



# PIDE Business Barometer

Based on a sample of industries listed in the Karachi Stock Exchange, this barometer provides an overall picture of business activity during January-June 2012 and expectations for July-December 2012.

No. 10

August 2012

## Overview

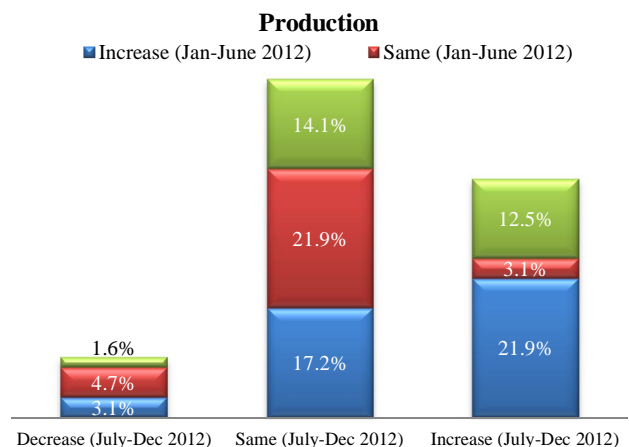
Though businesses continue to operate in a challenging environment with sluggish production and sales volumes they remain somewhat optimistic about their future prospects. Firms that have performed well in terms of production, sales and exports attribute their success to strong demand for their products while firms experiencing stagnant business activity have blamed shortage of utility supplies as a major bottleneck hindering their performance. Surprisingly, however, energy shortage is not the top most constraint faced by the firms which may be due to alternative arrangements made by the firms to cope with the energy crisis. A majority of firms have no plans to enhance their productive capacity. Most of the businesses have reported increase in the prices during the first half of the year 2012 and expect them to increase in the second half of the year as well. However, they expect the inflation to remain in single digits. Even though almost all the firms have reported to have a policy to increase wages once a year but not every industry is planning to increase wages. The recorded responses of the firms on input prices indicate that they deem the input prices to be too high and expect them to increase further due to irregular availability in the local market and taxes imposed on them. Firms do not perceive the 2012-13 budget to be investment friendly because, according to them, no specific policy is announced to promote investment while taxes on raw materials remain very high. Firms' overall ranking of the business environment remains very low highlighting the need for adopting policies to improve business climate in Pakistan.

## Production Remained Higher Despite Energy Problems

A significant number of firms (42 percent) experienced increase in production during January-June 2012 period whereas only 28 percent of the firms reported decline in production. Thirty percent of the firms surveyed reported no change in production. The analysis of the industry-wise break down of production reveals that cement and sugar industries saw major increase in their production while textile and fertilizer were the sectors that experienced major decline in production. Interestingly though, the extent of increase in production, in percentage

terms, was greater than the extent of decrease in production. Among different factors which affect increase/decrease in production, increase in demand is the major factor leading to increase in production, whereas non-availability of utility supplies is the major factor responsible for decline in production.

As far as expectations for the second half of the year 2012 are concerned, more than half of the firms expect their production levels to remain the same. However, a higher number of firms (38 percent) expect increase in production as compared with the firms which expect decrease in their production (9 percent) in the second half of the year 2012. Interestingly, 12.5 percent of the firms, mostly in textile and cement sectors, which expect increase in production saw their production level decrease in the first half of the year 2012. An important point to note, nevertheless, is that these firms are banking on better supply of energy and increase in the demand for their production to pick up and if this does not happen their production will remain stagnant.



