Star Special

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ECONOMIC OUTLOOK 2024

The economy 2024

The government aims to create a sustainable, inclusive and buoyant economy in line with the Madani framework

[1] Includes change in stocks
Source: Finance Ministry

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TheStargraphics

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Economy set to improve

Better prospects in global trade to spur growth

THE Malaysian economy is expected to strengthen in 2024, growing in the range of 4% to 5% amid expansion in all sectors and better prospects in global trade.

In its Economic Outlook 2024 report, the Finance Ministry said that world trade is likely to improve next year in tandem with stronger trade activities.

This in turn would benefit Malaysia, whose economy is heavily dependent on trade.

The Finance Ministry also said that efforts will be intensified to strengthen Malaysia's agility in keeping pace with the fast-changing environment.

This would require a paradigm shift and innovation culture to enhance economic growth, it added.

"The continuation of strategic projects, digitalisation, improved productivity and advanced manufacturing will further stimulate the growth of the economy in the medium term.

"All economic sectors are expected to benefit from the recent policies such as the National Energy Transition Roadmap, the New Industrial Master Plan 2030 and the Medium-Term Review of the 12th Malaysia Plan, which are in tandem with the Ekonomi Madani framework," the ministry said.

Breaking down by economic sectors, the Finance Ministry forecast the services sector to grow by 5.6% in 2024, driven by expansion in all subsectors.

In addition, vibrant tourism-related activities as well as continuous consumer spending are expected to further spur the growth of the sector.

In comparison, the services sector is projected to grow by 5.5%.

Meanwhile, the manufacturing sector is expected to expand by 4.2% next year, as compared to 1.4% in 2023.

The improved growth rate is driven by better performance in both export and domestic-oriented industries.

The export-oriented industries are expected to benefit from the recovery of external demand with the electrical and electronics segment projected to surge, primarily driven by memory products.

Moving up: Crude palm oil price is forecast to average within the range of RM4,000 to RM4,500 per tonne in 2024.

Similarly, domestic-oriented industries are anticipated to grow steadily, backed by higher output in transport and construction-related segments, in tandem with better consumer spending and business activities.

The agriculture sector is poised to grow by 1.2% in 2024, as compared to 0.6% this year, driven by expansion in most subsectors, particularly oil palm, other agriculture and livestock.

With minimal impact expected from the El Nino phenomenon and labour conditions returning to pre-pandemic level, the oil palm production is projected to increase.

"Furthermore, increased matured areas especially in Peninsular Malaysia and higher oil extraction rate arising from more frequent harvesting rounds are also expected to support the subsector's growth," stated the Finance Ministry.

It added that crude palm oil price is forecast to average between RM4,000 and RM4,500 per tonne in 2024, as compared to 2023's average of RM3,500 to RM4,000 per tonne.

The construction sector is forecast to increase by 6.8% in 2024 as compared to 6.3% in 2023, driven by continuation of large scale projects and affordable housing.

As for the mining sector, a rebound of 2.7% in growth is expected after the sector is projected to contract by 0.8% this year.

Development trajectory leading to a sustainable future for nation

THE Just Transition concept will be rolled out within the realm of climate action and equitable development, in line with the Madani Economy framework.

This approach holds the promise of harmonising these issues as the nation grapples with the entwined challenges of achieving a high-income nation status while managing its natural heritage as well as safeguarding the rakyat.

The Economic Outlook 2024 Report said it would be imperative for individuals, governments, corporations and civil societies to unite in shaping Malaysia's development trajectory.

The urgency of the climate crisis demands resolute action and a just transition provides a framework for action that traverses borders and sectors.

It demands a collective commitment from local communities to global platforms, encapsulating a future where social fairness and environmental sustainability intertwine seamlessly.

The report said that guided by the principles of Just Transition and the Madani Economy framework, Malaysia will chart a development trajectory leading to a sustainable future that is comprehensive and environmentally conscious, through the equilibrium between economic growth, climate mitigation and adaptation as well as social justice.

The concept of Just Transitions underscores the essential interplay surrounding nation building, climate mitigation and adaptation as well as social justice.

In the case of Malaysia, a nation blessed with social unity and well-being, ecological diversity and abundance as well as progressive economic and technological advancements, the concept of Just Transitions forge a pathway towards a sustainable future that leaves no one behind.

The climatic events and geopolitical shifts have been forcing nations to respond diversely in order to manage resource availability and avoid falling into a recession.

As the world reacts to these challenges, unilateral actions are being undertaken, translating into increasing economic pressures globally.

The European Union (EU) has just implemented new trade regulations, the Carbon Border Adjustment Mechanism and EU Deforestation-free Regulation, which will affect many products and businesses coming into the EU.

Other countries are also looking into introducing similar regulations, which further highlight the need for readiness by Malaysian industries to prepare for climate transition.

Many multinational corporations are bound by the home-country environmental, social and governance (ESG) laws and regulations, obligating compliance across the entire value chain. International investors are also increasingly looking to support strong ESG portfolios.

Due to these emerging trends, many nations are pushing to promote sustainable and ethical governance in policies and implementations, said the report.

Equally pivotal are environmental justice and equity, especially in balancing the complexity of reducing environmental impacts with mitigating adverse environmental consequences on society.

The demand for energy, water and food further accentuates the significance of having a just transition. Vulnerable communities are often the most susceptible to disruptions of these vital resources. Deliberate planning and collective endeavours are pivotal in building resilience to benefit all segments of society, while ensuring continuous availability of these resources.

Good governance takes precedence in budget

IN line with the visionary Madani framework, Budget 2023 is premised on three main pillars, namely inclusive and sustainable economic growth, institutional reform and good governance and combating inequality through social justice.

For this purpose, a total allocation of RM386.3bil was set aside, of which RM289.3bil was to be used for operating expenditure (OE) while RM97bil would go towards development expenditure (DE).

As of July this year, 49% of the total allocation has been utilised, with RM166.7bil spent on OE and the remaining on DE.

Among the initiatives that were identified and implemented under the three pillars included comprehensive measures to support businesses in particular micro, small and medium enterprises that were badly affected by the pandemic.

The government also looked at outlining measures to accelerate infrastructure projects, empower public-private partnerships and prioritise the digital agenda.

This was done to shape a dynamic foundation for the nation's growth, while demonstrating a strong commitment to transparency and accountability.

Budget 2023 also looked at eradicating hardcore poverty, fostering harmony and providing high-quality basic amenities for all. As of July 2023, RM10.4bil in the form of cash assistance had been given to 15.9 million recipients.

All these efforts have been in line with the Madani Economy which aims to be the framework to help build a better Malaysia while establishing the nation as an economic leader in Asia.

Starting from next year, fiscal reforms through the Fiscal Responsibility Act will be necessary to support economic growth while catering to the needs of the people.

This goal has been reflected in many policies including the National Energy Transition Roadmap, New Industrial Master Plan 2030 and the 12th Malaysia Plan Mid-Term Review.

