# MORE but not bold REFORMS

Budget 2025 is seen as targeted as it introduces more aid for the poor and taxes the wealthy, with promises of more tax and subsidy rationalisation to come. Critics, however, say bolder reforms are lacking.

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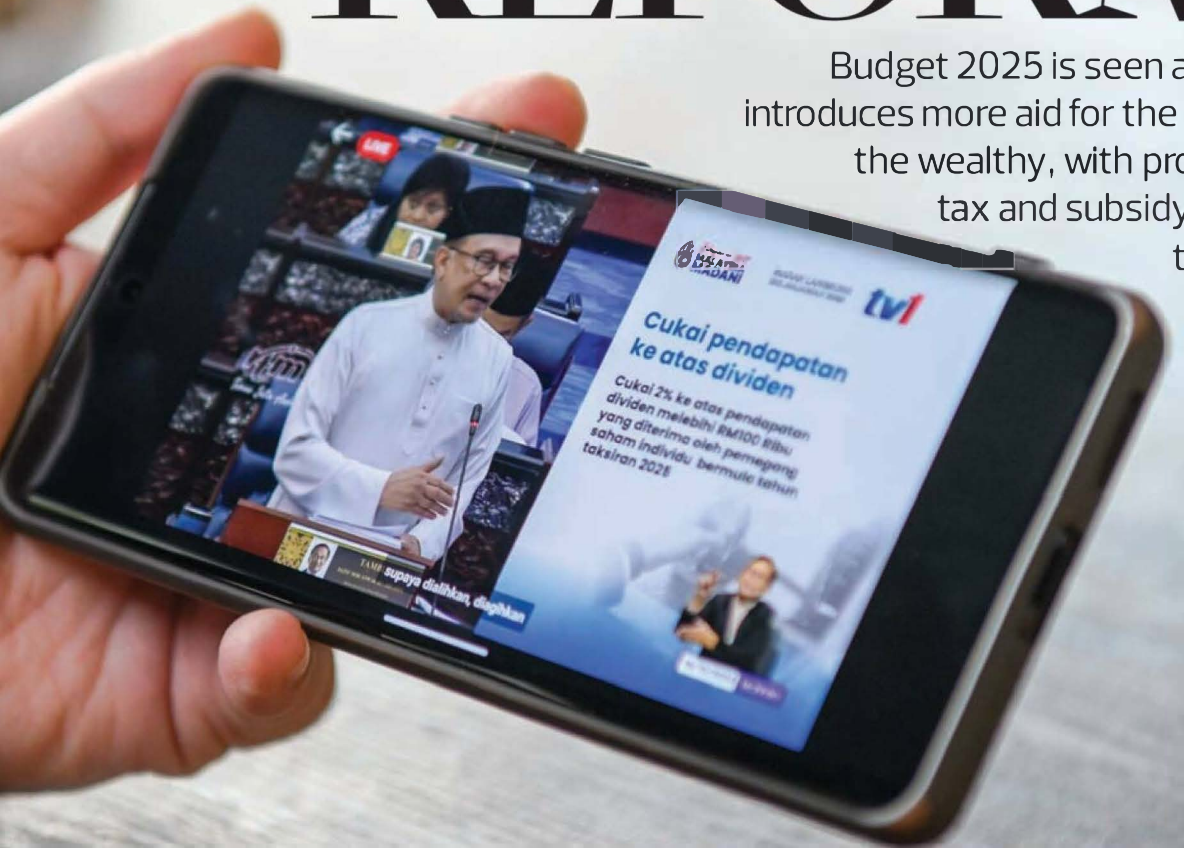


BERNAMA

# MORE but not bold REFORMS

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At a whopping RM421 billion, Budget 2025, which was unveiled last Friday, Oct 18, is 3.3% higher than the revised Budget 2024 estimate of RM407.5 billion, and marks the second time the federal government's budget has breached RM400 billion.

The allocation for operating expenditure is RM335 billion while that for development expenditure stands at RM86 billion.

The measures announced last Friday appear targeted, with the *mahakaya* (wealthy) paying more in taxes soon, while cost of living concerns were addressed with higher handouts for the low-income group.

Similar to Budget 2024, mega infrastructure projects were sidelined in favour of much needed development projects in various states for the rakyat. Sectors with a high multiplier effect that create high-paying jobs were in focus and incentives were given to only strategic sectors that the government is looking to propel.

Was it expected? Largely yes, say economists and tax consultants. There was only one surprise — the 2% tax imposed on dividend income of more than RM100,000 received by individual shareholders.

This targets the high income group without further burdening the other 85% of taxpayers, says KPMG Malaysia's head of tax Soh Lian Seng.

It fits the progressive goals of the Madani Economy while broadening the revenue base, says CIMB Securities economist Michelle Chia.

Dividend income is currently exempted from personal income tax, having been taxed at the corporate level. The introduction of a dividend tax is likely aimed at restoring horizontal equity with regards to a progressive tax system.

"This is tied to concerns about horizontal equity, a fundamental principle of taxation as outlined by the Organisation for Economic Co-operation and Development, which requires taxpayers in similar circumstances to be subjected to a similar tax burden," says Tratax Sdn Bhd executive director Thenesh Kannaa.

