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A budget that means business

M Shanmugam

THERE was no cut in corporate taxes, no reduction in import duties on motor vehicles and no initiation of mega projects. Does that signify that Budget 2003 is a non-event?

The fact of the matter is that the proposals to a large extent signify a paradigm shift in the economic planning of the authorities. The tax incentives for small- and medium-scale industries (SMIs) and companies that are export-oriented are in fact long overdue. They are perhaps just the stimulus needed for the private sector to take the lead in the economy again.

'Budget 2003 does have widespread incentives for business, notably the export sector. It spurs the country to be a global player since the cost of doing business is reduced,' says chartered accountant and tax practitioner Raymond Liew.

The Budget proposes that the corporate tax of SMIs be reduced from 28 per cent to 20 per cent on chargeable income of up to RM100,000. At present, SMIs are subject to the same tax regime as big companies.

Companies that record an increase in exports are given tax exemption of 30 per cent on the increase, while companies that penetrate new markets are given 50 per cent income tax exemption.

Further, companies that record the highest increase in exports according to categories will be given full income tax exemption.

These incentives for exporters are an improvement over the present structure whereby income tax exemption of 10 per cent of the increased export value is given to companies that attain a 30 per cent increase in exports.

Affin-UOB Research in its analysis says that the tax break for export-oriented companies is positive for semiconductor assemblers such as AKN Technology Bhd and Globetronics Bhd, ceramic-tile manufacturer White Horse Bhd and construction-material producer Hume Industries Bhd.

Without the spicy ingredients such as mega projects or cuts in corporate tax, the Budget poured cold water on the hopes of punters waiting to make a quick profit on the Kuala Lumpur Stock Exchange (KLSE).

In the run-up to Budget 2003 unveiled by Prime Minister-cum-Finance Minister Datuk Seri Dr Mahathir Mohamad on Sept 20, many were expecting corporate tax to be reduced to enhance Malaysia's business competitiveness.

The expectations were largely fuelled by Singapore's move in May this year to reduce corporate tax from 24.5 per cent to 22 per cent. Singapore aims to reduce the tax to 20 per cent by three years' time.

Speculation was also rife that in view of the implementation of the Asean Free Trade Area (Afta) in 2005, tariffs on imported vehicles would be reduced. Some were also hoping for the announcement of mega projects to spur the lethargic construction sector.

But is there any basis for such beliefs in the first place? Afta is two years away and anything can happen in the interim. As for mega projects, many have been announced over the past two years that have not taken off the drawing board.

And on the subject of corporate tax, should Malaysia follow Singapore and reduce it? If that were the case, why is South Korea, the fastest growing economy outside China, still sticking to its tough tax regime that ranges from 16 per cent to 28 per cent?

'Cutting corporate tax is not the answer to our long-term growth. It will further worsen the overall deficit. We cannot afford it,' says an economist with a local brokerage.

The 28 per cent corporate tax contributed to about 26 per cent of the Federal Government's revenue amounting to RM79.8 billion for 2001. The contribution from corporate tax is expected to increase in 2002 and 2003.

The budget deficit for 2002 was -4.7 per cent of the gross domestic product (GDP). The deficit is expected to reduce to -3.9 per cent in 2003. In 2000 and 2001, they were -5.8 per cent and -5.5 per cent respectively. The narrowing deficit signifies the diminishing role of Government in spurring growth.

Also, a reduction in corporate tax is not going to channel foreign direct investments (FDIs) into Malaysia. With or without cuts in corporate taxes, China is the favoured destination for FDIs.

To compare Singapore's move to reduce corporate tax with Malaysia's failure to follow suit would mean ignoring the differences in economic landscape and texture of the two countries. Put plainly, the economic structures of Malaysia and Singapore are different.

While Singapore is striving to further strengthen its base as a manufacturing, financial and service centre hub, Malaysia is promoting growth of SMIs to broaden the industrial base. Malaysia has natural resources such as oil and gas to bank on for income. The agriculture sector is being groomed as the third engine of growth after the manufacturing and services sector.

At the time of writing, the KLSE is down to 650 points. Besides the tension in the Middle East and profit warnings from companies in the United States, investors are also said to be disappointed with the non-reduction in corporate tax. Some are also sceptical of the GDP growth forecast of 6.0 per cent to 6.5 per cent for 2003.

Growth next year will be fuelled by the manufacturing sector, followed by services. If the electronic sector picks up as expected, war does not break out and the US does not go into recession, the Malaysian economy is on track for credible growth.

Tan Teng Boo of Capital Dynamics is optimistic that the present 'confusion' in the KLSE and the world financial markets will blow over. For the bespectacled fund manager who has in recent months turned into an optimist, US consumer spending will continue to hold long enough for business spending to recover.

If that is true, then the present bear phase on the KLSE is just a passing stage.