



**Lahore Chamber of
Commerce & Industry**



**Lahore School of
Economics**

Business Confidence Survey 2015



**Lahore Chamber of Commerce & Industry and Lahore School of Economics
Business Confidence Survey 2015**

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Executive Summary

In March 2015, Lahore Chamber of Commerce & Industry (LCCI) and the Lahore School of Economics signed a Memorandum of Understanding which established a link between academia and the business community. As part of this collaboration, the Lahore School and the LCCI conducted its first annual business confidence survey to understand the perceptions of the business community regarding the prevailing economic conditions.

Almost 200 firms completed the survey and results from these responses shed light on the prevalent economic conditions facing firms in Pakistan as well as the sector specific issues facing the business community. Firms that responded were put into different sectors (manufacturing, services and retail sectors) in order to see the differences in the economic performance across various sectors.

Some of the key results from the survey were:

- A majority of the survey firms said that their sales were higher over the past year and they also expected sales to be higher in 2015.
- A significant number of firms in the manufacturing sector said that their export sales increases over the last year and they expected it to increase again in 2015.
- A majority of firms said that investment increased over the last year and the largest increase in investment in 2014 came in the manufacturing sector where around 70% of firms were able to increase their investment.
- Across all firms, the increase in investment in 2014 was not financed by bank borrowing but by the enhanced sales revenues.
- More than 60% firms in the manufacturing and services sectors plan to increase their investment in 2015.

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- A significant majority of firms do not plan to utilize bank borrowing for financing their higher levels of investment in 2015.
- A significant proportion of manufacturing and service sector firms managed to increase their number of employees in 2014 and both these sectors seem optimistic about further increases in their employment levels in 2015.
- There was significant optimism when firms were asked about their expectations about Pakistan's Economy, with approximately 50% of the firms expecting the economy to do better in 2015.
- Access to finance was considered a critical element for conducting business since 58% of the firms (in the sample) found "access to finance" to have a major impact on their business.
- 52% of the firms considered shortage of skilled labour to have a major impact on business and this proved to be a key issue for the manufacturing and services sectors.
- Slow or ineffective mechanisms to enforce contracts were significantly more important for firms in the services sector as compared to the firms in the retail and manufacturing sector.
- As expected, energy shortages have had the most significant impact on firm level growth with about 8 out of 10 firms surveyed in the manufacturing and retail sector finding this to be their greatest constraint.
- The survey found that problems of law and order are almost as important to firms as energy shortages with almost 7 out of 10 of the firms considering law and order to have a major impact on business.
- 75% of the firms considered provincial taxes to have a major impact on business.
- 69% of the firms considered federal corporate tax policies to have a major impact on business and 76% of firms considered import or custom duty policies to have a major impact on business.

1. Introduction

In May 2015, the Lahore Chamber of Commerce & Industry (LCCI) and the Lahore School of Economics conducted its first annual business confidence survey as part of its recently signed MOU on collaborative activities. The reason behind this survey was the understanding that economic-growth is driven by private-sector economic activity. This in turn is critically dependent upon the perceptions of the business community regarding the prevailing economic conditions. In an attempt to measure these perceptions over the past years, this survey questioned the business community about the impact of economic conditions on their businesses over the past year, as well as their expectations for the future.

This survey was administered electronically by members of the LCCI. Realizing that firms are heterogeneous in terms of size and sector, firms were divided into three sectors for the sake of analysis: (1) the manufacturing sector (2) the services sector and (3) the retail sector.

The major themes of the questions asked in the survey were:

- a. Comparison of revenue from total sales in 2013 with 2014
- b. Comparison of revenue from domestic sales in 2013 with 2014
- c. Comparison of revenue from export sales in 2013 with 2014

- d. Expectations of export sales in 2015
- e. Expectations of domestic sales in 2015
- f. Expectations of total sales in 2015
- g. Comparison of bank borrowing in 2013 with 2014
- h. Expectations of bank borrowing in 2015
- i. Comparison of investment in 2013 with 2014
- j. Expectations of investment in 2015
- k. Comparison of number of employees in 2013 with 2014
- l. The Impact of factors such as access to finance, law and order, energy, recession in world markets such as EU and USA, foreign competition, shortage of skilled labour and slow mechanisms for dispute resolution. The Impact of provincial regulations such as taxes, law and regulations, industrial zoning policies and commercialization policies and costs.
- m. The Impact of federal regulations such as corporate tax policies, income tax policies and import and custom duty policies.

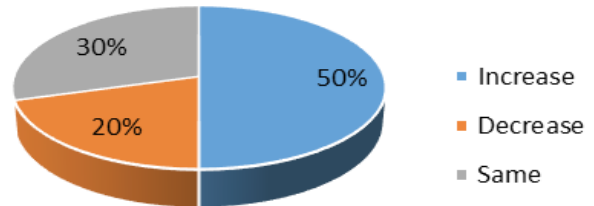
The results of the survey are discussed in sections appended below, and they highlight some of the key trends and lessons which can be used by not only the business community, but also policy makers and academics.

2. Analysis of Firm Level Sales

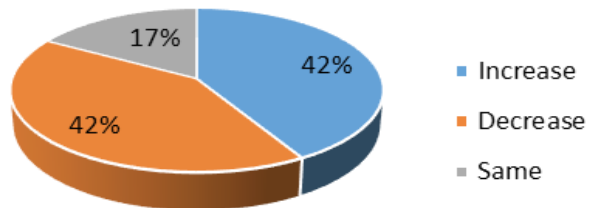
The first section of the survey focused on the sales of firms. This was done to see how both domestic and global factors impacted a firm's output. As discussed above, the firms were divided into manufacturing sector, services sector and the retail sector.

In response to the question asked regarding the comparison of revenue in 2013 and 2014, a greater percentage of manufacturing firms in 2014 (63%) showed revenue increase from total sales as compared to firms in services industry (50%). Retail firms lagged behind as only (42%) were able to increase their revenues from total sales in 2014 and the same percentage experienced a decrease in revenues. One of the reasons for this increase in domestic sales across sectors can be a better macroeconomic environment, especially a decrease in the inflation rate to around 6%, lower interest rates and a more stable supply of electricity.

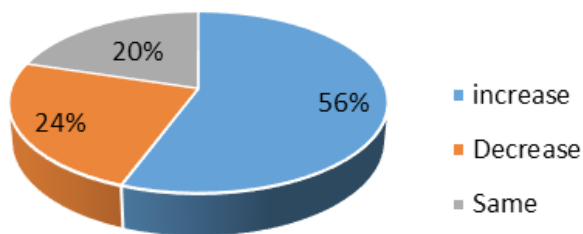
Comparison of Revenue from Total Sales in 2014 with 2013: Services



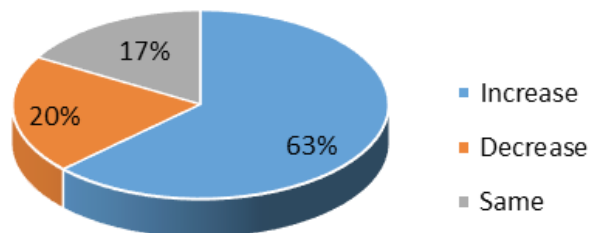
Comparison of Revenue from Total Sales in 2014 with 2013: Retail



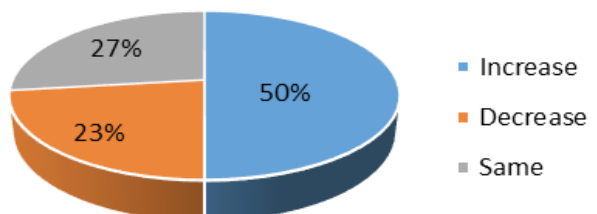
Comparison of Revenue from Total Sales in 2014 with 2013: All Firms



Comparison of Revenue from Total Sales in 2014 with 2013: Manufacturing

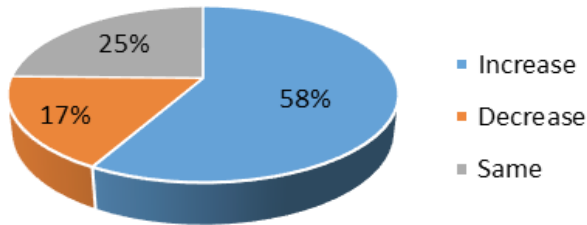


Comparison of Revenue from Domestic Sales in 2014 with 2013: All Firms

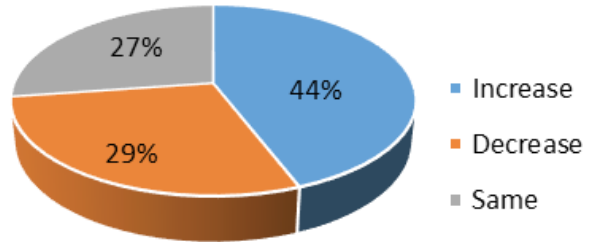


The survey also asked about sales in 2014, for both domestically targeted output and exports. Firms in the manufacturing sector stated that they experienced significant growth in both domestic and export sales in 2014 which is a positive economic indicator. Firms in the services sector said that they experienced significant growth in domestic sales but not in exports. This is important because it illustrates how Pakistan has yet to tap into the global market for service exports. The retail sector also experienced positive growth in domestic sales which indicates that the economy may slowly be gaining momentum after a few years of economic slow-down.

