

Fiscal Operations in 2006

Fiscal policy continued to support economic growth with consolidation on track...

The 2006 Budget was formulated with the continued aim of building economic resilience, enhancing growth and facilitating private businesses in light of increased challenges arising from sustained high oil prices, global hike in interest rates and increased competition from regional economies. In addition to addressing the demands of the growing economy, the Budget, being the first for the Ninth Malaysia Plan (9MP) 2006-2010, continued to stress on capacity building and improving efficiency in laying the foundation for medium and long-term sustainable growth. Towards this end, and as announced in the 9MP, the Government will continue to review, streamline and improve the implementation and monitoring processes to ensure speedier execution, greater accountability and more effective spending of Government allocations.

The supportive role of the Government remains important to facilitate the private sector as the main engine of economic growth, even though the Government has embarked on fiscal consolidation since 2000. Hence, the Budget proposed appropriate measures to enhance a business-friendly environment to improve competitiveness. These measures included the

granting of tax relief, improving the Government's service delivery systems, modernising the agriculture sector, identifying and developing new sources of growth as well as intensifying human capital development.

The role played by the Government in fostering economic activities has not jeopardised the pace of fiscal consolidation, given the relatively strong economic performance and significantly higher oil-related revenue which contributed RM45,002 million or 37.3% of total revenue compared with RM30,889 million or 29.1% in 2005. The increase has helped to sustain government expenditure without adversely affecting the financial position of the Federal Government. The fiscal deficit as a percentage of Gross Domestic Product (GDP) in 2006 is expected to decline gradually in line with the overall macroeconomic objectives of sustaining growth without unduly imposing pressure on Government's financing or debt position. The bulk of the Government's borrowing needs was sourced domestically. Given the excess liquidity in the financial system, it did not crowd out the private sector's accessibility to loanable funds. Debt service charges have also remained low and manageable.

The fiscal stance adopted continued to meet the short-term demands of the growing economy while ensuring sustainability and flexibility over the medium-term. The tax and expenditure measures introduced have helped to alleviate

some of the immediate concerns, particularly those which had adversely affected certain sectors of the economy or imposed burdens on the lower income groups. Over the medium-term, the sturdy financial position of the Government will continue to permit flexibility in countering new issues and overcoming challenges posed by uncertainties and developments in the external environment.

Federal Government

Federal Government finance remains strong...

The Federal Government's deficit is expected to reduce further to 3.5% of GDP in 2006, as shown in *Table 4.1*, on account of strong revenue growth particularly from oil-related sources. The strong financial position has helped to enhance policy flexibility and the ability to respond to any vulnerability in the future.

Revenue

The Federal Government anticipated a total revenue amounting to RM114,569 million in the 2006 Budget. However, after taking into consideration

the actual revenue performance in 2005 and during the first six months of 2006, total revenue was revised to RM120,625 million, as shown in *Table 4.2*. The higher revenue, which increased by 13.5%, was mainly contributed by direct taxes, particularly corporate income tax. Due to higher crude oil prices, which increased from an average of USD42 in 2004 to USD57 per barrel in 2005, the oil-related revenue and dividend also contributed to the significant increase.

Tax revenue is expected to contribute 72.8% or RM87,863 million of the total revenue. **Direct taxes**, which has been revised upwards, is expected to increase by 17% to RM62,637 million (2005: 9.9%; RM53,543 million). Individual income tax is higher by 11.6%, while corporate income tax is expected to increase by 7.7%, reflecting sustained economic performance as well as the ongoing efforts made to enhance the efficiency of revenue collection. To facilitate the filing of tax returns, the Inland Revenue Board (IRB) has recently introduced the e-filing system to enable taxpayers to submit their tax forms online. The IRB has received some 186,600 forms through e-filing by the end-June 2006 deadline, far exceeding the initial expectation of 50,000 filings. Petroleum income tax (PITA) is higher by 40.1% to RM20,404 million (2005: 26.9%; RM14,566 million) in line with sustained production and higher crude oil prices in 2005.

TABLE 4.1

Federal Government Financial Position 2005-2007

	RM million			Change (%)		
	2005	2006 ¹	2007 ²	2005	2006 ¹	2007 ²
Revenue	106,304	120,625	134,815	6.9	13.5	11.8
Operating expenditure	97,744	105,374	112,986	7.1	7.8	7.2
Current balance	8,560	15,251	21,829	5.7	78.2	43.1
Gross development expenditure	30,534	35,814	44,510	5.8	17.3	24.3
Less: Loan recoveries	3,250	1,274	2,485	141.5	-60.8	95.1
Net development expenditure	27,284	34,540	42,025	-0.9	26.6	21.7
Overall balance	-18,724	-19,289	-20,196	-3.6	3.0	4.7
% of GDP	-3.8	-3.5	-3.4			

¹ Revised estimate.

² Budget estimate, excluding 2007 tax measures.

