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Rise in 'sin' taxes will hurt brewery more than tobacco industry: Analysts

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WHILE it is unsure if the upcoming Budget will unveil an increase in "sin" taxes, analysts note that any such rise will likely hurt breweries more than it will the tobacco industry.

The market is largely expecting an increase in tobacco and liquor taxes in the Budget, to be tabled by Finance Minister Tun Daim Zainuddin on October 27.

Prime Minister Dr Seri Dr Mahathir Mohamad yesterday added fuel to the fire when he indicated that tobacco taxes might be raised. He said tobacco companies have still managed to make "a lot of profit" despite previous tax increases.

Asked if a rise in tobacco taxes would be steep this time, Dr Mahathir said he did not know yet, adding that the matter was "top secret", news wire Reuters reported.

Assuming there is a tax increase on tobacco and liquor, analysts say the brewery industry will come off the worse hit compared to the tobacco industry.

They say if excise duty on tobacco is raised, cigarette companies will just offset the impact on their earnings by transferring the cost to the consumer. "They'll just raise cigarette prices as was the case in 1998," said an analyst with a local stockbroking firm. The last time excise duty on tobacco was raised was in October 1998 by 40 per cent.

As it is, the industry is believed to be looking at a price increase in the coming year. Encik Hamdan Abdul Majeed of HSBC Securities noted that cigarette companies raised selling prices by an average of 4 per cent yearly between 1992 to 1998 - a period where there was no tax increase.

The three major cigarette companies currently in Malaysia are British American Tobacco Malaysia Bhd (BAT), JT International Bhd and Philip Morris Malaysia Sdn Bhd.

BAT has apparently indicated that if there is a tax increase, it is likely to be marginal.

According to Hamdan, if excise duties are increased by 10 per cent, BAT's earnings per share (EPS) will drop by 5.5 per cent, assuming there is no price increase. If BAT raises selling prices by 10 sen following the tax increase, its EPS will be up by 5.7 per cent, thus resulting in a net gain of 0.2 per cent.

In direct contrast, analysts say brewery companies such as Guinness Anchor Bhd and Carlsberg Brewery (M) Bhd will definitely feel the pinch of a tax rise as it will be difficult to raise their product prices due to already intense competition in the local market.

As it is, the market is currently prevalent with price wars, with each company trying to outdo the other by offering discounts in efforts to maintain their market share, even at the expense of a lower margin.

"The brewery market is very soft... it hasn't recovered from the previous tax increase in 1998. Growth and earnings of the breweries are flat," Hamdan said.

The last tax increase of about 20 per cent in October 1998 had aggravated demand for malt liquor by about 20 per cent, helped in no way by the economic downturn then.

The current recovery in the economy has yet to reinvigorate demand for beer and stout products. Hamdan expects consumption to continue to be sluggish what with consumers shifting to other beverages such as coffee,

wine and other forms of liquor as well as competition from smuggled beer.

Analysts therefore conclude that a tax increase on liquor will only serve to aggravate the current scenario in the brewery industry and further pull down the players' margins.

Several analysts contacted, however, were less concerned about the issue, convinced that a tax rise is not on the table this year. "Perhaps next year or the year after," commented one.

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