Socio-Economic Research Centre
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AmInvestment Bank Investors Forum

Budget 2024: Secure A Sustainable Path to Growth and Reform – Aspiration or Achievable

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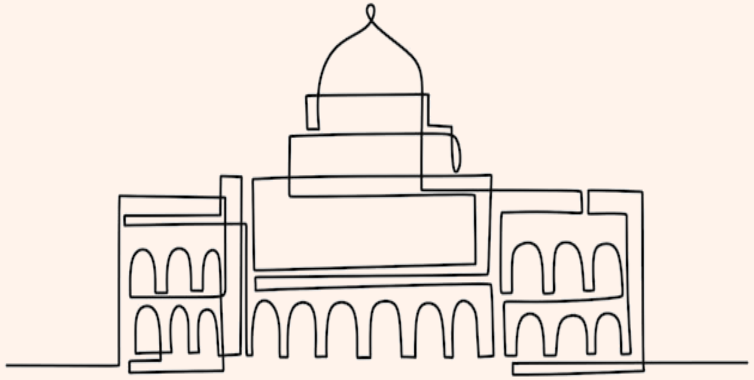
26 October 2023

Belanjawan 2024
MALAYSIA MADANI



A Budget can be an aspirational document – a signal of where we want to go; and how to get there?

Does the Budget meet expectations?

Will it enhance the willingness of the private sector to invest, compete and thrive?

Whether those delivering the Budget will hold implementing agencies to account for its delivery?

Will the Budget help the Ringgit ?

Striking a "Right" Balance between Sustaining Growth and Fiscal Consolidation

- Fiscal consolidation resumes; pursues reforms agenda for future-proofing Malaysia
- Challenging external headwinds and domestic environment
- The 2024 National Budget is framed as fiscally sustainable and responsible for sustaining economic growth, addressing the cost of living pressures, and effecting structural changes

Key elements of 2024 Budget

- Sizeable total expenditure; high Development Expenditure (DE)
- Revenue enhancement
- Subsidies rationalisation
- Focus on growth in investment, SMEs, food security, clean energy transition, ESG initiatives, human capital formation

Fiscal Deficit

% of GDP

-6.4%
(2021)

RM98.7bn

-5.6%
(2022)

RM99.5bn

-5.0%
(2023E)

RM93.2bn

-4.3%
(2024B)

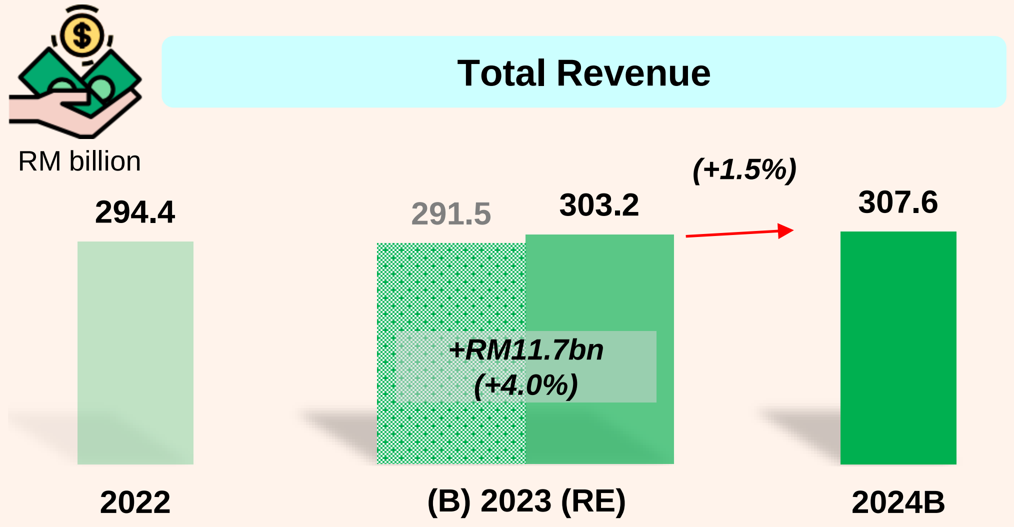
RM85.4bn

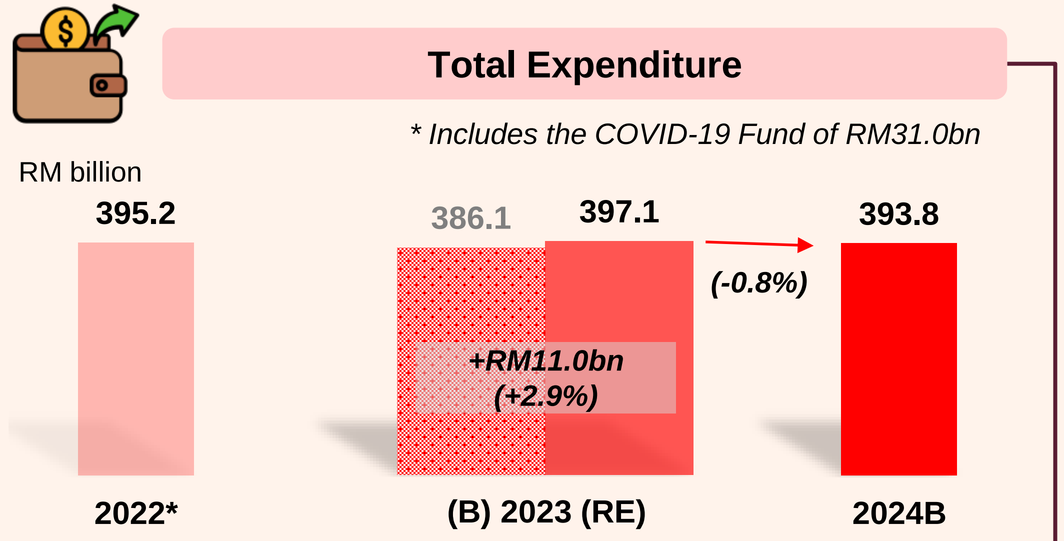
Gradual fiscal reduction path

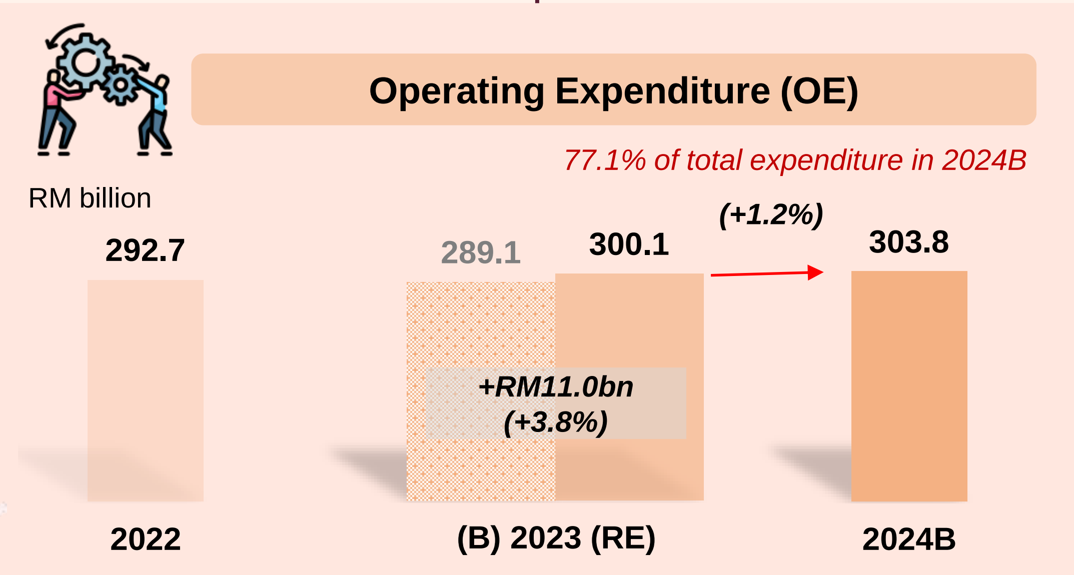
Persistent fiscal deficits for the 27th consecutive year in 2024

