



Public Sector Finance

4



Public Sector Finance

Overview

Challenges to fiscal policy...

The 2009 Budget was formulated amid moderating world growth, high prices of fuel, food, metals and other commodities, geopolitical uncertainties as well as the fallout from the financial market turmoil in the United States. The convergence of these factors on a small open economy like Malaysia has posed significant challenges to Government finance. The Government has to tread the delicate balance between sustaining growth momentum and managing inflationary pressures while maintaining fiscal discipline. Additional expenditure was incurred in 2008 despite the anticipated savings from the restructuring of various subsidies aimed at reducing wastage and plugging leakages. As oil price continues to remain high, the coverage of social assistance programmes was further extended to assist the lower and middle income groups to meet the rising cost of living. In addition, new and additional funds were allocated to finance food security programmes.

The high fuel and food prices necessitated the Government to adopt a more flexible stance towards fiscal consolidation which has been pursued since 2002. The budget deficit is expected to increase to 4.8% in 2008 after achieving a low of 3.2% in 2007. Despite a widening budget deficit, the conduct of fiscal policy and operations will continue to focus on fiscal discipline with budgetary controls in place

to ensure effective public spending. Towards this end, various measures were introduced through a series of administrative circulars to implement cutbacks in discretionary expenditure while development projects were reviewed, revised or reprioritised.

Given the challenging environment, the public sector is expected to expand by 4.7%, contributing 1.1 percentage points to GDP growth in 2008 (2007: 7.9%, 1.9 percentage points). The public sector's share to GDP will, therefore, remain high at 24.1% (2007: 24.3%).

Federal Government

Higher deficit due to increased commitments...

While revenue collection is envisaged to remain favourable amid high commodity prices and larger contribution from oil-related sources, operating expenditure is expected to increase significantly on account of increased fuel and food subsidy payments, measures to increase food production and stabilise prices of essential food items as well as other initiatives to mitigate the impact of rising cost of living, particularly on the lower income groups. Hence, in 2008, the total expenditure of the Federal Government is expected to increase significantly by 20.5% to RM197,211 million, compared with the 15.5% increase in revenue. Consequently, the overall deficit of the Federal Government is expected to widen to RM34,462 million or 4.8% of GDP (2007: -RM20,658 million; -3.2%), as shown in *Table 4.1*.

TABLE 4.1

Federal Government Financial Position 2007 – 2009

	RM million			Change (%)		
	2007	2008 ¹	2009 ²	2007	2008 ¹	2009 ²
Revenue	139,885	161,558	176,220	13.2	15.5	9.1
Operating expenditure	123,084	150,953	154,170	14.3	22.6	2.1
Current balance	16,801	10,605	22,050	6.0	-36.9	107.9
Gross development expenditure	40,564	46,258	51,729	13.3	14.0	11.8
Less: Loan recovery	3,105	1,191	1,229	267.0	-61.6	3.2
Net development expenditure	37,459	45,067	50,500	7.1	20.3	12.1
Overall balance	-20,658	-34,462	-28,450			
% of GDP	-3.2	-4.8	-3.6			

¹ Revised estimate.

² Budget estimate, excluding 2009 tax measures.

Revenue

Revenue collection remains favourable...

The Federal Government revenue in 2008 is expected to register a strong growth of 15.5% to RM161,558 million or 22.6% of GDP in 2008 (2007: 13.2%; RM139,885 million; 21.8% of GDP) on account of higher collection of both tax and non-tax revenue, as shown in *Table 4.2*. The increase in revenue is due to favourable commodity prices, higher crude oil prices, better tax administration and enforcement activities supported by sustained economic growth. Tax revenue is expected to increase by 13.2% to RM107,737 million, contributing 66.7% to total revenue (2007: 9.9%; RM95,168 million; 68.0%). Similarly, boosted by good returns on investment income, non-tax revenue is also expected to remain high at RM53,821 million or an increase of 20.4% (2007: RM44,717 million; 21.1%).

Direct tax is expected to increase by 11.8% to RM77,579 million (2007: 12.7%; RM69,396 million), mainly on account of a significant increase in individual income tax of 25.1% to RM14,593 million following the salary revision for the civil service, effective July 2007, and the enforcement of the automatic monthly tax deduction system in January 2008. The higher

growth in individual income tax is also attributed to increased efficiency in tax collection. More than one million taxpayers, including 146,522 sole proprietorships, used the e-filing system in 2008, an increase of 74.1% over 2007. The total number of registered taxpayers as at end-December 2007 was 6,345,258 of which 90.8% or 5,761,118 were individual taxpayers. Of this, taxable returns comprised 139,460 companies and 1,894,044 individuals. The Inland Revenue Board (IRB) is one of the many Government agencies aggressively promoting online payment services. New payment channels offered by several major commercial banks facilitated timely payment of income tax at no cost. Tax payers now have the option of paying their income tax through the automated teller machines, phone banking, internet banking services or over the counter at most branches nationwide. Meanwhile, revenue collection is also expected to be enhanced through more frequent audit activities and stringent tax investigations.

Corporate income tax is anticipated to grow at a steady pace of 3.7% to RM33,325 million despite rising operational costs. The oil and gas industry remains the largest taxpayer, followed by the wholesale and retail sector, financial intermediaries, manufacturing sector

TABLE 4.2

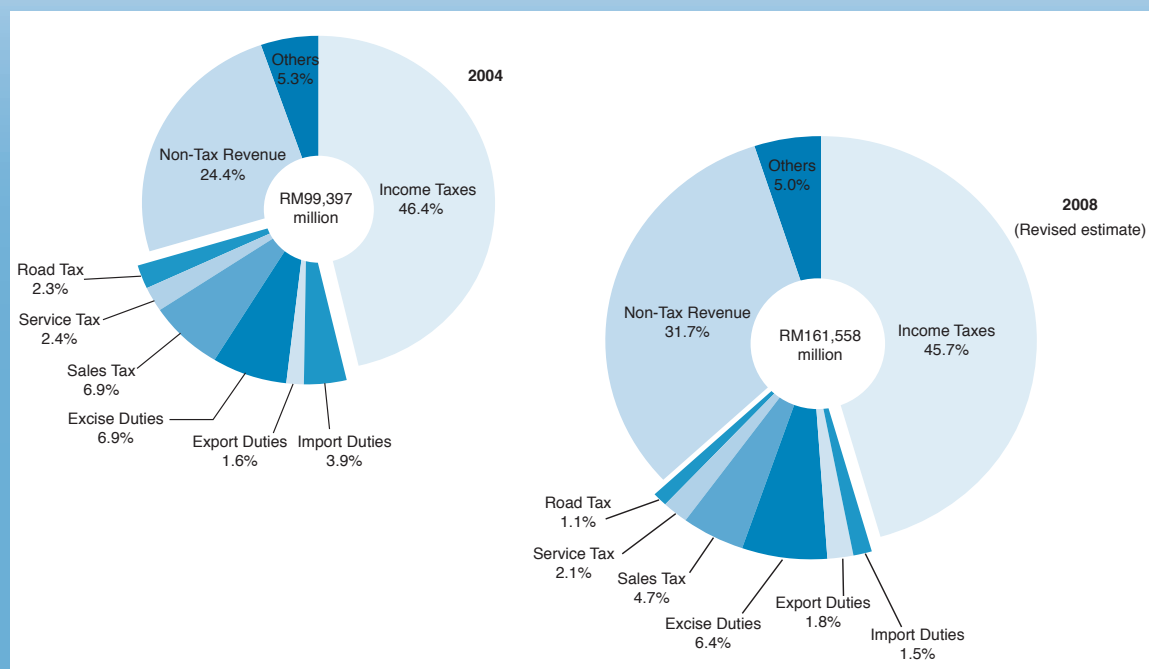
Federal Government Revenue 2007 – 2009

	RM million			Change (%)			Share (%)		
	2007	2008 ¹	2009 ²	2007	2008 ¹	2009 ²	2007	2008 ¹	2009 ²
Tax revenue	95,168	107,737	124,379	9.9	13.2	15.4	68.0	66.7	70.6
Direct tax	69,396	77,579	92,126	12.7	11.8	18.8	49.6	48.0	52.3
of which:									
Companies	32,149	33,325	35,780	21.4	3.7	7.4	23.0	20.6	20.3
PITA ³	20,453	24,511	35,826	-1.1	19.8	46.2	14.6	15.2	20.3
Individual	11,661	14,593	15,399	14.4	25.1	5.5	8.3	9.0	8.7
Indirect tax	25,772	30,158	32,252	2.8	17.0	6.9	18.4	18.7	18.3
of which:									
Excise duties	8,991	10,369	11,038	4.8	15.3	6.5	6.4	6.4	6.3
Sales tax	6,642	7,580	8,059	1.7	14.1	6.3	4.7	4.7	4.6
Non-tax revenue	44,717	53,821	51,841	21.1	20.4	-3.7	32.0	33.3	29.4
of which:									
Licences/permits	9,434	11,779	13,059	2.4	24.9	10.9	6.7	7.3	7.4
Investment income	32,408	38,874	35,442	30.7	20.0	-8.8	23.2	24.1	20.1
Total revenue	139,885	161,558	176,220	13.2	15.5	9.1	100.0	100.0	100.0
% of GDP	21.8	22.6	22.3						

¹ Revised estimate.² Budget estimate, excluding 2009 tax measures.³ Petroleum Income Tax.

