SECTION 3

Federal Government Expenditure

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Overview

The countercyclical measures undertaken by the Government through various fiscal stimulus packages and recovery plans during the COVID-19 pandemic have resulted in a positive impact to the economy, as reflected by the robust growth of 8.7% in 2022. The public expenditure management is crucial in strategising resource allocation to support the economic growth and nation-building while ensuring a sound public finance. The Government resumes the fiscal consolidation trajectory and recommence its reforms agenda in 2023 as the economy recovers post-pandemic. Nevertheless, maintaining a sound public finance is anticipated to be more challenging due to the external headwinds while meeting expenditure needs. Thus, the Government remains committed to strike a balance between providing fiscal support to effect long-term structural changes and ensuring prudent public spending.

Public expenditure policy will continue to emphasise on efficient and effective spending to enhance fiscal discipline. Expenditure management will be further improved through stringent budgetary and monitoring processes to optimise spending in ensuring value for money while minimising leakages and wastages. In this regard, the Government will undertake gradual subsidy rationalisation initiatives, shifting from broad-based subsidies to a more targeted approach. The savings from the subsidy rationalisation will be repurposed towards strengthening social protection agenda and fulfilling development needs, particularly for high growth high value programmes and projects. By pursuing expenditure discipline and reining in discretionary spending, the Government will ensure the productivity and quality of public service delivery remain uncompromised. In line with the Ekonomi MADANI framework, the Government will instill fiscal discipline as well as further enhance accountability and transparency in public expenditure management.

Expenditure in 2023

The Federal Government total expenditure for 2023 has been revised upwards to RM397.1 billion, equivalent to 21.5% of GDP, from the budget allocation of RM386.1 billion or 20.4% of GDP. The revision involved a net increment of RM11 billion in operating expenditure (OE) mainly to accommodate additional critical spending needs earmarked for existing programmes and projects, such as subsidies, supplies and services as well as initiatives under the Ekonomi MADANI framework. Of the total allocation, OE constitutes 75.6% or RM300.1 billion, while development expenditure (DE) accounts for 24.4% or RM97 billion.

In terms of total allocation by sector, the social sector received the highest allocation, amounting to RM133.7 billion or 33.7% of total expenditure, followed by the economic (RM76.5 billion; 19.3%), security (RM37.7 billion; 9.5%) and general administration (RM16.8 billion; 4.2%). In addition, charged expenditures and transfer payments, which include debt service charges (DSC), retirement charges and transfers to states, account for 33.3% of total expenditure.

For 2023, the revised OE is anticipated to increase by 2.5% to RM300.1 billion or 16.2% of GDP, predominantly due to higher subsidy outlays for electricity and cooking oil, cleaning and security services for schools as well as initiatives under the Ekonomi MADANI framework. The bulk of OE is allocated for emoluments, retirement charges, DSC as well as subsidies and social assistance, constitute 77.9% of OE.

TABLE 3.1. *Federal Government Operating Expenditure by Component, 2022 – 2024*

COMPONENT	RM MILLION			CHANGE (%)			SHARE (%)		
	2022	2023[1]	2024[2]	2022	2023[1]	2024[2]	2022	2023[1]	2024[2]
Emoluments	87,789	91,273	95,641	*2.3*	*4.0*	*4.8*	*30.0*	*30.4*	*31.5*
Retirement charges	31,397	32,079	32,446	*7.9*	*2.2*	*1.1*	*10.7*	*10.7*	*10.7*
Debt service charges	41,269	46,100	49,800	*8.4*	*11.7*	*8.0*	*14.1*	*15.4*	*16.4*
Grants and transfers to state governments	8,122	8,077	8,747	*7.6*	*-0.6*	*8.3*	*2.8*	*2.7*	*2.9*
Supplies and services	34,692	33,984	38,002	*39.2*	*-2.0*	*11.8*	*11.9*	*11.3*	*12.5*
Subsidies and social assistance	67,358	64,228	52,757	*192.3*	*-4.6*	*-17.9*	*23.0*	*21.4*	*17.4*
Asset acquisition	767	911	1,704	*28.8*	*18.8*	*87.0*	*0.3*	*0.3*	*0.6*
Refunds and write-offs	549	459	534	*13.9*	*-16.4*	*16.3*	*0.2*	*0.2*	*0.2*
Grants to statutory bodies	14,014	15,269	15,645	*4.7*	*9.0*	*2.5*	*4.8*	*5.1*	*5.1*
Others	6,736	7,760	8,524	*-20.9*	*15.2*	*9.8*	*2.2*	*2.5*	*2.7*
Total	**292,693**	**300,140**	**303,800**	***26.4***	***2.5***	***1.2***	***100.0***	***100.0***	***100.0***
% of GDP	***16.3***	***16.2***	***15.4***						