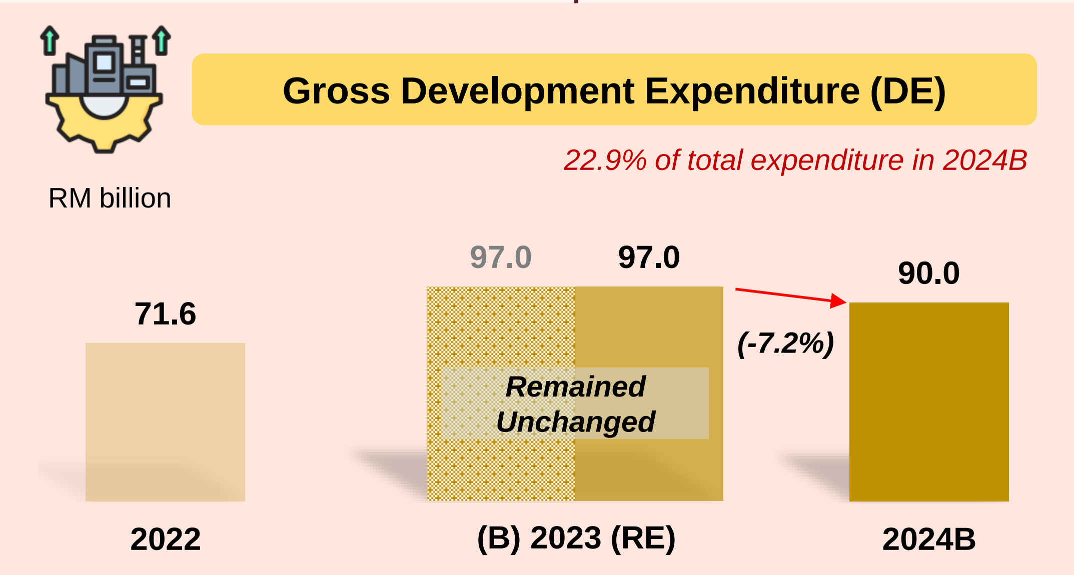
Source: MOF *E=Estimate; F=Forecast; RE=Revised Estimate; B=Budget Estimate*

Budget 2024: Budgetary Operations









Source: MOF (B)=Budget Estimate in new Budget 2023; (RE)=Revised Estimate; B=Budget Estimate Note: Excludes budget measures

Must Build a Sustainable Revenue Base

2024 Budget's key revenue measures	Net gain (+)/ loss (-) on revenue	Implications
Increase in **Service Tax rate** to 8% from 6%; broaden its scope (logistics services, brokers, underwriting, karaoke services). The increase does not include F&B, telcos, vehicle parking space and logistics.	**+RM3.5 billion**	• "Abridged" version of GST? • Higher living expenses for electricity bill, repair of motor vehicles and insurance services
Capital Gains Tax (CGT) of 10% on net gain of the disposal of non-listed shares, with an option of 2% on gross sales value for shares acquired before 1 Mar 2024	**Requires new for of legislation; no estimation**	• Exemptions to IPO approved by Bursa Malaysia and restructuring of shares within the same group • Lingering concerns CGT will extend to other asset classes • Dampen start-up; private equity and entrepreneurship
High-Value Goods Tax rate at 5%-10%, starting 1 May 2024	**Still in progress; no estimation**	• Refunds for tourists • Are all types of motor vehicles included? CBU; CKD; EV? • Dampen domestic high-end retail market • Grey market for consumer products (watches, jewellery, etc.)

Issue:

Creation of a sustainable revenue system is still not part of the fiscal consolidation plan.

- How can Malaysia ensure the long-term viability of its tax system without a proactive effort from now? We have to build a sustainable revenue system and there is much room for improvement.
- We cannot have a tax system if a small group of the people at the top-end pay more taxes all the time, while the rest get to piggyback on their contributions to enjoy more benefits.

- **Still high dependency on oil revenue** (2020-2024B: 22.9% of total revenue pa (2015-2019: 21.4% pa); **Petronas dividend**: RM36.2bn per year in 2020-2024B vs RM27.6bn per year in 2015-2019).

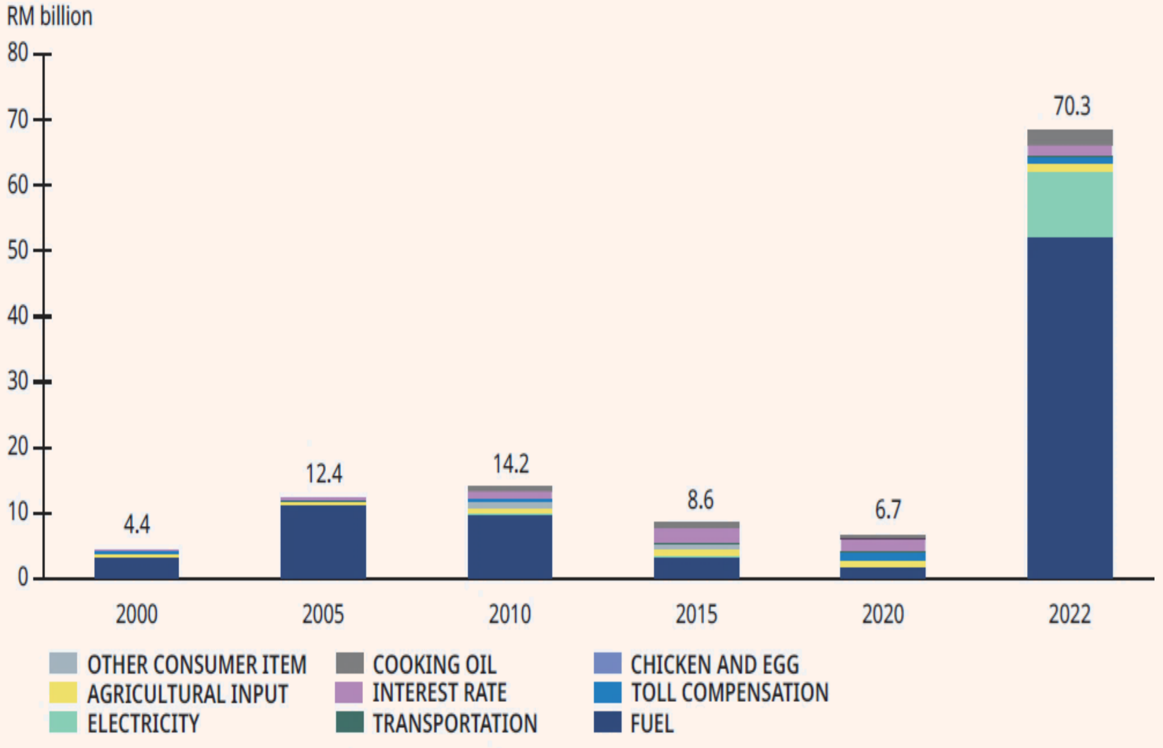
Questions:

- Will GST make a comeback?
- Enhancing SST vs. GST?
- SST and GST are good fiscal policy tools - a tough choice !

