Budget 2003 : Fewer Surprises But Heavier Responsibilities

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Budget 2003 is relatively different as it does not put as much emphasis on short-term growth strategies as it did in the previous budgets. Rather, it emphasises on the ways in which the k-economy can be developed and integrated into economic activities. The objective of this Budget is to create a knowledgeable, innovative and creative workforce, which will be able to penetrate and compete aggressively in both the domestic and international markets. Such manpower will enhance national competitiveness and bring the economy onto a sustainable growth path unvulnerable to external economic shocks. In this sense, this Budget looks generally sedate as it holds few surprises and offers short-term strategies that could be viewed as a quick-fix to economic problems.

Parallel to the government's objective of changing the orientation of the economy from one that is excessively reliant on external markets to one which is more domestically-oriented, Budget 2003 has put forth tax and non-tax strategies to increase disposable income in order to stimulate domestic investment and consumption. There are many ways in which the government could increase money circulation in the economy that, in turn, will raise the nominal income of the people. However, it is meaningless to have rising nominal income without accompanying rise in productivity as this will render purchasing power unchanged. Unless followed by sufficient improvement in the k-economy and productivity, the generated rise in nominal income will disappear into rising inflation subsequently.

Similarly, in diversifying and developing new sources of growth for the economy, k-economy is eminent. New sources of growth in areas such as tourism, transportation, education and health tourism have already passed their early stage of development. Thus, any further development will require highly skilled and caliber manpower, coupled with high technology and information technology. In turn, the development of these new sources of growth will generate stiff regional competition and institute new challenges for companies in the marketing of such products. Unless we are ahead in the k-economy arena, there is little chance to fully develop these new sources of growth into important sources of growth for our economy. Recognizing the importance of the k-economy, Budget 2003 had duly provided large allocations to the k-economy related sectors such as ICT and education.

A commendable aspect of this Budget is its small borrowing requirement. Totalling only 15.8 per cent of the total budget of RM106.7 billion, the determination of this borrowing is based on projections on government revenue performance in 2003. It is hoped that this small percentage of borrowing and heavy reliance on government revenue will reduce the possibility of rising inflation.

Despite the no-show tax situation, better GDP growth, which has been forecasted to be 4.0 per cent and 6-6.5 per cent for 2002 and 2003, respectively, is expected to generate more revenue for the government to finance the budget. It is worth noting, however, that if the GDP growth target cannot be achieved, the forecasted government revenue and the size of deficit will also change. But, in view of the market indicators, the confidence index and the low growth base of last year, it is very likely that the economy will be able to grow by 4 per cent this year. Again, if there were no unprecedented shocks in the international economy, GDP growth will then be expected to hover around 6 per cent in 2003.

Based on a GDP growth of 6-6.5 per cent, government revenue is expected to grow by 7.5 per cent and amounting to RM89.8 billion in 2003, adjusting only 2 per cent higher than the government revenue growth in 2002. One might say that this is a reasonable forecast because the recovery in the government revenue performance in 2001 was already comparable to the pre-crisis level of 23.1 per cent of GDP. During the crisis in 1999, the ratio declined to 19.5 per cent but is expected to rise to 23.4 per cent in 2003.

Although there is no tax increase or new tax being introduced, some cheer is expected to ring from the tax collection department. Total tax collection is expected to increase by 8.4 per cent and contribute 81.4 per cent to the total revenue in 2003, slightly surpassing 80.7 per cent in 2002. Like in the previous years, the bulk of the revenue comes from income taxes which are expected to contribute 66 per cent to the tax revenue and 53 per cent to the total revenue in 2003.

Interestingly, the expected deficit of just 3.9 per cent to GDP announced in the 2003 Budget is fairly small and much better than many had expected earlier. In the light of the prevailing weakness in the private sector, there was much anticipation that the expansionary budget this year will at least conjure a 5-6 per cent deficit. While this small deficit is in line with the government's effort to improve fiscal discipline, efficient and proper management with full transparency would definitely augur well for the economy as a whole, putting it at little or no risk at all of becoming a bubble economy once again.