Hence, in line with this goal, Budget 2024 will have three focus areas, namely delivering reforms to enhance governance and the public delivery system, transforming the economy and businesses and elevating the wellbeing of the rakyat.

However, some of the challenges Malaysia may face moving forward are a less robust global economic outlook and its fiscal constraints.

Hence, starting from next year, fiscal reforms through the Fiscal Responsibility Act will be necessary to support economic growth while catering to the needs of the people.

For this, incentives and funding will be given to promote a higher standard of economic success while initiatives will be undertaken to strengthen Malaysia as an internationally competitive investment destination.

Malaysia will also aim to energise innovation in Islamic economy, mainly through Islamic finance and the halal products sector.

Furthermore, initiatives to encapsulate the Madani framework's goal of "raising the ceiling" and "raising the floor" will see different efforts being undertaken to elevate the rakyat's quality of life.

This will include ensuring the lower income groups continue to be assisted with the cost of living challenges through targeted subsidies.

Budget 2024 will mark the beginning of Malaysia's journey towards a sustainable, inclusive and buoyant economy as envisioned in the Madani framework.

Budget 2024 will be geared towards articulating immediate initiatives and reforms for implementation next year.

On track to hit targeted social assistance

Positive spillover effects beyond economic stability key

IN 2023, about RM63.8bil or 3% of gross domestic product (GDP) was allocated for subsidies and social assistance.

Almost 60% of that is used for broad-based fuel and electricity subsidies while the rest for Sumbangan Tunai Rahmah.

This is targeted at the hardcore poor, who are considered eligible based on the poverty line index.

Although spending on subsidies and social assistance rises every year, its share from 2020-2022 is considered small at 2.2%. In comparison, the Organisation for Economic Co-operation and Development nations typically spend 10% of GDP on cash benefits only.

For that, Malaysia received a social assistance score of 2.1.

It lags significantly behind its Asean peers such as Singapore (100), Thailand (54.3), Vietnam (24.6), the Philippines (22.4) and Indonesia (16.5), according to Bank Negara's Economic Outlook 2024 Report.

Despite the current gaps in Malaysia's cash transfer programme, its effectiveness cannot be overlooked as social assistance has positive spillover effects beyond economic stability.

Malaysia's development journey began in 1957 and it has since made significant progress with several programmes.

The most recent, Malaysia Madani, will see the country making headway in achieving its goal of becoming an high-income and inclusive economy.

The report said Malaysia's current cash transfer programme is focused more on charity-based models, which can leave certain segments of the population without adequate coverage.

It is therefore necessary to transition from narrowly-targeted and stigmatising approaches to a more comprehensive development programme.

Focus has to be given on addressing underlying vulnerabilities instead of explicitly targeting poverty, it added.

Risk associated with life cycles such as childhood, maternity and old age, coupled with risk of disability can be targeted with a more holistic cash transfer programme.

Moving forward, a potential developmental model consisting of a combination of income-tested as well as categorically-based programmes can be an optimal solution in addressing valuable groups, it said.

This should include allowances for the hardcore poor, low income, child, old persons, maternity and people with disability.

For that, it is crucial to relook, reform and redesign the delivery of social assistance, in particular cash transfer to ensure inclusive and equitable protection.

This includes introducing an overarching act to oversee social protection as a whole for social assistance, social insurance and labour market intervention.

Without this act, accountability of social assistance programmes in particular will continue to remain ambiguous and thus impacting effective implementation including cash transfer programmes, the report said.

It added that the implementation of the cash transfer programme can be centralised under a single existing agency to address fragmentation issues, reduce implementation cost and standardised eligibility criteria for income tested aid.

For successful implementation, an autonomous data management approach is needed.

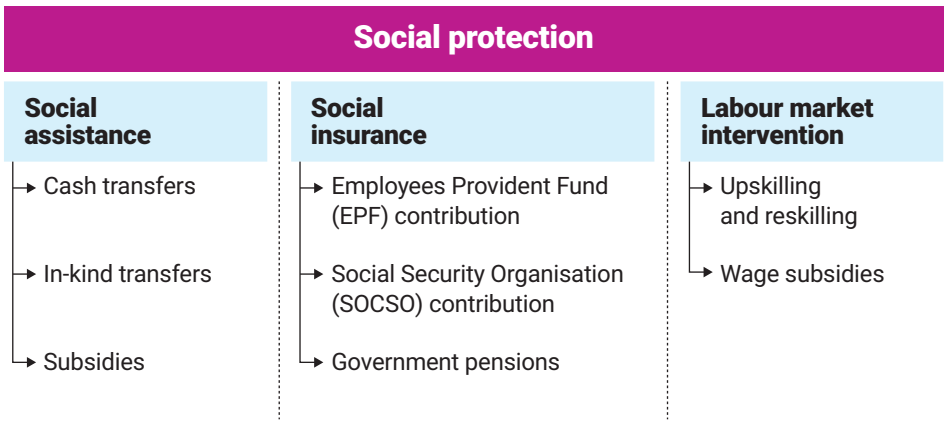
The government is dedicated to ensuring that every segment of society benefits from the nation's economic prosperity irrespective of gender, ethnicity, social economic status or geographical location.

Therefore, Budget 2024 will prioritise initiatives that nurture future generations and improve standard of living.

This entails focusing on efficiency in the implementation of initiative and programs though empowering good governance and fostering an agile public service delivery.

Collectively, adopting a whole-of-nation approach will elevate the overall competitiveness and safeguard the nation's wealth, ultimately enhancing the wellbeing of the rakyat towards sustainable, prospectus and high income nations, it added.

Malaysia's social protection framework



Source: Finance Ministry

The Star graphics

Focus on energy transition, digital and high-technology industries

QUALITY investments in high value-added industries will be propelled by the strategies and measures under the National Energy Transition Roadmap (NETR), New Industrial Master Plan 2030 (NIMP 2030) and the Mid-Term Review (MTR) of the 12th Malaysia Plan (12MP) as guided by the Madani Economy framework.

This is especially in energy transition, digital and high-technology industries that will ultimately create more high-income employment opportunities towards sustainable economic growth, according to Bank Negara in its Economic Outlook 2024 Report.

Without swift and effective reforms in investment-related policies, Malaysia is far from achieving its aspiration to be in the top 30 largest economies.

Notwithstanding the ongoing economic recovery post-pandemic, Bank Negara said several challenges persist in balancing the private consumption and investment that necessitate a renewed focus on investment-related policies.

Therefore, Malaysia needs to prioritise investment in innovative and advanced technology to achieve higher productivity and sustainable economic growth.

The central bank said the revival of private investment and foreign direct investment (FDI) is crucial in driving towards higher productivity.

Inflows of FDI can encourage technological adoption and increase the production capacity of economic sectors by forming supply chain linkages with local firms, including micro, small and medium enterprises (MSMEs). This in turn can lead to higher domestic investment and economic growth.

The government has also implemented a responsive fiscal and accommodative monetary policy to boost private investment.

In the long term, the government is focusing on structural reform strategies to strengthen economic growth

which include fostering industries with high-growth value, enhancing technological advancement through innovation, expediting digitalisation and developing a future ready workforce.