CHART 4.1

Federal Government Revenue



and real estate. Meanwhile, petroleum income tax (PITA) is expected to increase by 19.8% to RM24,511 million due to buoyant prices and higher sales volume. Other direct taxes, including stamp duties (RM3,588 million), withholding tax (RM1,216 million) and cooperative income tax (RM191 million) are projected to remain stable on account of sustained business transactions and other economic activities.

Indirect taxes are envisaged to increase by 17.0% to RM30,158 million, mainly from excise duties (RM10,369 million), sales tax (RM7,580 million) and service tax (RM3,415 million). Export duties are expected to increase by 28.2% to RM2,977 million, mainly on account of higher output and prices for palm oil, crude oil and other commodities. In contrast, import duties are anticipated to contract by 0.5% to RM2,411 million and continue to decline further due to progressive commitments on liberalisation of tariffs under the ASEAN Free Trade Area as well as other bilateral and regional trade arrangements.

In 2008, additional revenue in the form of windfall profit levy estimated at RM870 million will be collected from independent power producers (IPPs) and palm oil producers. For the IPPs, a 30% levy is imposed on returns on assets in excess of the 9% threshold in their audited accounts. Palm oil producers, on the other hand, will pay a windfall profit levy at the plantation level, based on output of fresh fruit bunches. Planters in Peninsular Malaysia are charged a levy of 15% while those in Sabah and Sarawak, 7.5%. However, oil palm plantations less than 40.5 hectares or 100 acres as well as millers of crude palm oil and crude palm kernel oil are excluded from the windfall levy. The windfall profit levy replaces the cess collected from plantations under the Cooking Oil Stabilisation Scheme (COSS) implemented since June 2007. Revenue from windfall profit levy is expected to cushion, in part, the payment under the COSS.

Collection of **non-tax revenue** is projected to increase by 20.4% to RM53,821 million. The main sources of non-tax revenue are dividend income, mainly from *Petroleum Nasional Berhad*

(PETRONAS) (RM30,000 million) and from licences and permits (RM11,779 million). The major components of licences and permits are petroleum royalties and road tax. While petroleum royalties are expected to contribute a substantial sum of RM6,272 million to revenue, road tax collection is envisaged to remain steady at RM1,715 million. Other sources of non-tax revenue include proceeds from securitisation of Government employees' housing loans (RM4,100 million) as well as dividend income from *Khazanah Nasional Berhad* (RM2,000 million) and *Bank Negara Malaysia* (RM1,500 million).

Over the years, the Government has introduced several tax measures through the annual budget to enhance the nation's competitiveness, stimulate economic activity as well as embrace policies to position Malaysia as a choice destination for foreign direct investment (FDI). Corporate tax was progressively reduced to 25% in 2009, while a single-tier tax system was introduced to facilitate the administration of corporate tax. Profits are taxed at company level while dividends received are tax-exempt. To enhance the quality, resilience and competitiveness of public-listed companies in Bursa Malaysia, stamp duty exemption given on all instruments pertaining to mergers and acquisitions was extended for a further three years to 2010. Effective 2008, newly-established small and medium enterprises (SMEs) are given a two-year flexibility to pay taxes at the end of financial year, instead of monthly instalments. This will enable SMEs to better manage their finances in the initial stages of business operations. In addition, to promote Islamic fund management activities, all local and foreign companies managing approved Islamic funds of local or foreign investors are granted income tax exemption till 2016 on all fees received.

Tax administration system was further improved through the establishment of the Customs Appeal Tribunal and the introduction of Customs Ruling and the Advance Ruling in income tax administration to promote greater transparency, certainty, predictability and enhance public confidence. Furthermore, a framework for audit and investigation was issued to clarify, among others, the duties and responsibilities of both

the IRB officers and tax payers. These, and other tax measures implemented over the years, are anticipated to spur higher economic activity, increase profitability of firms and, in turn, enhance revenue collection.

Expenditure

Competing demands on Government expenditure...

Guided by the goals of the Ninth Malaysia Plan (9MP) and the reassessment of priorities under the Mid-Term Review, the Government will continue to focus on enhancing the nation's competitiveness, strengthening human capital development as well as ensuring the well-being of the *rakyat*. In this regard, the public sector delivery system will be continuously improved to facilitate private sector initiatives. Focus will be on implementing people-centric projects and programmes that generate economic opportunities for all, in particular the rural and urban poor, thereby narrowing the development gap. Poverty alleviation programmes and targeted assistance for the hard-core poor will be improved to hasten the achievement of the zero poverty target by 2010.

The year 2008 has been a difficult year, given heightened inflationary pressures on account of high food and commodity prices in an environment of moderating growth. Coming from a position of strength built since the Asian financial crisis in 1997/1998, Malaysia has the appropriate policy options to weather the external and domestic challenges. The Government has adopted a proactive stance by restructuring fuel subsidies to ensure a more efficient allocation of resources and minimise leakages. In addition, fuel subsidies were restructured to ensure that future generations of Malaysians will also benefit from oil and gas revenue.

Steps have also been taken to stabilise food prices, improve food production and distribution as well as strengthen social assistance programmes for the poor and vulnerable groups. The Government has also made cutbacks in discretionary expenditure while projects and programmes are being reviewed and streamlined. In the light of escalating cost of building materials and to support the construction industry, variations in contract value for ongoing and newly approved development projects have been allowed to ensure that project implementation is not adversely affected and completed on schedule.

TABLE 4.3

Federal Government Operating Expenditure by Object 2007 – 2009

	RM million			Change (%)			Share (%)		
	2007	2008 ¹	2009 ²	2007	2008 ¹	2009 ²	2007	2008 ¹	2009 ²
Emolument	32,587	36,214	37,985	14.3	11.1	4.9	26.5	24.0	24.6
Debt service charges	12,911	13,101	13,473	3.3	1.5	2.8	10.5	8.7	8.7
Grants to state governments	3,904	4,402	4,903	36.9	12.8	11.4	3.2	2.9	3.2
Pensions and gratuities	8,251	8,412	7,279	17.7	1.9	-13.5	6.7	5.6	4.7
Supplies and services	23,622	25,900	26,488	12.9	9.6	2.3	19.2	17.2	17.2
Subsidies	10,481	34,103	33,799	3.7	225.4	-0.9	8.5	22.6	21.9
Grants to statutory bodies ³	10,707	13,064	13,805	16.4	22.0	5.7	8.7	8.7	9.0
Refunds and write-off	1,062	966	890	270.0	-9.1	-7.9	0.9	0.6	0.6
Others	19,559	14,792	15,548	20.0	-24.4	5.1	15.9	9.8	10.1
Total	123,084	150,953	154,170	14.3	22.6	2.1	100.0	100.0	100.0
% of GDP	19.2	21.1	19.5						

¹ Revised estimate.

² Budget estimate, excluding 2009 tax measures.

³ Includes emolument.

Given the increasing demand on fiscal resources, the Federal Government total expenditure is projected to increase by 20.5% to RM197,211 million in 2008 (2007: 14.0%; RM163,648 million). Of this, operating expenditure accounts for 76.5%, while the balance is for development expenditure.

Operating expenditure is expected to increase by 22.6% to RM150,953 million in 2008 (2007: 14.3%; RM123,084 million). Expenditure on *emolument*, the largest component constituting 24.0% of operating expenditure, is projected to increase by 11.1% to RM36,214 million (2007: 26.5%; 14.3%; RM32,587 million), mainly on account of the salary revision for civil servants, effective 1 July 2007.

