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Malaysia's budget goals still possible with sales tax, but future pain awaits: Experts

Most economists warned that dumping the GST will leave the country more vulnerable to oil price volatility unless the revenue hole is plugged.

KUALA LUMPUR — The Malaysian government is unlikely to miss targeted deficit cuts by switching to the Sales and Services Tax (SST) in September, but the reduced revenue will be of concern in subsequent years, said experts.

While economists and experts speaking to Malay Mail all agreed Malaysia could still bring the budget deficit to 2.8 per cent this year, most warned that dumping the Goods and Services Tax (GST) will leave the country more vulnerable to oil price volatility unless the revenue hole is plugged.

Kenanga Investment Bank economist Wan Suhaimie Wan Mohd Saidie said the current deficit target was attainable via higher Petronas dividends to the government if oil prices stay above US$70 (S$102.30) per barrel.

Budget 2018 was drawn up with a baseline of US$52 per barrel.

However, he said there was no guarantee that oil price will remain at that level next year and beyond, while other external factors such as slower global economic growth could also hamper the government's budget deficit ambitions.

RHB Research Institute chief Asean (Association of South-east Asian Nations) economist Peck Boon Soon also said the government's bid to rein in chronic overspending from next year onwards "would be very much dependent on global oil prices".

The controversial GST regime introduced in April 2015 was once hailed as the country's "saviour" that helped bring in RM44 billion (S$14.75 billion) in federal revenue in 2017, cushioning a dip in oil price over recent years for Malaysia that was once heavily reliant on petroleum income.

The SST is projected to bring in RM21 billion for the government, but that is still less than half of GST collections last year.

Tax consultant Veerinderjeet Singh said the government should not return to banking on Petronas dividends to pay for the Budget, and instead develop a long-term plan that goes beyond slashing costs to rein in the deficit.

“If revenue falls, expenditure remains the same; obviously the deficit goes up. I don't know how much the lower the expenditure can go,” he told Malay Mail.

Institute of Strategic and International Studies’ (ISIS) analyst Firdaos Rosli cast doubt on the sustainability of plugging leakages and wastages as the basis to fund the government, stressing that generating more revenue was as important as planning future spending.

Mr Firdaos highlighted that Malaysia is set to be an ageing nation by 2030, during which a significant proportion of the country will be retired and not pay income tax.

He pointed out that even retirees and migrant workers contributed to tax revenue under the broad-based GST.

Mr Firdaos also highlighted other factors that are already driving down government revenue, including the gradual reduction of personal and corporate tax rates since 2015 as well as lower collections on imports due to the gradual elimination of tariffs with Malaysia’s participation in multiple free trade agreements.

He questioned how the government will find enough revenue in the years to come to drive economic growth when it was opting for a tax system that will generate less income than its predecessor.

“Even with GST our growth is already slowing down; imagine without GST, how will the government drive growth without GST? This is a question of medium- and long-term prospects.

“But there will be a point of time when the government will have to face the reality, either you increase product coverage of SST, increase SST rates or widen tax base again by switching back to GST, or even increase rate of direct tax — both personal and corporate — to pre-2015 levels,” the ISIS director of economics, trade and regional integration told Malay Mail.

Mr Firdaos said the government could try to increase revenue by raising the capital gains tax, and predicted that personal and corporate tax rates are not likely to go down in the near future.

POSSIBLE SOLUTIONS: TRIM, MORE TAX, LET PRIVATE SECTOR LEAD

Sunway University Business School’s Professor Yeah Kim Leng said the federal government will have to reduce its spending by at least RM15 billion to RM20 billion annually from 2019 onwards in order to achieve a declining budget deficit, as volatile oil revenue cannot be depended on for government budgeting.

The government will need to be leaner and increase spending efficiency by cutting out wastage, which he said meant it could “still achieve the same results with a smaller budget”.

“In the medium term, they may need to postpone the balanced budget target beyond 2020,” the professor of economics told Malay Mail.

The Najib administration previously aimed for a zero budget deficit by 2020, before revising the target to a balanced budget by 2020 with a 0.6 per cent deficit, following a slump in oil prices in recent years.

Then second finance minister Johari Abdul Ghani on January 4 said it would be more feasible for Malaysia to achieve a balanced budget by 2022 or 2023 to avoid stifling economic development.

Prof Yeah believed the government would still be able to promote growth despite having less to spend, but said this meant Putrajaya must allow the private sector to be the main engine of the economy.

He said the push for a private sector-driven economy could be done with a well-planned divestment of government-linked companies (GLCs) that have been accused of crowding out the private sector, which could also provide an infusion to government coffers.

Noting the new Pakatan Harapan government's focus on fighting graft, enhancing good governance and promoting rule of law, Prof Yeah said a visible decline in corruption would boost confidence in the government and unleash activity by both domestic and foreign private sector players.

He listed out various ways that could be used to improve the government's revenue, including making GLCs more profitable for higher government dividends as well as raising gaming taxes.

Unpopular taxes such as the capital gains tax and inheritance tax could be revisited, but "sin tax" for alcohol and tobacco are unlikely to be further increased as it may lead to smuggling and the proliferation of counterfeits, he said.

"If we were to raise our corporate tax rate, we may jeopardise our competitiveness. So this is the risk that you will face if you were to consider raising income tax. That would be an antithesis to promoting private sector growth, so it's unlikely to be considered," Prof Yeah said, adding that it would be tricky to tax the rich more as it could cause tax shifting and capital outflows from Malaysia.

He said the government is unlikely to expand the SST or revive GST in the next few years, as such options are only possible when there is greater income equality and when earning levels of the poor rise so they can cope with price increases.

The government zero-rated the GST in June and is aiming to reintroduce the SST in September.
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