Malaysia

A. Medium-term economic outlook (forecast, 2019-23 average)

GDP growth (percentage change):	4.6
Current account balance (% of GDP):	2.1
Fiscal balance (% of GDP) (central government):	-2.5

B. Medium-term plan

Period: 2016-20

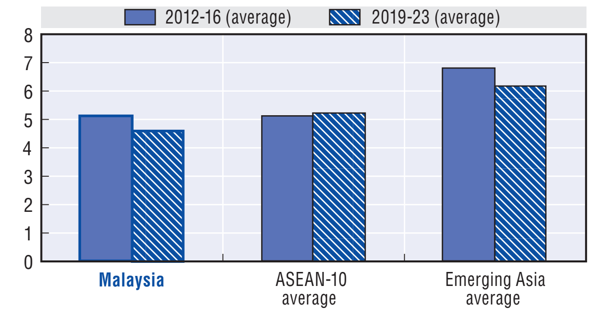
Theme: Anchoring growth on people

C. Basic data (in 2017)

Total population:	32.0 million *
Population of Kuala Lumpur	1.8 million *
Nominal GDP (US dollar):	312.4 billion **
GDP per capita at PPP:	29 144.3 (current International Dollar) **
Exchange rate in the first half of 2018 (period average):	3.9 (MYR/USD)

Note: * Population data are year-end government estimates.
** IMF estimate.
Sources: OECD Development Centre, national sources, CEIC and IMF.

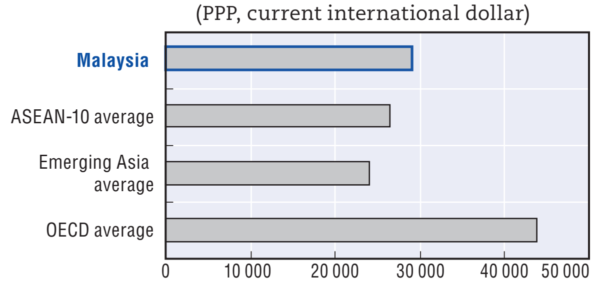
GDP growth rates (percentage change)



Source: OECD Development Centre, MPF-2019.

GDP per capita, 2017

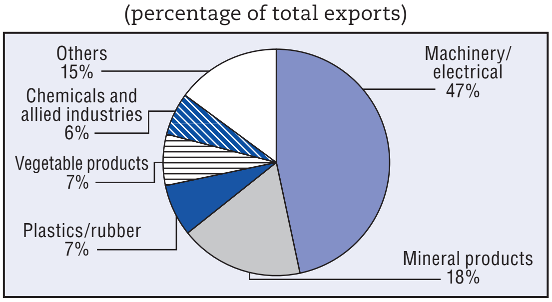
(PPP, current international dollar)



Source: IMF.

Composition of exports, 2017

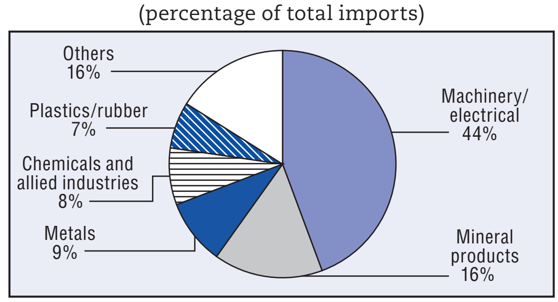
(percentage of total exports)



Source: Trademap.

Composition of imports, 2017

(percentage of total imports)



Source: Trademap.

Structural policy challenges discussed in previous editions of the Outlook

2014	Education	Improving the quality of education
	SME development	Improving the productivity of small and medium sized enterprises (SMEs)
	Taxation	Widening the tax base and improving tax administration and compliance
2015	Productivity	Improving productivity to support sustainable economic growth and transform Malaysia into a high-income developed nation
	ICT	Further development of Information and Communication Technology (ICT), which is particularly important in supporting growth
	Taxation and fiscal system	Enhancements to fiscal stability, and a reduction in the country's dependence on oil, including through the introduction of a goods and services tax (GST)
2016	SMEs	Raising the productivity of SMEs
	Education	Upgrading education to meet industry needs
	Urban green growth	Promoting urban green growth
2017	Housing	Keeping housing affordable and ensuring a supply of affordable housing
	Social safety net	Enhancing the social safety net to ensure citizens' well-being and participation
2018	Halal industry	Enhancing trade growth by strengthening the Halal sector

Recent developments in policy areas covered by previous editions of the Outlook

Taxation and the fiscal system: scrapping the goods and services tax (GST)

- Within 100 days of taking office, Malaysia's new government lowered the GST to 0%. The government replaced the GST by restoring the old system of a sales and services tax (SST). For goods, it is set to be between 5-10%, while tax on services is set at a 6% levy. The new rate came into force on 1 September 2018, following a three-month tax break. This temporary break in this kind of taxation led to an uptick in consumption. Legislatively speaking, the five bills to reinstate the old SST regime were successfully tabled in parliament and passed by the Senate in August 2018.