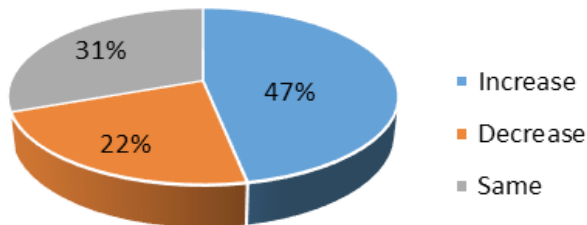
Comparison of Revenues from Domestic Sales in 2014 with 2013: Manufacturing



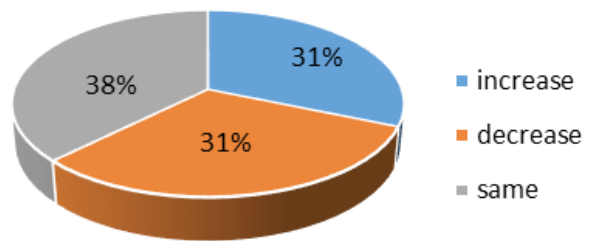
Comparison of Revenue from Export Sales in 2014 with 2013: Manufacturing



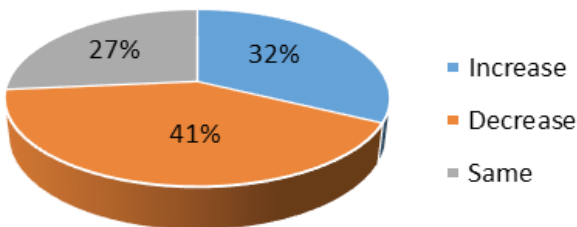
Comparison of Revenue from Domestic sales in 2014 with 2013: Services



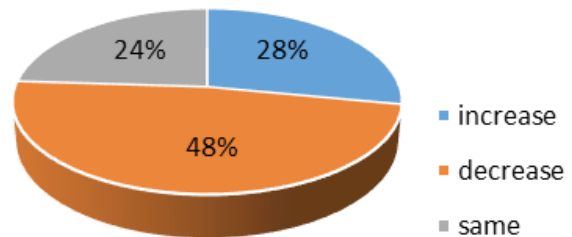
Comparison of Revenue from Export Sales in 2014: Services



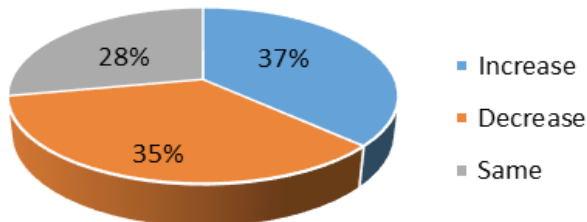
Comparison of Revenue from domestic sales in 2014 with 2013: Retail



Comparison of Revenue from Export Sales in 2014 with 2013: Retail

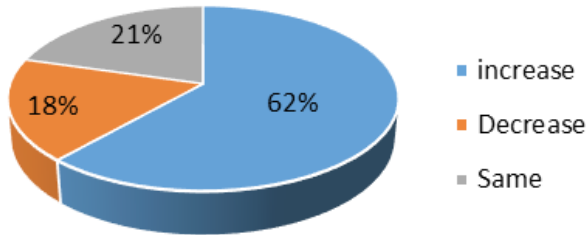


Comparison of Revenue from Export Sales in 2014 with 2013: All Firms

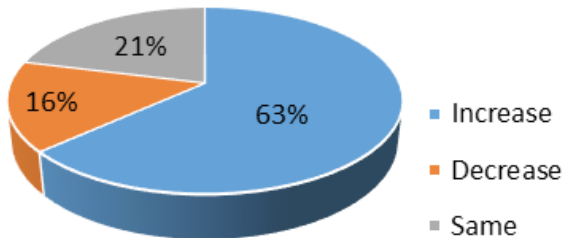


The second part of the sales analysis focused on expectations regarding the coming year. The results were interesting because across all three sectors, firms were exceedingly positive about having higher sales in the upcoming year.

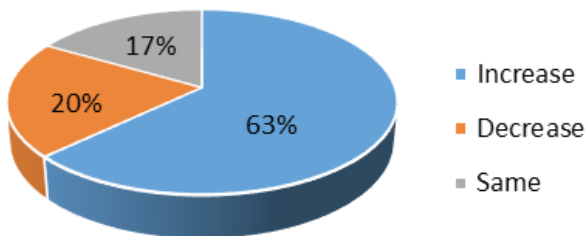
Expectations of Revenues from Total Sales in 2015: All Firms



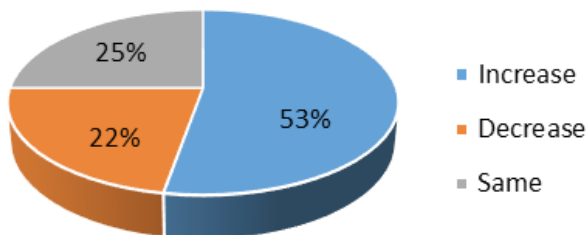
Expectations of Revenues from Total Sales in 2015: Manufacturing



Expectations of Revenue from Total Sales in 2015: Services

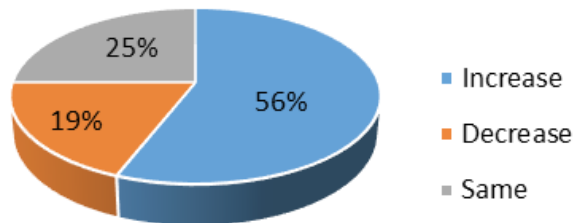


Expectations of Revenues from Total Sales in 2015: Retail

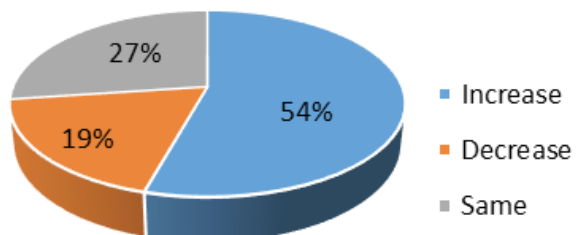


What is even more interesting is the break-down of this analysis between expectations of domestic and exports sales. The results show that firms are extremely optimistic about having higher domestic and export sales over the coming year. This is important in two ways: 1) expectations of higher sales both domestically and internationally shows that firms feel that the Pakistani economy as well as the international economy are pulling out of the economic slow-down experienced over the last few years 2) higher expected exports bode well for Pakistan's balance of payments which has been a source of weakness over the last decade. Expectations of higher exports may be driven by optimism in the textile sector which expects its exports to go up due to better energy supply, lower inflation, lower interest rates and GSP plus status.

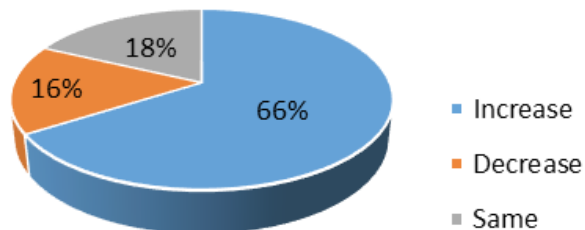
Expectations of Revenue from Domestic Sales in 2015: All Firms



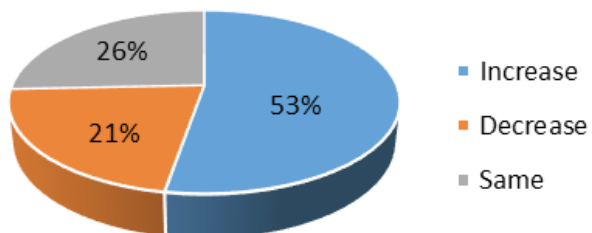
Expectations of Revenue from Domestic Sales in 2015: Manufacturing



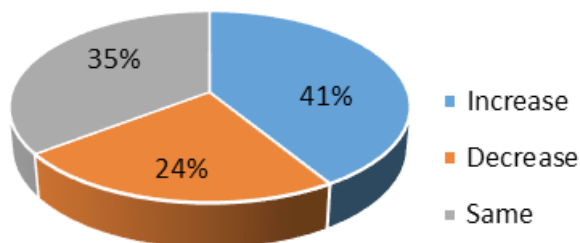
Expectations of Revenue from Domestic sales in 2015: Services



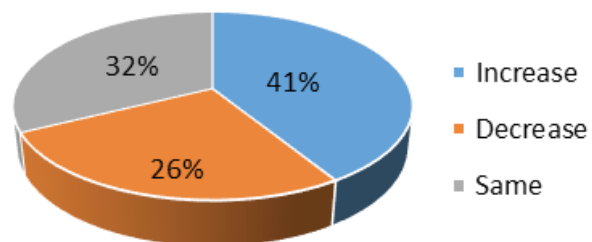
Expectations of Revenue from Export Sales in 2015: Manufacturing



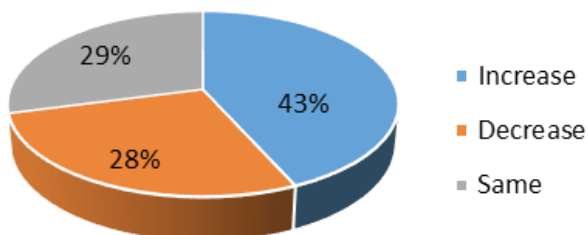
Expectations of Revenue from Domestic sales in 2015: Retail