Subsidy Reform is A Must

RM223.5 billion or 8.9% of total operating expenditure for subsidies (2012-2022) – **71.6% for fuels** and others for interest rate, agricultural inputs, cooking oil, electricity, toll compensation, transportation, chicken and eggs.

Trend of Subsidy Outlays



Source: MOF

Data Tracker

As of 30 June 2023, RM31.1 billion was spent to finance the following measures in the 2023 Budget, which aimed to reduce the cost of living burden:

- **RM5 billion** for **Sumbangan Tunai Rahmah**, benefitting 8.7 million recipients
- **RM2.6 billion** for **Bantuan Khas Kewangan**, benefitting 1.3 million public servants and more than 1 million pensioners
- **RM6.8 billion** for **electricity bill subsidy**, benefitting 9.7 million users
- **RM15.9 billion** for **subsidies on RON95 petrol, diesel and liquefied petroleum gas (LPG)**
- **RM825 million** for **Bantuan Awal Persekolahan**, benefitting more than 5 million students

Have We Done Enough in Operating Expenditure Rationalisation?

Targeted subsidy rationalisation

- **Subsidies and social assistances** are expected to decline by RM11.6 billion or 17.9% to RM52.8 billion in 2024 (estimated RM64.2 billion in 2023).
- Subsidy rationalisation is estimated to **save at least between US$1 billion (RM4.73 billion) to US$2 billion (RM9.47 billion) a year**. The targeted subsidies mechanism will be based on PADU (centralized database) to identify eligible recipients.
- Starting with diesel and electricity tariff in Q1 2024, followed by petrol in 2025?
- As better-targeted subsidies are a complex process, both technically and politically, **"buy-in" from the public** is crucial to ensure success.
- 3Cs to implementing price subsidy reforms – **Credible, Comprehensive and Communication**. Effective communication is needed to explain the reasons for shifting to a targeted mechanism and its benefits for the economy. Net savings from subsidy reforms should be transparently allocated to high-priority projects.

Emoluments, the largest component of OE (31.5% of total), is budgeted to increase further by 4.8% to a new high of RM95.6 billion in 2024 due to annual salary increments for 1.7 million civil servants and 971,000 pensioners as well as new hires in the education and healthcare sectors.

Credible civil service reforms are needed to improve the quality and value of public services-based performance and productivity-linked salary systems. These include rightsizing civil servants and accelerating digital government.

Retirement charges averaged RM29.2 billion in 2019-2023, and will increase further by 1.1% to RM32.4 billion or 10.7% of total OE in the 2024 Budget. It was estimated that pension payments could reach about RM46 billion by 2030.

A path to public pension reform entails **the transition to a defined contribution plan for new hires**; and also applied to existing public sector employees according to the number of years for which they had already contributed to the system. A key advantage of defined contribution plans is that it eliminates the potential risk of underfunding long-term pension liabilities.

Fiscal Governance is an Element of Fiscal Responsibility

Done:

- The most significant piece of tax legislative reform is the **Public Finance and Fiscal Responsibility Act (FRA) 2023**, which makes the Government accountable for ensuring sound fiscal rules to fortify fiscal discipline and contain fiscal risks.

What's next?

- The tabling of the **Government Procurement Act (GPA)** in 2024, which would make every Minister accountable for the failure to comply with finance regulations, management, and high-priced procurement.

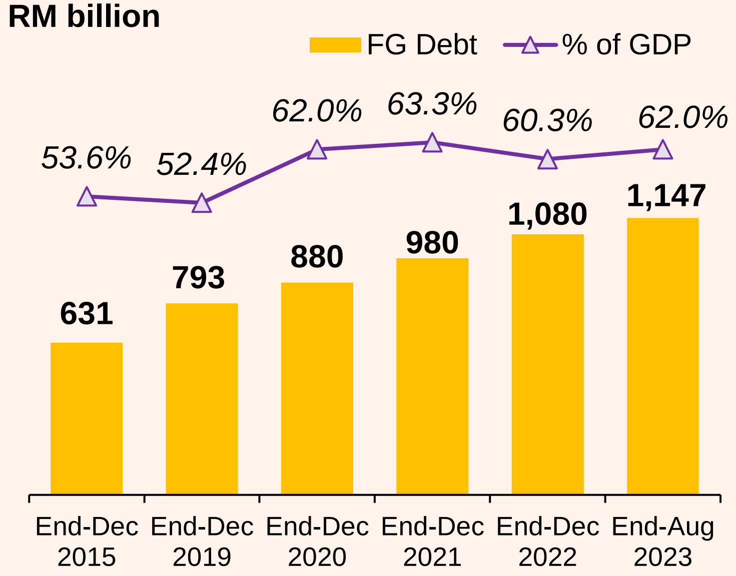
Notes

- FRA is aimed to ensure the responsibilities, accountability, governance and transparency of the Government in managing its public finances and fiscal risk, specifically in relation to revenue, expenditure, borrowing and debt; as well as the reporting of annual budget documents and publication of other documents.
- MOF shall lay the fiscal adjustment plan at Parliament after the approval given by the Cabinet concerning the assessment of any deviation from the fiscal objectives.

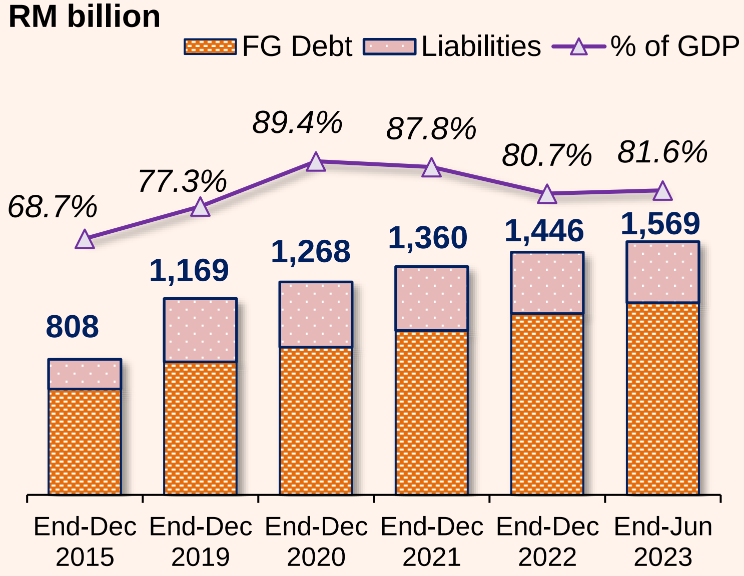
Fiscal Objectives	Quantified Values	Remarks
Annual development expenditure incurred as a percentage of gross domestic product	≥ 3%	Yearly average of 4% since 2015
Fiscal balance as a percentage of gross domestic product	≤ -3%	4.42% for past nine years
Debt level as a percentage of gross domestic product	≤ 60%	Currently at 56.3%
Financial guarantee as a percentage of gross domestic product	≤ 25%	17.8% for past eight years

Government's Debt and Liabilities in Focus

Federal Government (FG)'s debt



Debt and liabilities



Note: Liabilities in 2015 cover government guarantee only.