Subsidies accounting for 22.6% of operating expenditure now constitute the second largest component. The cost of subsidies is expected to reach RM34,103 million in 2008 on account of high prices of crude oil, food, metals and other commodities globally. The category encompasses, among others, fuel subsidies, subsidies, incentives and assistance given for food security programmes, scholarships and educational assistance schemes as well as social welfare programmes and provision for the *Orang Asli*. In 2008, the cost of subsidies is anticipated at RM27,255 million (79.9%), incentives RM937 million (2.7%), and assistance, RM5,911 million (17.3%).

Fuel subsidy, the largest component in the category is expected to increase substantially by 142.2% to RM18,100 million in 2008 (2007: -1.1%; RM7,473 million) despite measures taken to restructure it. As world crude oil prices increase, the Government has to incur additional expenditure to absorb the difference between the subsidised retail price and the market price. Effective 5 June 2008, the price of petrol was increased from RM1.92 per litre to RM2.70 and diesel, from RM1.58 per litre to RM2.58. The Government had planned that the retail price of petrol reflect the monthly market price of world crude oil with the Government maintaining the subsidy of 30 sen per litre, effective 1 September 2008. However, in view of softening world crude

oil prices in August, the price of petrol was reduced to RM2.55 per litre and diesel, by 8 sen to RM2.50 per litre on 23 August 2008.

As part of the restructuring of subsidies, a one-off cash rebate was disbursed to registered private vehicle owners, effective April 2008 to help them cope with rising costs. Rebates of RM625 are given to owners of private vehicles with engine capacity less than 2000 cc and RM150 for motorcycles up to 250 cc. About 95% of private vehicles registered in Malaysia are below 2000 cc. Owners of private vehicles with engine capacity above 2000 cc and motorcycles above 250 cc are given a road tax rebate of RM200 and RM50, respectively. The cash rebate of RM625 was also extended for private vehicles with engine capacity up to 3000 cc registered in Sabah and Sarawak on account of rough terrain in remote areas. The cash rebate is expected to cost the Government an estimated amount of RM5,000 million in 2008. As of 21 August 2008, *Pos Malaysia Bhd* disbursed RM1.6 billion to 3.7 million registered vehicle owners.

The price of diesel was increased and streamlined at RM1.43 per litre for approved transport operators, fishermen and Malaysian vessel owners registered with the Fisheries Department. A monthly incentive of RM200 is given to vessel operators and employees to encourage them to engage in fishing activities, while another 10 sen is offered for every kilogram of fish landed. Effective 27 July 2008, taxis nationwide using unleaded petrol were also given a subsidy to contain operational costs, thus keeping taxi fares low. Taxis are entitled to purchase petrol using the fleet card at the previously subsidised rate of RM1.92 per litre up to 720 litres a month. Purchase of petrol beyond the quota will be at the retail pump price.

In Budget 2008, several initiatives were introduced to improve the quality of life of the poor and vulnerable. A monthly allowance of RM300 per month was extended to the poor and needy senior citizens, disabled workers as well as for eligible persons taking care of the disabled, bedridden and patients suffering from chronic illnesses. To mitigate the adverse impact of inflationary

pressures on these groups, the coverage of social welfare programmes was widened. The eligibility criteria for the disabled has been revised to include those earning less than RM1,200 per month (previously RM750) while households earning less than RM720 (previously RM400) are now eligible for welfare payments.

Measures to curb inflation include, among others, streamlining the prices of sugar, flour and milk nationwide. Price controls have been maintained on essential food items, including sugar, milk, rice, bread and flour. The price of cooking gas has been standardised nationwide and maintained at RM1.75 per kilogramme while subsidies were extended to producers of bread and cooking oil to cushion the price of rising inputs, thereby stabilising the retail price of these food items. In addition, provision has been made to recruit 2,000 unemployed graduates to closely monitor the prices of essential goods and ensure their adequate supply as well as prevent indiscriminate price increases. To provide relief to food retailers and consumers, the service tax of 5% is levied on food outlets with an annual sales turnover of RM3 million, up from RM500,000.

The Government also set up an Anti-Inflation Council comprising members from the public and private sectors to study issues relating to inflation and make strategic policy decisions. The Council has since been subsumed under the Economic Council to address broader issues affecting the economy.

The long-term strategy to achieve food self-sufficiency, improve productivity in the food sub-sector, as well as maintain price stability of essential food items is being addressed through the National Food Security Policy announced in April 2008. The measures include, among others, increasing rice stockpile and food production in agriculture, fisheries and livestock; opening up new and idle land for food production; strengthening the marketing and distribution system; as well as providing incentives for farmers, fishermen and livestock entrepreneurs to ease the burden of rising cost of agriculture inputs. Towards this end, various subsidies, incentives and financial assistance costing RM2,500 million have been allocated for programmes in food security.

Financial aid is also extended for scholarships and various educational assistance programmes, including nutrition programmes, tuition vouchers and contribution to the *Kumpulan Wang Amanah Pelajar Miskin* or KWAPM. In addition, a sum of RM34 million is provided to improve the standard of living of the *Orang Asli*.

Another main component of operating expenditure is *supplies and services* which accounts for 17.2% of total operating expenditure or RM25,900 million (2007: 19.2%; RM23,622 million). Major expenditure in this component are repair and maintenance, professional and other services, communication and utilities, supplies as well as rentals. In tandem with measures taken by the Government to scale down discretionary expenditure, this component is expected to register a slower growth of 9.6% (2007: 12.9%).

Among the administrative measures put in place to rein in expenditure include a reduction in spending for supplies and services as well as asset acquisition under operating expenditure for all ministries. A freeze is imposed on renting new office space, renovation work in offices, restructuring of departments as well as the recruitment of personnel in non-critical positions. Overseas travel is limited to important meetings with the number of officials attending, reduced.

Debt service charges are envisaged to remain manageable at RM13,101 million or 8.7% of operating expenditure in 2008 (2007: RM12,911 million; 10.5%). *Grants to statutory bodies* are expected to surge by 22.0% to RM13,064 million (2007: 16.4%; RM10,707 million), mainly on account of increased transfers to the 21 IPTAs and three teaching hospitals which absorb 59.8% of the grants disbursed. Other major recipients of grants include *Majlis Amanah Rakyat* (MARA) (15.1%) and IRB (6.8%). Grants are allocated to statutory bodies to meet expenditure requirements, mainly emolument as well as supplies and services.

Pensions and gratuities which account for 5.6% of the total operating expenditure are anticipated to remain stable at RM8,412 million (2007: 6.7%; RM8,251 million). This is on account

TABLE 4.4

Federal Government Development Expenditure by Sector 2007 – 2009

	RM million			Change (%)			Share (%)		
	2007	2008 ¹	2009 ²	2007	2008 ¹	2009 ²	2007	2008 ¹	2009 ²
Economic services	20,116	20,718	27,745	15.6	3.0	33.9	49.6	44.8	53.6
of which:									
Agriculture and rural development	3,842	4,414	3,522	-3.9	14.9	-20.2	9.5	9.5	6.8
Trade and industry	4,904	4,450	4,303	44.7	-9.3	-3.3	12.1	9.6	8.3
Transport	8,500	7,813	7,605	9.7	-8.1	-2.7	21.0	16.9	14.7
Social services	12,893	15,594	17,794	35.4	21.0	14.1	31.8	33.7	34.4
of which:									
Education and training	6,271	8,483	10,087	17.2	35.3	18.9	15.5	18.3	19.5
Health	1,496	2,247	2,308	15.3	50.2	2.7	3.7	4.9	4.5
Housing	2,947	2,011	1,400	118.8	-31.8	-30.4	7.3	4.3	2.7
Security	5,702	7,032	4,073	18.7	23.3	-42.1	14.1	15.2	7.9
General administration	1,853	2,914	2,117	-54.5	57.3	-27.4	4.6	6.3	4.1
Total	40,564	46,258	51,729	13.3	14.0	11.8	100.0	100.0	100.0
% of GDP	6.3	6.5	6.5						

¹ Revised estimate.

² Budget estimate.

of the deferment of payment of pensions and gratuities arising from the extension in the optional retirement age of civil servants from 56 to 58 years. Other main components of operating expenditure are *grants and transfers to state governments* (RM4,402 million) and *asset acquisition* (RM2,194 million).

Development expenditure is projected at RM46,258 million in 2008 (2007: RM40,564 million), an increase of 14.0% over 2007. In terms of sectoral allocation, economic services remain the largest recipient, followed by social services sector, security and general administration.

