Dr Mohd Afzanizam Abdul Rashid
Chief Economist

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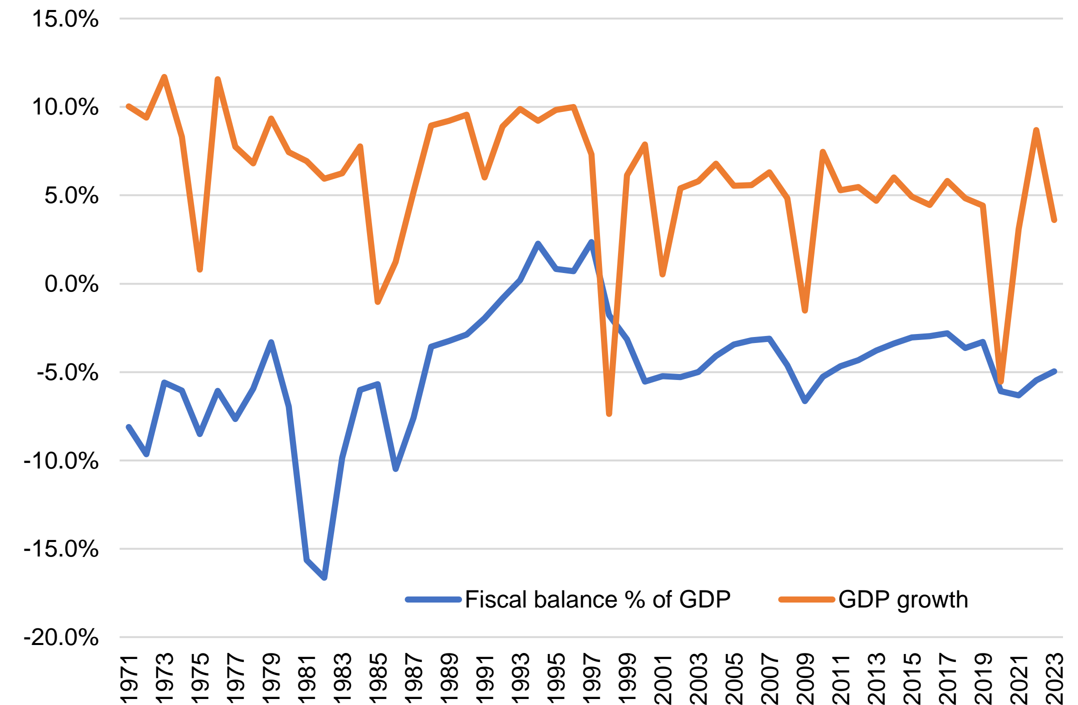
Preview for Malaysia's Budget 2025 – Navigating Fiscal Challenges & Opportunities for Growth.

Malaysia's Budget 2025 will be presented on 18 October 2024. As in previous years, it is important to assess the current state of the federal government's finances and the trajectory for the coming year. The federal government has consistently run fiscal deficits, despite continued positive economic growth. This points to a structural nature of the deficits, signaling that the government's capacity for countercyclical fiscal measures has been significantly constrained.

The federal government only achieved a fiscal surplus between 1993 and 1997, a period when the economy grew at an average of 9.3% annually. The current situation requires attention, as ongoing fiscal deficits not only hamper the government's capacity for countercyclical policies but also diminish overall economic productivity. Persistent deficits have led to private investment being crowded out, resulting in lower productivity levels.

If this situation persists, the economy will be unable to reach its full potential, leading to suboptimal growth. This could hinder the country's progress toward achieving high-income status. Additionally, it may worsen income and wealth inequality, as the benefits of economic growth will disproportionately favor capital owners.



Sources: MOF & CEIC

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Possible measures in Budget 2025

There have been discussions on several measures to boost government revenue, while also aiming to reduce wealth inequality and encourage positive societal behavior. One possibility is the reintroduction of the High Value Goods Tax, which was announced in Budget 2024 but postponed this year. It's likely that the government will include it again in the upcoming budget with a clearer timeline. Although the mainstream media speculated on an inheritance tax, this was dismissed by government officials. Similarly, a carbon tax, which could be vital in reducing greenhouse gas (GHG) emissions, has been discussed publicly, but the government has shown little interest in pursuing it. Additionally, there has been consideration of higher taxes on sugared beverages, in light of Malaysia's rising obesity rates and the associated risks of non-communicable diseases (NCDs) such as cardiovascular illnesses and diabetes.