Pre-budget sentiments rang high that the government would repeat its fiscal stimulus packages aimed at channeling more money quickly into the economy to stimulate the private sector. Instead, this time around, the government hopes to stimulate private sector spending by providing more perks and raising disposable income through various tax and non-tax incentives. Although the deficit is small, it is hoped that this new approach will still have strong expansionary effects on the economy.

One important objective of the new Budget is to help improve the foreign investment climate. In 2001, total foreign investments (in approved projects) declined slightly by 5.2 per cent year-on-year.

Much to the chagrin of the business community, the much awaited and anticipated corporate tax reduction did not materialise after all. Many had perceived a reduction in corporate tax as important to stimulate the current weak investment environment and improve the inflow of foreign direct investments (FDIs) into the country. Some were even hopeful that investments may even be diverted from China to Malaysia should corporate taxes be slashed. However, the government seems to have valid reasons to maintain the present level of corporate taxes (except that for SMIs). Furthermore, it is not exactly clear whether or not a further cut in corporate taxes will significantly change the inflow of FDIs amidst regional and world economic uncertainties. It may, perhaps, make more sense now for us to focus on further building and improving our domestic infrastructure and infostructure to attract FDIs instead. Even if all this is not effective in attracting FDIs, it will certainly stimulate domestic investment and consumption. In addition, relative to other developing countries, we are quite well ahead in terms of good corporate governance and transparency. The government, particularly after the 1998 crisis, has taken various steps in enhancing these important aspects which are also crucial for attracting FDIs.

Without a doubt, a sound and efficient financial system, particularly the banking system is important to the health of an economy. Serious efforts were taken by the Malaysian government through Danamodal and Danaharta to beef up its financial sector and they had made good progress in reducing non-performing loans and whisking the banking sector away from a risky situation. Subsequent merger programmes and the consolidation process further improved the overall performance of the banking system, as indicated by the increase of the Risk-Weighted Capital Ratio (RWCR) to 13.1 per cent in July this year. Presently, the Malaysian banking system is sound enough, and continues to work conscientiously alongside the government in steering the economy toward achieving the country's aspirations, as outlined in the 2003 Budget.

In a modern economic structure, market participants do not only view the bank as a financial intermediary that merely bridges up surplus and deficit units. To a certain extent, a strong and efficient banking system also reflects advancement in the ICT sector, the maturity of business and investment regulatory framework, adequacy of institutional development and efficiency of infostructure of a country. An advanced banking system operates on a high standard of electronic commerce that is capable of enhancing trade, investment and financial integration across countries. Thus, an efficient banking system could serve as an important channel that carries market signals, and links domestic and international markets. With its direct bearing on market confidence, banking institutions certainly have a greater responsibility of ensuring the success of national economic policies.

After being led out of a risky environment, the role played by banking institutions in helping others that were hit by the economic crisis still leaves much to be desired. The year-on-year growth of commercial bank lending was only 2 per cent in July 2002. This is fairly small in comparison to the growth of commercial bank lending of around 25 per cent prior to the economic crisis in 1998.

Perhaps this lack of effort by the banking institutions was due to the merger and re-structuring exercise within the banking industry that commenced after the 1998 crisis. Currently, most of the re-engineering exercises within the banking industry, to enhance professionalism, improve evaluation technique, improve assets quality and improve risk management procedures, are nearly completed. Notwithstanding the importance of a careful risk evaluation prior to loan approval, efficiency and aggressiveness are also vital ingredients for achieving world class banking standards. Perhaps the delay in the re-engineering process and over-cautiousness of banks in loan processing is difficult to avoid since many aspects of re-engineering are new to our banking industry. It is hoped that the banking industry will speed up its re-engineering exercise and, upon completion, the banking industry is expected to enhance its role and contribute more positively to the economy.

On close examination, it is clear that the new Budget carries with it heavy responsibilities and ambitious long-term economic objectives to enhance the country's competitiveness in the k-economy arena. Achieving this objective is very important as this will determine the survival and global position of our economy.

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