Debt legislative guidelines

Act	Statutory Limit	End-Aug 2023
Loan (Local) Act 1959 [Act 637] & Government Funding Act 1983 [Act 275]	**Outstanding MGS, MGII and MTIB not exceeding 65% of GDP**	59.9% of GDP (RM1,032 million)
External Loans Act 1963 [Act 403]	**Offshore borrowings not exceeding RM35 billion**	RM30 billion
Treasury Bills (Local) Act 1946 [Act 188]	**MTB not exceeding RM10 billion**	RM3.5 billion

Source: BNM; MOF

- The Federal Government (FG)'s direct debt continued to increase at a faster rate relative to GDP growth in recent years. **It stood at RM1.15 trillion as at August 2023 (62.0% of GDP)**. The FG debt to GDP ratio **is expected to rise further to around 64% at end-2024**.
- Combining with the committed government guarantees (GG) and other liabilities, **overall debt and liabilities amounted to RM1.57 trillion or 81.6% of GDP as at end-June 2023**. The infrastructure segment remained as the highest GG recipient (57.5%), followed by services segment and investment holdings.
- Given rising FG debt, the allocation for debt service charges (DSC) also increased rapidly over the years. **For 2024, the Government has allocated nearly RM50 billion or 16.4% of total operating expenditure for DSC** (RM38.6 billion per year or 14.8% of total OE in 2019-2023). **DSC to total revenue is 15.2% in 2023 and will rise to 16.2% in 2024.**

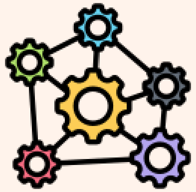
Belanjawan 2024 MALAYSIA MADANI

This is what Malaysia's economy will look like in 2024

"Levers of Change" to Anchor Better Economic Prospects Over Medium-term

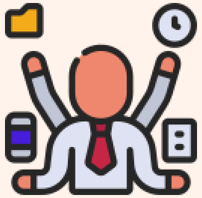
- MADANI Economy Framework, New Industrial Master Plan (NIMP) 2030, National Energy Transition Roadmap (NETR), Mid-Term Review of 12th Malaysia (MTR 12MP) 2021-2025
- Four key risks:
  - (a) The US and China's economic outlook; geo-economic conflicts
  - (b) Delay or weak implementation of domestic policies and projects
  - (c) Inflationary risk triggered by subsidy rationalisation
  - (d) Still elevating business costs

Issues and Challenges Hindering Malaysia's Growth Path



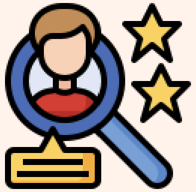
Economic complexity

Improved marginally



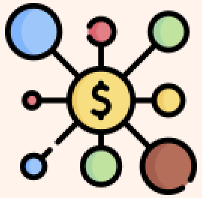
Labour productivity

Stagnated



Talent

Shortage and skills mismatch



Product & market diversification

Improved marginally

Ease of doing business

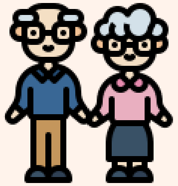
Need to improve

Private investment

FDI hampering; DDI decreasing

Fiscal space

Limited

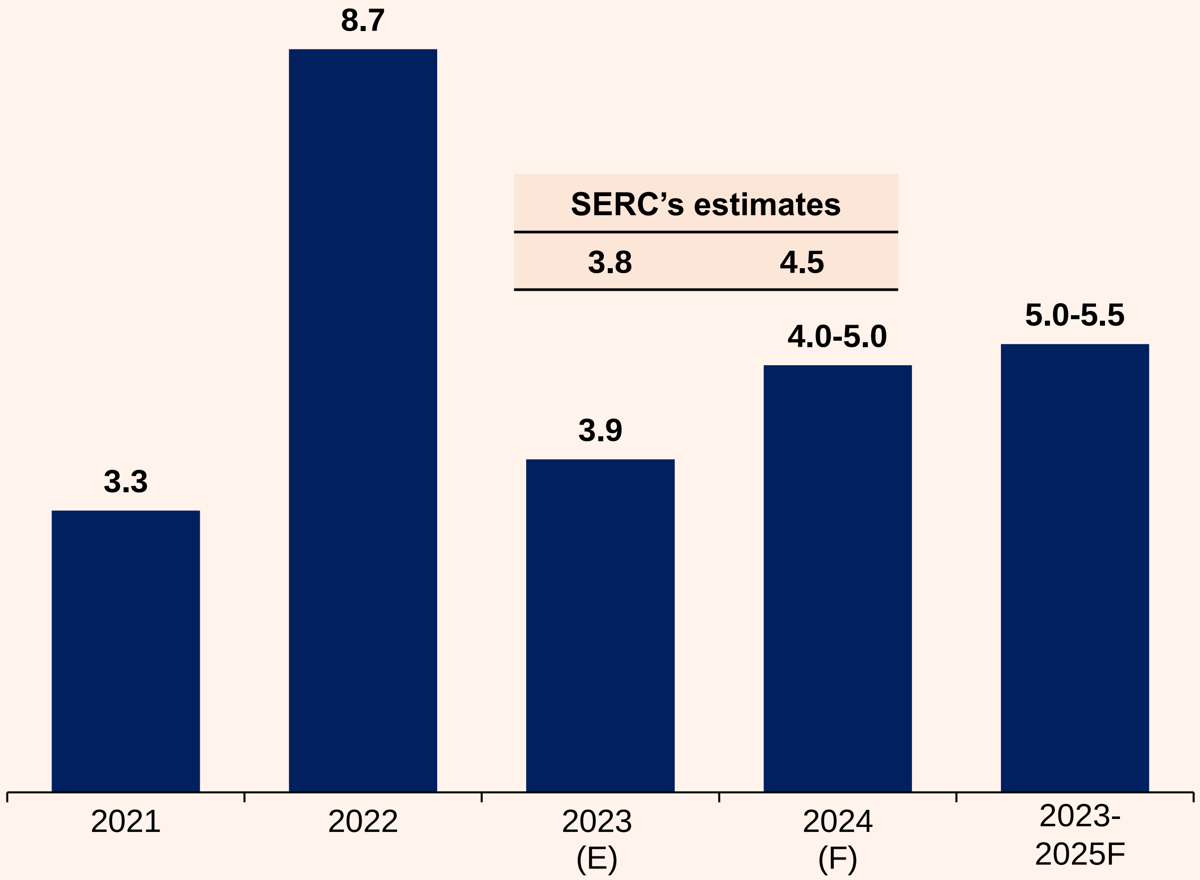


Demographic trend

Aged society

The Malaysian Economy to Expand by 4.0% - 5.0% in 2024

Malaysia's real GDP growth (%)



