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Investors should delve into Budget's deeper issues

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THE much-awaited 2004 Budget speech has finally come and gone and left many stock market players disappointed.

Many players had expected the Budget to hand out more goodies, like cuts in corporate and personal income tax rates, hikes in EPF and insurance premium rebates, etc.

After all, it was Prime Minister and Finance Minister Datuk Dr Mahathir Mohamed's last Budget presentation, and it would be logical to have more happy citizens what with the general election around the corner.

Other than the excitement in the oil and gas sector where speculation is rife about selected companies benefiting from participation in the proposed second consortium to develop marginal oil fields and undertake oil exploration, production and refining similar to what Petronas does today, the stock market generally has given a lukewarm reception to the Budget.

Although it is always nice to be able to personally benefit from such major annual events, I believe investors should delve into the deeper issues of the basis of and reasons for budgets to better understand why Budget 2004 is the way it is.

A country's Budget is really an income statement similar to a business or even your personal household budget.

First, we will have to find the entity's sources of revenue and then only can we work out how much can be allocated for expenditure and consequently what proportion to save.

So, the whole idea of budgeting is an exercise in keeping tabs on our spending habits, making sure we do not overstretch our financial resources in the pursuit of our targets and ambitions.

In this light, it is pleasing to note that Budget 2004 is put together with this conservatism in mind.

It actually emphasises bringing down deficits incurred over the past three years from above five per cent of GDP presently to a lower target of 3.3 percent of GDP for 2004.

In fact, the Government has promised to keep a tight rein on the Budget deficit going forward until it becomes balanced hopefully in a couple of years.

There are, of course, two sides to the Budget - one, the revenue stream and the other, the expenditure items. Tax cuts and rebate concessions will inevitably eat into the nation's revenue stream even in spite of GDP growth.

Therefore, it is prudent to reserve this option for times of need only. Just like in a normal business environment, we should not continually cut prices and give discounts and rebates unless it is necessary to do so i.e. to widen market share and/or to remain competitive.

In Malaysia's case, with the Budget running at a deficit even for 2004, it would be even more irresponsible for the Government to be pressured into lowering income tax and giving concessionary rebates simply to satisfy popular opinion.

On the expenditure side of the equation, controlling one's expenses and spending within one's means is very important.

To this end, I applaud the Government's intentions to reduce its allocation of 2004 development expenditure in an effort to lower its Budget deficit.

I see this as a necessary evil given that the country will risk having its credit ratings lowered if it continues to allow the large deficit to persist without showing some genuine effort and commitment to contain it.

Of course, spending within one's means does not necessarily mean one cannot gear up by taking up bank borrowings when a good investment opportunity presents itself, for example in real estate or in setting up and/or expanding a business.

In fact, a reasonable amount of gearing is encouraged if the expected investment returns exceed the cost of capital and such gearing will enable the business to grow and expand profitably.

Since cost of debt is normally lower than cost of equity, gearing will bring down the overall cost of capital of a company thereby enhancing business valuations. Always remember - it is over-gearing that is the issue; not simply gearing per se!

The Budget, in perspective, is really the nation's profit and loss account forecast for the coming year. As with any company or individual, business or family losses cannot be a good thing especially when it is prolonged. Malaysia has been running a budget deficit or loss since 1998. Understandably, whilst it was the result of the severe Asian crisis that brought about this unfortunate situation, such a proposition should not be unnecessarily allowed to continue unabated over a long period of time as this is detrimental to the economy.

Business and consumer confidence are currently at comfortable levels. The US is showing some signs of recovery.

There is even some hope that Japan will finally turn the corner and come out of its chronic down-cycle.

It is therefore now timely for the Government to step aside and let the private sector take the lead as the main engine of growth and an attempt at this is what we have witnessed in the recent Budget construction.

Steps in this direction included improving tax incentives for small and medium-sized industries (SMIs), locally owned manufacturing concerns and companies in Sabah, Sarawak and the eastern corridor of Peninsular Malaysia.

The venture capital (VC) industry has also been given prominence with increased Government allocation and tax incentives for VC investors and management companies.

Some focus has also been placed on the development of Malaysian brands and the promotion of Malaysian products overseas.

Realigning the responsibility of driving the nation's growth to the private sector is a step in the right direction with respect to resource allocation.

The Government is a political body and it is always more difficult as such for it to provide a totally economic-driven solution given socio-political responsibilities and considerations.

The practice of division of labour is highly advocated here hence it is best to let companies focus on what they are best at so that services and products can be delivered more efficiently and effectively.

Likewise, we should not let service professionals be relegated to tending their own poultry and vegetable farms as this would be inefficient utilisation of scarce resources, right?

The Government has been a good stimulator and engine for growth during depressed times when sentiments were low and confidence lacking. We then needed the Government involvement to ensure the nation does not over-save itself into a recession.

But to continually utilise fiscal muscles to build more roads, highways and bridges can only be taken so far.

After all, they do not directly contribute to productivity and therefore

have a lesser income multiplier effect on the economy!

All in all, Budget 2004 is prudent and necessary. Going forward, however, as our fiscal position strengthens, some tax cuts should be extended for Malaysian industries to remain competitive and for the nation to be able to attract the best brains.

A continuous emphasis on upgrading the level of education and skills training remains crucial.

As the marketplace we live in becomes increasingly global, it is imperative that we arm ourselves with skills and know-how to compete and become world class in all our endeavours.

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