[1] Revised estimate
[2] Budget estimate, excluding Budget 2024 measures
Source: Ministry of Finance, Malaysia

The largest component of OE is emoluments, accounting for 30.4% or RM91.3 billion. The outlay for emoluments is expected to increase by 4% due to special annual increment and cash assistance for civil servants disbursed in January, April and August 2023. Retirement charges is estimated to increase by 2.2% to RM32.1 billion with the number of pensioners exceeds 936,000 recipients.

Subsidies and social assistance outlays is expected to decrease by 4.6% to RM64.2 billion attributed to lower fuel subsidy following moderate global crude oil prices. Of the total, RM41.4 billion is channelled for subsidies while the balance are for social assistance and incentives. In addition, the Government continues to extend subsidies for electricity, cooking oil, paddy, chicken and egg as well as toll compensation with the aim to ease the burden of higher cost of living.

Over the past few years, higher borrowings to finance the COVID-19 fund and DE have led to an increase in DSC. Hence, DSC is currently the third largest component accounting for 15.4% of OE, and is estimated to surge by 11.7% to RM46.1 billion. In line with higher emphasis on prudent spending and optimisation of discretionary items, outlays for supplies and services are expected to remain stable at RM34 billion. Payments for services such as cleaning and security services for schools, repairs and maintenance, material supplies as well as telecommunication and utilities, constituting the bulk of the supplies and services at 71.5%.

A sum of RM15.3 billion or 5.1% of OE has been earmarked for grants to Federal Statutory Bodies, primarily to cater for emoluments as well as supplies and services. The largest share of the grants, accounting for 59.6% has been allocated for public institutions of higher learning and teaching hospitals. Meanwhile, grants and transfers to state governments is estimated at RM8.1 billion, with RM6.1 billion being constitutional transfers as stipulated under the Federal Constitution.

In 2023, the revised DE is maintained at RM97 billion to sustain the progress of programmes and projects under the Twelfth Malaysia Plan, 2021 – 2025 (Twelfth Plan). In terms of sectors, the economic sector remains the largest beneficiary at 56.7%, followed by the social (27.4%), security (11.9%) and general administration (4%). The economic sector is expected to record a significant increase of 40.7% to RM55 billion (2022: RM39.1 billion) mainly for the redemption of the USD3 billion 1Malaysia Development Berhad (1MDB) bond. The financial, transport and agriculture subsectors are the top three largest contributors within the sector with a combined share of 44.1%.

Transport subsector is anticipated to record the largest share of DE at 18.1% or RM17.6 billion attributed to the progress in construction of new roads and highways as well as upgrading of roads, airports and ports. This is followed by the agriculture subsector, which recorded RM3.3 billion or 3.4% of DE, mainly for oil palm and rubber replanting activities as well as to support agro-based production and enhance food security. Energy and public utilities subsector constitutes 3.3% or RM3.2 billion for maintenance and upgrading of rural public amenities as well as providing clean water, sanitation and affordable clean energy. The environment subsector is allocated RM2.7 billion or 2.8%, mainly for flood mitigation projects. Nevertheless, the outlays for financial subsector anticipated at RM21.9 billion or 22.6% is mainly due to the redemption of USD3 billion 1MDB bond.

Social sector, the second largest sector grew by 25.6% with an allocation of RM26.5 billion (2022: RM21.1 billion), predominantly channelled to the education and training subsector, which receives RM13.6 billion or 14% of DE. The allocation for this subsector is mainly for the construction and upgrading of schools, training institutions and universities as well as scholarship scheme for human capital investment and skill development programmes.