CHART 4.1

Federal Government Finance Current Account

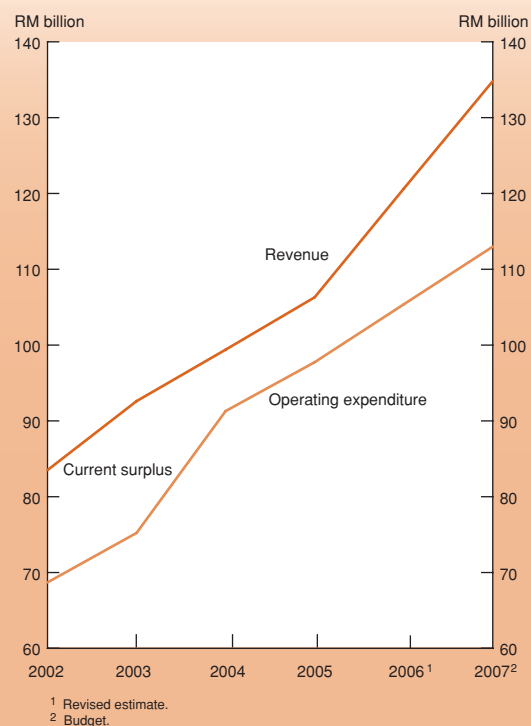


CHART 4.2

Percentage of Overall Deficit/Surplus to Gross Domestic Product

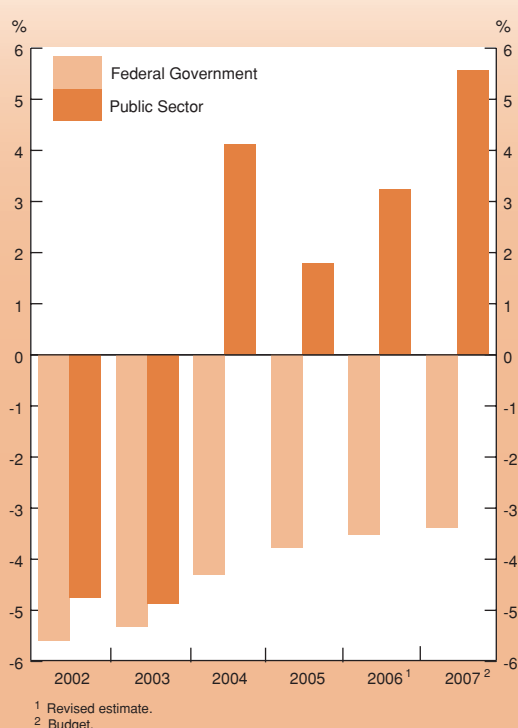


TABLE 4.2

Federal Government Revenue 2005-2007

	RM million			Change (%)			Share (%)		
	2005	2006 ¹	2007 ²	2005	2006 ¹	2007 ²	2005	2006 ¹	2007 ²
Tax revenue	80,594	87,863	95,794	11.9	9.0	9.0	75.8	72.8	71.1
Direct tax	53,543	62,637	70,116	9.9	17.0	11.9	50.4	51.9	52.0
of which:									
Companies	26,381	28,414	30,127	8.2	7.7	6.0	24.8	23.6	22.3
PITA ³	14,566	20,404	24,693	26.9	40.1	21.0	13.7	16.9	18.3
Individuals	8,649	9,649	10,555	-3.7	11.6	9.4	8.1	8.0	7.8
Indirect tax	27,051	25,226	25,678	15.9	-6.7	1.8	25.4	20.9	19.0
of which:									
Excise duties	9,321	8,798	9,463	36.5	-5.6	7.6	8.8	7.3	7.0
Sales tax	7,709	6,281	5,812	13.1	-18.5	-7.5	7.3	5.2	4.3
Non-tax revenue	25,710	32,762	39,021	-6.0	27.4	19.1	24.2	27.2	28.9
of which:									
Licences/permits	8,332	8,600	9,029	17.3	3.2	5.0	7.8	7.1	6.7
Investment income	14,849	21,608	27,398	-16.5	45.5	26.8	14.0	17.9	20.3
Total revenue	106,304	120,625	134,815	6.9	13.5	11.8	100.0	100.0	100.0
% of GDP	21.5	22.0	22.6						

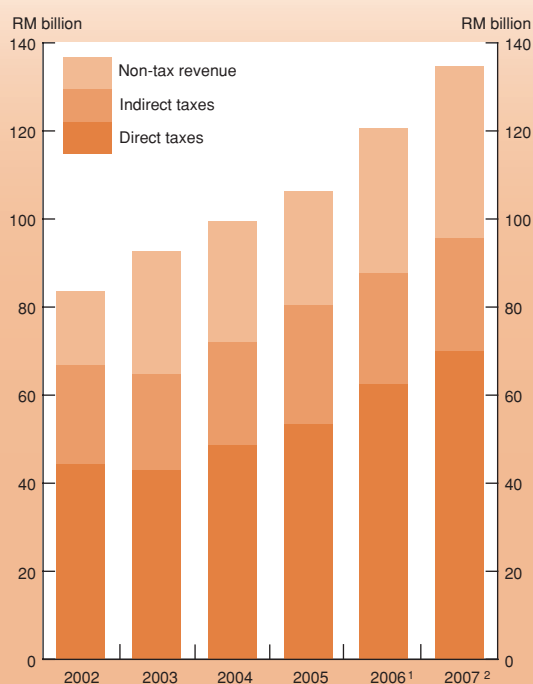
¹ Revised estimate.² Budget estimate, excluding 2007 tax measures.³ Petroleum Income Tax.

Indirect taxes, constituting about one-fifth of total revenue, is expected to decline by 6.7% to RM25,226 million. This is largely due to significant drop in sales tax caused by lower collection from petroleum products and motor vehicles, as well as rebalancing of taxes on liquor and tobacco products. Similarly, import and excise duties are also lower following the introduction of National Automotive Policy (NAP), which reduces the amount collected from imported and locally manufactured vehicles. The increase in export duties by 21% is largely due to higher commodity prices, particularly crude oil.

Collection from **non-tax revenue** is projected to increase to RM32,762 million (2005: RM25,710 million), following much higher dividend payments from Petroliaam Nasional Berhad (PETRONAS) and receipts of petroleum royalties. Other non-tax revenue such as licences and permits as well as fees is not expected to change significantly from previous years.