The *economic services* sector accounts for 44.8% or RM20,718 million of total development expenditure in 2008 (2007: 49.6%; RM20,116 million). The transport sub-sector is allocated the largest sum of RM7,813 million or 37.7% (2007: RM8,500 million; 42.3%), mainly for the construction, maintenance and upgrading of roads and bridges, railways, airports, ports and jetties as well as rural and village roads. Major ongoing projects in the sub-sector include the

construction of the Integrated Transport Terminal at Bandar Tasik Selatan, Sentul-Batu Caves electrified double tracking project, road works from Sepulut to Kalabakan in Sabah, the Trans Eastern Kedah Hinterland, upgrading of airports in Kuching, Kota Kinabalu and Labuan as well as purchase of rolling stock by *Keretapi Tanah Melayu Berhad* (KTMB). New projects slated for the year include the Ipoh-Padang Besar and the Seremban-Gemas electrified double tracking projects, the Seremban Middle Ring Road Phase 2 and the East Coast Highway Phase 2 from Jabur to Kuala Terengganu.

The trade and industry sub-sector is allocated an amount of RM4,450 million (2007: RM4,904 million). Major development programmes in the sub-sector include upgrading infrastructure facilities in industrial areas, funding of strategic investments, skills and entrepreneur development, vendor development programme for the automotive sector as well as the promotion, development and marketing of SME *halal* hub and *halal* parks in various states. SMEs account for 99.2% of total business establishments, employ 5.6 million

workers and contribute about 35.0% of GDP. Given the wide linkages in the economy, SMEs will continue to be given due attention through improved access to funding, technical expertise and greater exposure overseas to strengthen their resilience and improve competitiveness. The biotechnology sector will be given a boost through the provision of infrastructure and technological facilities. Funds will be allocated for the acquisition of technology, commercialisation of biotechnology initiatives, promotion of agrobiotechnology activities as well as research and development (R&D) in biodiversity.

The tourism sub-sector is given an allocation of RM370 million as concerted efforts are underway to implement various programmes, improve tourism-related facilities and amenities as well as diversify tourism products. Focus, among others, is on developing niche tourism products, including eco-tourism projects and increasing homestay activities which will also generate income for the rural community. Malaysia is leveraging on its rich cultural diversity to promote, among others, the *MalaysiaKitchen* programme abroad.

Substantial allocation is also provided to modernise and commercialise the agriculture sector. Towards this end, the agriculture and rural development sub-sector is allocated RM4,414 million (2007: RM3,842 million). Programmes undertaken include poverty alleviation in Sabah and Sarawak, drainage and irrigation improvements, land and regional development, fisheries and livestock as well as various agriculture projects. Projects to uplift the rural poor in Sabah and Sarawak include the provision of basic infrastructure, income generating activities such as livestock breeding, cultivation of fruits and vegetables as well as contract farming. To ensure sustainability of these activities, provision is also made for advisory services and skills training. Meanwhile, the focus on programmes in agriculture and rural development sub-sector is to improve padi production and encourage the cultivation of floriculture, herbs and spices. To promote greater food self-sufficiency and reduce the food deficit, allocation is provided to increase food production, in particular rice, fruits and vegetables. The public utilities and energy sub-sector is expected to expend RM3,131 million (2007: RM2,358 million) for water supply, sewerage and electricity

projects. Emphasis will be on improving access to public amenities in rural areas.

Investment in human capital development is an imperative as the nation moves up the value chain to become a knowledge-based economy. Hence, the *social services* sector is allocated RM15,594 million (2007: RM12,893 million), of which RM8,483 million is for education and training sub-sector. Higher education is provided the largest sum to improve accessibility and quality of tertiary education. Towards this end, various higher education projects and programmes will be implemented. Research, development and commercialisation (R&D&C) will be enhanced in four Research Universities, namely, *Universiti Malaya*, *Universiti Sains Malaysia*, *Universiti Kebangsaan Malaysia* and *Universiti Putra Malaysia*. Construction works are ongoing for the upgrading and expansion of *Universiti Pendidikan Sultan Idris*, *Universiti Malaysia Sabah* and *Universiti Malaysia Pahang*. To increase the number and quality of trained workers to meet industry requirements, programmes as well as infrastructure and facilities will be enhanced in Advanced Technology Training Centres (ADTEC), polytechnics, skills training centres and community colleges. Allocation is also provided for the maintenance and upgrading of equipment in these institutes. Ongoing projects in 2008 include, among others, ADTECs in Taiping, Bintulu, Kemaman and Jerantut as well as skills training centres in Marang, Tanjung Malim and Kuala Krai.

The health sub-sector is the second largest recipient in this category with an allocation of RM2,247 million, accounting for 14.4% of the social services sector (2007: RM1,496 million; 11.6%). The expenditure is for the building, upgrading and maintenance of hospitals and clinics, purchase of medical and health equipment as well as the provision of a comprehensive range of healthcare services. Rural health care services will be further improved while Phase 2 of the Hospital Information System or HIS will be implemented in 11 hospitals, including Sarikei, Jasin and Temerloh. Major ongoing projects in this sub-sector include the construction of Ulu Kinta Allied Health Science College, Kuala Pilah Nursing College, Tampin Hospital and Cheras Rehabilitation Hospital.

The housing sub-sector is allocated a sum of RM2,011 million (2007: RM2,947 million). Of this, a substantial sum is provided for the building of low-cost houses and Government quarters for civil servants, including the armed forces and police. Consistent with the Government's policy of providing adequate and affordable housing for the low income group, the implementation of the *Program Perumahan Rakyat* (PPR) and PPR *Bersepadu* will be accelerated while abandoned housing projects, rehabilitated. Currently, 17,660 units of PPR *Disewa* and PPR *Bersepadu* are under construction.

Apart from the health, education and housing sub-sectors, a substantial allocation of RM1,786 million is also provided to local authorities and community and welfare services, RM564 million for community and rural development as well as RM395 million for culture, youth and sports. Allocation for local authorities as well as community and welfare services sub-sectors is, among others, for solid waste management (RM350 million), fire-fighting services (RM506 million), welfare services for the elderly and marginalised groups (RM113 million), upgrading and building parks and recreational facilities as well as cleaning up rivers and flood mitigation projects. The Klang River Rehabilitation Project from *Jalan Jelatek* to *Masjid Jamek* is one such programme undertaken this year. To uplift the socio-economic standard of the rural poor, allocation is also provided for community and rural development with emphasis on village rehabilitation schemes and programmes that promote education, skills training and economic activities (RM425 million). While agropolitan projects in Pulau Banggi, Sabah and Tanjung Gahai, Pahang under the *Program Lonjakan Mega Luar Bandar* are well underway, development of similar projects in other states will be expedited to improve real incomes among the hardcore poor in the less developed and remote areas. Provision is also made to ensure the *Orang Asli* community have better access to public and social amenities as well as continue to be involved in income generating activities (RM107 million).

Development expenditure for the *security* sector is expected to increase by 23.3% to RM7,032 million (2007: 18.7%; RM5,702 million). Of this, RM4,712 million is for defence sub-sector, mainly

for the purchase and upgrading of equipment and surveillance for the armed forces. To ensure public safety as well as a safe business and investment environment, a sum of RM2,320 million is provided for the internal security sub-sector. The allocation will be utilised to strengthen civil defence, upgrade the capacity and capability of the uniformed personnel as well as enhance maritime enforcement and surveillance. Police presence and visibility will also be increased in crime-prone areas while efforts are underway to equip each police contingent with a mobile forensic unit.

Expenditure for *general administration* is projected to increase by 57.3% to RM2,914 million (2007: -54.5%; RM1,853 million) to further enhance productivity and efficiency of the public sector delivery system. Allocation is provided for various ICT projects, including computerisation of Government departments as well as the development and wider usage of e-government applications. In addition, provision is also made for land acquisition, buildings and fittings as well as for renovation, refurbishment and maintenance of government facilities. The maintenance culture in the public sector will be reinforced to prolong the economic life of Government assets and provide quality service to the public.

Financing

Continued reliance on domestic sources of finance...

The Federal Government borrowings are projected to increase following the higher deficit level for the year. However, the Government will continue to source its borrowings locally and mainly from non-inflationary sources, while ensuring that borrowings are primarily for financing development expenditure. Given the ample liquidity in the banking and financial system as well as the high savings rate in the country, the increased borrowings are not expected to impact negatively on private sector borrowings.

Total gross borrowings of the Federal Government for the year are expected to amount to RM60,533 million, as shown in *Table 4.5*. Of this, RM60,000 million constitutes domestic borrowing while

RM533 million is from external sources. Of the total gross borrowing, RM25,216 million is for the repayment of existing debt while the balance of RM35,317 million constitutes additional borrowings for the year which will be used mainly to finance the deficit.