TABLE 3.2. *Federal Government Development Expenditure by Sector, 2022 – 2024*

SECTOR	RM MILLION			CHANGE (%)			SHARE (%)		
	2022	2023[1]	2024[2]	2022	2023[1]	2024[2]	2022	2023[1]	2024[2]
Economic	**39,115**	**55,035**	**45,231**	***25.0***	***40.7***	***-17.8***	***54.6***	***56.7***	***50.3***
of which:									
Transport	16,560	17,565	19,128	*27.5*	*6.1*	*8.9*	*23.1*	*18.1*	*21.3*
Trade and industry	2,308	2,749	3,611	*31.4*	*19.1*	*31.4*	*3.2*	*2.8*	*4.0*
Energy and public utilities	2,359	3,240	3,070	*11.6*	*37.4*	*-5.2*	*3.3*	*3.3*	*3.4*
Agriculture	2,548	3,261	3,116	*3.4*	*28.0*	*-4.4*	*3.6*	*3.4*	*3.5*
Environment	1,736	2,673	3,330	*32.5*	*54.0*	*24.6*	*2.4*	*2.8*	*3.7*
Social	**21,132**	**26,546**	**28,320**	***-6.5***	***25.6***	***6.7***	***29.5***	***27.4***	***31.5***
of which:									
Education and training	10,029	13,557	14,268	*21.9*	*35.2*	*5.2*	*14.0*	*14.0*	*15.9*
Health	4,412	4,916	6,143	*-49.4*	*11.4*	*25.0*	*6.2*	*5.1*	*6.8*
Housing	1,653	2,114	1,998	*21.5*	*27.9*	*-5.5*	*2.3*	*2.2*	*2.2*
Security	**8,210**	**11,518**	**12,554**	***9.5***	***40.3***	***9.0***	***11.5***	***11.9***	***13.9***
General administration	**3,117**	**3,901**	**3,895**	***8.5***	***25.1***	***-0.2***	***4.4***	***4.0***	***4.3***
Total	**71,574**	**97,000**	**90,000**	***11.4***	***35.5***	***-7.2***	***100.0***	***100.0***	***100.0***
% of GDP	***4.0***	***5.2***	***4.6***						

[1] Revised estimate
[2] Budget estimate, excluding Budget 2024 measures
Source: Ministry of Finance, Malaysia

This was followed by the health subsector which receives RM4.9 billion or 5.1% of the total, mainly for the construction, renovation and maintenance of healthcare facilities across the nation. Meanwhile, the housing subsector is the third largest recipient amounting to RM2.1 billion or 2.2% of DE, primarily to provide affordable housing and refurbishment of the Government quarters.

The security sector, which comprises defence and internal security subsectors, receives an allocation of RM11.5 billion or 11.9% of DE. The allocation aims to further strengthen national security, with RM6.4 billion allocated to the defense subsector, while the remaining RM5.1 billion is for the internal security subsector. The remaining DE, amounting to RM3.9 billion or 4% of DE, is allocated to the general administration sector, of which the bulk of the outlays are for upgrading of ICT network system as well as maintenance of offices and equipment.

Outlook for 2024

In 2024, the Government will continue to pursue its two-pronged fiscal stance, namely diversifying revenue sources and optimising budget allocation. This strategy will further strengthen Government fiscal position and provide fiscal space to address potential future challenges and externalities. Towards ensuring fiscal sustainability and macroeconomic stability, the Government remains committed to medium-term fiscal consolidation despite higher spending commitments.

The Federal Government remains steadfast to allocate its resources to strengthen capital formation towards ensuring long-term growth sustainability. In this regard, a sum of RM393.8 billion or 19.9% of GDP is allocated for Budget 2024. Out of this amount, RM303.8 billion or 77.1% is channelled to OE, while the remaining RM90 billion is allocated for DE. The three primary beneficiaries of Budget 2024 are the Ministry of Finance, Ministry of Education and Ministry of Health, collectively accounting for 42.3% of the total.

