sales tax and other refunds based on the consumption of inputs to exporters immediately after the monthly filing of their returns as is the practice in the rest of the world."

Moreover, the PTEA chairman said the government has not provided price subsidy on gas supply to the exporters (from Punjab) since March and the funds of Rs4.5bn allocated for this lapsed due to the end of the last financial year. The government had in October last year announced to provide LNG to Punjab's exporters at a subsidised rate of $6.5 per million British thermal units, and electricity at $0.75 a unit to bring the energy prices in the province at par with those in Sindh and improve the industry's international competitiveness.

"New notification has not been issued and exporters are being charged normal tariffs, forcing them to get legal remedy from the courts in this respect. That is not all. The facility of purchasing raw materials from the domestic market for exports under the bond schemes has also been withdrawn. Furthermore, anti-dumping duties have been implemented on inputs like 51-count yarn and above and hydrogen peroxide imported under the duty and tax remission for the export scheme for re-export. These kinds of policies are unnecessarily increasing cost of exporters, affecting our international competitiveness and stalling export growth."

His message to the government: "facilitate exporters by removing the obstacles slowing down their business; stop punishing them for the Federal Board of Revenue's inability to enforce the laws and recover taxes from those who aren't paying their share. If immediate corrective actions aren't taken to remove obstacles to growth and investments, exports will go down and jobs will be lost."

Nasir Jamal