These strategies will further promote sustainable private investment for the future, added Bank Negara.

Moving forward, the Madani Economy framework will serve as a foundation in revitalising the economy to ensure the accumulated wealth is benefitted equitably among the rakyat.

In order to become a globally competitive investment destination, efforts will be intensified to strengthen investment promotion, enhance incentive measures to attract high quality investments, upgrade existing infrastructure and develop human capital to meet investor needs.

To date, several government policies have been introduced to complement the framework such as the NETR, NIMP 2030 and MTR of the 12MP. The NETR will guide investments in energy efficiency, renewable energy, hydrogen, bio-energy, green mobility as well as carbon capture, utilisation and storage.

As for NIMP 2030, it encompasses six goals namely increasing economic complexity, creating high-value job opportunities, extending domestic linkages, developing new and existing clusters, improving inclusivity and enhancing environmental, social and governance practices.

Meanwhile, the MTR of 12MP will focus on accelerating the development of high growth value industries, attracting quality investments in technology based industries as well as enhancing technological adoption and digitalisation.

Making progress in navigating high-impact economic growth

DIRECT investments play an important role in the economic growth of Malaysia.

Direct investments recorded a net outflow from 2008 to 2015 but turned positive from 2016 to 2022 helped by higher foreign direct investment (FDI).

Direct investment data include investments into the country by foreign interests and investments abroad by domestic investors and companies.

Malaysia remains an attractive investment destination despite macro headwinds and weaker global growth forecast for 2023 and 2024 by international agencies like the World Bank and the International Monetary Fund.

Data from the balance of payments show FDI inflows into Malaysia remain resilient during shocks like the Covid-19 pandemic of 2020 and the financial global crisis of 2008 to 2009 when the country attracted RM13.3bil and RM5.1bil net inflows respectively.

FDI surged to RM50.4bil in 2021 and a record RM74.5bil in 2022, driven by policies placing emphasis on FDI, a strong recovery and the spillover effects of trade diversion activity due to tensions between China and the United States.

The jump in inflows was led by multinational corporations relocating to circumvent high tariffs imposed and also by the growth of high quality investments mainly in the manufacturing sector, the Economic Outlook 2024 Report stated.

FDI has a positive effect on generating employment with some 44.7% or 700,000 employment opportunities created in 2000 to 2022 sourced from foreign owned projects in the country.

Such investments also help enhance employee skills, transfer of knowledge and technological capabilities and enhance the competitiveness of local companies on the global scale.

From a sectoral basis the focus of FDI into Malaysia has shifted from commodity based to manufacturing and services sector over the past decades.

Some 97% of FDI in 2022 was in the manufacturing and services sector due to a strategic change in policy direction towards value added activities and development of the services sector as the main engine of growth of the economy.

The evolution of the manufacturing sector from a conventional industrial production process to an inclusive concept also helped, the report noted.

Malaysia's main source of FDI is from Asian countries like Hong Kong and Japan, which accounted for 35% or RM497bil of the total FDI inflows between 2010 to 2022.

But for 2022, North America accounted for 49.8% of total FDI inflows into Malaysia.

Direct investments abroad (DIA) by Malaysian businesses has averaged RM35.7bil from 2005 to 2019 but the weaker ringgit has seen DIA trend lower from 2016 to 2018 and drop sharply in 2020 due to the Covid-19 pandemic before rebounding post pandemic.

DIA are primarily in the services sector such as financial and insurance and takaful. South-East Asia remains the main destination for DIAs of Malaysian companies, growing from 44% of DIA in 2010 to 50% in 2020.

DIA to Europe has gained traction, growing from 16% of total DIA in 2010 to 36% in 2022 while to North America it has risen from 0.5% of total DIA to 6.9% over the same period driven primarily by the attractive investment returns.

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Towards a progressive and successful nation

Government plans to push ahead with supportive fiscal policy

THE government will continue its counter-cyclical and supportive fiscal policy to propel the socio-economic agenda towards becoming a progressive and successful nation.

The federal government's revenue collection in 2024 is estimated to increase further to RM307.6bil or 15.6% of gross domestic product (GDP) driven by higher tax collection.

Tax revenue continues to be the major contributor and is expected to grow by 6.4% to RM243.6bil, attributed to expansion economic activities, higher company profitability and better employment conditions.

Meanwhile, the non-tax revenue is projected to decrease to RM64bil, mainly due to lower dividend from PETRONAS, reflecting reduced dependency on petroleum-related revenue.

In addition, several measures will be implemented, which include the introduction of capital gains tax for disposal of unlisted shares by companies and implementation of e-invoicing.

The total expenditure is projected to be lower at RM393.8bil or 19.9% of GDP, particularly attributed to the lower financial commitment resulting from the absence of 1MDB bond redemption.

The operating expenditure (OE) allocation is expected to record RM303.8bil or 15.4% of GDP, while the development expenditure (DE) allocation is projected at RM90bil or 4.5%.

The government will also undertake the subsidy rationalisation programme in which the savings will be partly channelled to enhance the social safety net programme.

Meanwhile, the 12th Malaysia Plan programmes and projects such as the construction of highways and railways, flood mitigation programme, health facilities and educational institutions will be accelerated to bolster economic activities.

Overall, in line with anticipated higher revenue and lower expenditure, the fiscal deficit level is expected to reduce further to 4.3% of GDP and remain on the consolidation path.

This in turn will provide ample fiscal space to cushion against global uncertainties and reduce debt burden in the long term. Consequently, the primary balance is estimated to record a lower deficit of 1.8% of GDP.

In the medium-term, total revenue is projected at RM986.9bil or 15.6% of GDP, mainly contributed by non-petroleum revenue which is forecast at RM816.3bil or 12.9% of GDP. Petroleum-related revenue is estimated at RM170.6bil or 2.7% of GDP.

Meanwhile, the total expenditure indicative ceiling is estimated at RM1,206.2bil or 19.1% of GDP with OE allocation projected at RM927.1bil or 14.7% of GDP, while DE at RM279bil or 4.4% of GDP.

Overall, the fiscal deficit is expected to consolidate further with the overall balance averaging at 3.5% of GDP.

Despite moderate economic growth due to external uncertainties and prolonged geopolitical tensions, the government's fiscal position in 2023 is expected to remain strong.

The fiscal stance remains responsive in providing sufficient fiscal support to ensure the rakyat's well-being is safeguarded and economic reform continues to be undertaken without jeopardising the fiscal consolidation plan.

However, operating expenditure also increased, particularly emoluments, debt service charges as well as supplies and services.

In addition, the government continues to provide substantial subsidies for petroleum products, electricity and basic necessities to mitigate the rising cost of living especially for vulnerable groups.

Concurrently, the government is finalising its targeted subsidy mechanism plan to reduce leakages and wastages.

Meanwhile, the acceleration of programmes and projects post-pandemic has resulted in higher development spending, particularly in the economic sector.