CHART 4.3

Major Components of Federal Government Revenue



¹ Revised estimate.

² Budget.

Expenditure

Adherence to prudent financial management with emphasis on efficiency and cost effectiveness remains the thrust of the Government's expenditure policy. The Government has continued to focus on capacity building to create a more conducive business environment and to improve the public delivery system, particularly among the implementing and monitoring agencies to ensure speedier execution of programmes and projects. In addition, meeting the socio-economic needs of the poor is also given high priority with large expenditure earmarked for modernising and commercialising the agriculture sector. In this regard, the Federal Government total expenditure is expected to reach RM141,188 million in 2006 or 10.1% higher than the RM128,278 million recorded in 2005. Of the total, RM105,374 million or 74.6% is operating expenditure while the balance development expenditure.

Operating expenditure is expected to increase by 7.8% to RM105,374 million, largely for charged and locked-in items such as debt service charges, emolument, subsidies and supplies and services, as shown in *Table 4.3*. Emolument, the largest component of operating expenditure, is expected to account for 23.8% of total operating expenditure. Total emolument is revised to RM25,089 million from the original budget allocation of RM23,587 million, taking into account the provision of cost of living allowance as well as other new and revised allowances for civil servants, which came into effect on 1 January 2006. Salaries of education and health-related workers, such as teachers, nurses and doctors, as a group, accounted for almost 60% of the total emolument. Disbursement on supplies and services, which comprised 20.5% of operating expenditure, is higher by 20.2% to RM21,608 million, largely for maintenance, repairs and rentals as well as payments for professional services to improve the quality of public service delivery.

Debt service charges, presently the third largest component, is contained at 12.1% of operating expenditure, lower than the average of the Eighth Malaysia Plan (8MP) period of 13.4%. Of the total debt service charges, 87.8% or RM11,175

TABLE 4.3

Federal Government Operating Expenditure by Object 2005-2007

	RM million			Change (%)			Share (%)		
	2005	2006 ¹	2007 ²	2005	2006 ¹	2007 ²	2005	2006 ¹	2007 ²
Emolument	25,587	25,089	25,815	7.6	-1.9	2.9	26.2	23.8	22.8
Debt service charges	11,604	12,726	13,127	6.3	9.7	3.2	11.9	12.1	11.6
Grants to state governments	2,614	2,907	3,645	-9.7	11.2	25.4	2.7	2.8	3.2
Pensions and gratuities	6,809	6,638	7,049	12.4	-2.5	6.2	7.0	6.3	6.2
Supplies and services	17,984	21,608	23,147	8.1	20.2	7.1	18.4	20.5	20.5
Subsidies	13,387	11,251	11,908	131.0	-16.0	5.8	13.7	10.7	10.5
Grants to statutory bodies ³	8,289	9,183	9,854	24.6	10.8	7.3	8.5	8.7	8.7
Refunds and write-off	288	357	1,815	-94.3	24.0	408.4	0.3	0.3	1.6
Others	11,182	15,615	16,626	-17.4	39.6	6.5	11.4	14.8	14.7
Total	97,744	105,374	112,986	7.1	7.8	7.2	100.0	100.0	100.0
% of GDP	19.7	19.2	18.9						

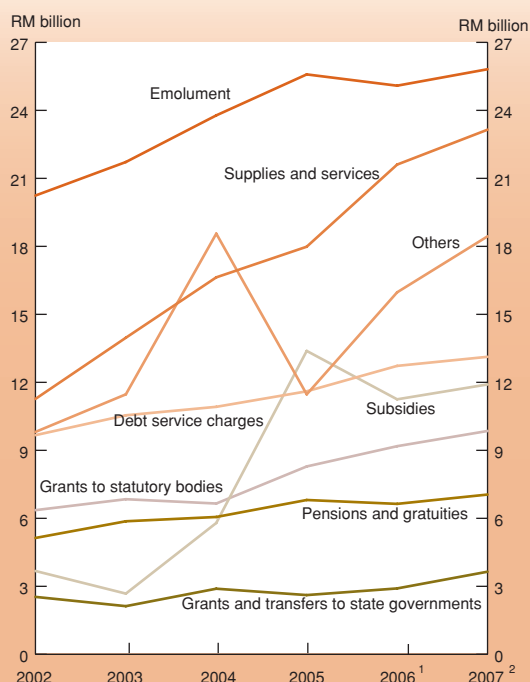
¹ Revised estimate.

² Budget estimate, excluding 2007 tax measures.

³ Includes emolument.

CHART 4.4

Federal Government Operating Expenditure



¹ Revised estimate.

² Budget.

million is to service domestic debt. Subsidy payments, which currently constitutes almost 11% of operating expenditure is lower by 16% to RM11,251 million, following adjustments to retail fuel prices. Despite the price adjustments, fuel subsidy remains significant, accounting for almost 76% of total subsidy payment. Expenditure under the “others” category such as asset acquisition, operating grants to schools and scholarships are at the previous year’s level.

Development expenditure is expected to increase by 17.3% to RM35,814 million in 2006, as shown in *Table 4.4*. The expenditure is in line with the blueprint of the 9MP, which is to sustain growth, build capacity and facilitate private sector investment. Greater emphasis is given to improve performance through better planning, implementation and monitoring mechanisms. Programmes and projects are prioritised based on needs, target groups and those that would generate the greatest impact to the economy. The bulk of the development expenditure is channelled to the economic and social sectors, particularly to provide public amenities, improve public transportation and reduce regional disparities.