In terms of sectoral allocation, the social sector is allocated RM149.7 billion or 7.6% of GDP, followed by economy (RM66.7 billion; 3.4%), security (RM40.1 billion; 2%) and general administration (RM16.9 billion; 0.9%). The remaining balance of RM120.4 billion is budgeted for charged expenditures and transfer payments.

To continue supporting public sector consumption, the allocation for OE is budgeted at RM303.8 billion or 15.4% of GDP. While there is a higher allocation for emoluments, DSC, retirement charges as well as supplies and services, the increases are offset by a lower subsidy allocation, causing in only a slight increase in OE by 1.2% as compared to 2023.

Emoluments for civil servants remain the largest component, comprising 31.5% of OE and is projected to expand by 4.8% to RM95.6 billion. The growth is predominantly attributed to annual salary increments and new hires to fill critical positions, particularly in health and education services.

Subsidies and social assistance, accounting for 17.4% of OE, is projected to decrease by 17.9% to RM52.8 billion, primarily due to the gradual implementation of subsidy rationalisation programmes mainly on fuel and electricity. Of the total, about 60% is allocated for subsidies while the remaining are for social assistance and incentives. In addition, the social assistance programmes will be further strengthened through the establishment of a new centralised database to address both inclusion and exclusion errors.

The DSC is a charged item mandated by the Federal Constitution to be paid prior to all other expenses. A sum of RM49.8 billion is allocated for DSC, which constitutes 16.4% of OE primarily driven by increased in the Federal Government debt. Of the amount, 98.5% or RM49 billion is for domestic charges while the remainder is for offshore loans.

FEATURE ARTICLE

Subsidy: A Double-edged Sword

Introduction

Subsidies have been an important policy instrument in many countries from economic, social and political perspectives. The term subsidy is derived from the Latin word *subsidium*, which means support, assistance, aid and protection (Steenblik, 2007). Subsidies are a transfer of resources from a government to a domestic entity without an equivalent contribution in return and can take many forms, including direct grants, tax incentives or favourable terms for financing (Van Heuvelen, 2023). According to the World Trade Organization, a subsidy is defined as a financial contribution by a government that provides a benefit to its recipients. Subsidies, whether provided to producers or consumers, are a form of transfer payment. Unlike expenditures, subsidies do not generate direct value-added (Hamid et. al., 2012).

A broad definition of subsidies is required to capture different forms of government intervention, both explicit and implicit. The IMF generally classifies subsidies based on the following seven categories:

(i) cash subsidies - direct government payment to producers or consumers;

(ii) credit subsidies - interest subsidies or soft loans;

(iii) tax subsidies - reduction of specific tax obligations;

(iv) equity subsidies - government equity participation;

(v) in-kind subsidies - government provision of goods and services at below-market prices;

(vi) procurement subsidies - government purchases of goods and services at above-market prices; and

(vii) regulatory subsidies - implicit payments through government regulatory that alter market prices or access.

In general, subsidies are one of the mechanisms to foster economic development and help disadvantaged groups in the effort to further boost business investment and improve quality of life. Subsidies, if implemented appropriately, are able to counteract market failures and externalities to attain economic efficiency. In times of economic recession or higher global commodity prices, subsidies can assist in stabilising the prices of essential goods to protect households against sudden price shocks and subsequent inflationary pressures.

Nevertheless, subsidies can also be harmful to the economy as they may cause price distortion and further contribute to market imperfection, causing wastage and misallocation of resources. In addition, inefficient and untargeted subsidy implementation may exacerbate inequality due to disproportionate benefits accorded to certain households and industries. Subsidies can impose a significant burden on government as they require a large amount of allocation. Certain subsidies, such as those provided for fossil fuel, undermines the environmental agenda as it promotes carbon emissions and worsens air pollution.

Advantages and Disadvantages of Subsidies

Subsidies act as a double-edged sword, while they may benefit certain individuals or industries, they can also have negative and unintended consequences. As global commodity prices increase, subsidies can cushion the impact of higher prices of goods and services yet potentially increasing the government financial burden and reducing fiscal space.

