

Budget 2016 – Winners and losers

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Budget 2016 was deemed by analysts as a juggling act of managing revenue gains and containing expenditure against the backdrop of plummeting oil prices over the past year that hurt government coffers. Who are the winners and losers of the Budget?

Budget 2016: The first to be announced under the five-year 11th Malaysia Plan (11MP), Budget 2016 tabled by Prime Minister Najib Abdul Razak on Oct 23 is widely seen as a “people friendly, market neutral” budget.

Government revenue is expected to increase 1.4% in 2016 to RM225.7 billion, while operating expenditure allocation increases by 0.9% to RM215.2 billion. The government is allocating RM50 billion for development expenditure, up from RM47.4 billion allocated in 2015.

Revenue gains in Budget 2016 depend largely on collection from the goods and services tax (GST), which adequately offsets the decline in oil-related contributions, projected to account for 17.3% and 14.1% of total revenue respectively.

GST, implemented since April 1 this year, is expected to contribute RM27 billion to government coffers in 2015, and is expected to contribute another RM39 billion in 2016.

The Budget also took into account the reduction in dividend expected from Petronas to RM16 billion from RM26 billion previously, after the crash in oil prices hurt its cash flow, forcing the state oil company to draw on its cash reserves to meet its financial obligations.

Budget 2016 is seen to be focusing largely on containing expenditure, prioritising spending on high-impact projects and alleviating cost of living on rural and lower-income households.

What comes as the most surprising is the increase in income tax rates for those who fall within the income bracket of between RM600,000 and RM1 million – who will see their tax rate being raised to 26% from 25% previously – and for those earning

above RM1 million, who will then see their personal tax rate being raised to 28% from 25% previously.

The national minimum wage will be increased from RM900 to RM1,000 per month for Peninsular Malaysia, and from RM800 to RM920 for East Malaysia, effective from July 1, 2016. The new minimum wage will be enforced across all sectors, except for domestic services or domestic maids.

The government lowers its gross domestic product (GDP) growth projection range to 4% to 5% in 2016, down from 4.5% to 5.5% in 2015 on the back of a challenging external macro situation, expected moderation in domestic demand and depressed commodity prices.

The fiscal deficit-to-GDP (sum of goods and services produced in a year) ratio is expected to decline marginally to 3.1% in 2016 from 3.2% in 2015.

Sectors which benefit from the Budget: HLIB Research views consumer and construction sectors as the biggest beneficiaries of Budget 2016, as both could experience minimal impact on margins from a higher minimum wage. Other sectors expected to benefit from the Budget include education, glove, oil and gas, real estate investment trusts, technology and air transportation.

While the positive impacts are unlikely to significantly boost profits, the research house noted that the advantages enjoyed by the sector are likely to sustain prospects.

The glove sector is also set to reap benefits from the proposal for a special reinvestment allowance (RA) for companies that have exhausted their eligibility to qualify for RA, according to AmResearch, outweighing the anticipated increase in labour and raw material costs.

The rate of claim is at 60% of qualifying capital expenditure and can be set off against 70% of statutory income from year of assessment 2016 to 2018.

This proposal, added AmResearch, is particularly significant for rubber glove players as most had expired their RA incentives between 2012 and 2014 considering their long operating history. RA incentives are valid for 15 consecutive years from the year of assessment RA is claimed.

On the other hand, export-oriented technology players and construction companies remain core buys for AllianceDBS, given more visible earnings and growth trajectory.

Gamuda, Inari Amertron, Globetronics, and Muhibbah Engineering were named as top picks.

Beaten down big cap stocks too deserve a relook due to government's announcement for government-linked companies and government-linked investment companies to invest domestically, added AllianceDBS, which named Public Bank, Hong Leong Bank, and Tenaga Nasional Bhd (TNB) as top picks.

As a result of the RM20 billion ValueCap fund, HLIB Research sees opportunity in undervalued big-cap stocks including Axiata, IJM, Maybank and TNB, though noting that impacts will only be felt in 2016 as the market rally months after initial announcement due to the time needed to mobilise funds.

Construction catalysts are expected when actual contract awards under the 11MP kick in come 2016. Gainers include Edgenta, IJM, KNM, Mitrajaya.

Sectors which stand to lose from the Budget: While Budget 2016 offers targeted tax incentives for certain industries, AllianceDBS expects business appetite for capital spending to dampen given the current business climate. While it is positive for domestic consumption, the impact of the Budget on corporates is seen to be muted due to rising cost of doing business.

The increase in minimum wage, according to CIMB Research, will increase operating costs for labour-intensive industries such as plantations, construction and manufacturing. The impact on the construction sector is mitigated by the fact that average wage is already within the range of between RM1,000 and RM1,200 in the sector.

“We deem this as negative for planters, as a higher minimum wage will raise the planters' cost of production unless it is offset by productivity gains. This is because labour costs form as much as 30% to 50% of the estates total costs and some estates workers are paid the minimum wage,” said CIMB Research.

The 11%-to-15% rise in minimum wage could raise cost of production for estates by 3% to 5%, leading to a potential cut in earnings of pure planters by as much as 10% for a full-year impact, added the research house.

StockStalk: Budget 2016 can be considered relatively neutral for the stock market as the winners and losers roughly offset each other. It is also considered by some as a

non-event due to the absence of a significant uplift to corporate earnings or sentiment.

Both AllianceDBS and CIMB Research view Budget 2016 as a no positive surprise to the market, as infrastructure projects announced are mostly “regurgitated”, with most of them being funded off balance sheet. Kenanga Research also noted that there have been no corporate tax cut as initially expected, but targeted tax incentives for certain industries were offered instead.

Broadly speaking, the consumer, construction, education, real estate investment trusts (Reits), healthcare and telco sectors are winners in the Budget. The consumer sector gains from higher spending power from lower-income earners and civil servants, while higher spending and incentives on education benefit the education sector.

Reits will gain from the extension of tax incentives, while telco and healthcare will gain from the GST categorisation.

The hike in minimum wage effective from July 1, 2016 will push up labour cost for various industries; this will increase operating costs for labour-intensive industries including plantations, construction and manufacturing.

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