Nevertheless, the fiscal deficit in the first eight months of 2023 improved to record RM46.8bil compared with RM51.9bil in the corresponding period of 2022, attributed to better revenue collection performance, coupled with rigorous expenditure management.

Federal Government Financial Position (2022 - 2024)

	RM mil			Change (%)			Share of GDP (%)		
	2022	2023[3]	2024[4]	2022	2023[3]	2024[4]	2022	2023[3]	2024[4]
Revenue	294,357	303,200	307,600	25.9	3.0	1.5	16.4	16.4	15.6
Operating expenditure	292,693	300,140	303,800	26.4	2.5	1.2	16.3	16.2	15.4
Current balance	**1,664**	**3,060**	**3,800**	-	-	-	**0.1**	**0.2**	**0.2**
Gross development expenditure	71,574	97,000	90,000	11.4	35.5	-7.2	4.0	5.2	4.5
Less: Loan recovery	1,407	700	800	41.8	-50.2	14.3	-	-	-
Non development expenditure	70,167	96,300	89,200	10.9	37.2	-7.4	4.0	5.2	4.5
Covid-19 Fund [1]	30,979	-	-	-17.9	-	-	1.7	-	-
Overall balance	**-99,482**	**-93,240**	**-85,400**	-	-	-	**-5.6**	**-5.0**	**-4.3**
Primary balance [2]	**-58,213**	**-47,140**	**-35,600**	-	-	-	**-3.2**	**-2.5**	**-1.8**

[1] A specific trust fund established under Temporary Measures for Government Financing (Coronavirus Disease 2019 (COVID-19)) Act 2020 to finance economic stimulus packages and recovery plans.
[2] Excluding debt service charges.
[3] Revised estimates.
[4] Budge: estimates, excluding 2024 Budget measures.

Source: Finance Ministry

The Star graphics

Subsidies: A double-edged sword that must be dealt with carefully

SUBSIDIES have been an important policy instrument in many countries from economic, social and political perspectives.

According to the World Trade Organisation, a subsidy is defined as a financial contribution by a government that provides a benefit to its recipients.

Subsidies, whether provided to producers or consumers, are a form of transfer payment. Unlike expenditures, subsidies do not generate direct value-added

In general, subsidies are one of the mechanisms to foster economic development and help disadvantaged groups in the effort to further boost business investment and improve quality of life.

Subsidies, if implemented appropriately, are able to counteract market failures and externalities to attain economic efficiency.

In times of economic recession or higher global commodity prices, subsidies can assist in stabilising the prices of essential goods to protect households against sudden price shocks and subsequent inflationary pressures.

Nevertheless, subsidies can also be harmful to the economy as they may cause price distortion and further contribute to market imperfection, causing wastage and misallocation of resources.

In addition, inefficient and untargeted subsidy implementation may exacerbate inequality due to disproportionate benefits accorded to certain households and industries.

Subsidies can impose a significant burden on the government as they require a large amount of allocation.

Certain subsidies, such as those provided for fossil fuel, undermines the environmental agenda as it promotes carbon emissions and worsens air pollution.

Subsidies act as a double-edged sword, while they may benefit certain individuals or industries, they can also have negative and unintended consequences.

As global commodity prices increase, subsidies can cushion the impact of higher prices of goods and services yet potentially increasing the government financial burden and reducing fiscal space.

A broad definition of subsidies is required to capture different forms of government intervention, both explicit and implicit.

The International Monetary Fund generally classifies subsidies based on the following seven categories: cash subsidies (direct government payment to producers or consumers); credit subsidies (interest subsidies or soft loans); tax subsidies (reduction of specific tax obligations); equity subsidies (government equity participation); in-kind subsidies (government provision of goods and services at below-market prices).

The categories also include procurement subsidies (government purchases of goods and services at above-market prices); and regulatory subsidies (implicit payments through government regulatory that alter market prices or access).

According to the World Bank, Malaysia needs to phase out broad-based subsidies and move towards subsidies through a cash transfer mechanism to better support vulnerable groups.

The mechanism is proposed to be applied gradually and reviewed periodically to avoid an abrupt subsidy removal that could lead to a sharp increase in inflation.

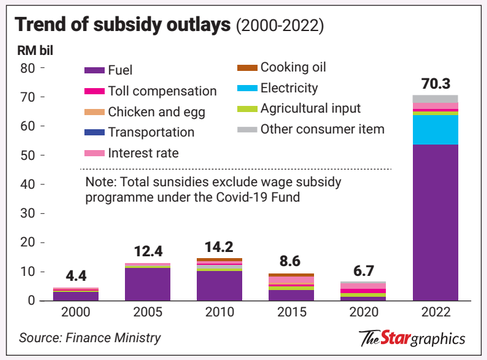
The subsidy rationalisation aims to enhance efficiency in the economy and rebuild fiscal space while minimising the risk of economic shocks.

In 2022, total subsidies recorded an all-time high of RM70.3bil, as compared to an average of RM15.2bil for the past 10 years and almost equal to the development expenditure of RM71.6bil.

This was triggered by, among other things, the Covid-19 pandemic, geopolitical tension and climate change, affecting global commodity prices.

In addition, the government also provided RM24,3bil for a one-off wage subsidy programme during the pandemic period as an effort to sustain jobs and reduce retrenchment.

Overall, this programme has benefitted close to 360,000 employers to retain about 1.95 million local employees.



Federal government expects 3% growth in revenue in 2023

DESPITE a sluggish global economy in 2023, the federal government anticipates a 3% growth in estimated revenue, reaching RM303.2bil from the RM294.4bil collection in 2022.

Bank Negara in its Economic Outlook 2024 Report said this estimate, revised higher by 4% or RM11.7bil compared to the initial forecast of RM291.5bil, reflects the positive impact of increased tax revenue collection.

Tax revenue is anticipated to increase by 9.7% to RM229bil, constituting 12.4% of the gross domestic product (GDP), up from RM208.8bil in 2022.

This lift is attributed to improved income tax collection, measures outlined in Budget 2023 and continuous administrative initiatives to broaden the revenue base.

In contrast, non-tax revenue is expected to reach RM74.2bil, equivalent to 4% of GDP, marking a 13.3% decrease from the RM85.6bil recorded in 2022, primarily attributed to reduced returns from investment income.

In the fiscal landscape, direct tax is poised for a 12.7% surge to RM173bil, fuelled by robust corporate profitability, stable employment conditions and sustained wage growth.

Companies income tax is expected to remain as the largest contributor to direct tax collection, anticipated to increase by RM16.3bil or 19.8% to record RM98.4bil.

Likewise, individual income tax is estimated to surge by 17.6% to RM39.7bil, in line with the revision of the individual income tax rate announced in Budget 2023.

However, petroleum income tax is forecast to fall by 12.4% to RM20.5bil, in tandem with the expected moderation in global crude oil prices averaging at US$80 per barrel in 2023, compared to the US$100 per barrel in 2022.

Meanwhile, indirect tax is anticipated to see a modest increase of 1.3%, reaching RM56bil. Within this, sales and service tax is poised for a notable 9% expansion, totalling RM34.2bil, while excise duty is also expected to grow by 4.3%, amounting to RM13.1bil.