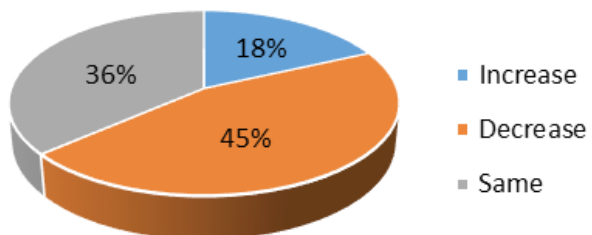
Expectations of Revenue from Export sales in 2015: Services



Expectations of Revenue from Export Sales in 2015: All Firms



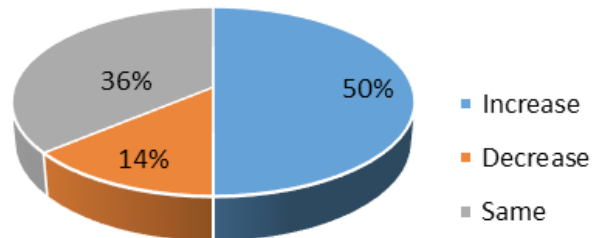
Expectations of Revenue from Export Sales in 2015: Retail



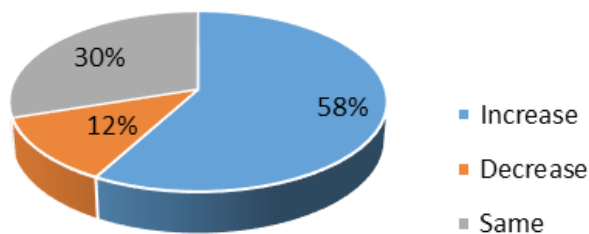
3. Analysis of Investment Levels and Bank Borrowing

In the second section of the survey, firms were asked to compare their level of investment in year 2013 with year 2014 alongside expectations about investment in 2015. The results of the survey show that the largest increase in investment in 2014 came in the manufacturing sector where around 70% of firms were able to increase their level of investment. Even in the services and retail sector, around 50% firms were able to enhance their investment in 2014.

Comparison of Level of Investment in 2014 with 2013: Retail

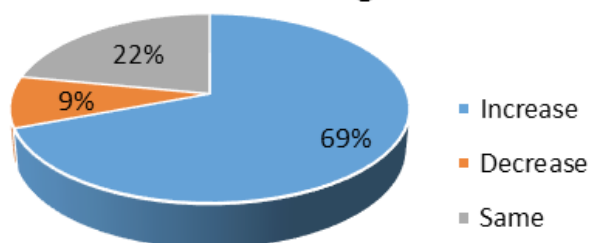


Comparison of Level of Investment in 2014 with 2013: All Firms

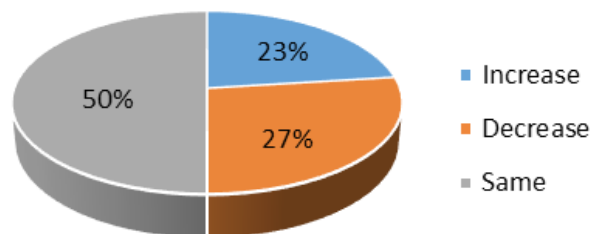


Interestingly, increase in investment in 2014 was not financed by bank borrowing but by the enhanced sales revenues. Only 30% of firms in the manufacturing sector increased their bank borrowing in 2014. This percentage gets lower in services and retail sectors where only 11% and 21% firms respectively increased their investment in 2014.

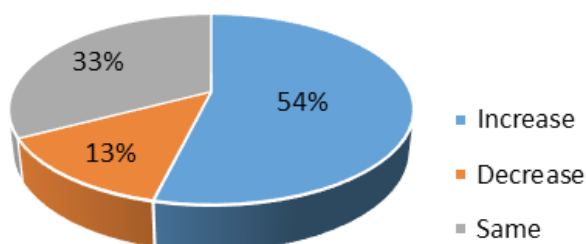
Comparison of Level of Investment in 2014 with 2013: Manufacturing



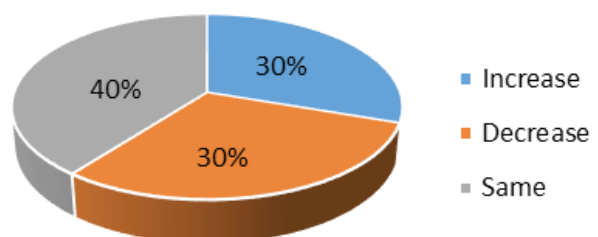
Comparison of Bank Borrowing in 2014 with 2013: All Firms



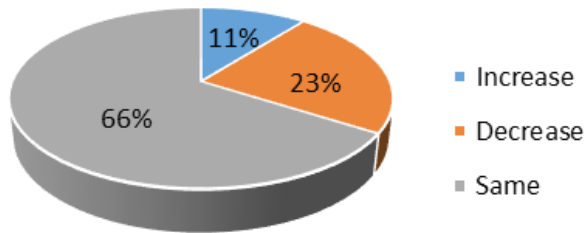
Comparison of Level of Investment in 2014 with 2013: Services



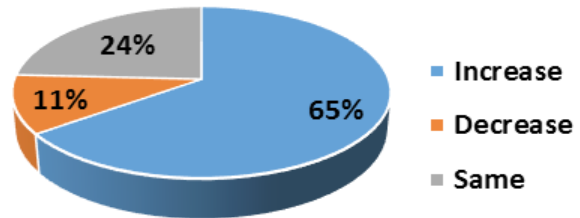
Comparison of Bank Borrowing in 2014 with 2013: Manufacturing



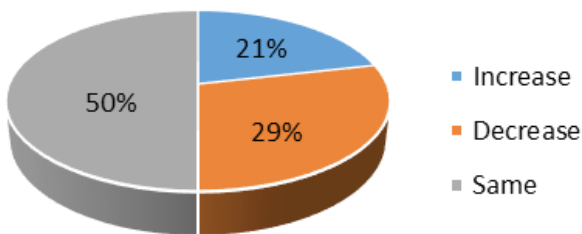
Comparison of Bank Borrowing in 2014 with 2013: Services



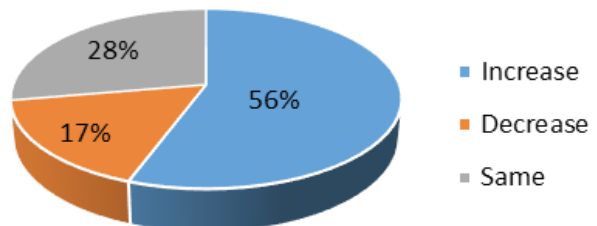
Expectation of Level of Investment in 2015: Manufacturing



Comparison of Bank Borrowing in 2014 with 2013: Retail

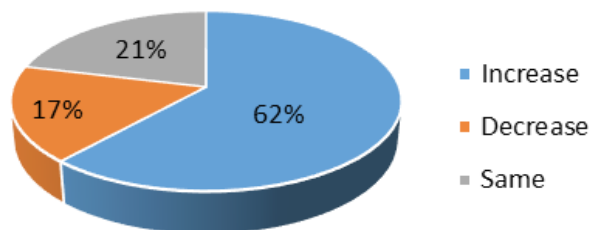


Expectation of Level of Investment in 2015: Retail

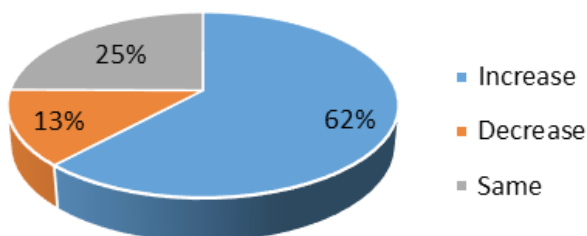


When the firms were asked about their expectations over the coming year, there was a high level of positivity regarding future investment. More than 60% firms in the manufacturing and services sectors plan to increase their investment in 2015, while the figure for retail sector is also more than 50%. This shows that firms are confident that Pakistan's economy will grow significantly over the coming year.

Expectation of Level of Investment in 2015: Services

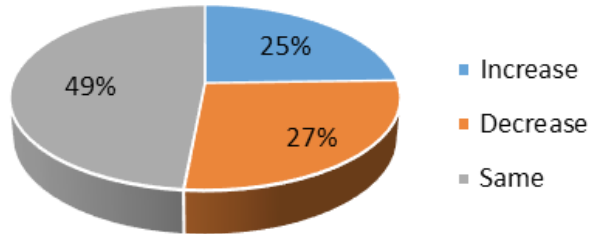


Expectation of Level of Investment in 2015: All Firms

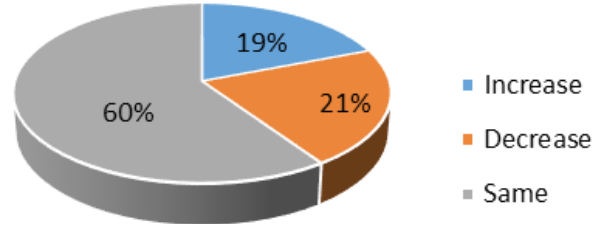


Finally, firms were asked whether they expect bank borrowing to increase, decrease or remain the same. Interestingly, firms in all the three sectors do not plan on utilizing bank borrowing facility to finance their investment. This may be indicative of both supply and demand side problems when it comes to bank lending, especially when one takes into account the fact that interest rates are falling in Pakistan. This also shows that the financial sector is failing to meet the needs of the business community.

