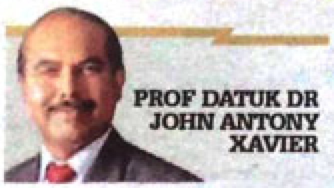
What 2016 Budget must address

JUGGLING ACT: Govt needs to balance increased public spending and fiscal sustainability



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As Budget Day draws nigh amid the gloom within and without the country, what would be the chief concerns of our national budget planners? We consider investor confidence, fiscal sustainability, price stability and inclusiveness as being uppermost in their minds.

First, investor confidence. The recent RM20 billion stimulus measure to boost the stock market and, thereby, strengthen the drooping investor confidence in our economy is but a drop in the ocean of equities. Recently, China learned the hard way — it burned RM83 billion of its foreign reserves to stabilise the stock market — that governments cannot inflate a sagging stock market. Investor confidence, therefore, is better tackled by a pro-growth agenda.

The export-growth model, since abandoned by China, may not be the answer, either. The 23 per cent depreciation of the ringgit this past year should have enhanced our export competitiveness, but for a similar depreciation of regional currencies. With private-sector investments flagging, private consumption-driven growth is an alternative, as in China. But at 88 per cent of the gross domestic product (GDP) — the highest in Southeast Asia — our households are so mired in debt. So much so, that further private consumption may not be forthcoming as households try to balance their shrinking budget amid the rising cost of living. We can look to the government for succour to grow the economy. But, there is a huge cost to it — the cost of swelling the public debt and fiscal deficit.

Such an outcome will impinge on the second concern of fiscal sustainability. Our sovereign credit ratings have been intact due largely to prudent macro-economic management. Our public debt is 54 per cent of the GDP. Although this position is well above the 40 per cent average for emerging countries, it is still within the self-imposed statutory limit of 55 per cent. Our fiscal deficit is targeted at 3.2 per cent of GDP this year.

Increased public spending — especially for infrastructure to cater to the increasing urbanisation of the country — will jeopardise these targets and invoke the wrath of rating agencies. Just last week, two big and rich nations, France and Japan, suffered the indignity of cuts to their sovereign ratings. They were perceived to be impotent over their public debts. A similar cut to our credit rating will further erode investor confidence.

So, how can we juggle increased public spending and fiscal sustainability? The government has undertaken public-private partnerships for big infrastructure projects, especially. Such an arrangement can be extended for the private provision of public services: healthcare, education, welfare, skills training, preschool care. That will obviate the huge public expenditures that would otherwise be incurred.

The Goods and Services Tax (GST) will rake in RM10 billion after discounting for the abolished Sales and Services Tax and the many exemptions under the system. That should enrich the government's coffers that have been battered by the halving of oil prices.

We need to strengthen other revenue sources. As one such source, government charges for its services are ripe for review. For example, the RM1 charge for general outpatient treatment is unreasonable against the enormous costs for such provision. Surely, the rising middle class will not mind paying more for a service that is equal, if not better, than the private provision.

Third is price stability. Undeniably, GST has contributed to inflation. Profiteering and the difficulty or reluctance of traders to claim offsets for GST paid on their intermediate materials have compounded the price hike. The ringgit's depreciation has made our imports expensive. As roughly 70 per cent of our imports constitute intermediate products in the final manufacture, the cost of production is bound to rise to compound the inflationary effects from GST.

To dampen inflation, productivity growth becomes all the more urgent. The government does not spend as much as other developed nations that spend as much as four per cent of their GDP on research and development (R&D). But at roughly one per cent of GDP, government largesse for R&D offers plenty to help industries boost productivity.

Additionally, the 2015 Budget offered tax incentives for factory automation. It also allocated RM10 million to encourage companies to set up research centres in high-end technology, information and communications technology, and knowledge-based industries. We can expect similar incentives in the 2016 Budget. This is all the more imperative amid our slipping global innovation index. Malaysia is ranked 33rd among 144 countries, against the enviable seventh position of Singapore.

The fourth concern is inclusiveness. The government will want to address the plight of the Bottom 40 per cent of households. Already, increases to the 1Malaysia People's Aid (BR1M) have been announced. GST is here to stay. But the government will want to soften its impact on the populace. Generally, GST introductions the world over are accompanied by reductions in income-tax rates. Singapore, for example, brought down its income-tax rates upon introducing GST in 1994. (The personal income-tax rate is currently capped at 20 per cent.) It also offered a raft of tax offsets, including income-tax (corporate and personal) and property-tax rebates.

To alleviate the pain of the public and business, especially from GST, we can expect the government to lower its income-tax structure in the 2016 Budget without neutralising GST's revenue-generation.

Formulating the national budget is arduous. Hard choices have to be made. In making them, we must be mindful of what George Washington once said: "We must consult our means rather than our wishes."

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