In contrast, both import duty and export duty are projected to decrease by 4.8% and 31.4%, settling at RM3bil and RM1.8bil, respectively.

Regarding non-tax revenue, investment income is expected to decline, influenced by an anticipated lower dividend receipt from Petroliam Nasional Bhd (PETRONAS), dropping to RM40bil from RM50bil in 2022 and from Bank Negara, decreasing to RM2.75bil from RM5bil in 2022.

Additionally, receipts from licences and permits are expected to amount to RM15.5bil compared to RM15.6bil in 2022, reflecting reduced proceeds from motor vehicle licences and levies on foreign workers.

Looking ahead, Bank Negara anticipates the federal government to experience a modest 1.5% growth in revenue, reaching RM307.6bil in 2024, driven by improved economic prospects.

Tax revenue, anticipated at RM243.6bil, is expected to continue as the primary contributor, constituting 79.2% of total revenue.

This is supported by measures to broaden the tax base and enhance compliance.

Direct tax is projected to increase by 6.9% to RM185bil, while indirect tax collection is anticipated to rise by 4.7% to RM58.6bil.

Non-tax revenue, however, is estimated to decline by 13.8% to RM64bil, reflecting lower investment income, with anticipated PETRONAS dividend receipt further dropping to RM32bil.

The government is committed to boosting revenue, closing tax gaps and improving efficiency through various initiatives.

These initiatives includes optimising incentives and enhancing compliance, with a focus on transparency through medium-term revenue strategy and tax expenditure reporting.

Debt-to-GDP ratio estimated at 63% this year

THE country's debt-to-gross domestic product (GDP) ratio is estimated to record about 63% in 2023 and dip to slightly below 60% in 2028, under a baseline scenario based on Malaysia's debt sustainability analysis (DSA).

Likewise, the annual gross borrowing size reflects the fiscal consolidation trajectory with gross financing needs (GFN)-to-GDP ratio forecast to gradually reduce to 5.6% in 2028 compared with 12.3% in 2023.

Under the DSA framework, the threshold of debt burden for emerging markets is set at a level of 70% for debt-to-GDP ratio and 15% for GFN-to-GDP ratio.

A country's debt sustainability is determined by the government's ability to serve all its current and future payment obligations without requiring exceptional financial assistance or experiencing default.

The DSA illustrates that higher economic growth and fiscal surplus are the two main determinants which could quickly bring down the nation's debt level.

The government has applied the DSA framework developed by the International Monetary Fund and the World Bank as a risk assessment tool since 2019.

The DSA assessment serves to guide the government's fiscal conduct as well as borrowing and debt strategy, to enable the country to absorb any shocks in the medium- and long-term, and avoid payment difficulties.

As such, conducting sensitivity analyses or stress tests enable governments to evaluate potential impacts of various macro-fiscal shocks on the level of indebtedness.

Consequently, appropriate policy measures can be tailored and implemented ahead in order to mitigate the effects if such circumstances arise.

In addition to the macro-fiscal and contingent liabilities stress tests, the DSA also provides a comprehensive risk assessment in evaluating the current debt profile of a country.

Under this assessment, the external debt financing requirement is categorised as high risk since it surpasses the upper early warning threshold which increases the government exposure to foreign exchange risk.

In terms of debt profile vulnerabilities, the share of short-term debt has significantly improved in 2023 as compared to 2021 and no longer poses a high risk to the country.

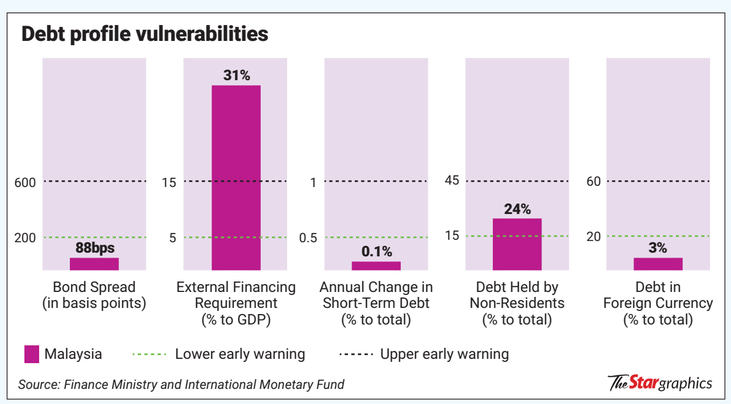
This is due to the high repayment of treasury bills which leads to a reduction in the outstanding of short-term financing instruments.

Even though the external debt financing requirement remains at high risk, the possibility of defaulting in the offshore borrowing is unlikely.

This is due to the sizable asset availability and good creditworthiness among external debt issuers.

Furthermore, prudential requirements on liquidity and funding risk management imposed by the regulator also support to alleviate the risk.

Overall, the identified risks are manageable given the implementation of fiscal measures but continuous effort should be taken in order to rebuild wider fiscal buffers, thus ensuring all shocks are within the low-risk parameters.



Unravelling the conundrum of consumption taxes a key aspect

CONSUMPTION taxes play a crucial role in complementing income taxes as a primary source of funding for the government to uphold nation-building, which will contribute towards economic stability and social well-being.

Malaysia has undergone significant changes in its consumption tax system, experiencing both the sales tax and service tax (SST), which is a single-stage tax system, and goods and services tax (GST), or value-added tax, which is a multi-stage tax model, over the past five decades.

The government has noted that the choice between the SST and GST hinges on the nation's economic goals, administrative capabilities and the need to achieve an optimal balance between revenue generation and the promotion of fairness and equity among the rakyat.

The SST, characterised by its narrower scope that concentrates on specific goods and services, serves as a subtle strategy in consumption tax.

The GST model, on the other hand, broadens the tax base; enhances compliance and transparency; improves efficiency and business-friendliness; and mobilises efficient revenue collection.

Despite the differences in structures, both the SST and GST offer an important fiscal tool for the country to fund the government's programmes and projects for the benefit of the people.

The consumption tax Malaysia has in place currently is the SST, which was reintroduced on Sept 1, 2018, to replace the GST, which was abolished in May 2018.

The reintroduction of the SST incorporated enhancements to minimise the inherent weaknesses associated with this model and increase tax efficiency.

Nevertheless, the model's narrower tax base could mean the SST would generate less revenue for the government.

Conversely, the GST has the potential to generate more revenue by virtue of its broader tax base.

The GST was implemented in April 2015 to replace the old system of SST, which had been in place since 1972.

The aim was to streamline the tax structure, as well as to enhance revenue collection, reduce tax evasion and conform to international best practices.

The then-GST was designed to incorporate several features to make it less regressive at a low standard rate of 6%, which included the zero-rating of certain supplies of essential items and exempting certain supplies such as education, healthcare, financial services and public transport.

The adoption of a consumption tax system offers numerous advantages, including promoting savings and streamlining tax administration.

However, similar to other taxation models, consumption taxes have its own challenges such as susceptibility to evasion and avoidance, being regressive and creating administrative burden.