Social safety nets for workers

- Recently, Malaysia's Social Security Organisation – known locally as Sosco – has been addressing the challenges that workers face due to uncertainties posed by a number of global trends. These include: demographic ageing, the coverage gap, and enduring youth unemployment. They also include the transformation brought about by the rise of the digital economy. These challenges require fundamental and long-term strategic responses on the part of policy makers and administrators in the domain of social security.
- In this connection, Sosco aims to bridge the coverage gap in social security to ensure that a wider spectrum of workers benefit from social protection. These efforts include developing coverage for self-employed taxi drivers under the Self-Employment Social Security Act 2017: a new legislation, the Employment Insurance System Bill, will set up a system to provide protection in the event of loss of employment.
- As of 1 July 2018, Sosco also expanded its coverage to include housewives, single mothers, widows, and spouses working with their entrepreneur partners. Regulations disqualifying spouses of business partners from working with them were removed on the same date. Previously, people in this group were not deemed to be employees under the Social Security Act 1969 and the employment insurance scheme that dates from 2017.

POLICY FOCUS

Reintroducing a sales and services tax after the scrapping of the goods and services tax

Malaysia's 14th general election, held on 9 May 2018, saw a victory for the Alliance of Hope, or Pakatan Harapan. This is a milestone in Malaysia's history due to the fact that the same coalition had governed the country since its independence from the United Kingdom in 1957. At the age of 93, Dr Mahathir Mohamad once again became prime minister. Although the new government has not been in power for long, and the directions in which it will take policy remain uncertain, it has already made significant fiscal, institutional and administrative changes in line with the commitments in the Alliance of Hope manifesto.

As a way to reduce the cost of living for Malaysians – one of the objectives in Alliance of Hope's manifesto – the new government announced via the finance ministry that the GST would fall to 0% as of 1 June 2018, from its previous rate of 6%. This new measure fulfilled the government's campaign promise to abolish the GST within its first 100 days in office.

Malaysia's experiment with a general sales tax

Malaysia introduced the GST in 2015 as a consumption tax based on the logic of added value. GST was applied to goods and services at every stage of production and distribution in the supply chain, including the importation of goods and services, giving it a more comprehensive coverage than the old system of SST (Royal Malaysian Customs, 2013). When the GST came into force on 1 April 2015, the rate was set at 6%. The previous dual regime, with a sales tax rate set at 10% and a services tax rate at 6%, was thereby abolished.

Following the introduction of the GST, selected goods and services became exempt from taxation. These included piped water, the first 200 units of electricity per month for domestic consumers, transport services such as buses, trains, light rail transit, taxis, ferries, boats, highway tolls, and also education and health services (Razak, 2014). Even though exemptions were made, the implementation of the GST had a negative impact on low and middle-income groups, as it led to price increases for essential household goods, while wages remained sticky.

The elimination of this relatively recent tax was a way for the government to seek to reduce Malaysians' rising cost of living. As a result of its abolition, the annual revenue of the federal government is expected to fall by 21 billion Malaysian ringgit (MYR) annually. Still, the government is expected to introduce other fiscal measures in order both to make up for some of the fall in revenue and to support the reinstated petrol and diesel subsidy. The re-introduction of the SST took effect on 1 September 2018, giving consumers and businesses a three-month tax break from June to August 2018 (OECD, 2018).

In line with the new government's commitment to stabilise retail fuel prices and to reduce living costs in the country, the Ministry of Domestic Trade and Consumer Affairs announced in May that petrol and diesel subsidies would be reinstated. Diesel and RON 95 petrol were to stay at their current price, with the price of RON 97 petrol to be revised every Wednesday.

Reintroducing the sales and services tax to compensate for lost revenues

Malaysia's finance minister, Lim Guan Eng, made clear that the SST would tax the provision of services at 6% and the sales of goods at 10%. The sales tax is imposed only at the time at which the goods are either manufactured or imported. The service tax is imposed on specific services at the time at which the services are provided to the consumer.

The reintroduction of the SST will shift the burden from end users to the manufacturing sector and trade-related sectors. According to Central Bank Governor Nor Shamsiah Mohd Yunus, however, its impact on the country's inflation rate should be much smaller than that of the GST. This, she explained, is because 52% of the items in the basket that defines the consumer price index were subject to the GST. By comparison, only 28% of these items were subject to the SST under the old framework.