In 2008, RM43,500 million will be raised through the issuance of Malaysian Government Securities (MGS), of which RM37,500 million will be raised through open tender while the balance of RM6,000 million, through private placement. Of this, new issues amounting to RM8,000 million will be issued through three open tenders and one private placement while the balance of RM35,500 million are re-openings of 14 existing MGS, of which four are private placements. MGS accounts for 72.5% of the total gross domestic borrowings. During the first seven months of the year, the coupon rates for new issues of MGS with 5 and 10 year maturities were more favourable, ranging between 3.46% - 3.58% per annum, compared to 3.81% - 3.89% for MGS with similar maturities during the same period in 2007.

The Government is also expected to issue five new Government Investment Issues (GIIs) up to RM16,500 million for the year, including one through private placement. As at end-June 2008, major investors of MGS and GIIs continue to be Employees Provident Fund (49.1%), foreign holders (18.6%), banking institutions (11.4%) and insurance companies (8.2%). The regular issuance of Government securities provides the benchmark yield curve for further development of the domestic bond market.

The Government remains committed to reducing external debt to minimise exposure to foreign exchange risk. Since 2005, repayment of existing loans have exceeded drawdowns. As no new market loans are envisaged for the year, drawdowns will be from existing project loans to finance projects and programmes related to education and training, power generation, water supply, sewerage services, poverty eradication as well as ICT infrastructure and rail transport. In 2008, a total of RM533 million is expected to be drawn down from bilateral (RM453 million) and multilateral (RM80 million) sources.

TABLE 4.5

Federal Government Financing 2007 – 2008

	RM million		Share (%)	
	2007	2008 ¹	2007	2008 ¹
Gross borrowings	54,570	60,533	100.0	100.0
Domestic	54,081	60,000	99.1	99.1
Investment Issues	10,000	16,500	18.3	27.3
Government Securities	44,081	43,500	80.8	71.9
External	489	533	0.9	0.9
Market loans	-	-	-	-
Project loans	489	533	0.9	0.9
Repayments	33,084	25,216	100.0	100.0
Domestic	28,281	24,291	85.5	96.3
External	4,803	925	14.5	3.7
Net Borrowings	21,486	35,317		
Domestic	25,800	35,709		
External	-4,314	-392		
Change in assets²	-828	-855		
Total	20,658	34,462		

¹ Estimate.

² (-) indicates accumulation of assets.

Debt

Government debt sustainable...

The adoption of prudent debt management strategies remain an essential part of fiscal policy. Effective policies coupled with an efficient and up-to-date debt monitoring system will ensure that debt levels remain manageable and sustainable. By end-2008, both the Federal Government and the national debt as percentage of GDP are projected to be 42.4% and 31.9%, respectively (2007: 41.6%; 29.2%).

Total **Federal Government debt** is projected to increase by 13.7% to RM303,227 million as at end-2008 (end-2007: 10.1%; RM266,722 million), as shown in *Table 4.6*. This is on account of higher domestic debt incurred during the year to meet financing requirements. In contrast, the Federal Government external debt continues to decline, from RM37,284 million in 2003 to RM18,307 million as at end-2008 in the absence

TABLE 4.6

**Federal Government Debt
2007 – 2008**

	RM million		Share (%)		GDP (%)	
	2007	2008 ¹	2007	2008 ¹	2007	2008 ¹
Domestic debt	247,120	284,920	92.7	94.0	38.5	39.8
Treasury Bills	4,320	4,320	1.6	1.4	0.7	0.6
Investment Issues	28,000	42,500	10.5	14.0	4.4	5.9
Government Securities	191,700	213,800	71.9	70.5	29.9	29.9
Housing Loan Fund	23,100	24,300	8.7	8.0	3.6	3.4
External debt	19,602	18,307	7.3	6.0	3.1	2.6
Market loans	12,586	11,458	4.7	3.8	2.0	1.6
Project loans	7,016	6,849	2.6	2.3	1.1	1.0
Total	266,722	303,227	100.0	100.0	41.6	42.4

¹ Estimate.

of new external loans except for drawdowns from existing project loans. Hence, the external debt as a percentage of total debt is expected to decline further to 6.0% (2007: 7.3%) due to repayments of external debt through domestic borrowings at more favourable interest rates. Total debt service charges as a proportion of operating expenditure and revenue remain low at 8.7% and 8.1%, respectively in 2008 (2007: 10.5%; 9.2%). The Federal Government external debt is denominated mainly in US dollars, pound sterling and yen.

National debt comprises the external debts of the Federal Government, Non-Financial Public Enterprises (NFPEs) and the private sector. In tandem with better risk assessment practices for the economy and consistent with international standards and best practices on the treatment of offshore entities in external data compilation, adjustments have been made in the national debt data. Effective January 2008, all entities in Labuan International Business and Financial Centre or Labuan IBFC are regarded as residents, hence their debt exposure with the rest of the world will be part of the national debt.

As a result of the new classification in the external debt data, national debt is expected to increase by 21.8% to RM228,353 million or 31.9% of GDP as at end-2008 (end-2007: 1.6%; RM187,445 million; 29.2% of GDP), as shown in *Table 4.7*. Of the medium and long-term debt, the public sector external debt accounts for 31.2% of the total compared to 32.8% in 2007.

The major portion of the nation's external debt is of medium- and long-term maturities comprising the external debts of Federal Government (8.0%), NFPEs (23.2%) and the private sector (29.7%). Short-term debt constitutes 39.1% of the total national debt, of which the major holder is the banking sector. External debt service ratio, the ratio of principal payment and interest charges to the country's exports of goods and services, is projected to remain low at 3.8%, reflecting the strength of export earnings to service the external debt obligations. As at 15 August 2008, the ratio of international reserves to short-term debt, a measure of reserve adequacy to meet short-term external obligations, is more than sufficient to cover 5 times the short-term debt.

TABLE 4.7

National Debt 2007 – 2008

	RM million		Share (%)		GDP (%)	
	2007	2008 ¹	2007	2008 ¹	2007	2008 ¹
Medium-and long-term debt	132,977	139,126	70.9	60.9	20.7	19.4
Public sector	61,456	71,250	32.8	31.2	9.6	10.0
Federal Government	19,602	18,307	10.5	8.0	3.1	2.6
NFPEs	41,854	52,943	22.3	23.2	6.5	7.4
Guaranteed	17,848	12,081	9.5	5.3	2.8	1.7
Non-guaranteed	24,006	40,862	12.8	17.9	3.7	5.7
Private sector	71,521	67,876	38.2	29.7	11.1	9.5
Short-term debt	54,468	89,227	29.1	39.1	8.5	12.5
Total	187,445	228,353	100.0	100.0	29.2	31.9

¹ Estimate.

CHART 4.2

Federal Government External Debt By Currency



¹ Revised estimate.

² Includes pound sterling.

Note: Figures in the bar are % to total.

State Governments

Marginal deficit...

The consolidated financial position of State Governments will register a steady current account surplus despite higher operating expenditure. However, as development expenditure is expected to grow faster than revenue growth due to higher commitments, the consolidated financial position of State Governments is expected to register a deficit of RM1,216 million or 0.2% of GDP in 2008 (2007: +RM205 million; +0.03% of GDP), as shown in *Table 4.8*. As in the past, the overall deficit will be financed mainly by loans from the Federal Government and from the States' own financial assets.

Total revenue of states comprises both direct and indirect taxes as well as non-revenue receipts which are mainly grants and reimbursements from the Federal Government. Total revenue is projected to grow 4.4% to RM14,086 million (2007: 5.9%; RM13,498 million) on account of better tax revenue performance, in particular from land taxes, and non-revenue receipts. States own sources of revenue are anticipated to remain stable at RM10,417 million, contributing 74.0% to total revenue (2007: RM10,378 million; 76.9%). The major contributors are petroleum and forestry royalties, land premiums and taxes as well as dividends and interest on investment. Grants and reimbursements from the Federal Government are expected to amount to RM3,669 million (2007: RM3,120 million), mainly for financing infrastructure projects, social and public facilities and amenities.