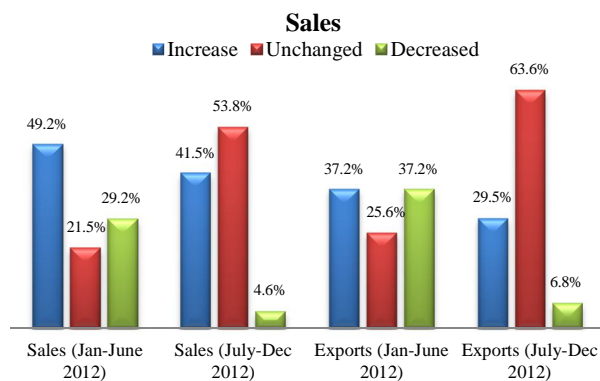
## Expectation of Improvement in Domestic Sales and Exports

Reported trends in sales during the January-June 2012 period are very similar to trends in production. About half of the firms reported increase in their sales, while 29 percent reported decline in sales, which is consistent with the production patterns. As was the case with production, the textiles and fertilizer sectors experienced major decline

in sales due to slack demand and shortage of energy supply, while the cement industry posted significant increase in sales due to strong demand. Most of the firms reported increase or decrease in sales in the range of 0-10 percent. However, some firms also reported change in sales between 11-20 percent, 21-30 percent, and more than 40 percent. Since majority of the firms reported increase in sales the overall sales increased in the first half of the 2012. One cause for worry, however, is the decline in sales by more than 40 percent of the 25 percent of the surveyed firms in the textile sector.

As with production volumes, more than fifty percent of the firms expect unchanged sales during July-December 2012. However, more firms have expectations of higher sales than the firms that expect decrease in their sales. This hints towards the possibility that upward trend in sales, witnessed in January-June 2012 period, is likely to persist in the second half of the ongoing year. Indeed, the major factor contributing to the bullish expectations is the expectation of increase in the demand for their products.

Export performance of the firms in the first half of the 2012 was not very encouraging. Even though 37 percent of the firms reported increase in exports and the same number of firms reported decrease in exports but the extent of decline in exports is more than the extent of increase in exports, which explicitly implies decline in overall exports. Decline in exports is mostly observed in the textile sector. Slight improvement in net exports, based on the responses of the firms, is expected in the second half of the year 2012.

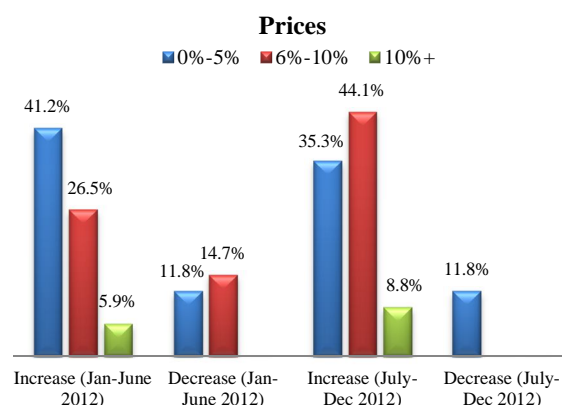


### Inflationary Expectations

Inflation is among those indicators which are likely to be overstated by firms and common people. Our survey results show that more than twice the firms reported increase in prices than the firms which reported decrease in prices during January-June 2012 whereas 43 percent of the firms reported no change in prices during the same period. Most of the firms reported their increase in prices between 0-5 percent, followed by 6-10 percent but very few firms reported increase in prices by 10 percent or more. Interestingly, 50 percent of the firms associate

increase in the prices of their products with general inflation followed by a very few firms which cited increase in the cost of production and increase in demand for their products as a source of increase in prices. On the other hand, decrease in the demand for the products is reported as the major factor contributing to decline in prices.

Firms set prices of their products keeping inflation expectations into consideration and inflation expectations tend to be higher than announced by the Central Bank. In line with this trend, one half of the firms expect prices to increase in the second half of the year 2012 and about the same number of firms expect their prices to remain unchanged. Only a few firms expect the prices of their products to go down. An interesting thing to note is that firms in the cement industry expect the prices to increase probably due to increase in the demand for their product. The firms in the textile sector also expect output prices to go up despite the decrease in demand. However, they do not expect increase in their sales or exports. More alarmingly, firms associated with sugar industry also expect the price of sugar to go up. Since sugar industry is cartelized, it is feared that sugar price will surge in the second half of the 2012 as well. In order to check the upward trend in the sugar prices, strict policy measures are needed. In terms of numbers, one-third of the firms expect their prices to increase by 0-5 percent and 44 percent expect their prices to go up by 6-10 percent. Since half of the firms are expecting prices to remain unchanged or decline we can expect single digit inflation during the second half of the year 2012.