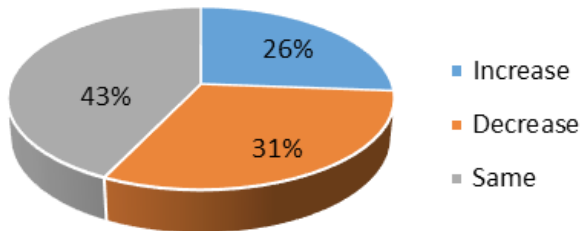
Expectation of Level of Bank Borrowing in 2015: All Firms



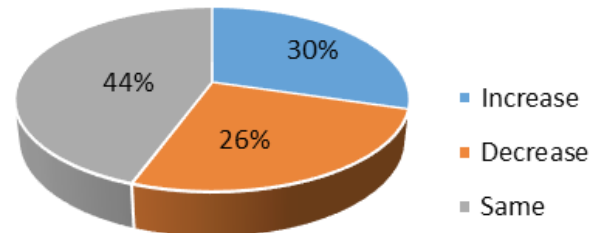
Expectation of Level of Bank Borrowing in 2015: Services



Expectation of Level of Bank Borrowing in 2015: Manufacturing



Expectation of Level of Bank Borrowing in 2015: Retail

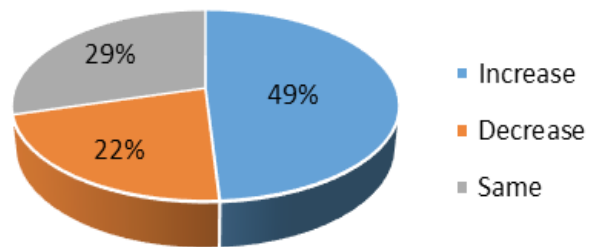


4. Analysis of the Number of Employees at the Firm Level

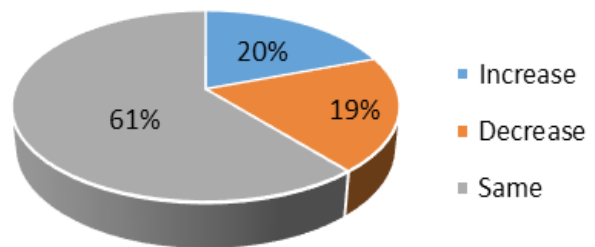
Since information on firms sales-levels are both notoriously unreliable and extremely difficult to maintain, this survey tried to determine firm size and whether firms were planning to expand by asking questions regarding the number of employees.

The survey results showed that a significant proportion of manufacturing and service sector firms managed to increase their number of employees in 2014. Also, both these sectors seem optimistic about further increase in their employment levels in 2015. However when we look closely at the retail sector, only 19% of the firms said that they increased their level of employment whereas a majority of firms in the retail sector expect their employment levels to remain the same in 2015.

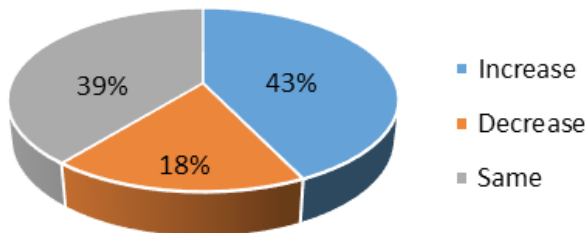
Comparison of Number of Employees in 2013 with 2014: Services



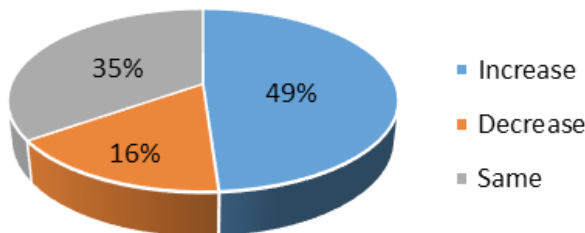
Comparison of Number of Employees in 2013 with 2014: Retail



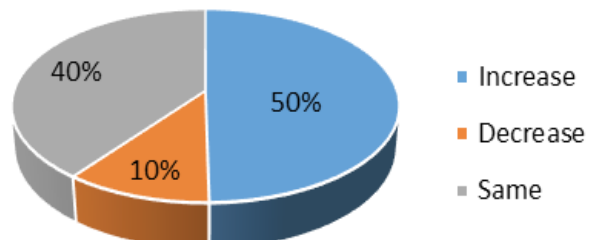
Comparison of Number of employees in 2013 with 2014: All Firms



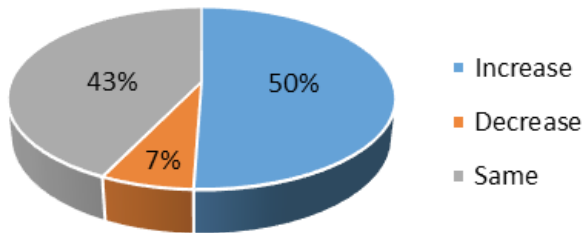
Comparison of Number of Employees in 2013 with 2014: Manufacturing



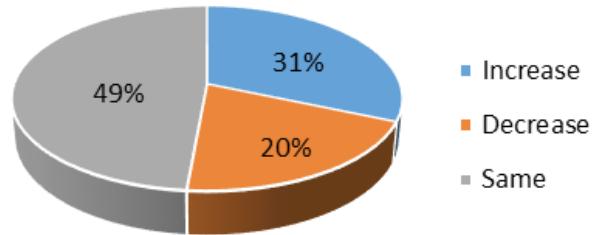
Expectation of Number of Employees in 2015: All Firms



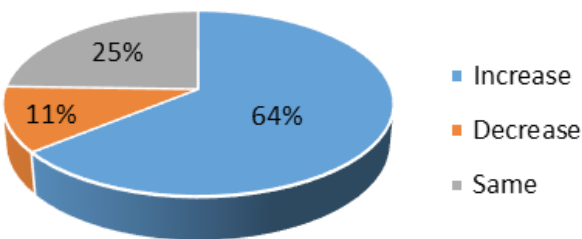
Expectations of Number of Employees in 2015: Manufacturing



Expectation of Number of Employees in 2015: Retail



Expectation of Number of Employees in 2015: Services



The overall increase in employment levels in the manufacturing and services sectors may be explained by the positive impact of higher sales in these sectors. Also, their planned expansions may be driven by higher anticipated domestic and export sales.

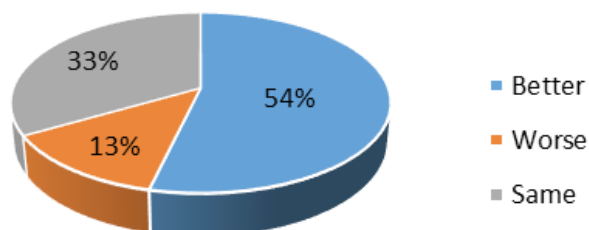
On the other hand, the more stagnant employment trend in the retail sector may be because of the different set of constraints faced, such as high commercialization costs and high rates of import / custom duties faced during purchase of goods. Lack of optimism regarding sales growth adds to retailers being skeptical about increasing employment in 2015.

5. Analysis of Firm Level Expectations about Pakistan's Economy

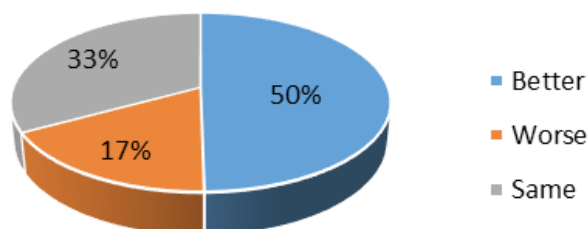
In order to get a general sense of feeling amongst the firms concerning the state of Pakistan's economy, firms were asked a general question about their expectations of the economy in 2015.

Overall, there is significant optimism when firms were asked about their expectations about Pakistan's economy, with approximately 50% of the firms expecting the economy to do better in 2015. Interestingly the level of optimism is almost uniform across firms in manufacturing, services and retail sectors.

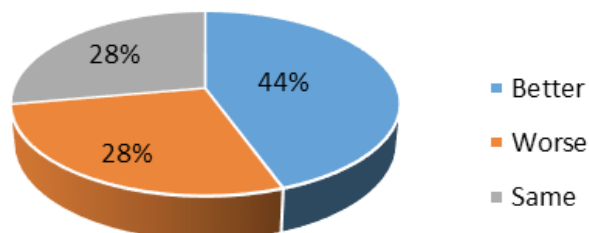
Expectations about the Performance of the Pakistan Economy in 2015: Services



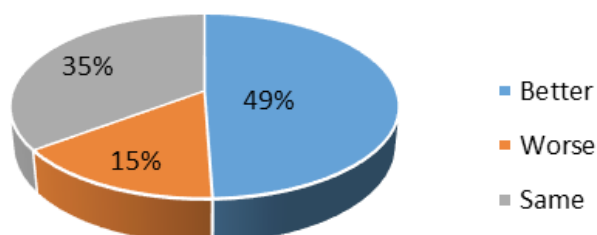
Expectations about the Performance of the Pakistan Economy in 2015: All Firms



Expectations about the Performance of the Pakistan Economy in 2015: Retail



Expectations about the Performance of the Pakistan Economy in 2015: Manufacturing



The recent trend in GDP growth, improvement in law and order conditions, Pakistan's new economic partnership with China, lower inflation, lower interest rates, decrease in the fiscal deficit and expected completion of various energy and infrastructure projects may be some of the factors driving this optimism.