Hence, it is essential to understand and address the various challenges in order to reap the benefits, while mitigating potential pitfalls.

Essentially, an effective consumption tax policy has the potential to enhance the overall tax system that is economically efficient and socially equitable.

Financing the country's external debt

Easing maturity profile, meeting investors demand crucial

DEBT management strategies have proved to be vital in today's climate.

The federal government's borrowing programme is needed to finance the fiscal deficit and refinance maturing debt.

According to Bank Negara in its Economic Outlook 2024 Report, total gross borrowings for 2023 are estimated to be at RM228.5bil with RM93.2bil for deficit financing, and RM135.3bil for principal repayments.

"The principal repayments consists of Maturing Malaysian Government Securities (MGS) at RM38.3bil, Malaysian Government Investment Issues (MGII) at RM39bil, treasury bills at RM54bil, government housing sukuk at RM3.6bil and offshore borrowings at RM0.3bil," the report said.

As at the end of August 2023, the government had raised RM166.5bil through 26 issuances from both MGS and MGII.

It also raised RM37bil through 16 issuances of treasury bills. The fundraising activities this year were conducted mainly through auctions followed by private placements.

The government offers a wide range of instruments with maturities ranging from three months to 30 years to help smoothen debt maturity profiles while meeting investors demands.

Other factors also play a role fiscally, for example when the US Federal Reserve raised its Federal Fund Rates by a cumulative 525 basis points to the range of 5.25% and 5.5%, recording the highest level in two decades.

Additionally, Malaysia's public sector debt at the end of June 2023 had also increased 4% to RM1.54 trillion on the account of higher federal government debt which constituted 74.3% of total debt.

Bank Negara's Monetary Policy Committee then increased the overnight policy rate by 125 basis points from 1.75% to 3%.

Meanwhile, the report said Malaysia's external debt increased by 6% to RM1.21 trillion at the end of June 2023 on the back of high offshore borrowings, non-resident holdings of ringgit-denominated debt securities and non-resident deposits.

"Overall it remained manageable given its favourable maturity, with medium and long-term debt constituting a higher share at 58.2% compared to short-term debt at 41.8%," the report noted.

Additionally, Malaysia's public sector debt at the end of June 2023 had also increased 4% to RM1.54 trillion on the account of higher federal government debt, which constituted 74.3% of total debt.

Moving forward, in line with the Madani Economy framework, the government will aim to restructure and rebuild the country's fiscal resilience and capacity.

"The government has also committed to prudent debt management to reduce debt and liabilities exposure, as well as realising the need for a robust financing strategy," the report said.

Hence, its gross borrowings are estimated to be lower at 10% of gross domestic product (GDP), while efforts will be focused on ensuring a well spread debt maturity profile by reducing the issuance of short term instruments and managing refinancing risks.

On the other hand, the federal government debt is projected to be around 64% of GDP at the end of next year, mainly from financing development projects as well as the National Fiberisation and Connectivity Plan.

Diversified economy among key strengths

THE Covid-19 pandemic and ensuing economic ramifications have led to an almost unprecedented worldwide sovereign borrowing boom, causing governments' debt levels breaking an all-time high.

Notwithstanding, the federal government debt level has also surged from 52.4% of gross domestic product (GDP) before the pandemic to 60.3% in 2022, to finance Covid-19 stimulus and recovery packages.

The government is cautious of the key risks that continue to rattle global and domestic markets which may affect investor sentiment.

Thus, the stability of the rating and any probable changes are closely monitored.

Ratings are published by various independent credit rating agencies (CRAs), in which the three main global agencies are Fitch Ratings, Moody's Investors Service and S&P Global Ratings.

These CRAs use a transparent methodology for assessing national credit risk.

Malaysia's rating was initiated by Moody's in 1986 at *BAA1*, which was subsequently upgraded to *A3* in 1990 and peaked at *A1* in 1995.

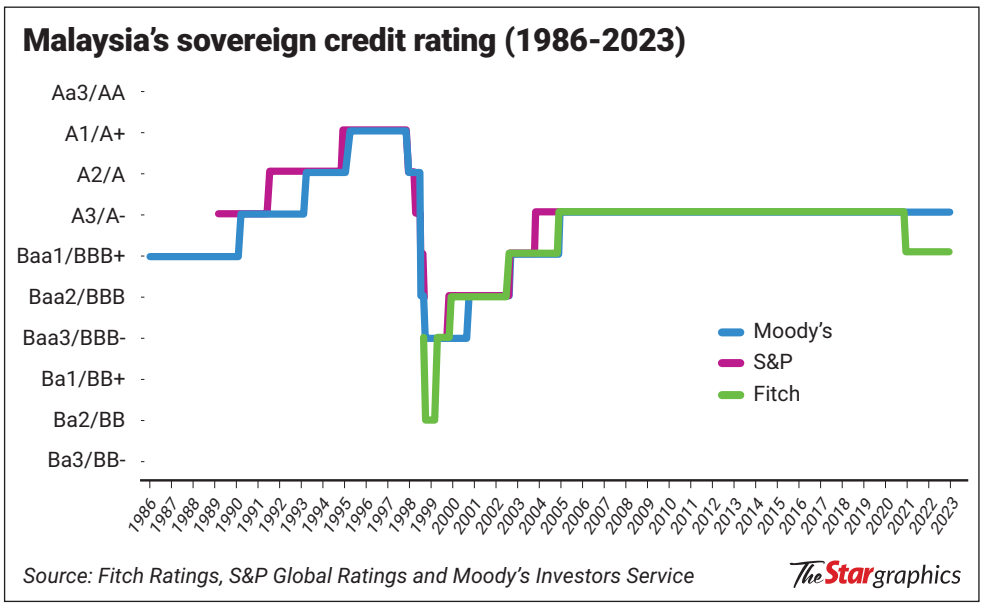
S&P began rating Malaysia at *A-* in 1989, whereas Fitch first issued the rating of *BBB-* in 1998.

Consequently, the Asian financial crisis in 1997 and 1998 caused significant pressure on Malaysia's ratings as well as most of the nations in the region, which resulted in several notches of rating downgrade.

Currently, Malaysia is rated at *A3* (Moody's), *A-* (S&P) and *BBB+* (Fitch) which carry a "stable" outlook.

According to these CRAs, while there are various drivers for the present rating, fiscal performance is emphasised as the most important element for Malaysia, cited as a credit weakness.

This is mainly a result of Covid-19 stimulus and recovery packages that saw a deviation from the previous focus on fiscal consolidation, compounded by a low revenue base.



Therefore, fiscal performance is closely monitored as the CRAs are expecting Malaysia to revert to its previous path of consolidation.

Malaysia's key rating strengths identified by the CRAs include diversified economy; resilient growth; overall predictable and stable institutions; established and strong banking system; as well as low exposure to foreign currency-denominated government debt.

As the sovereign credit rating reflects Malaysia's creditworthiness, it also sets the bar for domestic issuers who are seeking to tap international markets.