TABLE 4.4

Federal Government Development Expenditure by Sector 2005-2007

	RM million			Change (%)			Share (%)		
	2005	2006 ¹	2007 ²	2005	2006 ¹	2007 ²	2005	2006 ¹	2007 ²
Economic services	14,957	16,283	20,827	26.2	8.9	27.9	49.0	45.5	46.8
of which:									
Agriculture and rural development	2,482	3,681	4,157	-13.8	48.3	12.9	8.1	10.3	9.3
Trade and industry	3,221	3,791	5,102	168.2	17.7	34.6	10.5	10.6	11.5
Transport	7,660	6,198	7,298	15.5	-19.1	17.7	25.1	17.3	16.4
Social services	7,450	10,194	14,218	-27.4	36.8	39.5	24.4	28.5	31.9
of which:									
Education and training	3,736	5,175	7,941	-13.4	38.5	53.4	12.2	14.4	17.8
Health	1,220	1,297	1,629	-48.1	6.3	25.6	4.0	3.6	3.7
Housing	1,082	1,895	2,153	-32.1	75.1	13.6	3.5	5.3	4.8
Security	4,803	5,781	6,817	16.2	20.4	17.9	15.7	16.1	15.3
General administration	3,324	3,556	2,648	26.9	7.0	-25.5	10.9	9.9	5.9
Total	30,534	35,814	44,510	5.8	17.3	24.3	100.0	100.0	100.0
% of GDP	6.2	6.5	7.5						

¹ Revised estimate.

² Budget estimate.

The **economic services** is the largest component of development expenditure, accounting for 45.5% of total in 2006. The transportation sub-sector accounts for the largest share of 38.1% or RM6,198 million, which is used mainly to improve the transportation infrastructure networks through the construction and upgrading of roads, bridges, ports as well as airports. The sub-sector also focuses on providing an integrated and efficient transportation system in urban centres to reduce congestion and increase connectivity.

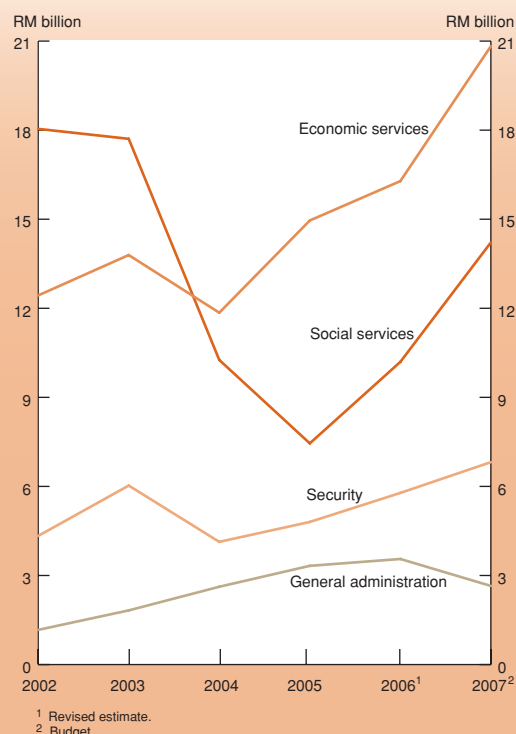
The expenditure on agriculture and rural development is expected to increase significantly by 48.3% to RM3,681 million, in tandem with the Government's thrust to make the agriculture sector the third pillar of economic growth. Agriculture programmes undertaken places greater emphasis towards more modern and commercial farming methods, higher value-added primary and agro-based products, as well as better marketing approaches and farm accreditation. This transformation is expected

to increase the production capacity of food industries such as fruits, vegetables, fish and livestock. Presently, a number of projects such as the Beef Valley in Selangor and Negeri Sembilan as well as *Projek Pertanian Modern* in Johor are being undertaken to achieve the objectives of modern farming. The expenditure for public utilities is also expected to increase substantially by 59.5% to RM2,361 million (2005: 56.6%; RM1,480 million), in line with efforts to narrow the rural-urban divide by improving public amenities such as supply of electricity, water and telecommunication facilities to the rural areas.

A total of RM10,194 million was allocated for the **social services**, the second largest component of development expenditure. The education and training sub-sector was accorded the highest priority, given the 9MP's emphasis on human capital development. A higher increase of 38.5% was allocated for educational infrastructure including the construction of pre-schools and

CHART 4.5

Federal Government Development Expenditure by Sector



primary schools, 12 Mara Junior Science Colleges, University Kuala Lumpur and 22 industrial training institutes. The expenditure for the health sub-sector is expected to increase marginally by 6.3% to provide better healthcare and to meet the increased demand for public health services. These include upgrading of hospitals and clinics as well as the construction of new hospitals in Kluang and Permai in Johor. The outlay for the housing sub-sector amounts to RM1,895 million in 2006, of which almost RM1,000 million is for *Perumahan Rakyat* and *Perumahan Rakyat Bersepadu* programmes. The balance is for the construction of housing quarters for armed forces and police personnel. The Government has also set up a special-purpose vehicle (SPV) company to undertake the new construction as well as rehabilitation of abandoned housing projects for police personnel.

The expenditure for **internal security and defence** accounts for RM5,781 million, an increase of 20.4% in 2006. The bulk is

channelled to upgrade the capabilities of the police, the Malaysian Maritime Enforcement Agency as well as the various wings of the defence forces. Some of the ongoing development projects include Teluk Sepanggar naval base, Gong Kedak airbase and army hospital in Genting Klang. The expenditure for **general administration** amounting to RM3,556 million is geared mainly for upgrading of information and communications technology (ICT) equipment, acquisition of land as well as renovation of government buildings.