Total operating expenditure of state governments is estimated to increase 7.7% to RM7,707 million in 2008 (2007: 7.3%; RM7,157 million), on account of higher emolument and expenditure on supplies and services, which constitute 69.0% of total operating expenditure. Similarly, development expenditure is expected to further increase 18.2% to RM7,815 million (2007: 24.8%;

TABLE 4.8

Consolidated State Governments Financial Position 2007 – 2008

	RM million		Change (%)	
	2007	2008 ¹	2007	2008 ¹
Current account				
Revenue	13,498	14,086	5.9	4.4
Operating expenditure	7,157	7,707	7.3	7.7
Current account balance	6,341	6,379	4.5	0.6
Development account				
Gross development expenditure	6,613	7,815	24.8	18.2
Development fund	6,258	7,274	24.7	16.2
Water supply fund	355	541	28.2	52.4
Less: Loan recovery	477	220	18.7	-53.9
Net development expenditure	6,136	7,595	25.4	23.8
Overall balance	205	-1,216		
% of GDP	0.03	-0.2		

¹ Revised estimate.

RM6,613 million) to finance housing, public amenities, agriculture and rural development, as well as water supply projects.

General Government

Financial position of general government manageable...

The consolidated accounts of the Federal Government, state governments, local authorities and statutory bodies, after netting out intra-government transfers and lending, is estimated to register a deficit of RM32,418 million or 4.5% of GDP, as shown in *Table 4.9*. The deficit is slightly smaller than the Federal Government deficit of RM34,462 million or 4.8% of GDP on account of a higher surplus generated by statutory bodies.

TABLE 4.9

Consolidated General Government Financial Position 2007 – 2009

	RM million			Change (%)		
	2007	2008 ¹	2009 ²	2007	2008 ¹	2009 ²
Current account						
Revenue	162,504	181,366	191,900	13.2	11.6	5.8
Operating expenditure	135,398	162,622	167,345	13.9	20.1	2.9
Current account balance	27,106	18,744	24,555	9.8	-30.8	31.0
Development expenditure	44,926	51,162	51,827	9.7	13.9	1.3
Overall balance	-17,820	-32,418	-27,272			
% of GDP	-2.8	-4.5	-3.5			

¹ Revised estimate.

² Budget estimate, excluding 2009 tax measures.

Non-Financial Public Enterprises

Lower surplus for NFPEs...

The consolidated financial position of the NFPEs is projected to record a lower surplus of RM4,504 million (2007: RM27,372 million), as shown in *Table 4.10*. The surplus is attributed to the anticipated slower growth in consolidated revenues coupled with a higher increase in both operating and capital expenditure.

The consolidated revenue is forecast to grow by 1.7% to RM322,835 million (2007: 17.2%; RM317,505 million), contributed mainly by PETRONAS, *Tenaga Nasional Berhad*, Malaysia Airlines System Berhad, *Telekom Malaysia Berhad*, TM International Berhad and United Engineers (Malaysia) Berhad. Higher petroleum price, improved operational efficiency, increased returns on overseas investment as well as a revision in energy tariffs are expected to have positive impact on revenue growth. The operating expenditure is expected to grow 8.6% to RM258,981 million (2007: 13.4%; RM238,561 million), mainly due to increase in the cost of energy and raw materials as well as for improvements in product and service delivery. Despite rising operational costs, the

NFPEs are expected to perform well and remain resilient, strengthened by the significant progress made from the ongoing Government-Linked Companies transformation programmes. NFPEs continue to play a prominent role in the economy as they contribute to capital formation, transfer of technology and skills development as well as provide employment opportunities. Development expenditure is expected to increase further by 15.1% to reach RM59,350 million (2007: 12.9%; RM51,572 million). This is mainly for expanding,

TABLE 4.10

Consolidated NFPEs Financial Position¹ 2007 – 2008

	RM million		Change (%)	
	2007	2008 ²	2007	2008 ²
Revenue	317,505	322,835	17.2	1.7
Current expenditure	238,561	258,981	13.4	8.6
Retained income	78,944	63,854	30.6	-19.1
% of GDP	12.3	8.9		
Development expenditure	51,572	59,350	12.9	15.1
Overall balance	27,372	4,504		
% of GDP	4.3	0.6		

¹ Refers to 30 major NFPEs.

² Revised estimate.

upgrading and rehabilitation of existing production facilities and undertaking major investments abroad to strengthen future earnings and generate value for its stakeholders.

The overall financial position of **PETRONAS** is expected to be strong on account of higher revenue as well as operational efficiency and plant reliability coupled with prudent business strategies. For the financial year end-March 2008, the Federal Government received RM62.8 billion from PETRONAS while a sum of RM4.8 billion was disbursed as royalties to Terengganu, Sabah and Sarawak. Oil-related revenues from PETRONAS were in the form of dividend (RM30 billion), corporate tax and PITA (RM26 billion), royalty payments (RM4.7 billion) and export duties (RM2.1 billion). Since its incorporation in 1974, a total of RM403.3 billion has been paid out to the Government, including royalties to the relevant state governments. PETRONAS remains the single largest contributor to the nation's revenue, impacting positively on economic growth.

PETRONAS also contributes to the economy through the sale of subsidised natural gas at RM14.31 per million British thermal units (mmbtu) (RM6.40 per mmbtu before the subsidy revamp in June 2008) to the power sector, as against the market price of RM63 per mmbtu. Cumulative revenue loss or subsidy provided since 1997 stands at RM77.9 billion, of which RM62.6 billion was for TNB and IPPs and the balance of RM15.3 billion, to the non-power sector, including small industrial, commercial, residential users and natural gas for vehicles (NGV).

PETRONAS operates in a challenging environment. While the high crude oil price is a boon to PETRONAS, it is also expected to have an impact on the operating and capital expenditure. Demand for crude oil from China, India and other emerging economies remains strong and has intensified activity in the oil and gas sector. However, supply side constraints such as insufficient refinery capacity, acute shortage of skilled personnel and rising cost of metals and equipment have driven up costs in the industry. In addition, speculative activities, geopolitical tensions and an increasingly difficult

working environment due to inclement weather and technologically challenging conditions have worsened the situation. Nevertheless, PETRONAS remains active in the international oil and gas industry. A joint venture agreement was signed with Santos Limited of Australia to acquire a substantial stake in the latter's proposed integrated liquefied natural gas (LNG) project in Gladstone, Queensland. As the partners will also cooperate in the exploration and production of upstream coal seam gas (CSG), the acquisition marks its maiden entry into the CSG industry.

The corporate social responsibility (CSR) contribution of PETRONAS is in terms of educational assistance and human capital development. It supports the University Technology of PETRONAS and Malaysian Maritime Academy or ALAM. To date, scholarships worth RM2 billion have been disbursed to more than 30,000 students in various fields. In addition, PETRONAS also undertakes community and humanitarian programmes at home and abroad through smart partnerships with non-government organisations.

Telekom Malaysia Berhad is expected to continue sustaining its revenue performance despite a more competitive operational environment. Following the demerger exercise, the international operations of TM have been subsumed under TM International Berhad (TMI), a new entity. This will enable TM to give greater focus to the further development of the ICT infrastructure and services in the country, in particular, the advancement of the broadband services. TM will be involved in the High Speed Broadband (HSBB) mega project through a public-private partnership with the Government, which is expected to be rolled out in phases over a 10-year period. Phase 1 of the project, covering Klang Valley and Iskandar Malaysia, is anticipated to cost RM11.3 billion. The Government will co-invest in the project which comprises end-to-end infrastructure covering access, core network and international connectivity, aims to provide better coverage as well as faster access to quality broadband services. The comprehensive rollout of broadband services for corporate, universities and home users will not only enhance the nation's competitiveness but also draw in more FDI.

The ICT and creative industries is one of the focus sectors in Iskandar Malaysia and TM is poised to play an active role in providing HSBB and telecommunications infrastructure to more than 700,000 commercial and residential premises. Beneficiaries include Nusajaya, Central Business District, Eastern Gate Development, Western Gate Development and Senai–Skudai corridors. Spread over a 10 year period, TM's investment in ICT facilities is expected to boost economic activities within the corridors as well as attract more investments into the targeted ICT and multimedia industry in Iskandar Malaysia.

TM actively contributes to society through education, sports development and community building. It finances the Multimedia University which is also a research institution with more than 25 centers of excellence. Through its foundation, *Yayasan Telekom Malaysia*, scholarships and loans have been provided to more than 10,000 students to pursue their studies locally and abroad. TM is also active in sports development, in particular football, and is heavily involved in developing grassroot talent. In the area of community and nation building, TM undertakes graduate re-training programme to equip graduates with language and other soft skills to meet the needs of the private sector. Other initiatives include the promotion of broadband in schools through its TMeSchool project and charity work among the needy and underprivileged children.