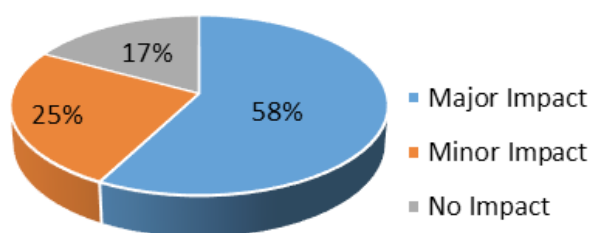
6. Analysis of Other Factors Affecting Firms

In the final section of the survey, firms were asked to give their opinions on a wide range of other factors that may have an impact on their business. These factors ranged in scope from domestic factors to foreign factors and the impact of each of these factors is discussed below:

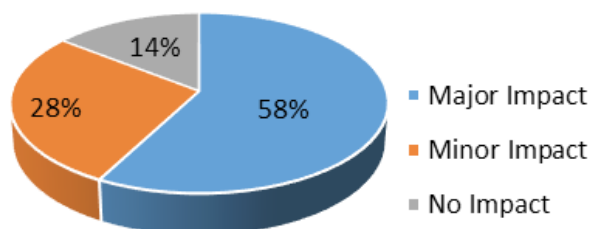
6.1 Access to Finance

Firms were asked how 'access to finance' impacts their business. This seems to be a key element for conducting business since 58% of the firms (in the sample) found 'access to finance' to have a major impact on their business. Access to finance seemed to hold a similar importance for all firms; 58% of the firms in the manufacturing sector consider access to finance to have a major impact on their business, 55% of the firms in the services sector consider access to finance to have a major impact on their business, and 60% of the firms in the retail sector consider access to finance to have a major impact on their business.

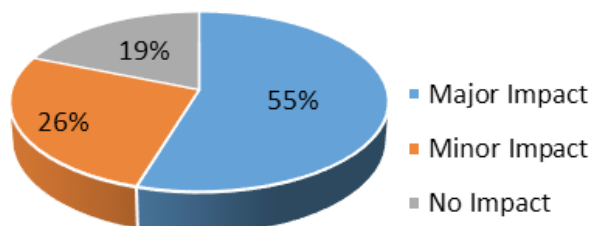
**How Access to Finance Impacts
Business: All Firms**



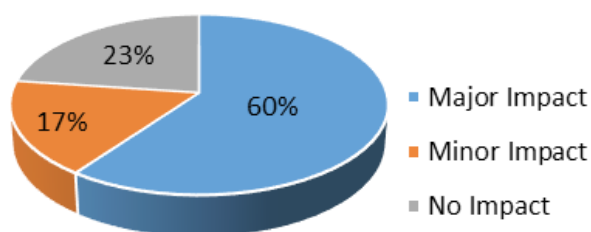
**How Access to Finance Impacts
Business: Manufacturing**



**How Access to Finance Impacts
Business: Services**



**How Access to Finance Impacts
Business: Retail**

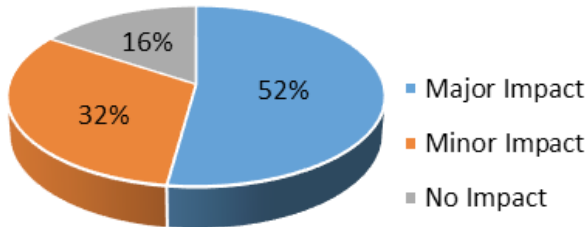


The results seem to imply that access to finance seems to be a major growth impediment for firms in the manufacturing, services and retail sector. The main reasons behind this result may be the irregular availability of financing facilities and lack of government initiatives in this area. Firm owners stated that banks offer high rates of interest and lengthy documentation procedures which ultimately act as a hindrance for sectors to avail such facilities.

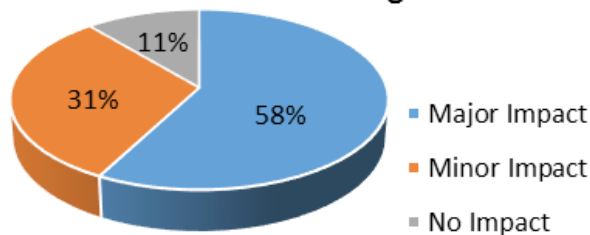
6.2 Shortage of Skilled Labour

Firms were also asked about how the shortage of skilled labour has impacted their business. 52% of the firms consider shortage of skilled labour to have a major impact on business. Shortage of skilled labour seems to be a more important variable for the manufacturing and services sectors as compared to the retail sector, since 58% of the firms in the manufacturing sector and 52% of the firms in the services sector found this shortage to have a major impact on their business.

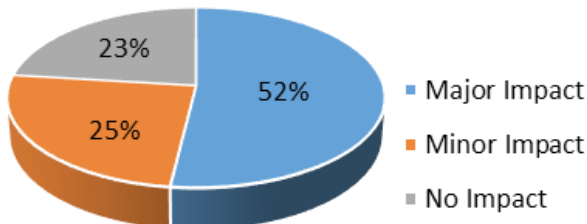
Impact of Shortage of Skilled Labour on Business: All firms



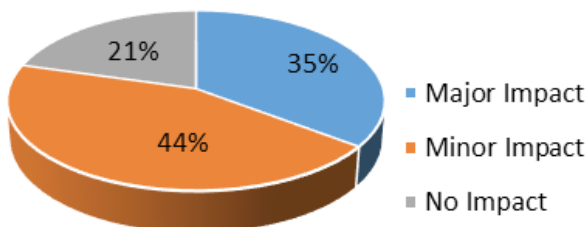
Impact of Shortage of Skilled Labour on Business: Manufacturing



Impact of Shortage of Skilled Labour on Business: Services



Impact of Shortage of Skilled Labour on Business: Retail



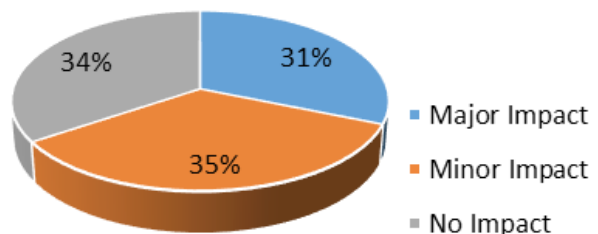
These results show that shortage of skilled labour is a greater impediment to growth in the manufacturing

and services sector as compared to the retail sector. Firm owners stated that the shortage of skilled labour stems from lack of vocational training institutes, in Pakistan. This shortage in turn results in firms relying on in-house training to impart skills to workers. For example, the textile and ready-made garments sector, has often complained that hiring trained stitching operators seems to be a challenge due to lack of training institutes.

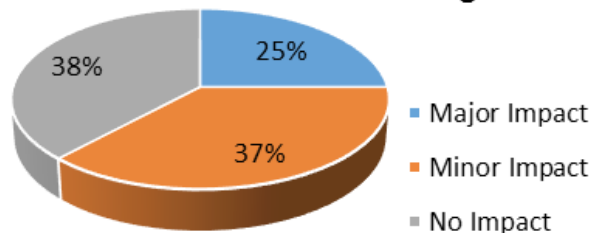
6.3 Economic Recession in the world markets

Firms were asked how the economic recession in the world markets impact their business. 31% of all firms consider economic recession to have a major impact on business, and the economic recession in world markets like EU and USA seemed to be relatively more important for firms in the services sector as compared to firms in the manufacturing and retail sectors.