One lingering question that remains on tax consultants' minds is the mechanism of the said tax, whether it would be in the form of withholding tax or if it would take shape in some other form.

"Dividend tax has been adopted by many countries. The more commonly adopted approach is in the form of a withholding tax where corporations deduct withholding tax before dividends are paid to shareholders. In other words, the obligation to deduct tax on dividend payment lies with the payer," says Deloitte Malaysia tax and legal leader Sim Kwang Gek.

"Countries like Vietnam, Thailand and Indonesia have dividend withholding tax ranging from 5% to 20%, depending on the profile of the shareholders."

Other revenue expansion methods were also aimed at the high-income group, with Prime Minister Datuk Seri Anwar Ibrahim, who is also the minister of finance, proposing that the sales tax be extended to "non-necessities like imported premium goods such as salmon and avocados" while the scope of service tax will be expanded to include fee-based financial services. This is expected to be done progressively beginning May 1, 2025.

Economists say the larger scope on the sales and service tax (SST) will add RM5 billion to the nation's coffers. However, there is also concern about the cascading effect from SST.

"With every ringgit of revenue collected, there is a ripple effect on the prices paid on goods and services at the retail level, which is difficult to quantify," says Sim.

Thenesh says he is hopeful that the government will take the needful steps, such as the enactment of business-to-business (B2B) exemptions on a timely basis to avoid a cascading effect.

It is worth noting that Anwar mentioned in his speech that the government will engage with the relevant industries and stakeholders before finalising the scope of SST and the tax rate.

### Ending subsidies for 'T15', more handouts for low-income group

Quite early in his speech, the PM highlighted that the government will stop subsidising RON95 petrol for the "T15" group and foreigners. He added that together, these two groups enjoy 40% of the petrol subsidy totalling RM8 billion. However, he proposed that the RON95 petrol subsidy rationalisation begin in mid-2025, eight months from now.

Economists say pushing the timeline for the RON95 petrol subsidy rationalisation to mid-2025 is intentional.

CIMB's Chia calls it a deliberate choice of design over haste, pointing out that the government is following in the footsteps of the diesel subsidy rationalisation that was executed in June this year.

"I think the reason they decided to do it in mid-2025 is that they may still be considering the best method of implementation to do RON95. Based on the diesel Budi Madani low take-up rate, perhaps they want to find a better approach to it," notes CGS International economist Ahmad Nazmi Idrus.

Lee Heng Guie, executive director of the Associated Chinese Chambers of Commerce and Industry of Malaysia's (ACCCIM) Socio-Economic Research Centre, says it is a good time to rationalise the subsidy, given that crude oil is forecast at between US$75 and US$89 a barrel in 2025.

The RON95 petrol subsidy is not the only item that will be rationalised for the T15 group. The PM also proposed that this group will have to pay more for public healthcare and public tertiary education soon. It will be done in stages, he said, but the quantum of the increase has not been made known.

How the T15 group is defined is unclear at the moment, whether it is based on household income or by using other metrics. Will it take into account the number of people in a household?

If it is any indication, Minister of Economy Rafizi Ramli had in previous news reports defined the T20 group as the 20% of Malaysian households that have income above RM10,960 per month. Truth be told, many consider this a low threshold for the classification of the top 20% of income earners in the country.

It is also worth mentioning that the tax on remittance of foreign-sourced income for individuals, which have been subject to tax in the source country, will continue to be deferred until Dec 31, 2036, to the relief of those who derive foreign-sourced income and are likely from the high-income group. The deferment was initially due to end on Dec 31, 2026.

Ernst & Young Tax Consultants Malaysia tax managing partner Farah Rosley deems this a good move and a way to encourage more remittance of foreign-sourced income to the country and hopefully spur economic activity locally.

KPMG's Soh calls this a significant step that provides much-needed certainty for taxpayers as it allows individuals to plan their finances more effectively and reduces the potential tax burden, which can encourage investment and overall economic stability.

With the rich expected to foot more of the nation's bill next year, the handouts for low-income earners have been increased.

Cash handouts under Sumbangan Tunai Rahmah and Sumbangan Asas Rahmah have been increased to RM13 billion from RM10 billion in 2024. The Department of Social Welfare received an allocation of RM2.9 billion for 2025 from RM2.4 billion in 2024.

With the increased allocation, the PM said a low-income household with three children will be eligible to receive up to RM13,000 per year in cash handouts. Under Budget 2025, RM1 billion was also allocated to addressing concerns about the rising cost of living.

Economists, however, find the proposal for mandatory Employees Provident Fund (EPF) contributions for non-citizens working in the country perplexing.

"There are no details on how this will work yet. But if employers are also required to contribute to the fund for non-citizens, it will be an extra cost to them," says SERC's Lee.

Some think this could add to EPF's pool of funds in the light of the large withdrawals made as a result of the Covid-19 pandemic.