Advantages

Subsidies provide relief and support to the general population, particularly the low-income and vulnerable groups by making essential goods and services more accessible and affordable. In addition, subsidies can alleviate poverty and improve the well-being of the poor by easing the pressure of higher cost of living associated with necessities such as food, education, transportation and healthcare.

The implementation of subsidies can contribute towards price stability for essential items, particularly due to undesirable events such as geopolitical tensions and economic uncertainties. Through this approach, consumers can be shielded from unexpected shock in prices while controlling inflation to ensure sustainable economic growth. In addition, subsidies can serve as a mechanism for mitigating income disparity and nurturing social equity. Similarly, subsidies provided during the infancy stage of certain companies may offer initial support to kick-start and grow further.

The price stabilisation of domestic products and services resulting from the efficient subsidy implementation promote competitiveness, which will boost domestic demand and decrease reliance on imported goods. This will further enhance the overall supply in the domestic market, hence encourage investment, stimulate and support targeted sectors growth towards long-term economic sustainability.

Disadvantages

While subsidies can be a valuable tool in achieving certain policy objectives, its implementation should be balanced between the benefits and its drawbacks. From consumer perspective, implementation of subsidies could impact their consumption decision due to asymmetric information on the true cost of production that lead to overconsumption and create wastages. This could also pose an obstacle to economic development following overproduction and imbalances in the market, causing inefficient allocation of resources.

A recent study by the IMF revealed that subsidised products and services lead to overconsumption and do not encourage the industry to upgrade and enhance productivity because the input prices are subsidised. Prolonged subsidies also create over reliance on cheaper input and industries may struggle to survive without subsidies. While in the energy sector, overconsumption due to subsidised pricing raises import demand or decreases exports, affecting the balance of payments and causing energy security issue (Yingzhu Li et.al., 2017).

Most subsidies are broad-based and consequently become more regressive as the economy develops. In the middle- or high-income economies, the benefits of broad-based subsidies will accrue more to the wealthy groups, as they consume more subsidised products and services. According to the IMF, many subsidies exhibit inadequate targeting mechanisms, resulting in a disproportionate advantage to higher income brackets. For example, fuel subsidy is enjoyed disproportionately by high-income earners as this group is likely to own multiple vehicles with larger engine capacities.

With growing incomes, more households progress from low to middle- or high-income bracket. Thus, broad-based subsidies lead to leakages as they could benefit people outside of the targeted groups. In addition, the disparity between the subsidised and actual market prices encourage smuggling activities causing leakages of government resources.

When subsidies are not efficiently directed to the intended recipients, the country will miss out the potential of leveraging the substantial subsidy allocation towards more effective spending. This opportunity cost could involve investing in affordable housing, providing quality education facilities and healthcare services, enhancing social programmes, as well as building infrastructures that may yield broader and more sustained benefits. Prolonged inefficient and untargeted subsidies will add to the fiscal burden and financial strain to the government as they are financed through either higher taxes or trading-off of other expenditure items.

Subsidy Outlays and Fiscal Implication in Malaysia

In terms of the government financial capacity, universal and untargeted subsidies have an adverse impact on fiscal position and create unsustainable budgetary. For decades, while Malaysia is pushing for socio-economic growth to become a more developed and prosperous nation, the subsidy was aimed to improve the well-being and ease the cost of living of the rakyat. During 2012 to 2022, the Government spent RM223.5 billion on subsidies or 8.9% of the total operating expenditure. The bulk of the subsidies is mainly for fuel at 71.6% while the remaining are for interest rate, agricultural inputs, cooking oil, electricity, toll compensation, transportation, chicken and egg as well as others as shown in Figure 1.

In 2022, total subsidies recorded an all-time high of RM70.3 billion (OE: RM58 billion; COVID-19 Fund: RM12.3 billion), as compared to an annual average of RM15.2 billion for the past 10 years and almost equal to the development expenditure of RM71.6 billion. This was triggered by among others, the COVID-19 pandemic, geopolitical tension and climate change, affecting global commodity prices. In addition, the Government also provided RM24.3 billion for a one-off wage subsidy programme during the pandemic period as an effort to sustain jobs and reduce retrenchment. Overall, this programme has benefitted close to 360,000 employers to retain about 2.95 million local employees.