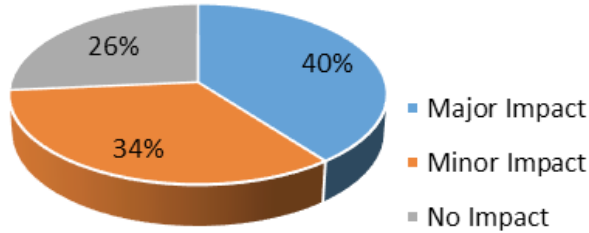
Impact of Economic Recession in world markets like EU and USA: All Firms



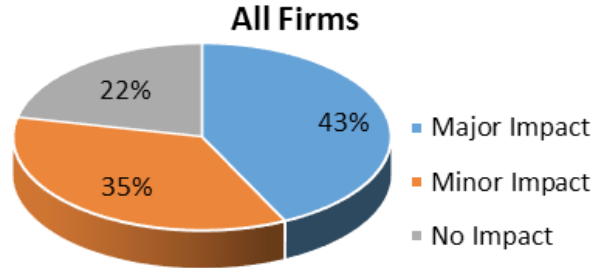
Impact of Economic Recession in world markets like EU and USA on Business: Manufacturing



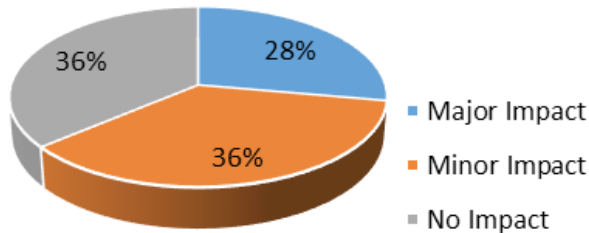
Impact of Economic Recession in world markets like EU and USA on Business: Services



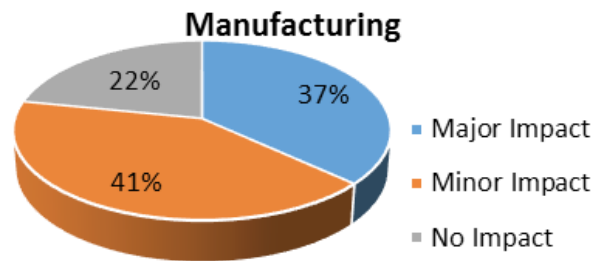
Impact of Slow or Ineffective Mechanism to Enforce Contracts or Resolve Disputes on Business: All Firms



Impact of Economic Recession in world markets like EU and USA on Business: Retail

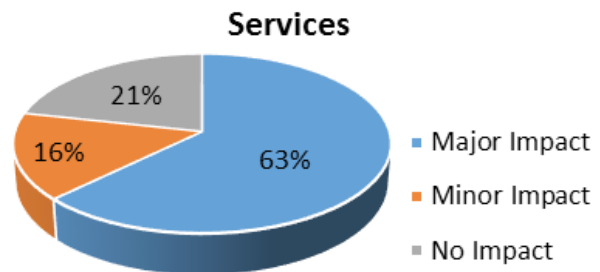


Impact of Slow or Ineffective Mechanism to Enforce Contracts or Resolve Disputes on Business: Manufacturing



Though the majority of exporting firms fall in the manufacturing sector, only 25% of the firms in this sector feel that the global economic slow-down is an impediment to growth. This is interesting, as it may show that the demand for Pakistani exports is relatively inelastic, or alternatively, Pakistani exporters have been able to diversify production into goods which protects them against fluctuating global demand.

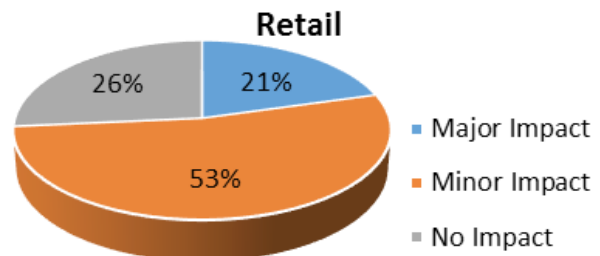
Impact of Slow or Ineffective Mechanism to Enforce Contracts or Resolve Disputes on Business: Services



6.4 Ineffective Mechanism to Enforce Contracts or Resolve Disputes

Firms were also asked about how slow or ineffective dispute resolutions impact their business. 43% of the firms consider slow or ineffective mechanism to enforce contracts as a major impact on business, and slow or ineffective mechanism to enforce contracts were significantly more important for firms in the services sector as compared to the firms in the retail and manufacturing sector.

Impact of Slow or Ineffective Mechanism to Enforce Contracts or Resolve Disputes on Business: Retail



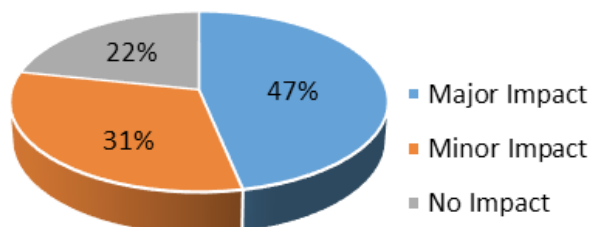
This result is important at multiple levels: Firstly, it seems to imply that firms in the Services Sector are the ones most exposed to problems in contract enforcement and dispute resolution. This could be because of the type and number of clients they deal with or the relative price and influence in having contracts enforced. Also, it may also show that the services sector may rely more heavily on less formal mechanisms of contract enforcement and dispute resolution which slows down the process.

6.5 Foreign Competition

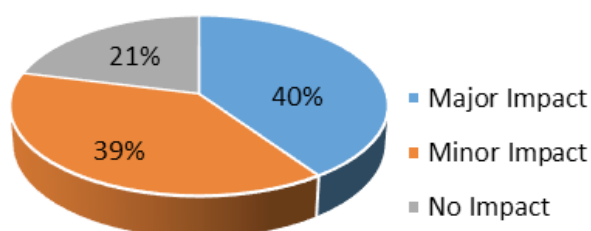
Firms were then asked how foreign competition impacted their business. 47% of the firms consider foreign competition to have a major impact on business, and foreign competition seems to hold similar importance for all three sectors as 40% of the firms in the services sector, 47% of the firms in the manufacturing sector and 43% of the firms in the retail sector consider foreign competition to have a major impact on business.

The result of the impact of foreign competition on firm growth shows that firms across all three sectors find it to be a significant but not a major obstacle. A point worth noting is that firms in the manufacturing sector, are more likely to be exporters and these are the ones who find foreign competition to be the greatest impediment to growth.

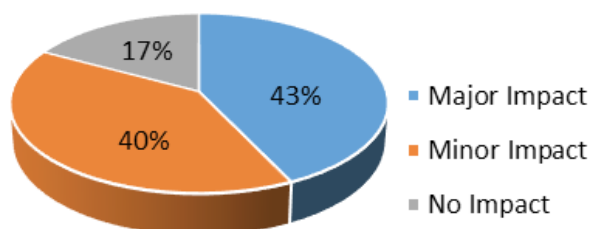
How Foreign Competition Impacts Business: Manufacturing



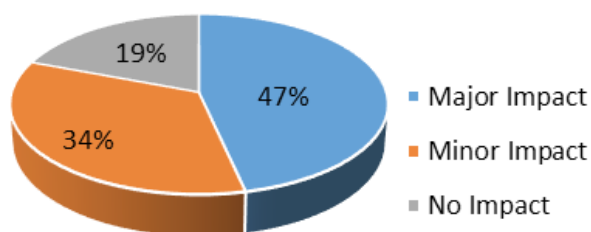
How Foreign Competition Impacts Business: Services



How Foreign Competition Impacts Business: Retail



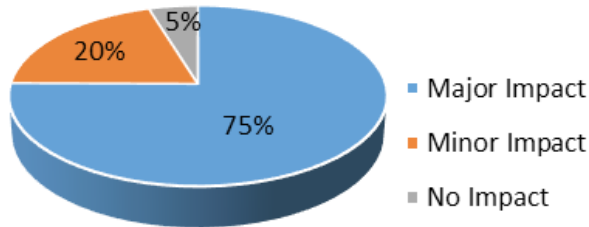
How Foreign Competition Impacts Business: All firms



6.6 Energy Shortages

Firms were asked how the energy crisis impacts their business. As expected, energy shortages have had the most significant impact on firm level growth. About 8 out of 10 firms surveyed in the manufacturing and retail sector find this to be the greatest constraint pointing to the urgent need for a coherent and long term solution to the problem.

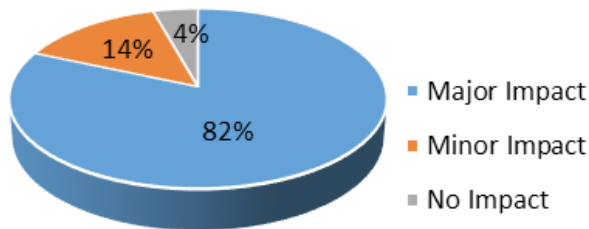
How Energy Impacts Business: All Firms



The main reasons behind this problem are extensive but the main issues have been pointed out by the National Transmission and Despatch Company (NTDC):

“The circular debt, the weak financial position of energy companies, falling gas production, high dependence on oil/gas (over 80%), low exploitation of indigenous coal and hydel resources and unutilised power generation capacity are some of the factors leading to severe energy shortages.”

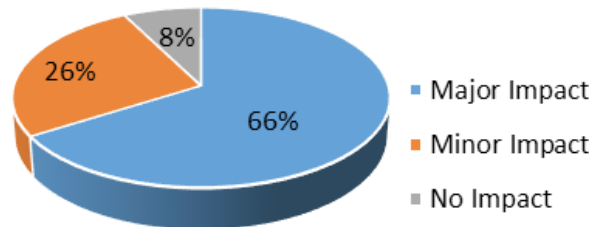
How Energy Impacts Business: Manufacturing



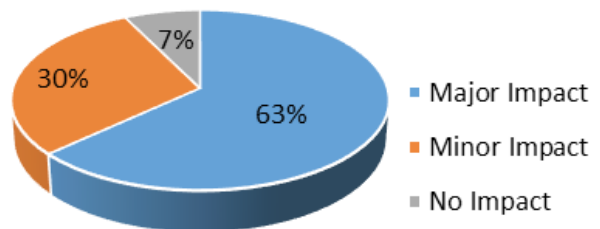
6.7 Law and Order Situation

Firms were also asked about how the law and order situation impacted their business. 63% of the firms consider law and order to have a major impact on business. Law and order seems to be most important for the services and retail sectors, with 70% of the firms in the services sector and 74% of the firms in the retail sector saying that law and order has a major impact on business.