Meanwhile, among the ministries, the Ministry of Education got the highest allocation at RM64.1 billion, higher than the RM58.7 billion allocated for 2024. Funds will go towards the upgrading and maintenance of schools across Malaysia and the building of 44 new schools, while more than RM5 billion was allocated for 17 types of education assistance and broadband connectivity for rural schools.

The Ministry of Health received the second highest allocation at RM45.3 billion, higher than the RM41.2 billion allocated for 2024.

### No mega infrastructure projects

Those hoping for announcements of much-awaited mega infrastructure projects were likely disappointed with Anwar saying early in his budget speech that the country does not need new mega projects worth billions of ringgit.

This time around, the infrastructure spend will be disbursed across various states in the country, focusing on connectivity such as road works, new highways and airport expansions in Sabah and Sarawak.

There was no hint of the Mass Rapid Transit Line 3 (MRT3) and Kuala Lumpur-Singapore high-speed rail during the Budget 2025 speech.

"Now is not the time to implement mega projects. The country's development will focus on projects that benefit the people and infrastructure that supports industrial areas based on state priorities," said Anwar in his speech.

He also said development projects will be implemented based on the "user pays" principle to alleviate the government's fiscal burden. The projects that will be based on this principle through private-public partnership (PPP) include the Juru-Sungai Dua (JSD) elevated highway in Penang, West Ipoh Span Expressway (WISE) from Gopeng to Kuala Kangsar in Perak, and the extension of the West Coast Expressway (WCE) from Banting in Selangor to Gelang Patah, Johor.

The initial plan was to have the WCE span from Banting in Selangor all the way to Taiping, Perak. No estimated value was mentioned for the highway projects.

Sabah and Sarawak received their highest ever development allocation in Budget 2025 at RM12.6 billion, RM200 million more than the RM12.4 billion allocated in Budget 2024. An estimated RM253 million has been allocated for the expansion of Tawau Airport in Sabah and Miri Airport in Sarawak, as well as RM1 billion for the Sarawak Cancer Centre.

Apart from these, there was a focus on necessary infrastructure for clean water, electricity, roads and schools.

To bridge the urban-rural development gap, basic infrastructure in villages, rural areas and remote regions will continue to be prioritised

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## Bridging the urban-rural development gap

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with an allocation of RM2.9 billion for the development and upgrading of basic infrastructure. Of this amount, RM1.8 billion will be allocated for the construction and upgrading of village connection roads, including in Kota Belud, Sabah; Pasir Puteh, Kelantan; and Kuala Lipis, Pahang.

Despite the absence of new mega projects, MIDF Research says the construction sector is still an obvious beneficiary of the budget, on the back of ongoing public projects and infrastructure developments such as airport expansion, PLUS highway expansion in Johor, the Penang LRT and continued work on the Pan Borneo Highway.

In the light of the recent sinkhole incidents, the federal government has allocated more than RM250 million to repair dangerous slopes across the country, RM21 million to curb sinkholes in Perak, Kedah and Perlis, and RM10 million to carry out geotechnical study of the structure of the soil in the main roads around Kuala Lumpur's Golden Triangle.

The government also allocated RM2.8 billion for the maintenance of federal roads and provided Malaysia Road Record Information System (MARRIS) funds of RM5.5 billion for state roads.

Meanwhile, for the palm oil industry, after much lobbying, the threshold for the imposition of the windfall profit levy of 3% and 3.5% for Peninsular Malaysia and Sabah and Sarawak respectively, were raised by RM150 per tonne to RM3,150 and RM3,650 per tonne of crude palm oil, effective Nov 1, 2024.

Datuk Dr Ahmad Parveez Ghulam Kadir, director-general of the Malaysian Palm Oil Board, says that despite the moderate increase, it will contribute to mitigating the rising cost pressures faced by palm oil producers.

"The move will create breathing space for palm oil companies to become more efficient, given the competitive nature of the global vegetable oil market. Furthermore, they will be able to better plan for their long-term investments," he says in a statement.

### Possible challenges in the longer term

Overall, while the response to the budget has been positive, it has its shortcomings. UOB Global Economics & Markets Research's economists Julia Goh and Loke Siew Ting say in their report: "The government chose a more gradual path of fiscal consolidation in order to balance fiscal responsibilities and ensure stable growth drivers. However, the fiscal reform efforts do not appear to be making sufficient progress to rebalance some of its burgeoning fixed expenditure items and raise the revenue-to-GDP ratio.

"Fixed expenses such as emoluments, retirement charges and debt service charges are higher by 6.2%, 17.7% and 7.7% respectively in 2025 compared to 2024 while revenue-to-GDP is expected to come in at a lower 16.3% in 2025 compared to 16.5% in 2024.

"This could present challenges in the longer term for fiscal sustainability and resiliency as the journey to rebuild fiscal buffer and ensure fiscal resilience is expected to become more challenging as the country transitions into an ageing status by 2030, just as geoeconomic fragmentation rises and climate-related and technology risks increase economic uncertainty."

They add that strong political will, consistency and effective execution are key to succeeding in both economic and fiscal reforms to reach high-income nation status. "Timely adjustment and adapting to the rapidly evolving global market developments are imperative to enhance the country's competitiveness and quality of living standards with comprehensive and inclusive social safety nets." E