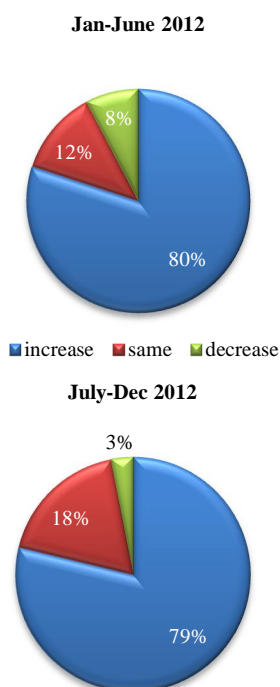


### Irregular Availability of Inputs and Taxes are Raising Input Prices

Input prices are one of the main components of cost of production and if these increase then prices of the products are most likely to increase as well. Our survey results show that 80 percent of the firms show increase in input prices during January-June 2012, however, not every firm/industry has increased their prices. The extent of increase in wages remained less than 10 percent for 88

percent of the firms and 12 percent reported increase in wages by more than 10 percent. Irregular availability of inputs in local market is the major factor affecting prices of inputs followed by increase in taxes, and inflation. It is, however, interesting to see that irregular availability of inputs raise input prices less than taxes/tariffs on inputs.

The expectations of the firms for increase in input prices are not different from that of first half of the year 2012. Firms expect tariffs on inputs to increase, thus inputs prices will also increase. As far as the extent of increase in input prices is concerned, 45 percent of the firms expect them to increase between 0-5 percent, 41 percent expect them to increase between 6-10 percent, while the remaining 14 percent expect them to increase by more than 10 percent.

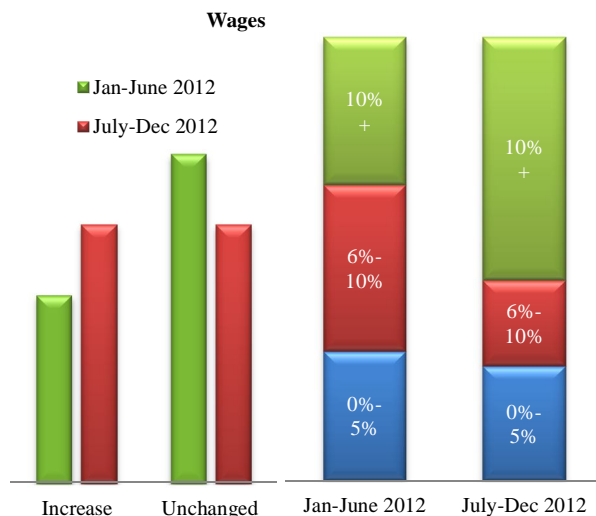


### Wages are Not Increasing in Every Industry

For real wages to remain constant, increase in nominal wages should keep up with increase in inflation. However, the survey results show that only 36 percent of the firms increased the nominal wages, whereas wages remained unchanged in 64 percent of the firms. For the firms which increased the wages, the main reason reported was the annual increment which they grant to their employees. However, one-third of the firms did not report any increase in wages in the first half of the year and neither do they plan to increase wages in the next half of the year, even though 90 percent of the firms have the policy of increasing wages once a year. Given the level of inflation, it is not an ideal situation for the workers of the industries which are not raising their wages, which mainly

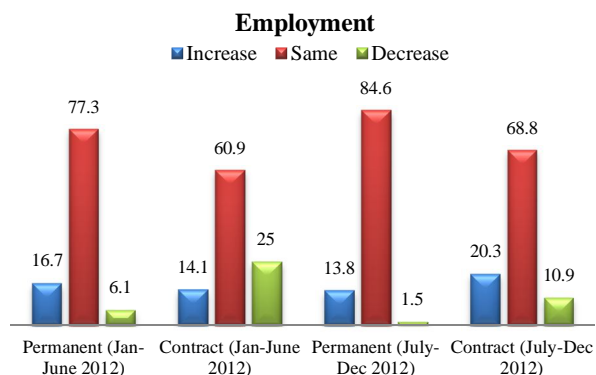
include cement, textile, oil and gas, and petroleum industries.