TM International, the holding company of international mobile operation is expected to deliver higher earnings due to aggressive marketing and competitive pricing as it sets its sights on regional expansion. Currently, TMI has strategic mobile and non-mobile telecommunication operations and investments in a number of Southeast Asian countries and South Asia. Profitable ventures include, among others, XL of Indonesia, Dialog in Sri Lanka and Celcom in Malaysia. A major portion of its capital expenditure is expected to be directed towards developing, expanding and upgrading its ICT infrastructure and services at home and abroad as well as for expansion of its overseas operations. Furthermore, to increase

customer base in new markets, intensive efforts are also underway to develop and expand its broadband and data-related services facilities.

Tenaga Nasional Berhad turnover is expected to further increase, following the upward revision in electricity tariffs effective July 2008. This is also supported by higher electricity sales to commercial, industrial and domestic sectors in tandem with sustained economic activity. However, higher global prices of gas, coal and metals, including copper and steel are expected to result in increasing operating costs, impinging on operating margins. In addition, the upward revision in the price of gas, effective July 2008, by 123.0% to RM14.31 per mmbtu will impact further its margin. However, the revision in electricity tariff is expected to cushion the impact of this increase.

TNB continues to rehabilitate and upgrade its existing infrastructure as well as undertake new investments to ensure adequate system capacity and supply reliability. Capital expenditure will be made for systems improvement to strengthen the transmission and distribution network, building new transmission lines, substations, regional control centers as well as installing the Geographical Information System to improve asset maintenance and security. Major projects underway include the installation of a 750 MW gas fired combined cycle plant at the Tuanku Jaafar Power Station scheduled for completion in December 2008. Also due for completion by year-end is the Cameron Highlands Rehabilitation Project which involves the upgrading of a 40-year old hydro scheme. Presently, TNB is replacing old distribution switchgears and transformers nationwide to enhance power generation and distribution facilities. In view of the rising cost of fossil fuels, TNB has embarked on two new hydro power projects in Ulu Jelai (Cameron Highlands) and Hulu Terengganu. The projects are slated for completion by 2014. Overseas projects undertaken by TNB include the expansion to the Shoaiba Phase 3 IWPP desalination plant in Saudi Arabia. The expansion project worth USD232 million utilises reverse osmosis desalination technology and is expected to commence commercial operation by early 2009.

TNB's CSR activities are centred on "powering the nation" through education, R&D, sports, environment and community welfare development programmes. TNB funds *Universiti Tenaga Nasional* and *Institut Latihan Sultan Ahmad Shah* and provides scholarships and loans through *Yayasan Tenaga Nasional*. In powering a 'green nation', TNB ensures that projects undertaken are environmentally friendly. For instance, the coal-powered *Stesen Janakuasa Sultan Azlan Shah* in Manjung, Perak employs clean coal technology to conserve the natural environment. TNB also supports the firefly conservation project in Kuala Selangor and continues to undertake research on the lampyridae firefly through its subsidiary, TNB Research. In offshore islands and remote areas away from the common electricity grid, TNB uses renewable energy to produce electricity. The wind/solar hybrid plant in Pulau Perhentian Kecil in Terengganu taps on the strong wind presence to power its wind turbines. Other remote areas use solar hybrid power plants which run on diesel and the sun's

rays tapped from solar panels. In the area of sports development, TNB concentrates on hockey and cricket, and works at all levels to promote the games.

Consolidated Public Sector

The financial position of the consolidated public sector comprises the accounts of the general government and the NFPEs after netting out transfers and net lending. In 2008, the consolidated public sector financial account is expected to register a lower current account surplus of RM82,373 million (2007: RM105,852 million) on account of higher operating expenditure at all levels of the public sector despite a better revenue performance. Coupled with a significant increase in development expenditure, the consolidated public sector finance is expected to record an overall deficit amounting to RM27,926 million or 3.9% of GDP (2007: +RM9,542 million; +1.5% of GDP), as shown in *Table 4.11*.

TABLE 4.11

Consolidated Public Sector Financial Position 2007 – 2009

	RM million			Change (%)		
	2007	2008 ¹	2009 ²	2007	2008 ¹	2009 ²
Revenue	110,733	126,844	140,640	8.6	14.5	10.9
Operating expenditure	134,953	161,353	166,833	14.6	19.6	3.4
NFPEs current surplus	130,072	116,882	103,039	29.2	-10.1	-11.8
Public sector current balance	105,852	82,373	76,846	24.7	-22.2	-6.7
Development expenditure	96,310	110,299	95,718	11.3	14.5	-13.2
General government	44,738	50,949	51,496	9.5	13.9	1.1
NFPEs	51,572	59,350	44,222	12.9	15.1	-25.5
Overall balance	9,542	-27,926	-18,872			
% of GDP	1.5	-3.9	-2.4			

¹ Revised estimate.

² Budget estimate, excluding 2009 tax measures.

Outlook for 2009

Fiscal consolidation on track...

The public sector financial position is expected to be stronger and reflect a much better overall balance in line with the continued expansion in the Malaysian economy in 2009. Private sector activity is envisaged to strengthen further, in tandem with the recovery in the electrical and electronics cycle, firm commodity prices, increased intra-regional trade, diversified export markets as well as improved prospects for the global economy towards the second half of the year. This is expected to stimulate investment and consumption activities, contributing positively to GDP growth. While the private sector strengthens its position in the economy, the Government will continue to further improve the public sector delivery system through streamlining processes and procedures, expediting approvals and introducing wider ICT applications. A marginal increase in operating expenditure and slower growth in development expenditure, supported by prospects of a strong revenue performance in 2009 will enable the Government to resume consolidating its finances. Consequently, the Federal Government fiscal deficit is projected to decline to 3.6% of GDP in 2009.

Fiscal policy will continue to remain prudent, effective and efficient to support economic growth. Total Federal Government expenditure in 2009 is expected to increase 4.4% to RM205,899 million, with operating expenditure increasing 2.1% to RM154,170 million and development expenditure, 11.8% to RM51,729 million, respectively. Given the impact of high prices of fuel, food and other commodities as well as construction-related materials, the Government will provide funding for subsidy payments, including food security, social assistance and welfare programmes, as well as ensure timely implementation of development projects. The increase in overall expenditure will, therefore, take into account the revised priorities in the Mid-Term Review to ensure growth momentum with price stability and improved quality of life. In tandem with

the anticipated increase in economic activities, better performance of NFPEs and state-owned companies as well as improved tax collection, overall revenue is envisaged to increase by 9.1% to RM176,220 million.

While the 2009 Budget addresses current concerns which include, among others, sustaining growth momentum amid domestic inflationary pressures against a challenging external environment, it will also contribute towards enhancing the long-term productive capacity and resilience of the nation. The 2009 Budget will, therefore, implement programmes and projects that ensure the well-being of the *rakyat*, improve public transportation system, develop quality human capital and enhance the nation's economic resilience.

The 2009 Budget will allocate RM154,170 million for **operating expenditure**, accounting for 74.9% of total expenditure. The bulk of operating expenditure is for locked-in and charged items such as *emolument*, *debt service charges*, as well as *pensions and gratuities*. A sum of RM26,488 million or an increase of 2.3% will be allocated for *supplies and services* to ensure proper maintenance of public assets and improve the quality of public services. Sub-items include, among others, maintenance and repair services, rental payments, telecommunications and utilities as well as professional fees. An allocation of RM86,328 million will also be provided for *grants, transfers and fixed charges*, including subsidies and contributions to statutory bodies and state governments. Total payments for *subsidies* are expected to remain high at RM33,799 million or 21.9% of operating expenditure. Subsidies will be allocated mainly for fuel (RM21,000 million), interest rate differentials, including loans for higher education (RM978 million), *padi*-related schemes (RM1,160 million), as well as the cash rebates for private vehicle owners till March 2009 (RM2,000 million). In addition, an allocation of RM1,200 million will be provided to subsidise the retail price of cooking oil. The Government will continue to ensure adequate supplies of essential goods nationwide and monitor their prices to prevent hoarding, smuggling and profiteering.

Incentives will continue to be provided for the farming community under the National Food Security Policy to defray the high costs of inputs and increase food production in agriculture, fisheries, aquaculture and livestock. An allocation of RM345 million will be provided to implement this programme which will benefit about 350,000 farmers and livestock entrepreneurs. Another 148,000 farmers will be given incentives amounting to RM244 million to increase rice production. Likewise, efforts will also be accelerated to improve the welfare of fishermen. Fishing vessel operators and employees will continue to be given the monthly incentive of RM200 and the 10 sen incentive for every kilogramme of fish landed. Operators of river passenger boats mainly in Sarawak and Sabah will also be assisted through cash payments totalling RM11 million.

