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Corporate Malaysia hails new budget

DECISIVE MEASURES, INCLUDING GST AND ABOLITION OF SUGAR SUBSIDY, SHOW GOVERNMENT'S RESOLVE TO COMBAT DEFICIT

By **ELAINE TAN** in Kuala Lumpur
For China Daily Asia Weekly

Malaysian Prime Minister Najib Razak unveiled a 264.2 billion ringgit ($84 billion) budget for 2014 on Oct 25 that has been simultaneously lauded as decisive, balanced, economically and socially sound, as well as lambasted for favoring the rich while burdening the lower- and middle-income groups.

Themed *Strengthening Economic Resilience, Accelerating Transformation and Fulfilling Promises*, it aims to address the country's burgeoning fiscal deficit, shrinking current account surplus and growing debt pile.

Malaysia has recorded budget deficits every year since 1998. Concurrently, national debt has ballooned to 54 percent of GDP, the second highest of 12 emerging Asian economies. This had prompted ratings agency Fitch to downgrade the country's sovereign credit rating from neutral to negative in July.

A day before the budget was presented, foreign investors holding 40 percent of government bonds also joined the call for fiscal reforms, telling business and investment weekly *The Edge Malaysia* that they would pull out funds if the budget deficit did not drop to below 4 percent of GDP.

Najib, who is also the finance minister, has responded by braving some unpopular measures to show the government's commitment toward fiscal consolidation.

Topping this is a long overdue 6 percent goods and services tax

AFP
Najib Razak, Malaysia's prime minister and finance minister, holding the briefcase containing the 2014 budget, outside the Finance Ministry office on Oct 25.

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(GST). The new tariff, which will replace the current sales and service tax on April 15, 2015, is expected to add an estimated 8 billion ringgit to government coffers.

The move, though expected, has been largely applauded by analysts. In a statement, OCBC Bank economist Selena Ling called it "a very positive development as it exceeded our expectations and will broaden the revenue base and help to narrow the budget deficit going forward".

"While a 4 percent GST rate would largely be revenue-neutral, the 6 percent rate bodes well in terms of signaling the government's serious intent to improve its fiscal housekeeping," she added.

The country's sugar subsidy was also abolished with immediate effect to save the government some 350 million ringgit. Lower provisions for subsidies also indicate that further hikes in petrol prices and gas and electricity tariffs are to be expected.

None of these plans are going to go down well with citizens who are already complaining about the spiraling cost of living.

To soften the blow, Najib has offered additional one-off cash handouts to low- and medium-income households amounting to 4.6 billion ringgit under the 1Malaysia People's Aid (BR1M 3.0) program. The budget also includes tax incentives such as lowering individual income tax rates between one and three percentage points, tax rebates and raising the ceiling of chargeable income subject to the maximum tax rate from 100,001 ringgit to 400,001 ringgit.

While Ling believes these measures should sufficiently help soothe the GST transition pains, Ong Kian Ming, a member of parliament from the opposition Democratic Action Party, feels otherwise.

"The GST will definitely increase the cost of living for most Malaysians even after the adjustments in the income tax rate," he says. "While BR1M 3.0 will cushion the blow somewhat, it may not be enough. For example, if a family with income below 3,000 ringgit has to pay an additional 100 ringgit a month on GST, that would come up to 1,200 ringgit a year which is not sufficient for the BR1M payment of 650 ringgit to cover."

Many staples will be exempt from the new tax to help lower the burden on the lower income group; these include rice, sugar, salt, flour, cooking oil, piped water, the first 200 units of electricity per month for domestic consumers, public transportation and health services. However, many goods that were previously exempt from the sales tax will be taxed under the GST.

"I am concerned about the potential of the GST to cause an inflationary cycle which would lead to a permanent increase in the inflation rate," Ong adds. Current inflation stands at about 2 percent but could accelerate to 3 to 3.5 percent next year.

Meanwhile, the corporate sector received a modest sweetener in the form of a one percentage point cut in tax rate from 2016 — from 25 percent to 24 percent for companies and 20 percent to 19 percent for small and medium enterprises.

Nazri Khan, vice-president and head of retail research at Affin Investment Bank, told Malaysia's national news agency Bernama this is expected to "attract more investors, spur stronger private sector participation while addressing the deficit by boosting revenue, lowering operating costs and development expenditures".

But while the reduction has been welcomed, Sridharan Nair, managing partner of PricewaterhouseCoopers Malaysia, said a larger cut would have bode better for regional competitiveness.

"At a 24 percent tax rate in 2016, we would still be higher than many of our neighbors and higher than the new norm of 20 percent in the region," he told *The Star* newspaper.

Sector-wise, oil and gas, and construction emerged winners with the prioritization of large-scale infrastructure projects such as the West Coast Expressway and Kuantan Port expansion, and major investments in oil field exploration and development.

Tourism players including the aviation and hospitality sectors also have much to cheer about with 3.2 billion ringgit set aside for tourism promotion and development to tie in with Visit Malaysia Year 2014. Malaysia hopes to welcome 28 million visitors next year.

"The launch of the Services Sector Blueprint in 2014 will be interesting to watch as it could invigorate the services engine for the Malaysian economy and provide an additional thrust for growth," said Ling from OCBC Bank.

But the property sector was dealt several blows at once in an effort to cool the market.

"Measures affecting the sector are hard hitting, with a considerable jump in Real Property Gains Tax alongside the imposition of a higher minimum price for property purchases by the foreigners and the discontinuation of the Developer Interest Bearing Scheme, which has helped drive buying interest," reports Maybank Investment.

Though politically unpopular with the man on the street, Najib's budget is generally viewed as a step in the right direction toward assuaging foreign investors and preventing further ratings cuts.

Revenue is projected to increase to 224.1 billion ringgit (from 220.1 billion ringgit) and the fiscal deficit will be capped at 3.5 percent of the GDP (from 4 percent).

But is it enough?

"While government efforts to address long-standing structural issues is applauded, questions remain whether enough has been done to allay concerns among international credit rating agencies and foreign investors," Alliance Research, a subsidiary of Alliance Bank, reports.

"We would have preferred to see further clarity on the timeline of subsidy rationalization. Another area where improvement is much needed is government debt which is projected to hit 54.8 percent of GDP in 2013 and stay flat at 54.7 percent in 2014, which is just shy of the 55 percent threshold."

"The budget does not identify any cost-cutting measures by the government beyond the removal of subsidies," Ong points out. The opposition, he says, would have preferred to see more concerted efforts to cut wastage using the auditor general's report.

"If operational expenditures in all departments are cut by 10 percent it would translate into cost savings of between 20 to 30 billion ringgit."

The recently released *2012 Audi-*

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tor General's Report revealed embarrassing widespread wastage and mismanagement of funds in the civil service such as the loss of firearms worth 1.33 million ringgit, and 120,000 ringgit to purchase clocks and scanners at inflated prices.

For now, there is a buzz of optimism. Bloomberg reports that forward contracts in Malaysia's ringgit rose by a half percent while stocks, bonds and the ringgit had advanced post-budget announcement. And most of corporate Malaysia was full of praise for what they deem to be a budget that sufficiently addressed fiscal challenges.

"The growth outlook for 2014 is brighter," said Ling. She supports the official forecasts for real GDP growth in 2014 of 5 to 5.5 percent on the back of improvements in exports, the services and construction sectors, private investments and private consumption.

But the report card on Budget 2014 will depend very much on execution and implementation. Najib will need to show political will to see through these tough measures while restraining expenditure.

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