Financing

As a prudent measure, the Government always ensures that borrowing is only for financing of development expenditure. Given the ample liquidity in the country, the bulk of the funding requirements will be raised from non-inflationary domestic sources.

Total **gross domestic borrowing** is expected to amount to RM36,100 million, of which RM17,750 million is new borrowing, with the balance RM18,350 million for repayment of existing loans, as shown in *Table 4.5*. Of this total,

TABLE 4.5

Federal Government Financing 2005-2006

	RM million		Share (%)	
	2005	2006 ¹	2005	2006 ¹
Gross borrowing	32,151	37,232	100.0	100.0
Domestic	31,500	36,100	98.0	97.0
Investment issues	4,000	10,000	12.4	26.9
Government securities	27,500	26,100	85.5	70.1
External	651	1,132	2.0	3.0
Market loans	-	-	-	-
Project loans	651	1,132	2.0	3.0
Repayment	22,954	22,428	100.0	100.0
Domestic	18,800	18,350	81.9	81.8
External	4,154	4,078	18.1	18.2
Net Borrowing	9,197	14,804		
Domestic	12,700	17,750		
External	-3,503	-2,946		
Change in assets²	9,527	4,485		
Total	18,724	19,289		

¹ Estimate.

² (+) indicates a drawdown of assets.

RM26,100 million will be raised through the issuance of Malaysian Government Securities (MGS) while the remainder RM10,000 million through Government Investment Issues (GIIs). In 2006, RM11,700 million will be raised through four new issues via open tenders and private placements while the remaining RM14,400 million through the reopening of six existing MGS. During the first seven months of 2006, MGS with maturities of 5 and 10 years were issued at coupon rates ranging between 3.756% and 4.635% per annum. The rates on MGS issued during the same period in 2005 with similar maturities ranged from 3.644% to 4.720% per annum.

There will be no new external borrowing in 2006. However, a drawdown from existing loans amounting to RM1,132 million will be from bilateral and multilateral sources to finance ongoing projects, primarily for education as

well as for upgrading and rehabilitation of water supplies.

Debt

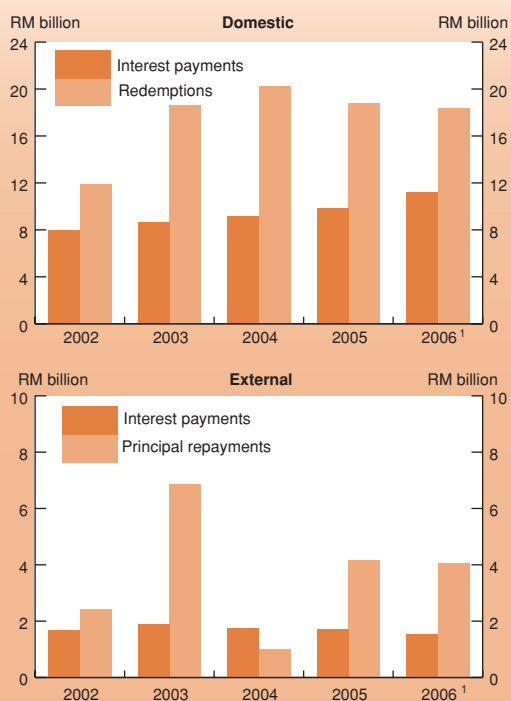
Prudent debt management remains an integral thrust of fiscal policy. Effective policies and an efficient debt monitoring system ensure that the debt level is contained at a manageable level. By the end of 2006, both the Federal Government and the national debt as a percentage to GDP are projected at 44.6% and 35.2%, respectively.

Total **Federal Government debt** is higher by 6.9% to RM244,374 million, with domestic debt increasing to RM217,320 million, while external debt declining to RM27,054 million, as shown in *Table 4.6*. Although total Federal Government debt has increased, its percentage to GDP remained low. This shows that the nominal GDP grows faster than the growth in debt, indicating that deficit financing has been successful in generating value-added activities. Debt service charges as a percentage of operating expenditure remains low at 12.1%.

The **national debt**, comprising all short, medium and long-term external debts of the government, Non-Financial Public Enterprises (NFPEs) and the private sector is expected to decline to RM193,278 million or 35.2% of GDP, as shown in *Table 4.7*. The lower outstanding debt is largely due to higher net repayments by the Federal Government. Short-term debt constitutes only 22.4% of the total external debt while the remainder is medium and long-term. The international reserves, in terms of its ratio to short-term debt which is a measure of reserve adequacy to meet short-term external debt obligations, is more than sufficient to cover 6.2 times of short-term debt as at end-July, 2006. The external debt service ratio, a measure of principal repayment and interest charges against the country's exports of goods and services, remains low at 4.3%, indicating the sustainability of export earnings to service the external debt obligations.

CHART 4.6

Federal Government Loans Principal Repayments, Redemptions and Charges



¹ Estimate.

TABLE 4.6

**Federal Government Debt
2005-2006**

	RM million		Share (%)		GDP (%)	
	2005	2006 ¹	2005	2006 ¹	2005	2006 ¹
Domestic debt	198,670	217,320	86.9	88.9	40.1	39.6
Treasury Bills	4,320	4,320	1.9	1.8	0.9	0.8
Investment Issues	10,100	20,100	4.4	8.2	2.0	3.7
Government Securities	166,050	173,800	72.6	71.1	33.5	31.7
Housing Loan Fund	18,200	19,100	8.0	7.8	3.7	3.5
External debt	30,000	27,054	13.1	11.1	6.1	4.9
Market loans	21,169	17,805	9.3	7.3	4.3	3.2
Project loans	8,831	9,249	3.9	3.8	1.8	1.7
Total	228,670	244,374	100.0	100.0	46.2	44.6

¹ Estimate.