One way in which the new legislation reinstating the SST is different from the past system, is that it sets out harsher punishments for tax evaders. Repeat offenders face up to seven years imprisonment and fines of up to 40 times the amount of the sales tax they avoided. Under the old legislation, there was maximum jail time of three years and a cap on fines at MYR 50 000.

The introduction of the GST was actually part of the previous government's programme of tax reform, and was intended to enhance the capability, effectiveness, and transparency of tax administration and management. However, this proved to be a failure due to the abuse of the GST fund. At the moment, moreover, there is a shortfall in the fund for unpaid GST input tax amounting to MYR 19.25 billion which corresponds to the period between 2015 and 31 May 2018.

An increase in the national debt

Another challenge is on cutting the public debt and helping people in their fight against rising living costs. When it comes to the public debt, the finance ministry confirmed on 24 May 2018 that the federal government's debt and liabilities accounted for 80.3% of gross domestic product as of December 2017, much higher than the 50.8% of GDP reported by the previous government. As of December 2017, the government's liabilities comprised three parts. The first of these was the federal government's debt of MYR 686.8 billion (50.8% of GDP). Secondly, there were government guarantees of MYR 199.1 billion, or 14.6% of GDP (the government is committed to paying the debt of entities that are unable to pay for themselves, and this includes MYR 42.2 billion for Danainfra Nasional Berhad, MYR 26.6 billion for Prasarana Malaysia Berhad, and MYR 38 billion for 1Malaysia Development Berhad). Thirdly came lease payments of MYR 201.4 billion (14.9% of GDP) for public-private partnership projects. The government must pay for rental, maintenance and other costs on a number of projects, such as the construction of schools, hospitals and roads.

Ongoing structural and administrative reforms include a 10% salary cut for ministers, and the elimination of several non-essential and political government agencies. In May 2018, for example, the prime minister announced that a commission for land-based public transport, which had led negotiations with Singapore for a high-speed rail project under the previous government, would be shut down. Its tasks and responsibilities will be taken over by the transport ministry. Other agencies will be abolished as well, including the department for special affairs, the National Council of Professors, the Federal Village Development and Security Committee, the Residents' Representatives Committee, and Malaysia's external intelligence organisation. Moreover, the new government has introduced a new economic affairs ministry to promote economic growth, transparency and structural reforms. The new ministry will oversee matters related to economic policy and will also take over the economic planning unit, which was formerly under the supervision of the Prime Minister's Department (OECD, 2018).

As part of the new government's objective of curbing the ballooning public debt, the prime minister confirmed during a recent visit to Beijing that three China-backed projects totalling USD 22 billion will be cancelled until Malaysia can find a way to pay its debts. The projects include a railway connecting Malaysia's east coast to southern Thailand and Kuala Lumpur, as well as two gas pipelines. Additionally, the government's plans to optimise revenue include the collection of MYR 5 billion from higher dividends from government-linked companies and institutions, such as Khazanah Nasional Berhad, Bank Negara Malaysia, and PETRONAS.

Key government ministries in Malaysia

Prime Minister	Mahathir Mohamad
Deputy Prime Minister	Wan Azizah Wan Ismail
Agriculture and Agro-based Industries	Salahuddin Ayub
Communication and Multimedia	Gobind Singh Deo
Defence	Mohamad Sabu
Domestic Trade and Consumer Affairs	Saifuddin Nasution Ismail
Economic Affairs	Mohamed Azmin Ali
Education	Maszlee Malik
Energy, Science, Technology, Environment and Climate Change	Yeo Bee Yin
Entrepreneur Development	Mohd. Redzuan Md. Yusof
Finance	Lim Guan Eng
Foreign Affairs	Saifuddin Abdullah
Health	Dzulkefly Ahmad
Home Affairs	Muhyiddin Muhammad Yassin
Housing and Local Government	Zuraida Kamaruddin
Human Resources	Kula Segaran Murugeson
International Trade and Industry	Ignatius Darell Leiking
Primary Industries	Teresa Kok Suh Sim
Rural Development	Rina Mohd Harun
Territories	Khalid Abdul Samad
Tourism, Arts and Culture	Mohammadin Ketapi
Transport	Anthony Loke Siew Fook
Water, Land and Natural Resources	Xavier Jayakumar Arulanandam
Women, Family and Community Development	Wan Azizah Wan Ismail
Works	Baru Bian
Youth and Sports	Syed Saddiq Syed Abdul Rahman
Central Bank Governor	Nor Shamsiah Mohd Yunus

Note: Valid as of 16 October 2018.

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