The extent of increase in wages is the same for all the three categories (i.e., 0-5 percent, 6-10 percent and more than 10 percent) during January-June 2012. Nonetheless, among the firms planning to increase wages in the second half of the year 2012, a majority expect to increase wages by more than 10 percent.



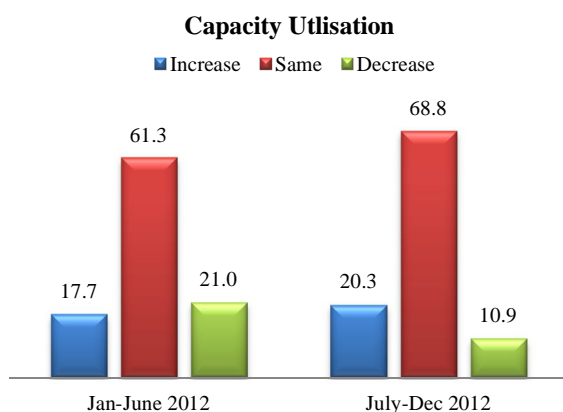
### Employment Opportunities Remain the Same

A slight increase in permanent as well as contractual employees shows a little improvement in the labour market. On the other hand, a small percentage of firms reported decline in permanent employees and 25 percent of the firms reported decline in contractual employees. The only significant change is observed in the textile sector where some firms laid off contractual employees but the extent of firing contractual employees is not more than 10 percent. The laying off of contractual employees is consistent with the decline in the production and sales. Although most of the firms expect no change in employment status, however slight improvement is expected in both the contractual and permanent employment statuses, especially in the sugar industry.



### Capacity Utilisation Remains the Same

Looking at the numbers and extent of change in capacity utilisation of the firms, it can be unambiguously said that capacity utilisation of the firms during the first half of the year 2012 declined and not surprisingly, textile firms are producing lower than their capacity, which is consistent with the declines in production and employment levels. The firms do not expect much improvement in the capacity utilisation apart from the fact that a higher number of firms have expectations that their capacity utilisation will improve.



### Insufficient Energy Supply is Not the Biggest Constraint

Surprisingly, one-third of the firms do not report any constraints in conducting business. However, the rest of the firms reported several constraints among which insufficient skilled labour force emerged as the number one constraint. Interestingly, energy availability is not ranked among the top constraints by the firms, which implies that they might have adjusted to the problem by either changing the working hours or installing power generators which is highly likely as all the firms in the sample are large-scale firms, employing 100 or more employees. Insufficient demand for their products is ranked among the top most constraint to business investment along with cost of capital.

Small number of firms has enhanced their production capacity and very few are expecting to enhance their production capacity. Most of the firms who are expecting to increase production are those who reported no constraints to investment. Thus constraints are negatively associated with the production capacity enhancement.

### Budget 2012-13 is not Pro-Growth

Since the survey was carried out soon after the budget was announced, firms were asked to give their opinion on the 2012-13 budget whether it was beneficial or detrimental to their businesses. Not surprisingly, almost half of the responses were in the negative, while 35

percent said that it did not impact their business in any way. Only 16 percent of the firms perceived the 2012-13 budget to impact their businesses positively. Most of the firms which think that budget would have a detrimental effect on their business blame taxes on raw materials, inflation, and energy crisis.

### Business Perception Index (BPI)

In the end, the survey also asks firms to rank the state of the economy to get an idea about the overall business environment. The index ranges from zero to ten, where zero implies the worst and 10 the best. Most of the firms ranked either 3 or 4 or 5 and on average BPI for the second half of the year 2012 is 3.77, which is below average. This implies that the economy is not in good shape and that the government needs to provide better incentives (e.g., by reducing taxes on raw materials etc) and infrastructure to attract more investment and enhance business activity.

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