TABLE 4.7

**National Debt
2005-2006**

	RM million		Share (%)		GDP (%)	
	2005	2006 ¹	2005	2006 ¹	2005	2006 ¹
Medium and long-term debt	150,215	149,950	76.2	77.6	30.3	27.3
Public sector	86,118	84,082	43.7	43.5	17.4	15.3
Federal Government	30,000	27,054	15.2	14.0	6.1	4.9
NFPEs	56,118	57,028	28.5	29.5	11.3	10.4
Guaranteed	17,579	21,824	8.9	11.3	3.5	4.0
Non-guaranteed	38,539	35,204	19.6	18.2	7.8	6.4
Private sector	64,097	65,868	32.5	34.1	12.9	12.0
Short-term debt	46,798	43,328	23.8	22.4	9.4	7.9
Total	197,013	193,278	100.0	100.0	39.8	35.2

¹ Estimate.

CHART 4.7

Federal Government External Debt by Currency

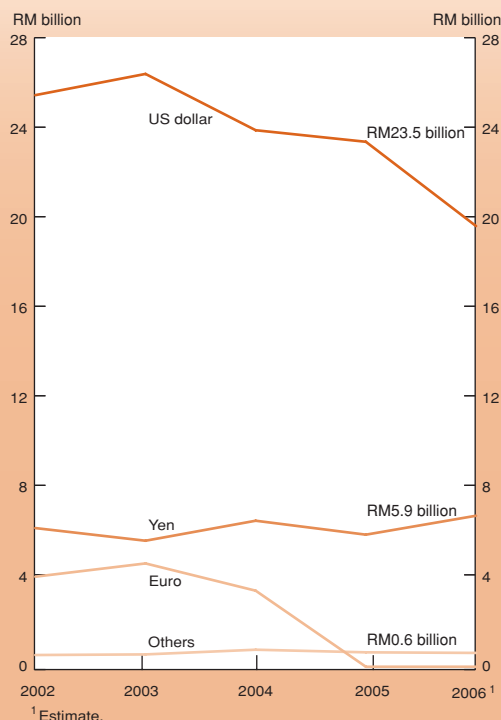


TABLE 4.8

Consolidated State Governments Financial Position 2005-2006

	RM million		Change (%)	
	2005	2006 ¹	2005	2006 ¹
Current account				
Revenue	11,968	12,668	19.7	5.8
Operating expenditure	6,144	7,360	9.5	19.8
Current account balance	5,824	5,308	32.9	-8.9
Development account				
Gross development expenditure	4,548	5,628	18.9	23.7
Development fund	4,221	5,180	19.9	22.7
Water supply fund	327	448	7.2	37.0
Less: Loan recoveries	202	127	11.0	-37.1
Net development expenditure	4,346	5,501	19.3	26.6
Overall balance	1,478	-193		
% of GDP	0.3	-		

¹ Revised estimate.

State Governments

Financial position of state governments remains healthy...

Despite higher operating expenditure, the consolidated state governments' current account in 2006 is expected to register a surplus amounting to RM5,308 million. However, as development expenditure is expected to remain large, the overall financial position of the state governments is envisaged to record a small deficit of RM193 million, as shown in *Table 4.8*. The overall deficit is financed largely by Federal Government grants and loans as well as the use of accumulated financial assets of state governments.

Total revenue is projected to grow by 5.8% to RM12,668 million on account of better performance, particularly land taxes, the rates of which have been revised upwards by most

states early this year. States' own revenue sources consisting of direct and indirect taxes as well as non-tax revenue remains the major component, contributing 71.9% of total revenue while the balance is grants from the Federal Government. The performance of states' own revenue sources is envisaged to remain at previous year's level at RM9,119 million (2005: RM9,264 million), particularly from contribution of petroleum and forestry royalties, land premiums and taxes as well as profits and dividends from investments, which together account for more than 60%.

Operating expenditure is expected to increase by 19.8% to RM7,360 million while development expenditure by 23.7% to RM5,628 million in 2006. Emolument and supplies and services constitute 60.5% of the total operating expenditure. As for development expenditure, more than 50% is directed to the agriculture and rural sectors, housing, public amenities as well as expansion and upgrading of infrastructure.

The 9MP places increased emphasis on balanced development to narrow the gap between regions, states as well as between rural and urban areas. Disparities in terms of per capita income, incidence of poverty, digital divide and inadequacy of infrastructure and amenities will be tackled through specific programmes and projects to spearhead economic activities at the state level.

General Government

As shown in *Table 4.9*, the financial position of the general government, which consists of the consolidated accounts of the Federal Government, state governments, local authorities and statutory bodies after taking into account inter-government transfers and net lending, is expected to register a deficit of RM16,811 million or 3.1% of GDP. Statutory bodies and state governments together accounted for more than 80% of the overall deficit. This indicated that they do not have adequate resources from their own sources of revenue and will have to rely on grants from Federal Government. In 2006, the Government has allocated RM9,183 million and RM2,907 million for the operating expenditures of statutory bodies and state governments, respectively, as shown in *Table 4.3*.

Non-Financial Public Enterprises (NFPEs)

NFPEs continue to outperform...