E=Estimate; F=Forecast

Source: DOSM; MOF

Note: 2023-2025F was forecasted in MTR of 12MP

Drivers of Economic Growth in 2024

Supply-side

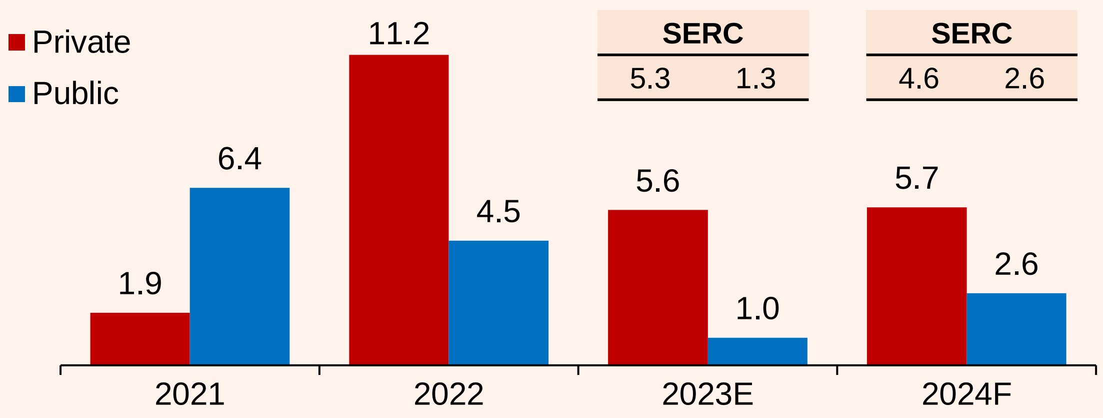
- Broad-based growth, led by the services sector as intermediate and final services groups, is anticipated to rise further, driven by sustained domestic consumption and improved export activities.
- Acceleration in the manufacturing sector.
- Brighter prospects in the agriculture sector and a turnaround in the mining sector.
- All subsectors of the construction sector will expand.

Demand-side

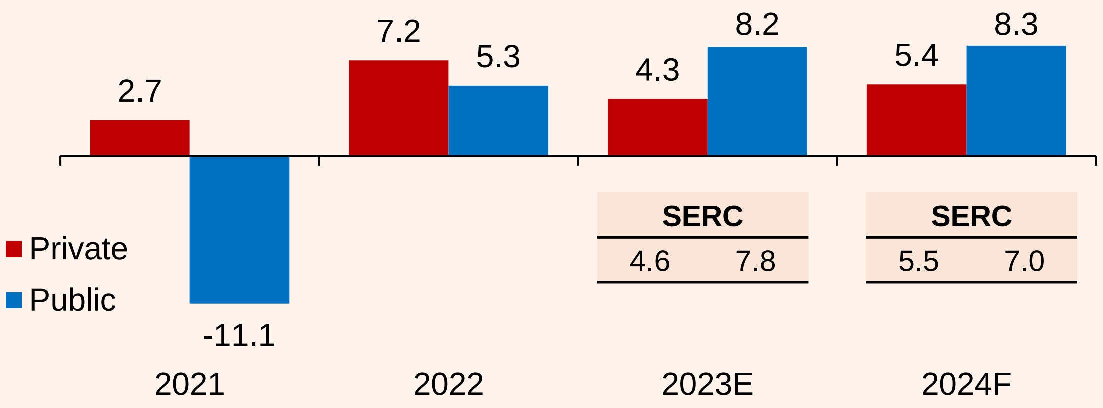
- Buoyed by strong private sector expenditure and improving global demand.
- Implementation of various business policies and blueprints is expected to provide a conducive business and investment environment.
- Robust consumption supported by improved labour market conditions.

Domestic Demand Continues to Drive the Economy

Private and public consumption (%)



Private and public investment (%)



Private Consumption

- Continued improvement in the labour market
- Stronger domestic economic and social activities
- Cash transfers
- Growing social commerce trend

Public Consumption

- Higher spending on supplies and services

Private Investment

- Favourable business sentiments and improved external environment
- Realisation of approved investments, mainly in the E&E, transport equipment, and information and communications subsectors

Public Investment

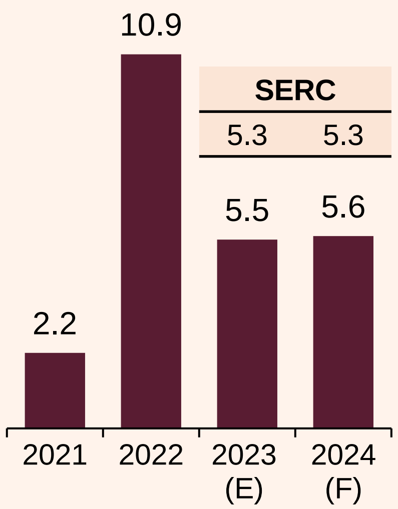
- Higher development expenditure and non-financial public corporations expenditure
- Continuation of transport-related projects
- Commencement of strategic projects

Source: DOSM; MOF

All Economic Sectors to Register Positive Growth in 2024

Real GDP growth by sector (%)

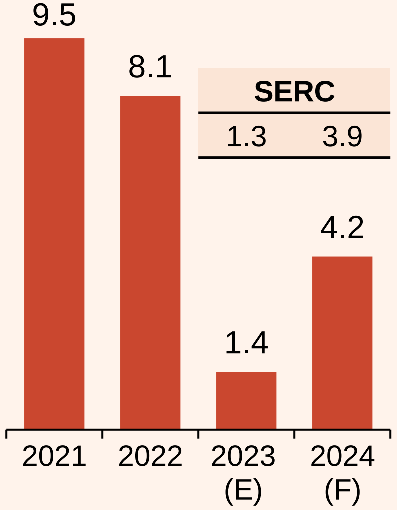
Services (%)



Factors:

- Sustained domestic consumption supports retailing, restaurants, accommodation and communication segments
- Higher trade-related activities help wholesale trade, transport and storage subsectors

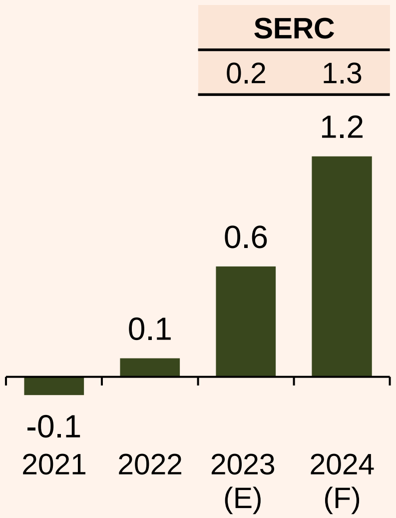
Manufacturing (%)



Factors:

- Recovering external demand helps export-oriented industries, particularly E&E products
- Favourable domestic-oriented industries, backed by higher output in transport and construction-related segments, in line with robust consumption and investment

Agriculture (%)

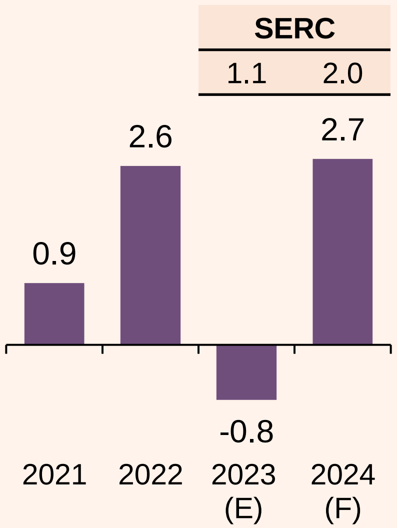


Factors:

- Higher production of crude palm oil (CPO), other agriculture and livestock
- CPO production supported by minimal impact expected from El Nino, better labour supply, increased matured areas and higher oil extraction rate

CPO price: RM4,000-RM4,500/tonne (RM3,500-RM4,000/tonne in 2023)

Mining and Quarrying (%)