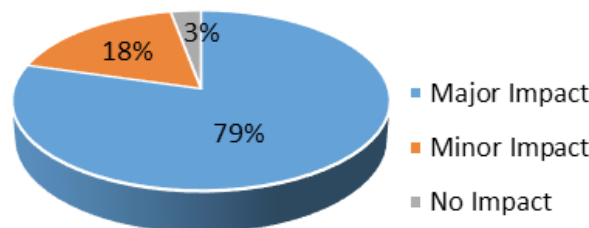
How Energy Impacts Business: Services



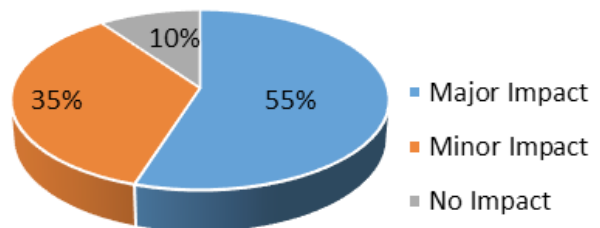
How Law and Order Impacts Business: All firms



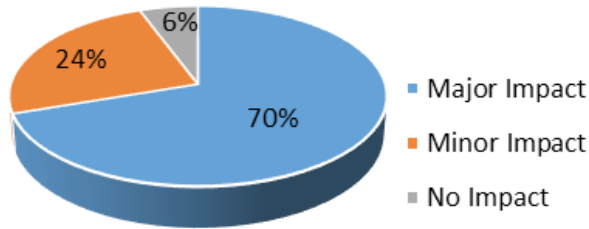
How Energy Impacts Business: Retail



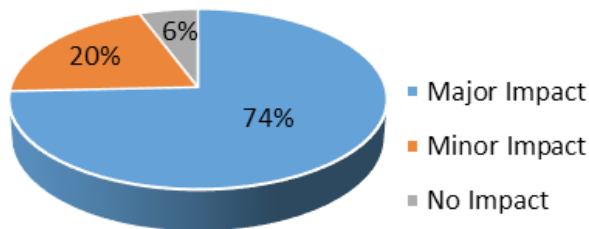
How Law and Order Impacts Business: Manufacturing



**How Law and Order Impacts
Business: Services**



**How Law and Order Impacts
Business: Retail**



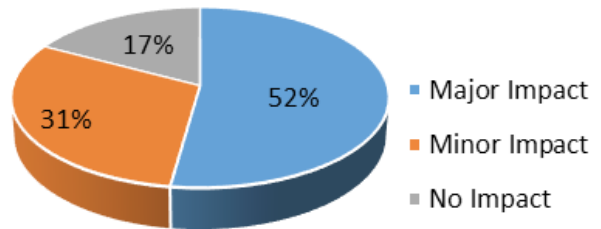
Although the result related to energy crisis being a constraint to growth was expected, the survey found that problems of law and order are almost as important to firms as energy shortages. For manufacturing firms that export, law and order problems result in smaller export orders while for local manufacturing and retail firms, law and order problems have both demand and supply side effects. This result means that while the government should focus on a coherent energy policy, it must also develop a strategy to address the law and order problems if firms are to grow.

6.8 Provincial Commercialization costs and policies

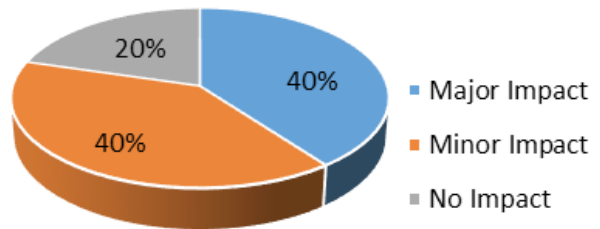
Firms were asked how commercialization costs and policies impact their business. 52% of the firms consider commercialization costs and policies to have a major impact on business, and policies related to commercialization costs seem to be a more important factor for firms in the retails sector. 74% of the firms in the retail sector consider it to have a major impact on business, while 40% of the firms in

the manufacturing sector consider it to have a major impact on business, and 54% of the firms in the services sector consider it to have a major impact on business.

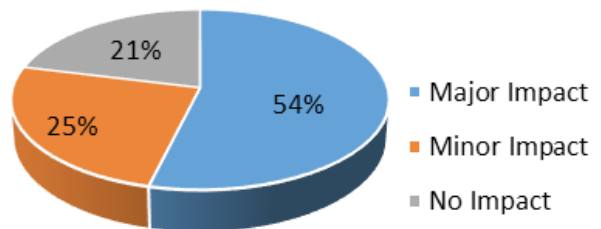
Impact of Commercialization costs and Policies: All Firms



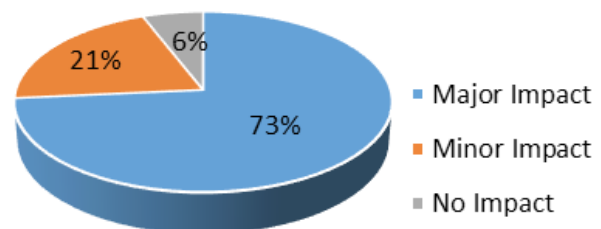
Impact of Commercialization costs and Policies: Manufacturing



Impact of Commercialization costs and Policies: Services



Impact of Commercialization costs and Policies: Retail



The commercialization fee charged for the change of use of property (from residential to commercial) in Punjab is 20% of the value of property. This however is the official amount; additional costs are mostly incurred due to inefficiencies and corruption.

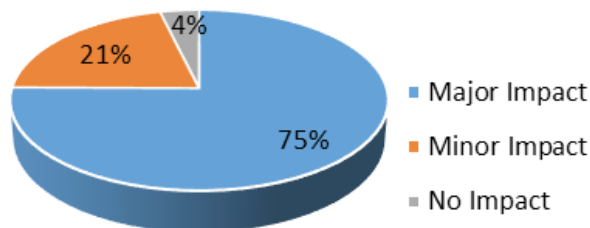
Firm owners' state that the reason why retail sector is most affected by such policies is the poor conditions of the retail markets prevalent in various cities. Retail outlets /shops are mostly small, cramped and in congested areas with limited space (sq. ft.) allocated to every shop. Other than the lack of commercial space in different areas, high commercialization fees raise investment cost(s) to a considerably large amount.

Firm owners also explain that the service sector is affected by the lack of space, for restaurants/ hotels and mixed use areas. There remain poor provisions for office complexes, and where space is available, the rent prices are extremely high. Furthermore, the authorities charge very high development charges for water and sanitation which makes development highly cumbersome.

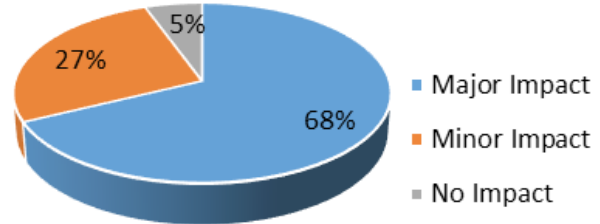
6.9 Provincial Taxes

Firms were asked about how provincial taxes impact their business. 75% of firms consider provincial taxes to have a major impact on business, while 68% of the firms in the manufacturing sector consider taxes to have a major impact on business, 81% of the service sector firms consider taxes to have a major impact on business, and 79% of the firms in the retail sector consider taxes to have a major impact on business.

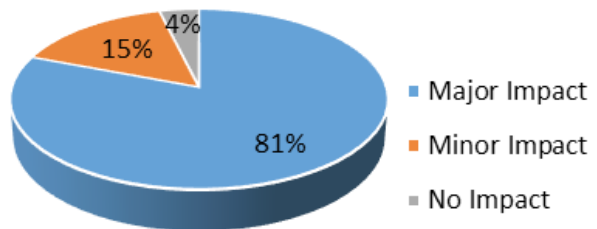
Impact of Provincial Taxes: All Firms



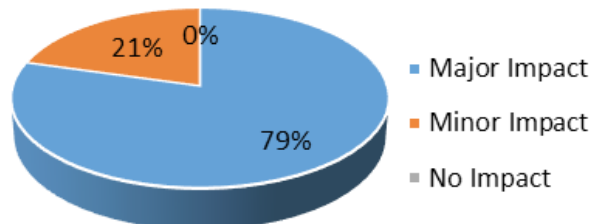
Impact of Provincial Taxes: Manufacturing



Impact of Provincial Taxes: Services



Impact of Provincial Taxes: Retail



The results of the survey show that more than 70% of the firms in the retail sector found commercialization costs and policies to be a major impediment. Similarly, more than 60% of the firms found provincial law and regulations to be a major impediment, while 75% of the firms found provincial taxes to be a problem. This points to a dire and urgent need for provincial authorities to reform both the provincial regulatory and tax system in order to promote firm level growth.