The consolidated financial position of the NFPEs is expected to record another bumper current surplus of RM83,395 million in comparison to the previous year (2005: RM57,890 million), as shown in *Table 4.10*. This is largely contributed by better revenue performance, which is envisaged to increase by 18.1% to RM287,476 million. Operating expenditure is higher by 10%, mainly to enhance capacity to improve products and service delivery. Despite the rising trend in cost of doing business, the NFPEs continue to perform well and remain resilient to the challenging environment. Coinciding with the launch of the 9MP, the NFPEs will continue to play a prominent role in the development and expansion of the Malaysian economy, as well as strengthening its presence in the region. In this regard, development expenditure is expected to increase further by 41.7% to RM48,723 million in 2006. The bulk of the development expenditure is directed towards building new capacity as well as upgrading and rehabilitation of existing facilities. NFPEs as a group, is expected to achieve a higher overall surplus amounting to

TABLE 4.9

Consolidated General Government Financial Position 2005-2007

	RM million			Change (%)		
	2005	2006 ¹	2007 ²	2005	2006 ¹	2007 ²
Current account						
Revenue	123,583	138,607	153,113	6.2	12.2	10.5
Operating expenditure	107,126	116,260	124,656	5.4	8.5	7.2
Current account balance	16,457	22,347	28,457	12.1	35.8	27.3
Development expenditure	30,989	39,158	45,517	-3.1	26.4	16.2
Overall balance	-14,532	-16,811	-17,060			
% of GDP	-2.9	-3.1	-2.9			

¹ Revised estimate.

² Budget estimate, excluding 2007 tax measures.

TABLE 4.10

**Consolidated NFPEs Financial Position¹
2005-2006**

	RM million		Change (%)	
	2005	2006 ²	2005	2006 ²
Revenue	243,455	287,476	12.8	18.1
Current expenditure	185,565	204,081	19.6	10.0
Retained income	57,890	83,395	-4.7	44.1
% of GDP	11.7	15.2		
Development expenditure	34,373	48,723	39.5	41.7
Overall balance	23,517	34,672	-34.8	47.4
% of GDP	4.7	6.3		

¹ Refer to 30 major NFPEs.² Revised estimate.

RM34,672 million in 2006 despite significant increase in development expenditure.

PETRONAS' continued efforts to discover more oil and gas reserves have achieved significant results with new gas discoveries in offshore Peninsular Malaysia and Sarawak. During the year, PETRONAS has also concluded new long-term sale and purchase contracts with parties in Japan and China for the supply of liquefied natural gas (LNG). In addition, PETRONAS has established a retail business presence in Indonesia with the official opening of its first gas service station there. Recently, a second liquefied petroleum gas (LPG) facility in Vietnam was launched to cater for the local retail market. These developments are expected to further boost revenue growth in the near future.

During the year, PETRONAS has also increased the number of LNG tankers to strengthen its global market position as the single largest operator. Among other significant investments undertaken was a joint venture by its subsidiary AET Tanker Holdings, which owns and operates Very Large Crude Carrier (VLCC) and other tankers to haul crude oil and condensates. The construction of production, storage and

handling facilities in Kikeh for Murphy Sabah Oil is another significant investment in addition to other ongoing projects such as Mega Methanol Plant in Labuan and oil refinery base in Malacca. In order to strengthen its position as a global player, PETRONAS has continued to invest internationally, including entering into new concession agreements in Egypt and Turkmenistan as well as taking equity position in Rosneft in Russia.

Leveraging on its strong presence in the South Asia and ASEAN region, Telekom Malaysia Berhad's (TM) revenue is expected to increase, particularly in the mobile, internet and multimedia segments with the largest contribution coming from Indonesia. The introduction of new products, such as iTalk with Mobile and new product packages in broadband segment, will help to mitigate the declining fixed line sales in the domestic market. On capital expenditure, the bulk is geared towards expanding and enhancing the network for cellular services both locally and abroad. Other investments consist of further expansion of broadband and data-related services facilities and the establishment of a Research and Development (R&D) Complex in Cyberjaya.

Following the upward revision of electricity tariffs and supported by increased electricity demand, Tenaga Nasional Berhad's (TNB) income outlook is expected to remain positive. Current expenditure is also expected to increase following hike in fuel costs and additional generation capacity payments to two new Independent Power Producers (IPP). One of the TNB initiative was to adopt a "preventive rather than reactive maintenance strategy" in order to reduce cost and minimise supply disruptions. TNB has also taken steps to enhance productivity and efficiency through the implementation of Automatic Meter Reading System (AMR) to improve the accuracy of meter reading. On development expenditure, the bulk is for the rehabilitation and upgrading of power stations, transmission and distribution networks. The projects undertaken, among others, include Ulu Terengganu Hydroelectric Scheme Development, Prai Power Station rehabilitation and upgrading of Manjung and Sepang power stations. On overseas investment,

a significant amount is directed towards Shoaiba Independent Power and Water Project in Saudi Arabia, which is expected to generate good investment returns.

Consolidated Public Sector

In 2006, the consolidated public sector account is expected to continue to record a higher current balance of RM105,008 million, an increase of 43.3% (2005: RM73,301 million; -2.6%), on account of better revenue performance of NFPEs, particularly PETRONAS. Despite a significant increase in development expenditure, the overall surplus is expected to be higher amounting to RM17,687 million or 3.2% of GDP in 2006 (2005: RM8,850 million; 1.8% of GDP), as shown in *Table 4.11*.

Outlook 2007

Translating the 9MP into effective programmes and projects...

The 2007 Budget, like the previous year's budget, is also a building block to the 9MP which seeks to build a strong foundation for sustaining long-term growth whilst taking measures to mitigate short-term concerns such as persistent high oil

prices, inflationary pressures and rising global interest rates.