Hence, market participants and the government continuously observe the stability and momentum of the rating as any change could affect the economy.

A sovereign credit rating downgrade can have an adverse impact on the bond market, which may trigger negative sentiment in the foreign exchange as well as stock markets and influence foreign direct investment decisions.

Malaysia remains vigilant to safeguard and ultimately improve the country's relative standing with the CRAs as well as strengthen its position among rated peers.

Meanwhile, the federal government tax revenue stood at an average of 12.8% of GDP in the past 10 years.

As a result, ratings will be under pressure if there is a continuous rise in public debt and contingent liabilities, lower revenues, slower fiscal consolidation and unpredictable political circumstances.

Hence, fiscal performance is a crucial driver that can steer Malaysia back to the previous path of fiscal consolidation.

Government backing for nation building

AS Malaysia continues its journey towards becoming a developed economy, the establishment of an extensive infrastructure network becomes imperative for nation building and economic advancements, necessitating substantial fiscal backing from the government.

Nevertheless, the government will cautiously use quasi-fiscal instruments to finance strategic projects or unsolicited vendor driven arrangements to reduce risk exposure and unnecessary fiscal burden.

In addition, the government has outlined fiscal sustainability reforms to improve governance and enhance public finances as key enablers towards achieving sustainable and inclusive growth, in line with the Madani Economy framework.

Debt and liabilities exposure consist of federal government debt, committed guarantees and other liabilities, namely financial commitment from public-private partnership (PPP) and private finance initiatives projects.

As at the end of June 2023, total debt and liabilities exposure were at RM1.5 trillion or 81.6% of gross domestic product (GDP).

As at the end of June, total outstanding government guarantee (GG) stood at RM317.9bil or 17.2% of GDP. During the first half of 2023, there were several GG financing disbursements for the continuation of public transportation infrastructure projects under Danalnfra Nasional Bhd, Prasarana Malaysia Bhd and Malaysia Rail Link Sdn Bhd.

Nonetheless, these disbursements were offset with repayments by other GG recipients, namely Lembaga Pembiayaan Perumahan Sektor Awam, Perbadanan Tabung Pendidikan Tinggi Nasional, Suria Strategic Energy Resources Sdn Bhd and Pengurusan Air SPV Bhd.

The infrastructure segment remains the highest GG recipient at 57.5% mainly on public transportation projects such as Mass Rapid Transit, East Coast Rail Link, Light Rail Transit 3 and highways.

Services segment represents the second largest GG recipient at 28.8% particularly for education, housing and finance. The remaining segments include investment holdings (6.2%), utilities (5%) and plantation (2.5%).

The 10 main GG recipients represent more than 85% of total outstanding guarantees. In addition, more than 90% of the GGs is denominated in ringgit, hence minimising currency risk exposure to the government. The weighted average maturity for GG financing stood at 11.4 years, in which 52% of total GGs' maturity period is more than 10 years.

Given the limited fiscal space, the government will continue to support ongoing people centric infrastructure projects financed through quasi-fiscal instruments while mitigating further liabilities exposure.

Meanwhile, GG issuances are being re-evaluated and further prudent measures have been imposed on new GG issuances to manage risks and exposures.

The government will enhance the reporting of financial risks, including guarantees approved under Act 61 and Act 96 in line with the upcoming Public Finance and Fiscal Responsibility Act (FRA).

Furthermore, numerical limits on government financial guarantees will be introduced, in accordance with international best practices on prudent fiscal and risk management.

In the medium term, other liabilities are expected to moderate due to measures which include re-evaluating the PPP approach through PPP 3.0 framework, enhancing the existing policy frameworks and guidelines, as well as ensuring sufficient allocations for repayment of obligations and commitments.

The PPP 3.0 will emphasise on implementing user-pay projects with minimal financial requirements from the government. In addition, the upcoming FRA will impose the need to assess the government's risk exposure and formulate the corresponding mitigation plan.

Ensuring sufficient liquidity

Financial sector maintains prudent lending activities

EXCESS capital buffers stood at RM142.3bil as at end-July 2023, while the Common Equity Tier-1 Capital, Tier-1 Capital and total capital ratios remain stable at 15.1%, 15.6% and 18.8%, respectively, well above the Basel III minimum regulatory levels 2.

Lenders continued to maintain sufficient liquidity with a healthy liquidity coverage ratio of 154.8% and supportive of credit intermediation activities with a stable aggregate loan-to-fund ratio of 82%.

The banking sector maintained prudent lending activities during the first seven months of 2023. For that period, the expansion in total loan outstanding moderated by 4.2% year-on-year (y-o-y) to RM2.1 trillion mainly due to the slower growth in the business segment.

On the household front, financial assets totalled RM3 trillion as at the end of June and exceeded total household debt by 2.05 times.

With improvements in income and employment conditions, most borrowers have exited the repayment assistance programme and resumed loan payments. These developments will augur well for household financial position.

At the same time, the formulation of the Consumer Credit Act non-bank credit providers and credit service providers offering credit products or credit services and management agencies will be subjected to authorisation, governance and proper conduct requirements.

These measures are expected to strengthen consumer protection in Malaysia and heighten the level of professionalism within the industry.

Gross funds raised in the capital market during the first seven months of 2023 rose by a commendable 11.4% y-o-y to RM184.1bil, attributable to increased fundraising activities by the public and private sectors, which grew by 10.8% and 12.4% to RM114bil and RM70.1bil, respectively.

The private sector's gross funds raised grew by 11.8% y-o-y to RM67.1bil despite the tighter financing environment, while at the same time funds raised via the domestic equity market during the period were recorded at RM2.9bil.

For the public sector, Malaysian Government Securities (MGS) issuances increased by 8.3% y-o-y to RM57.4bil, while Malaysian Government Investment Issues (MGII) increased by 13.5% y-o-y to RM56.6bil.

The outlook for MGS, MGII, as well as corporate bonds and sukuk, remains positive, buoyed by expectations of sustained economic growth and the anticipated conclusion of Bank Negara's rate hiking cycle this year.

In the meantime, the local equity market was affected throughout the first eight months of 2023 by external challenges, including uncertainties surrounding global economic growth which dampened investor sentiment.

In July, the government reduced the stamp duty rate on shares traded on Bursa Malaysia from 0.15% to 0.1% as one of the measures to reinvigorate the domestic capital market.

Perhaps as a consequence, the FBM KLCI recovered, and coupled with the launching of the Madani Economy framework, supported by foreign buying interest and impending policy announcements, the index rose and closed notably at 1,462.03 points on Aug 9.

Subsequently, improved local job openings data and stimulus measures announced by China also helped uplift the local index.

As at end-July 2023, the total assets of Islamic banking expanded by 8.1% to RM1.3 trillion, accounting for 36.4% of the market share. Meanwhile, the total Islamic financing outstanding grew by 9.1% y-o-y to RM844.1bil as at end-July.

The outlook for Islamic banking remains promising, supported by a mature ecosystem that promotes social and financial inclusion.