Social assistance programmes will be further strengthened and given an allocation of RM6,268 million to assist the rural, urban and hardcore poor, the disabled, single mothers, senior citizens and the *Orang Asli*. Food and nutrition programmes for kindergartens and schools will be intensified while tuition vouchers will continue to be provided for poor students.

Existing poverty alleviation programmes will be further improved to be more effective and well-targeted. The Budget will focus on measures to increase household income, promote entrepreneurship and skills training as well as provide housing assistance for the poor through *Skim Pembangunan Kesejahteraan Rakyat*. Capacity building programmes for targeted groups will be intensified through *Program Pembangunan Minda Insan*. For the urban poor, an allocation of RM13 million is provided through *Program Pembasmian Kemiskinan Bandar* under the Ministry of Housing and Local Government to address issues on urban poverty and reduce the income gap. Furthermore, a sum of RM61 million will be provided through *Amanah Ikhtiar Malaysia* (AIM) under *Skim Kewangan Mikro Bandar* and *Skim Srikandi* to promote greater self reliance and nurture entrepreneurship among urban poor. About 140,000 participants are expected to benefit from these schemes. To ensure that

the benefits of growth and development are more equitably distributed, an allocation of RM72 million is allocated through the *Jabatan Hal Ehwal Orang Asli* to implement projects and programmes aimed at improving the quality of life of 149,700 *Orang Asli*.

Development allocation in 2009 will increase to RM51,729 million in line with the revised overall ceiling of the 9MP from RM200 billion to RM230 billion. The increased allocation will be for food production, projects and programmes in the regional growth corridors as well as to meet the rising cost of approved infrastructure projects.

The Government remains committed to improving public transportation, especially in urban centres. A public transport system that is safe, efficient and integrated reduces travelling time and cost of doing business, promotes a cleaner environment and improves productivity. In this regard, greater emphasis will be given to improving the capacity of and accessibility to light-rail transit, train and bus services in the Klang Valley. To reduce congestion and increase connectivity in other major cities and urban centres, concerted efforts will also be made to provide an integrated and efficient transport system.

Infrastructure development will continue to be given priority as it contributes to building capacity and efficiency in the economy. Towards this end, a sum of RM7,605 million is allocated for construction, upgrading and maintenance of roads, bridges, the railway network, ports and airports. New and ongoing construction works include the electrified double tracking projects between Seremban–Gemas, Sentul–Batu Caves and Ipoh–Padang Besar, the Seremban Middle Ring Road Phase 2, East Coast Highway Phase 2 from Jabur to Kuala Terengganu and the Jalan Ampang/Jalan Jelatek flyover as well as purchase of rolling stock by KTMB.

A substantial allocation of RM3,216 million is also provided for utilities, telecommunications, sewerage services as well as drainage and irrigation projects. Of this, a sum of RM614

million is for rural water supply and electrification projects nationwide. To expedite development in the five regional growth corridors, an allocation of RM5,000 million is provided. Major works to be undertaken include the provision of basic infrastructure and public amenities, upgrading and building of roads and bridges, improving drainage, irrigation and agriculture infrastructure, developing tourism-related facilities and amenities as well as low cost housing and other people-centric projects.

Projects and programmes to boost agricultural productivity and efficiency will be accelerated to enable agriculture to become a major source of economic growth and for the country to be a net food exporter by 2010. To realise this goal, the agriculture and rural development sector will be allocated RM3,522 million. Focus will be given to further develop and promote projects identified for their high commercial potential such as the Aquaculture Industry Zone initiative in Terengganu, Beef Valley Project in Gemas as well as Permanent Food Production Parks and Contract Farming in various states. To serve the sector more effectively, agriculture extension services will be enhanced through a substantial allocation of RM234 million while access to credit facilities made easier to farmers and firms involved in commercial agriculture. Meanwhile, Malaysia's reputation as a leading producer of *halal* products will be further enhanced through intensive promotional activities.

As Malaysia becomes a service-oriented and knowledge-based economy, quality human capital is a prerequisite for higher value added growth. To ensure that the education system meets the demand for a workforce with the right set of knowledge, skills and attitude, education and training will be given priority and allocated the largest sum of RM10,087 million or 19.5% in the 2009 Budget. Of this, RM1,021 million is for primary education, RM1,388 million for secondary education, RM4,357 million for higher education and RM1,421 million for training programmes. In addition, pre-school education, especially in rural areas, will also be expanded to nurture a strong foundation in education.

Total student enrolment in primary and secondary schools is expected to reach 5.48 million in 2009. To accommodate the increase, a total of 291 school projects will be undertaken, of which 110 are for primary schools, and 181 for secondary schools, including 15 hostels. In addition, a substantial allocation of RM467 million is also provided for the refurbishment and upgrading of schools in rural areas, including Sabah and Sarawak. Computer literacy and IT education in schools will be further enhanced through an allocation of RM65 million benefiting 574 schools. The Strategic Plan for Higher Education envisions a highly knowledgeable workforce and the creation of world class institutions in the country. To support the Strategic Plan, a sum of RM4,357 million is allocated for upgrading and improving facilities in 21 IPTAs with an expected student enrolment of 457,854 in 2009. R&D&C in four Research Universities will be enhanced through an allocation of RM362 million.

Skills training in various disciplines will be constantly improved to meet the changing demands of the labour market. Currently, there are 27 polytechnics and 90 community colleges with a student population of more than 118,800. As such, sufficient funds will be allocated to operate, refurbish and upgrade facilities as well as provide financial assistance to students. Skills training centres such as ADTEC and institutes under MARA will also be adequately funded to ensure quality training programmes are offered to meet industry demands. In 2009, a total of 23 new skills institutes, including 14 GIATMARA centres will be operational.

R&D activities will be further intensified in the biotechnology sector. Initiatives to be taken include technology acquisition, R&D in agrobiotechnology, genomics, molecular biology, pharmaceuticals as well as commercialisation of the findings. In addition, Technology Park of Malaysia will be allocated funds to carry out work on herbal biotechnology. R&D activities in science and technology as well as agriculture will be more market driven with the aim of building the sector to be one of the new sources of growth. To enhance the resilience and competitiveness

of SMEs, the sub-sector will be allocated RM629 million. Projects and programmes to be implemented through *Tabung Ekonomi Kumpulan Usahawan Nasional* or *TEKUN Nasional* and state economic development corporations include the building, purchase, renting of business premises and floor space, upgrading infrastructure and facilities in industrial areas as well as providing financial assistance. Small and Medium Industries Development Corporation (SMIDEC) will also be allocated grants amounting to RM293 million to implement various capacity building initiatives targeted to benefit 1,205 companies and 26,000 workers. Effective January 2009, SMIDEC will be known as SME Corporation Malaysia and be responsible for the overall coordination of SME policy formulation. It will also be the focal point of information, reference and advisory services for SMEs.

Tourism is the largest contributor to earnings in the services sector and has immense potential for further growth. In June 2007, Langkawi was declared a geopark, the first of its kind in Southeast Asia. In addition, the recent listing of Georgetown and Melaka as World Heritage Sites, apart from the two existing sites, Mulu Caves and Kinabalu National Park, is a testament to the concerted efforts taken by the Government and industry to promote the sector. As such, an allocation of RM936 million will be provided to the Ministry of Tourism to improve and upgrade tourism-related facilities and amenities nationwide, develop new tourism products and undertake intensive promotional activities at home and abroad. Eco-tourism will be further developed while homestay programmes increased and facilities upgraded.

About 23 million tourists are expected in 2009 bringing in RM53 billion in foreign exchange.

An allocation of RM637 million will be provided for the national service training programme which is designed to instill positive values and promote character development in youths. A total of 110,000 trainees in 87 camps nationwide are expected to benefit from the training programme.

Overall **revenue** is projected to increase by 9.1%, from RM161,558 million in 2008 to RM176,220 million in 2009, the bulk of which is expected to be contributed by tax revenue. This is on account of favourable fuel and commodity prices as well as steady corporate performance which are expected to boost collection of tax revenue by 15.4%, from RM107,737 million in 2008 to RM124,379 million in 2009. However, non-tax revenue, comprising mainly investment income, licences and permits as well as service fees, is projected to decline to RM51,841 million. The Government will continue to improve tax administration, streamline tax incentives as well as carry out tax audits to enforce greater compliance, enhance revenue collection and broaden the tax base.

The Government remains committed to improving its fiscal position while supporting growth momentum and enhancing the long term capacity of the nation. Given the better revenue prospects and prudent spending in 2009, as reflected in the slower growth in overall expenditure, fiscal consolidation will be resumed and Government finances, strengthened.