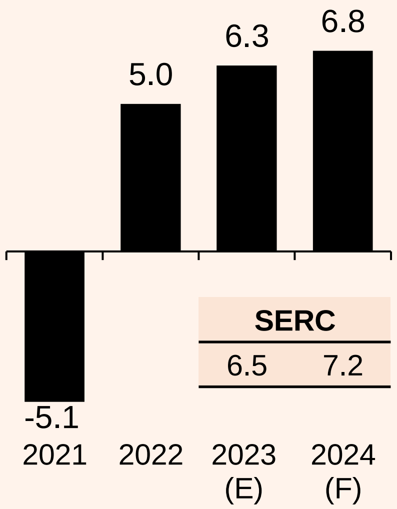


Factors:

- Recovery in production of natural gas from new and existing gas fields, and crude oil and condensates
- Anticipation of higher demand on a positive global outlook

Brent crude oil price: US$85/barrel (US$80/barrel in 2023)

Construction (%)



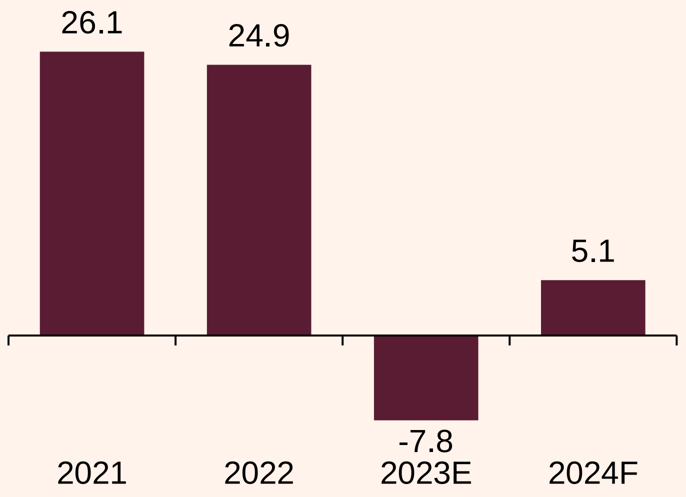
Factors:

- Expansion across all sub-sectors
- Strategic infrastructure and utilities projects

Source: DOSM; MOF

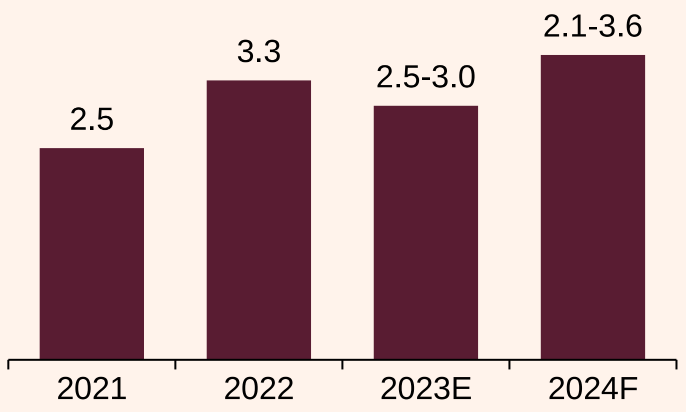
Exports Recovery; Inflationary Risks; Solid Job Market

Gross Exports (%)



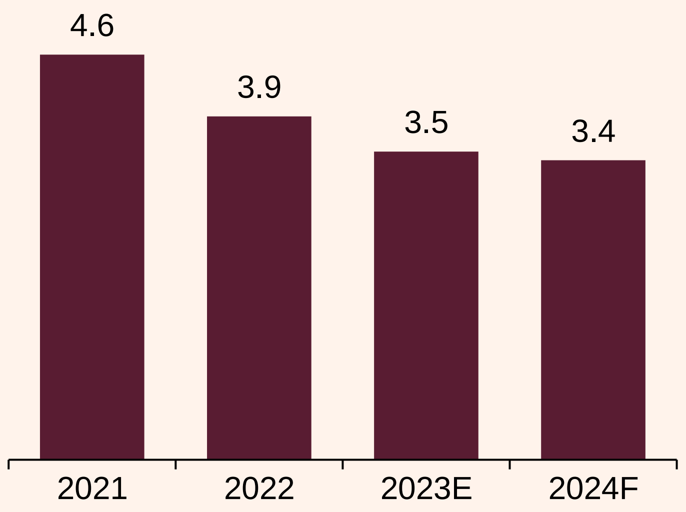
- Anticipate better performance in global trade and improved prospects in the commodity sector
- The trade expansion effects from RCEP and CPTPP
- Steady demand for semiconductors and upcycle trend in E&E
- Higher demand for petroleum products, chemicals and chemical products, manufacturers of metal, palm oil and mining goods

Inflation (%)



- Gradual shift towards a targeted subsidy mechanism
- Risks come from fluctuation in exchange rates and supply-related factors, such as global commodity prices, geopolitical uncertainties and climatic conditions

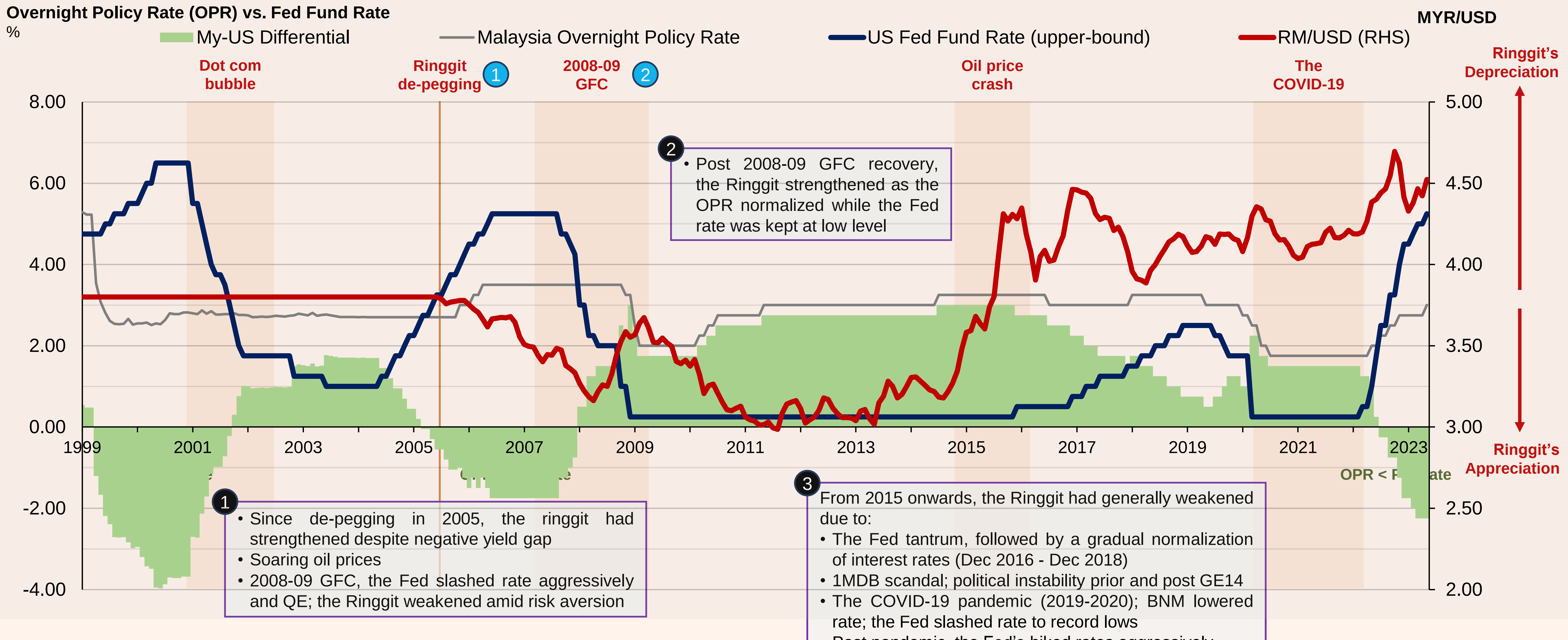
Unemployment Rate (%)