The announcement of two Islamic digital banks in 2022 and intensification of digitalisation efforts undertaken by existing Islamic banks will further enhance access to affordable and quality financial solutions, particularly for the underserved and unserved market segments.

Social finance is also envisioned to play a greater role in complementing public sector finance, commercially-driven financial solutions and corporate social responsibility activities of financial institutions to promote greater social resilience.

For example, social finance programme iTEKAD has expanded to include 11 participating banks, onboarding over 3,000 participants while mobilising over RM40mil of diverse social finance funds in 2023.

The Islamic Capital Market (ICM) continues to lead Malaysia's capital market in fundraising and investing. As at end-July, the domestic size of ICM was valued at RM2.4 trillion, accounting for 64.4% of total capital market size.

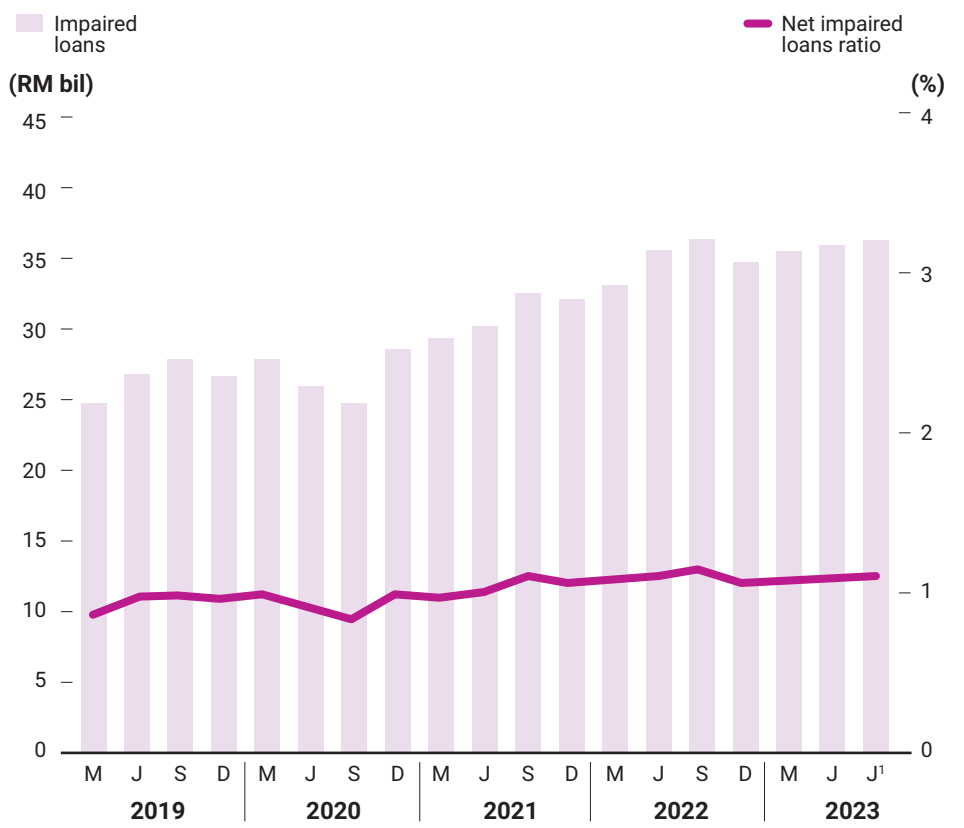
Furthermore, the size of ICM increased further by 7.9% with the sukuk market becoming more attractive to investors.

Despite near-term volatility, the medium-to-long-term outlook for global sukuk is expected to be positive amid sustained Islamic investors' demand, issuer refinancing needs, and government support in core markets.

As at end-July 2023, a total of 807 or 81.8% out of the total of 987 public listed companies are syariah-compliant.

The market capitalisation of syariah-compliant securities stood at RM1.1 trillion or 65.1% of the overall total market capitalisation of listed companies on Bursa Malaysia.

Banking system: Impaired loans and net impaired loan ratio
(end period)



[1] End-July 2023
Source: Bank Negara
TheStargraphics

Addressing the longstanding issue of low-income workers

AS Malaysia aspires to become a high income nation, various measures have been undertaken to accelerate the shift to a high technology and knowledge intensive economy.

The initiatives have borne fruit as evidenced by the encouraging economic growth trend recorded over the past few decades.

Nonetheless, the absolute benefit of the growth has yet to be translated into fair income distribution, including the need to address the longstanding low labour income issue.

Malaysians are finding it increasingly difficult to cope with the rising costs due to structural wage stagnation, thereby placing an added burden on the government to provide subsidies and cash transfers to alleviate pressures on the rakyat.

The introduction of the minimum wage in 2013 was a significant progressive step, but more needs to be done if the Madani Economy framework's target of raising compensation of employees to 45% of gross domestic product is to be realised.

A study by Khazanah Research Institute in 2023 on wage growth from 2010 to 2019 produced three key findings.

First, the Malaysian labour market is dependent on policy interventions such as minimum wage to ensure equitable and inclusive wage growth.

The introduction of the minimum wage in 2013 was a significant progressive step, but more needs to be done if the Madani Economy framework's target of raising compensation of employees to 45% of gross domestic product is to be realised.

The study also finds that wage growth is suppressed and broadly regressive without policy measures.

Second, the effects of the minimum wage are limited to the lowest wage earners, with the middle wage earners experiencing the lowest growth during the period.

In ringgit terms, the wage growth of the middle wage earners is even lower than the growth of the lowest 30% wage earner group.

Third, wage stagnation is found to be a central feature of the Malaysian labour market despite the effects of minimum wage.

The bottom 50% of workers only experienced an increase of the real monthly wage by approximately RM500 during the 2010-2019 period, which translates to a rough increase of RM65 per year.

These findings provide a basis to comprehend the vulnerability of Malaysian households when confronted with the rising costs, as their wage increments have arguably been insufficient to provide a buffer against future shocks.

While structural challenges are a source of the wage conundrum, dismal wage levels are themselves at the root of trends that feed back to Malaysia's structural problems.

Two prominent trends that are linked to the lack of well-paying employment are brain drain and the increasing levels of non-standard employment such as gig work.

Brain drain, though not rare from a global perspective, severely inhibits the economic and social potential of developing countries.

Based on a study by the World Bank in 2010, about 54% of Malaysians' brain drain were in Singapore.

Higher salary is the predominant motivator in pulling Malaysians to work in Singapore.

Findings from interview sessions highlighted that Malaysians were offered higher salaries and compensation for the same job.

Meanwhile, the Malaysian Employers Federation's Salary Survey For 2022 showed that a manager in the manufacturing industry received a basic monthly salary of RM10,304, while a similar role in Singapore offered S$7,532, which is equivalent to RM24,695.

Likewise, a clerk in the administration and support services would earn a monthly wage of RM2,065, as compared to S$2,000 in Singapore.

Meanwhile, the accommodation and food and beverages sub-sector pays nearly five times more in Singapore.

The wage discrepancies between Malaysia and Singapore is applicable to a wide range of occupations and industries.

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