For 2007, a total allocation amounting to RM157,496 million, an increase of 11.6% over 2006 is budgeted for both operating and development expenditures. The increased expenditure is aimed at sustaining the growth momentum given the more challenging external environment. Total revenue is expected to remain buoyant, contributed mainly from much higher oil-related revenue which is expected to contribute RM53,730 million or 39.9% of total revenue (2006: RM45,002 million; 37.3%).

In keeping with fiscal consolidation, the deficit is, however, expected to fall further to 3.4% of GDP to preserve fiscal soundness in the event of adverse or unintended developments. Government will continue to judiciously manage its finances to ensure value-for-money and effective spending, particularly in ensuring that the benefits from Government expenditure reach the targeted groups. Operating allocation is expected to increase by 7.2% to RM112,986 million in order to sustain Government operations, particularly in its continuing quest to provide better services and amenities to the public. On development expenditure, the Government will continue to focus on spending that can build income-generating capacity, help enhance

TABLE 4.11

Consolidated Public Sector Financial Position 2005-2007

	RM million			Change (%)		
	2005	2006 ¹	2007 ²	2005	2006 ¹	2007 ²
Revenue	94,961	102,456	111,504	-0.1	7.9	8.8
Operating expenditure	106,633	115,084	124,108	5.6	7.9	7.8
NFPEs current surplus	84,973	117,636	128,923	4.6	38.4	9.6
Public sector current balance	73,301	105,008	116,319	-2.6	43.3	10.8
Development expenditure	64,451	87,321	83,153	13.6	35.5	-4.8
General government	30,078	38,598	45,115	-6.2	28.3	16.9
NFPEs	34,373	48,723	38,038	39.5	41.7	-21.9
Overall balance	8,850	17,687	33,166			
% of GDP	1.8	3.2	5.6			

¹ Revised estimate.

² Budget estimate, excluding 2007 tax measures.

economic efficiency as well as to create a more conducive investment climate. In this regard, total development allocation is expected to increase significantly by 24.3% to RM44,510 million in 2007.

Mindful of inflationary pressures, the Government will monitor prices of essential goods to ensure sufficient supplies to curb indiscriminate price increases, hoarding and profiteering activities. The Government's subsidy allocation remains high to help mitigate the higher cost of living. In the 2007 Budget, total subsidy amounting RM11,908 million (2006: RM11,251 million) will be allocated mainly for petroleum products, interest rates including loans for higher education, paddy and fertilisers, school textbooks and nutrition schemes.

In the face of increasing competition from regional economies, the Government will continue to provide a business friendly environment to attract foreign direct investment (FDI) as well as promote private investment. Projecting Malaysia as a moderate, modern and progressive nation is important. Equally imperative is the need for improvements in the public service delivery system, logistics, and infrastructure. In this regard, the government will continue to improve the administration and work processes in critical departments and agencies. In addition, instituting key performance indicators (KPI) among government-linked companies (GLCs), particularly public utilities providers, local authorities and land offices as well as establishing clear and consistent investment policies and guidelines will create a more competitive and conducive business environment. The efforts, thus far, have been positive as reflected in the improved ranking for Malaysia from 28th place in 2005 to 23rd in 2006 among 60 countries by Institute for Management Development (IMD) as published in the World Competitiveness Yearbook 2006.

The government will launch another Visit Malaysia Year in 2007 in line with the growing importance of tourism revenue. For this purpose, RM400 million will be allocated for promotion of tourism, including eco-tourism and upgrading of tourism infrastructure.

With regard to medium and longer-term strategies, the Government will continue to drive the private sector to move the economy up the value chain. Several aspects are incorporated in the Budget, among which are more focused R&D spending, developing new sources of growth, particularly in biotechnology, ICT, automation, agro-based industries as well as design and marketing in manufacturing. In this regard, the Budget will allocate RM1,000 million for focused research in these areas. Quality human capital is a pivotal element in moving the economy up the value chain. Hence, the Budget will continue to place emphasis in ensuring good education, retraining, linkages between universities and industries as well as encouraging venture capital and protection of intellectual property rights. Towards this end, the Budget will allocate RM6,600 million for the Ministry of Education and the Ministry of Higher Education under the development expenditure.

Disparities continue to exist between the rural and urban population, regions and states. In line with the National Mission and the 9MP, efforts will focus on ensuring that the benefits of development will be more evenly distributed. Public amenities, employment opportunities and income-generating activities will be made more accessible through regional growth centres. The Budget will provide allocation amounting to RM4,000 million for programmes aimed at eradicating poverty and for narrowing the rural-urban divide.

Issues relating to the environment and its impact on quality of life remain a concern. These include improving water quality and rivers, proper management of landfills, preservation of catchment areas and reducing air pollution. The Government will continue to provide adequate allocation to ensure better management of the nation's natural resources and environment. Proper accounting of costs and benefits of development projects as well as taking firm actions against those responsible for environmental degradation will be enforced more stringently. At the same time, more incentives will be provided for adopting energy-saving technologies and environmental-friendly ways in extracting depleting resources or in carrying out development projects.

The Government will continue to foster caring values among Malaysians to ensure the disabled and disadvantaged groups are not left out of the mainstream development. The Government will also continue to address social ills such as drug addiction, juvenile delinquency and crimes. In this regard, RM73 million is allocated for National

Strategic Plan for HIV/AIDS and National Influenza Pandemic Preparedness Plan. At the same time, the Government will continue to streamline the administration of welfare and disbursement of welfare payments to minimise incidences of recipients receiving multiple benefits whilst ensuring that no deserving cases are left out.