Given the government's commitment to broadening the tax base, as outlined in the Pre-Budget 2025 Statement issued in July, it is anticipated that a clear timeline for the reintroduction of the Goods and Services Tax (GST) may be set. This would strengthen the government's credibility in its efforts to reduce fiscal deficits, as GST is an efficient and transparent tax system. Historically, GST has proven to generate more revenue than the current Sales and Services Tax (SST). Therefore, it would be logical for the Malaysian government to reintroduce GST, potentially under a new branding.

Regarding entrepreneurship, more measures to improve access to finance are expected. Reports have highlighted a funding gap of RM290 billion for Micro, Small, and Medium Enterprises (MSMEs) and Mid-Tier Companies (MTCs), which could prompt announcements of additional soft loans and guarantee schemes by relevant government agencies. Furthermore, there is likely to be increased allocation for cash transfer programs such as Sumbangan Tunai Rahmah (STR), Sumbangan Asas Rahmah (SARA), and early school financial assistance. These measures aim to mitigate the impact of subsidy rationalization, particularly for fuel, which would have an immediate effect on the cost of living. In line with this, an announcement regarding RON95 subsidy rationalization is anticipated during the upcoming budget presentation. Such measure is urgently required as the country has been recording trade deficits in crude petroleum totaling RM24.0 billion during the first 8 months of this year (8M2023: -RM18.4 billion).

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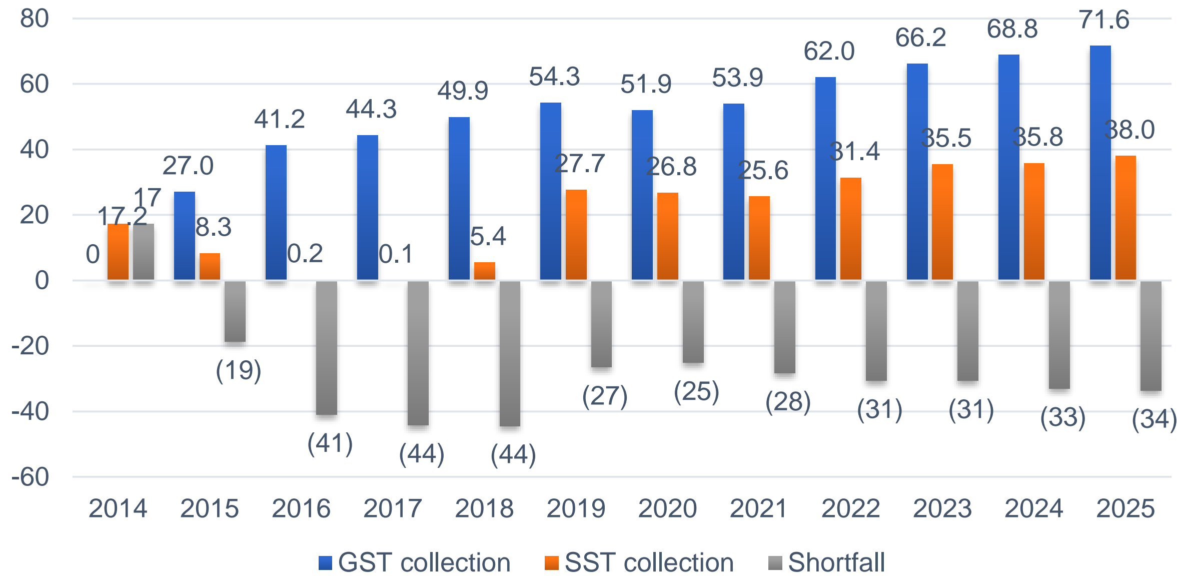
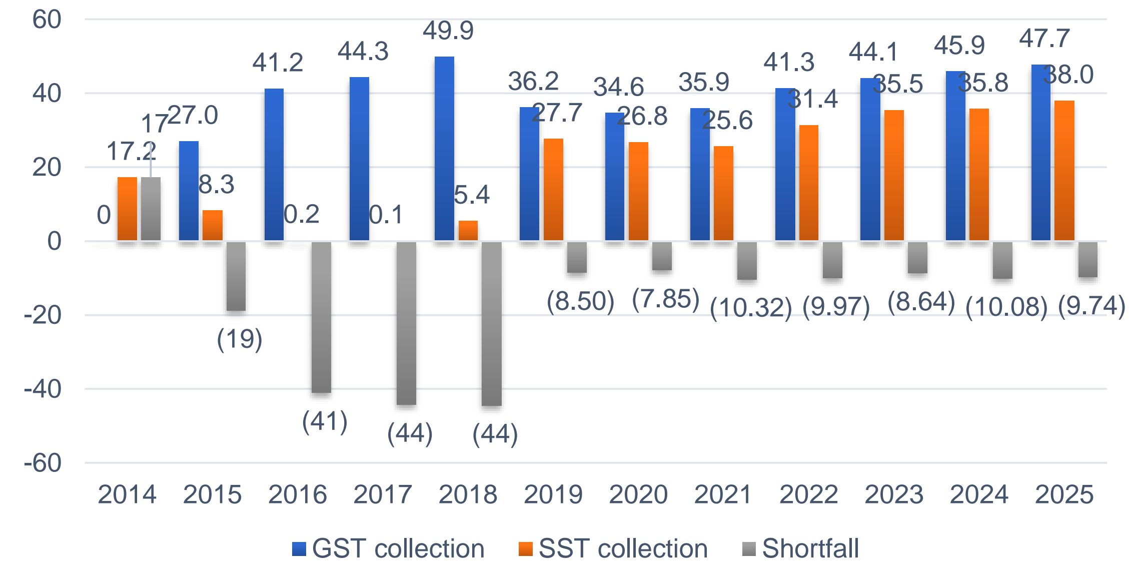
GST vs. SST