- Stable domestic and external economy
- More demand-driven skill training programmes
- More conducive working environment for women
- Expanding social protection coverage to all workers

Source: DOSM; MOF

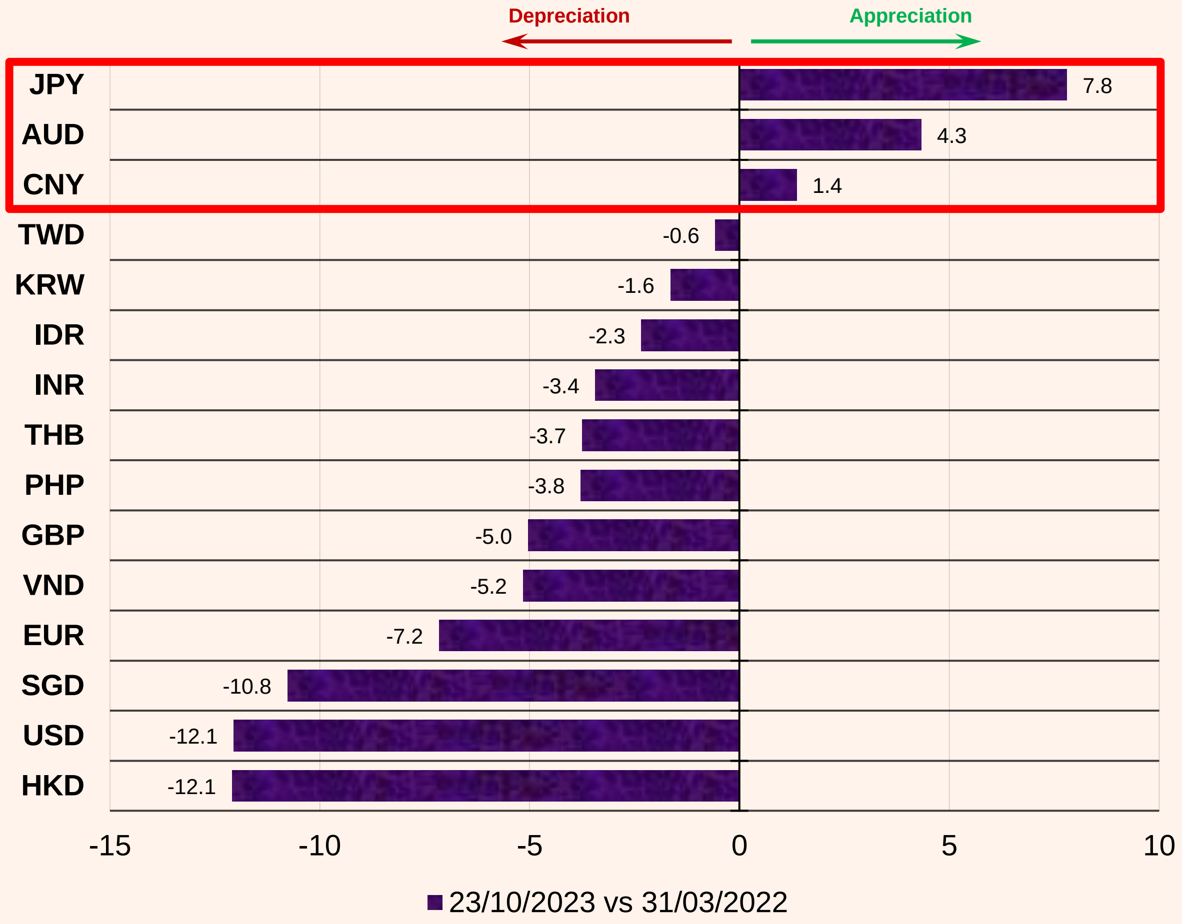
Since 2015, the Ringgit had depreciated by an average of 0.9% pa against the US dollar in 2005-2023 (appreciated in nine years: 2005, 2006, 2007, 2009, 2010, 2012, 2017, 2019, 2020)



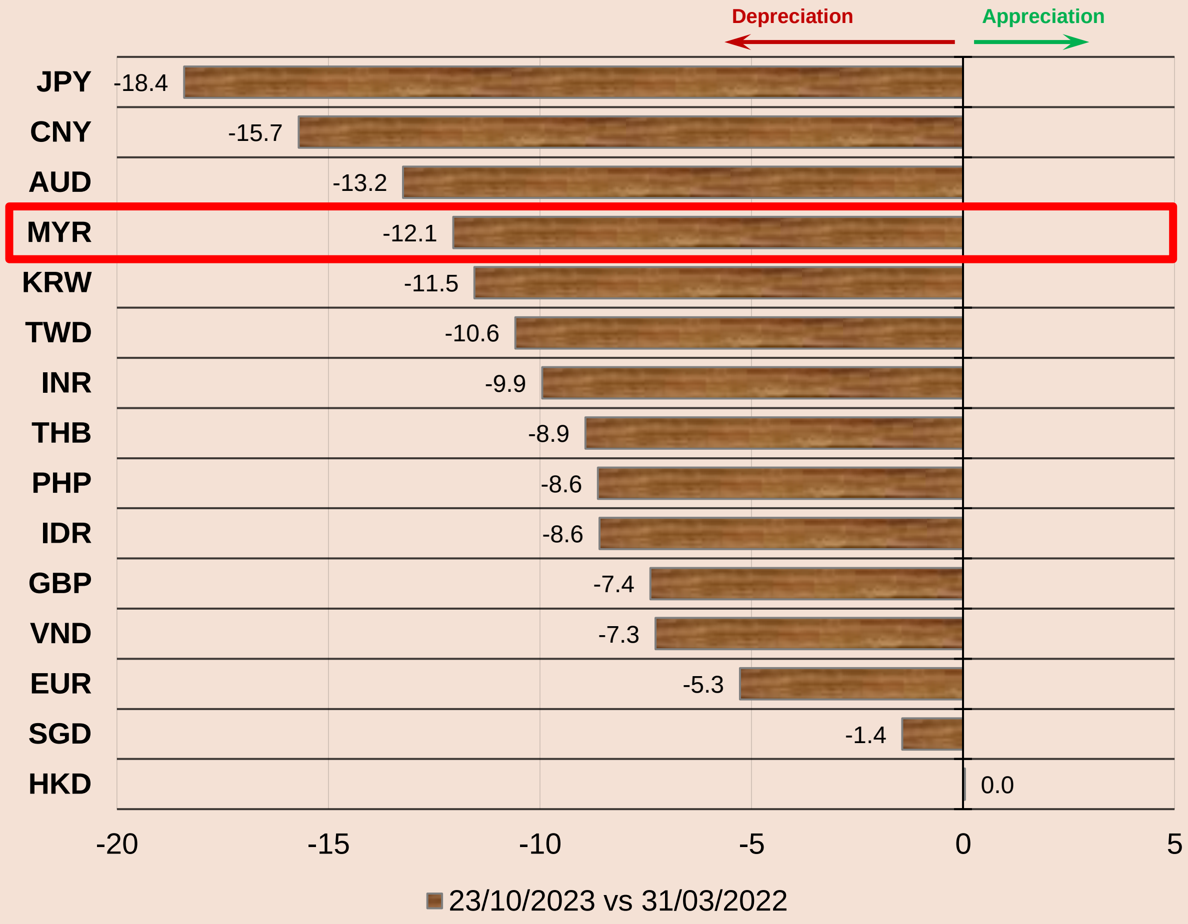
Note: For currency other than Ringgit against USD, cross rate applied.
Source: Bank Negara Malaysia (BNM)

The ringgit's Movement Since the Fed's Rate Hike Cycle Starting in March 2022

The Ringgit against major and regional currencies (%)



Major and regional currencies against the USD (%)



Note: For currency other than Ringgit against USD, cross rate applied.
Source: Bank Negara Malaysia (BNM)

The ringgit is massively undervalued

Have our fundamentals deteriorated?