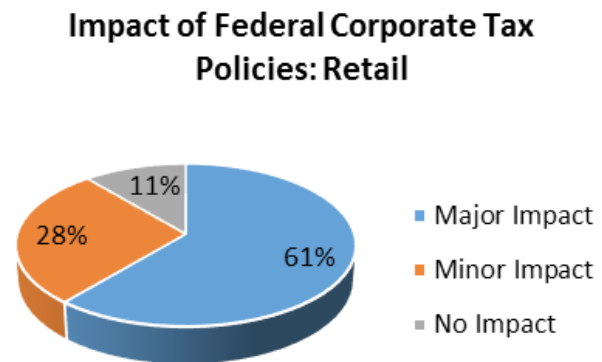
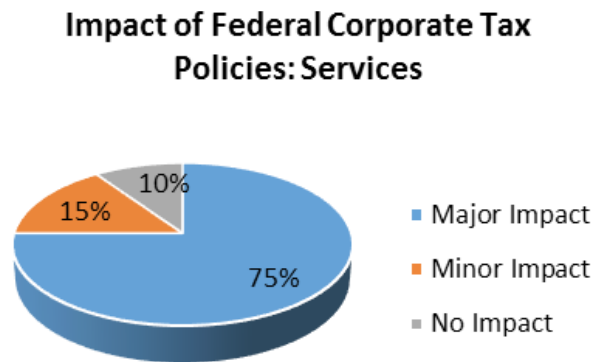
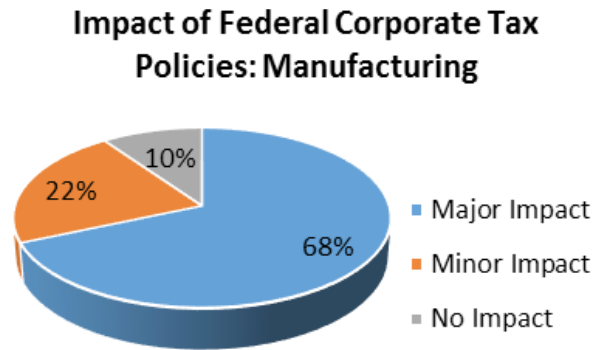
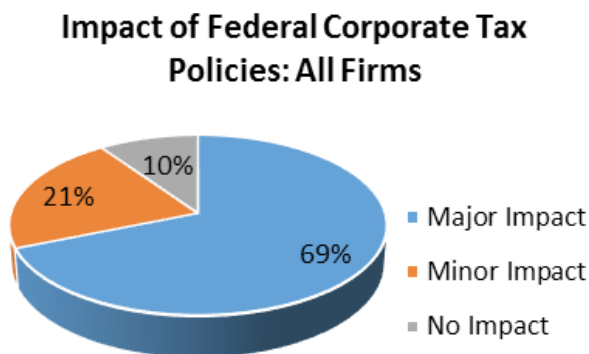
The service sector suffers from giving 32% corporate tax, which in fact is the highest in South Asia as compared to India and Bangladesh. When it comes

to sales tax, the retail sector is the most effected. Retailers are required to pay 3% sales tax if they have turnovers below a certain limit and pay 15% sales tax if they move beyond that bracket. This regime has made sales tax extremely high for retailers. This in turn creates incentives for businesses to report lower levels of turnover, and in case they do go over, it creates incentives for businesses to subdivide, at least on paper, rather than cross the threshold, which in fact is penalizing for a person who wants to grow in a legally sound manner.

While not shown in these results, other studies have found that it is not the presence of laws, regulations and taxes that firms find problematic, but rather the ad hoc implementation of these which makes them susceptible to corruption and abuse. Greater transparency and accountability even in the present system will help firms effectively deal with the existing structure as opposed to finding it a major impediment to growth.

6.10 Federal Corporate tax policies

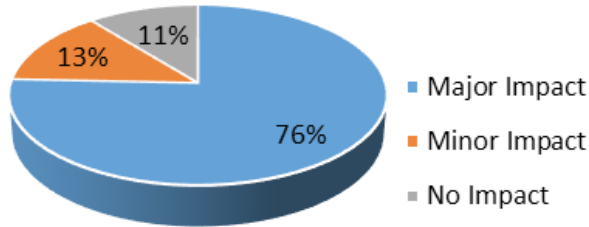
Firms were asked how corporate tax policies impact their business. 69% of the firms consider it to have a major impact on business, with 68% of firms in the manufacturing sector considering it to have a major impact on business, 75% of firms in the services sector considering it to have a major impact on business, and 61% of firms in the retail sector considering it to have a major impact on business. Corporate tax policies seem to be a more important factor for firms in the manufacturing and services sector than firms in the retail sector.



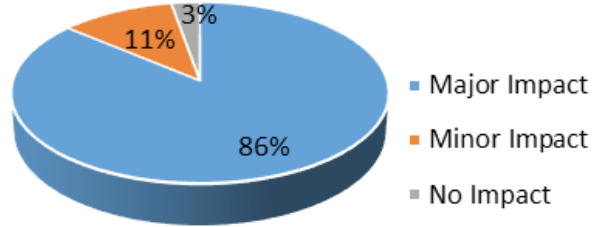
6.11 Import and Custom Duty Policies

Firms were asked how import or custom duty policies impact their business. 76% of the firms consider import or custom duty policies to have a major impact on business, with 62% firms in the manufacturing sector considering it to have a major impact on business, 71% of firms in the services sector considering it to have a major impact on business, and 86% of firms in the retail sector considering it to have a major impact on business.

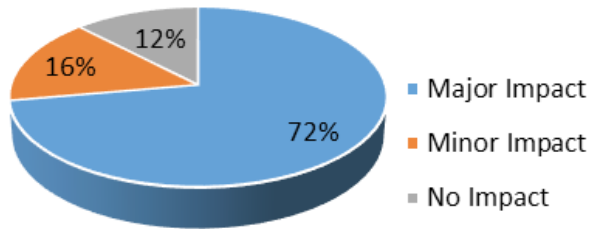
Impact of Import or Custom Duty Policies: All Firms



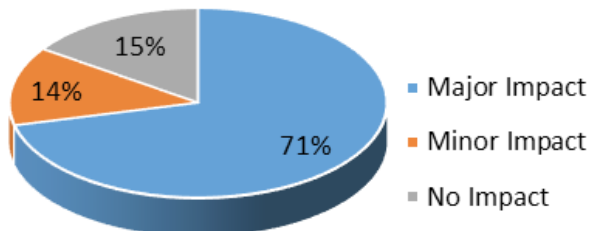
Impact of Import or Custom Duty Policies: Retail



Impact of Import or Custom Duty Policies: Manufacturing



Impact of Import or Custom Duty Policies: Services



As found on the provincial level regulations, federally administered policies like corporate tax, income tax and custom duties are found to have a major impact on growth in all sectors. This is probably because of the constantly changing nature of these policies which are susceptible to political nature as well as the firm's aversion to dealing with tax and customs authorities at any level. The lack of monitoring of these policies combined with the inconsistent application of these policies and the slow system of tax refunds has led to firms wanting to avoid any interaction with the tax authorities. So, it is not that firms do not want to pay taxes but rather firms not wanting to deal with the tax authorities, which leads to low levels of tax collection in Pakistan. In turn, this also results in a low tax to GDP ratio in Pakistan.

7. Conclusion

Over the past few years the Pakistani economy has faced a host of challenges and there is a general consensus that economic growth has slowed down significantly. Presently, the Pakistani economy has begun to stabilize and during this time it is critical to develop policies that take into account both the long term economic needs of the country as well as the short term needs of the business community.

Lahore Chamber of Commerce & Industry and the Lahore School of Economics have recently conducted a business confidence survey of firms in order to determine industry specific trends as well as the general macroeconomic trends. The survey was conducted with a variety of firms across three sectors, the manufacturing sector, the services sector and the retail sector, and the results from the survey show that the feeling amongst the business community is cautiously optimistic.

The first point that emerges from the survey is that firms have grown over the last year in terms of sales, investment and size. This is an extremely positive message which points to renewed economic growth in all three sectors covered in the survey.

The second point that emerges is that firms across all three sectors anticipate higher growth in 2015 and are also planning to increase their investment levels which has further spillover effects on growth. A related point that comes out in the survey is that the firms are extremely concerned about sources of financing and that the banking sector is falling far short of meeting their needs. Though firms are presently expanding based on their own internal sources of funding, the failure of the financial sector

to provide adequate capital will be a significant drag on future growth and urgent policies are needed to create ways in which the financial sector can play a more constructive role in economic growth.

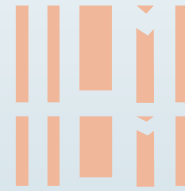
Another important result from the survey is that firms feel that there are significant shortages in the pool of skilled labour which is a major constraint to growth. The general feeling amongst the business community is that there has to be coherent governmental policy to impart vocational training to bridge this growing skill gap.

The firms also pointed to energy shortages as a major constraint on growth, with 8 out of 10 firms saying that this is a significant and persistent problem. At the same time, what was surprising was that almost the same number of firms found the deterioration in law and order to be a major constraint on growth. This points to the need for a coherent set of policies to not just address the energy crisis but to also address the security related issues affecting firms, which is sometimes ignored.

Finally, firms find both provincial and federal regulations and taxes extremely cumbersome and a significant drag on growth, because of the ad hoc nature of many of the policies, inconsistent application of the policies and because of the lack of transparency of these policies. The business community feels that while regulations and taxes are important, they must take into account the needs and requirements of the business community, since there is an urgent need for closer collaboration between the government and the business community in developing an overall industrial strategy that promotes growth.



**Lahore Chamber of
Commerce & Industry**



**Lahore School of
Economics**

Business Confidence Survey 2015