Source: BMMB's Economics Department
* GST collection is estimated by multiply the GST rate (6% or 4%) with the nominal private consumption

Ideally, the Goods and Services Tax (GST) should be reintroduced, given the significant revenue boost it can provide. Our estimates show that the current Sales and Services Tax (SST) lags considerably behind GST at 6%, with an average annual shortfall of RM28.3 billion between 2019 and 2024. Even at a 4% GST rate, the SST is still trailing by an average of RM9.1 billion annually over the same period. Should the government decide to reinstate GST, it could significantly reduce fiscal deficits, potentially bringing them down to around 2.1% of GDP at a 6% GST rate, or 3.3% of GDP at a 4% rate. While reintroducing GST requires strong political will, we believe that at some point in the future, this measure will be necessary to effectively address fiscal deficits.

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GST could potentially become a stabilization tools

Dr Mohd Afzanizam Abdul Rashid
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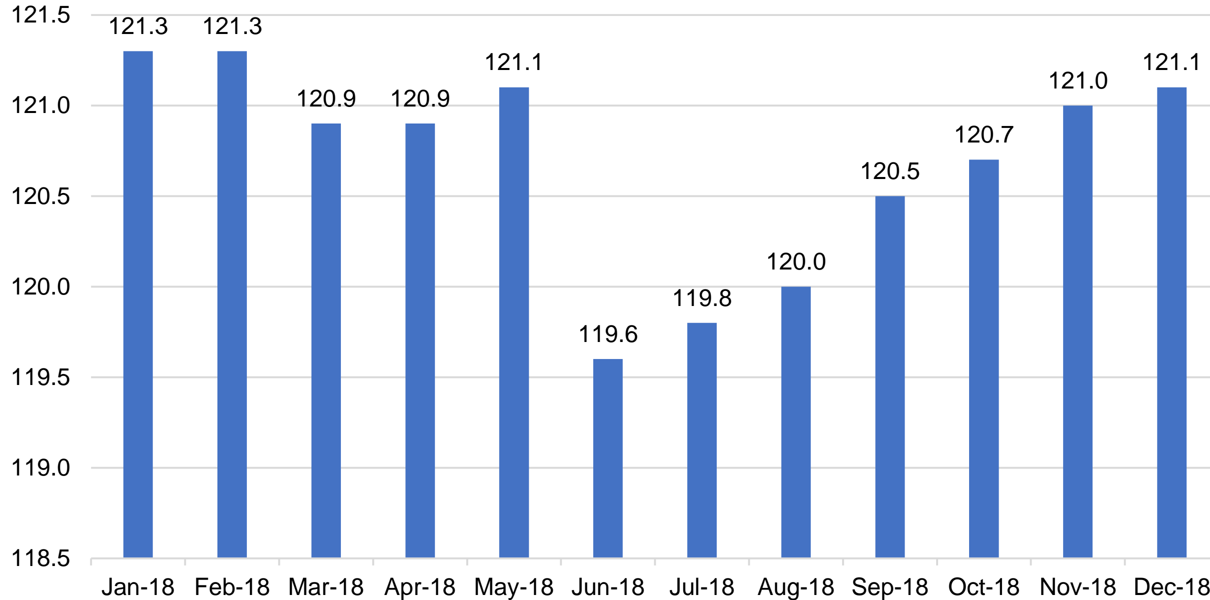