Malaysia

Positive:

- **Economic growth prospects –** Growing, albeit downside risks
- **Budget deficit –** Reducing
- **Monetary policy –** OPR held steady
- **Banking system –** Strongly capitalised
- **Capital market –** Deep and diversified
- **Approved MIDA investment –** High levels

Negative:

- **Inflation outlook –** Rising
- **BOP current account surplus –** Decreasing
- **FG debt and liabilities –** Rising

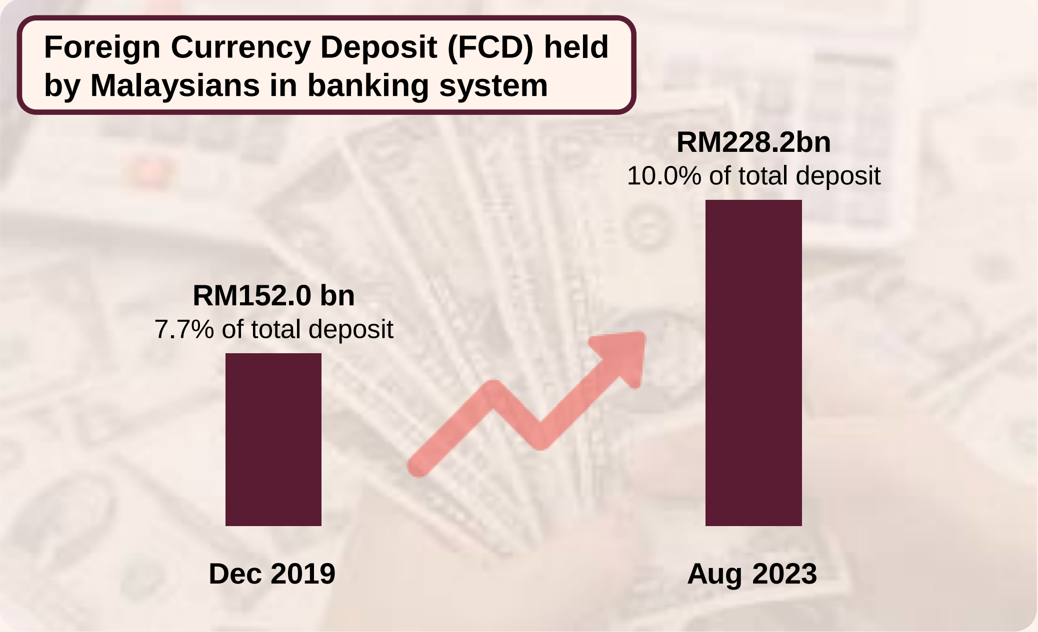
Neutral:

- **FDI flows –** Uneven
- **Portfolio flows in equity and debt** – Net selling of equities; lower debt inflows

External sources

Negative:

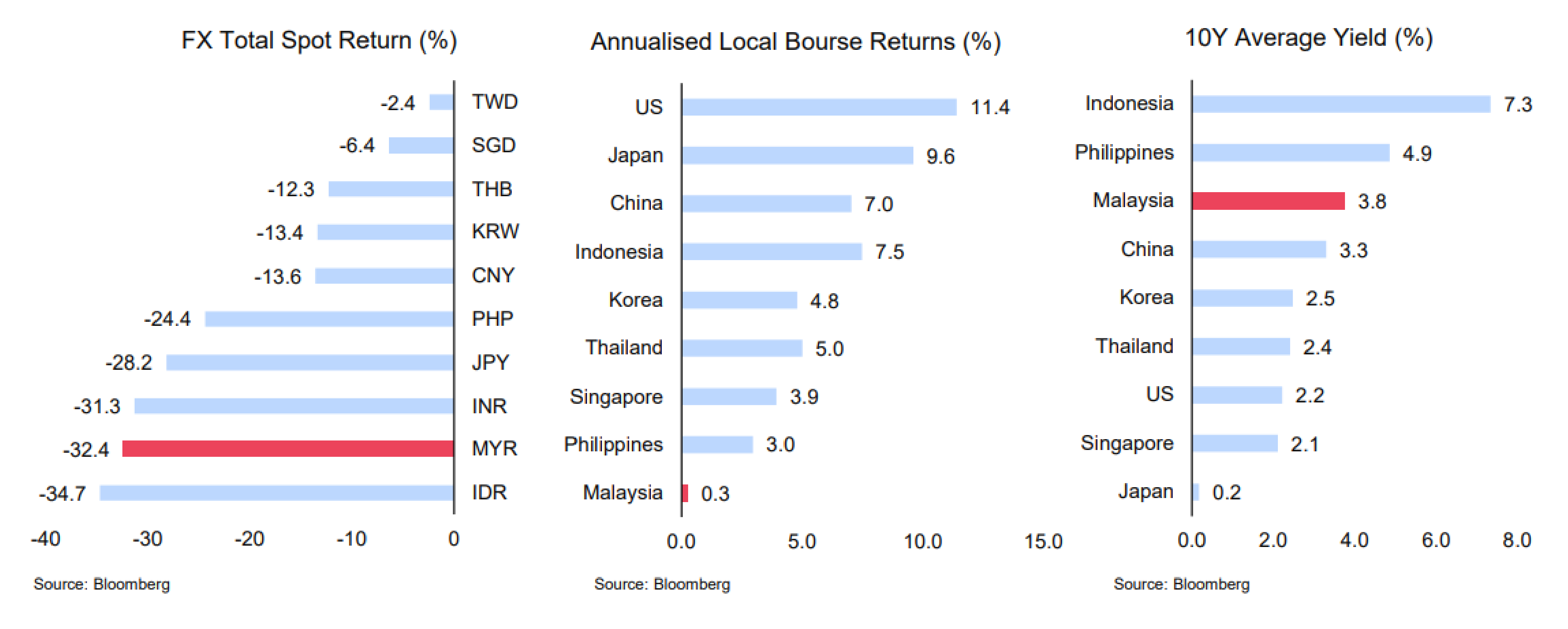
- **US interest rate to stay high and for longer**
- **Wide interest rate differential; better return on investment**
- **Market concerns and investors' sentiment**



Returns on MYR Assets over 10-Year Period

The Ringgit Conundrum

- Will the Ringgit reverse its depreciation trend against the US dollar?
- Relative interest rate and inflation; exports performance; balance of payments
- Budget deficit and debt sustainability
- Political stability; market sentiment
- Structural reforms key to supporting the economy and ringgit



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