

19/10/2001

2-pronged strategy to boost growth (HL)

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UNCERTAINTIES over the state of the world economy, worsened by the September 11 attacks in the US and the bombing of Afghanistan, have prompted the Government to look at internal elements to stimulate growth.

The Finance Minister, who will table Budget 2002 today, will attempt to stimulate domestic spending by giving back money to consumers, corporations and keeping the economic infrastructure ticking until the economy picks up again.

Beside stimulating consumer spending, the budget proposals may no doubt also aim to float the economy, which economists expect to grow by less than 1 per cent this year, through lowering the cost of business dealings.

If the expectations sound familiar, it is because Malaysia has been down this road before. In the darkest days of the Asian economic crisis, in 1998, Prime Minister Datuk Seri Dr Mahathir Mohamad also presented a budget that was bold and effective in insulating the domestic economy from the worst.

For this financially difficult time, the corporate sector, consumers and foreign investors can expect tax breaks as the Government sacrifices revenue in favour of increased economic activities.

This may mean that Malaysia will present today its fifth consecutive deficit budget because the Government is not expected to go down the normal path of increased indirect taxes to offset lower direct tax revenues - in line with its intention to provide more disposable income for the people.

The Government has indicated that the deficit will be financed through local borrowings as well as the issuance of sovereign bonds.

Research houses expect the deficit to be in the region of between 4 per cent and 5 per cent of the gross national product, which is still well within the manageable ceiling of 6 per cent.

The widely anticipated corporate tax reduction will give companies a bigger capital to work on towards better performance.

The move will simultaneously create a more conducive business environment in Malaysia, hence, attracting more foreign direct investment into the country as the cost of engaging in business is low.

Analysts foresee the budget slashing Malaysia's corporate tax rate by 1 percentage point to 27 per cent, shaving the Government's revenue by some RM600 million.

Compared with some Association of South-East Asian Nations members, Malaysia's corporate tax rate was the third highest in 2001 at 28 per cent. The Philippines was the highest at 32 per cent, Indonesia (30 per cent), Thailand (30 per cent) and Singapore at 25.5 per cent.

The budget is also expected to give the middle-income group the bulk of the tax breaks, based on the assumption that this segment is more likely to spend if given any windfall.

As such, the budget may see income tax rate being reduced to allow more deductible income among Malaysians. Economists estimate a 1 per cent deduction in such a rate.

The budget will also reflect Malaysia's commitments as a member of the World Trade Organisation and signatory of Asean's free trade pact that will call for near zero tariffs by 2003.

A reduction of import taxes for the automotive sector is also widely expected as that commitment draws near.

Malaysia has agreed to reduce tariffs on its completely-knocked-down and completely-built-up automotive parts to below 5 per cent by the year 2005.

A reduction is expected because any immediate reduction of tariffs for such items would create havoc to the automotive and the financial sectors. Since gradual reduction is the way to go, Budget 2002 may reflect on this.

Pressure to globalise the economy may also be addressed by the budget via incentives for companies to consolidate their operations. Stockbroking and insurance firms are the likeliest candidates for the expected perks.

For the last few years, the country's insurance industry has not been getting the budget's allocation. Analysts see the sector being included in the list of industries that will be enjoying the perks.

The small- and medium-sized industries (SMIs), being the backbone of the economy, may have more reasons to merge and strengthen their competitiveness if the Government offers some form of tax breaks for them to do so.

Therefore, Budget 2002 may have incentives for them to consolidate their operations. Tax breaks for the SMIs may also be given for the purchase of machinery or information and communications technology equipment to enhance their operations.

The budget is expected to carry a two-pronged strategy, namely to stimulate the country for further growth and fairly distributing Malaysia's wealth to the people.

At the same time, it will keep its door open for additional pump-priming measures to better respond to the uncertainties in global economic conditions that are worsened by the attacks on the US and conflicts in Afghanistan.

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