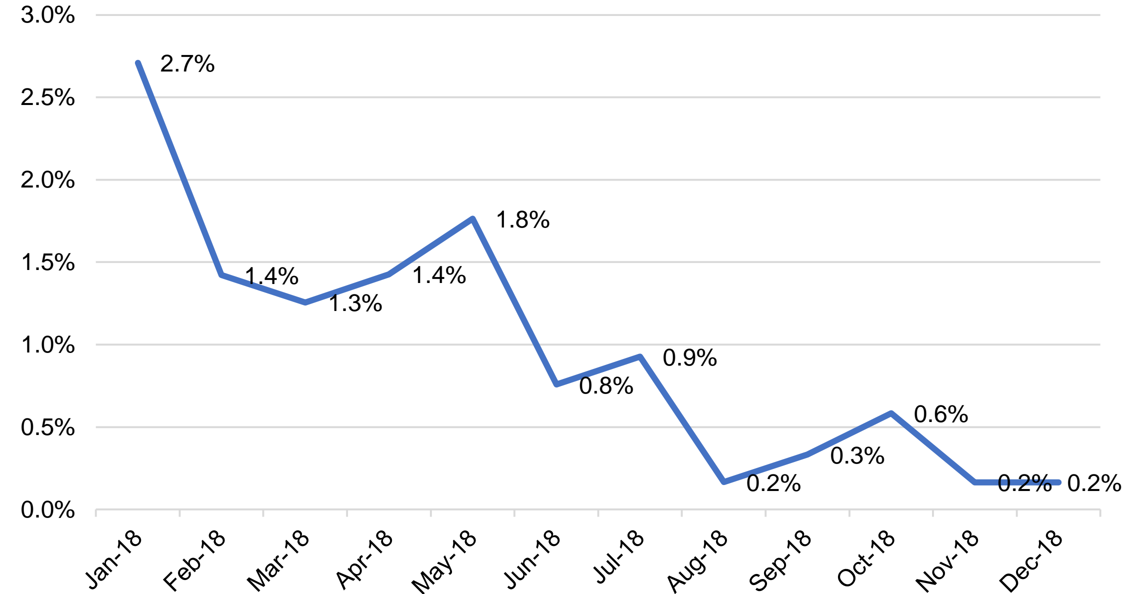

Sources: DOSM & CEIC

During the transition from GST to SST, the government implemented a zero-rated GST between June and September 2018. During this period, the Consumer Price Index (CPI) decreased from 121.1 points in May 2018 to 119.6 points in June, before gradually rising again. Similarly, inflation, measured on a year-on-year (y-o-y) basis, dropped from 1.8% in May 2018 to 0.8% in June. This suggests that GST can serve as a stabilizing tool in response to negative economic shocks. For instance, during the 2007-2008 US subprime crisis, the UK government temporarily reduced the Value-Added Tax (VAT) from 17.5% to 15% in 2010. Therefore, it is timely for the Malaysian government to reintroduce GST, as it would not only boost revenue collection but also provide an additional stabilization tool in times of economic uncertainty.

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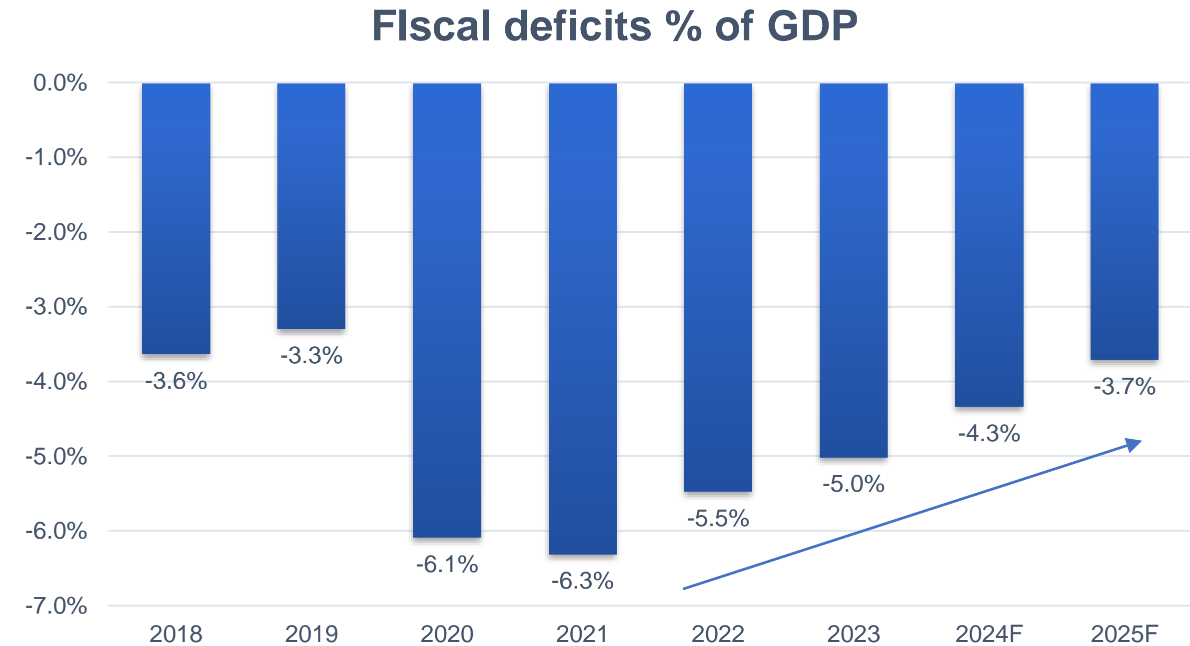
Fiscal deficits could be further reduced to 3.7% of GDP in 2025.

RM Million	2021	2022	2023	2024F	2025F
Revenue	233,752	294,357	314,960	307,600	315,000
%chg	3.9%	25.9%	7.0%	-2.3%	2.4%
Operating expenditure	231,516	292,693	311,267	303,800	308,000
%chg	3.1%	26.4%	6.3%	-2.4%	1.4%
Current balance	2,235	1,664	3,693	3,800	7,000
Gross development expenditure	63,282	70,167	96,091	90,000	85,000
%chg	26.3%	10.9%	36.9%	-6.3%	-5.6%
Less: Loan recoveries	975	1,407	1,000	800	1,000
Net development expenditure	62,307	68,760	95,091	89,200	84,000
%chg	27.6%	10.4%	38.3%	-6.2%	-5.8%
Covid-19 Fund	37,711	30,979	-	-	-
Overall balance	(97,782)	(98,075)	(91,398)	(85,400)	(77,000)
Overall balance % of GDP	-6.3%	-5.5%	-5.0%	-4.3%	-3.7%

Sources: MOF, CEIC & BMMB's Economics Department



The Malaysian economy is projected to grow by 5.0% in 2025, up from an estimated 4.9% in 2024. With the economy expected to remain resilient despite external challenges, this should lead to an improved fiscal position next year. The labor market is likely to maintain full employment, while businesses are expected to continue capital investments to scale up and boost productivity. Overall, the government is anticipated to post a fiscal deficit of RM77 billion or 3.7% of GDP, driven by higher revenue collection and more moderate growth in expenditure, particularly operating expenditure (OE). A downward trajectory in fiscal deficits would likely receive positive responses from Credit Rating Agencies (CRAs) and investors. Additionally, reduced deficits would provide the government with greater fiscal space to invest in areas that enhance national productivity. Therefore, Budget 2025 will be a crucial opportunity to promote responsible and inclusive economic growth.

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