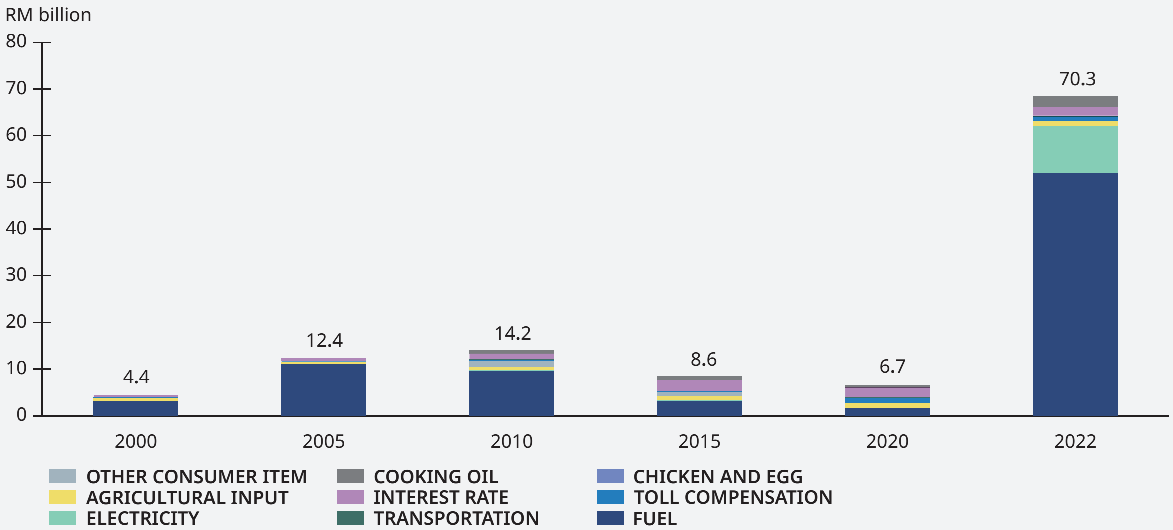
In 2014, fuel subsidies were recorded at RM18.5 billion with an average crude oil prices at USD99 per barrel. At the end of that year, the Government implemented the managed float fuel pricing mechanism for petrol and diesel, resulting in substantial fuel subsidies reduction to only RM3.2 billion in 2015. However, in July 2018, the Government withdrew the mechanism and reintroduced fuel subsidies for RON95 and diesel which led to higher subsidies of RM7.5 billion by year end. With an average crude oil price at USD100 per barrel in 2022, fuel subsidies peaked at RM52 billion or 74% of total subsidies. The average market prices per litre for RON95 was RM3.39 and RM3.44 for diesel as compared to retail pump price of RM2.05 and RM2.15 per litre, respectively. This reflected averaged subsidy per litre for RON95 at RM1.34 and RM1.29 for diesel.

Higher commodity prices, particularly coal has added to the rise in electricity production cost which requires additional subsidy allocation in the absence of tariff increment. In this regard, since 2022, the Government allocates around RM10 billion to RM12 billion annually under the Imbalance Cost Past Through (ICPT) mechanism to ensure no additional charge is borne by consumers. Furthermore, effective July 2023, households consuming electricity not exceeding 1,500kWh per month will continue to receive ICPT rebate of RM0.02/kWh.

The higher crude palm oil price also affected cooking oil prices which require additional subsidy allocation for the Cooking Oil Stabilisation Scheme (COSS). In 2022, subsidy outlays for COSS surged to RM2.4 billion as compared to RM500 million in 2018, a substantial increase of RM1.9 billion. The subsidy quota provided under COSS is 60,000 metric tonnes per month. Meanwhile, in addressing the food security concern and rising global food prices, the Government allocates subsidies exceeding RM1 billion annually for paddy including paddy price, fertilisers and seeds. In addition, the Government introduced subsidies for chicken and egg in 2022, amounting to around RM2 billion, with a subsidy rate of RM0.80 per kilogramme for chicken[1] with an average monthly consumption of about 70 million chicken. In the same period, the average monthly consumption of eggs was about 1.1 billion with a subsidy of RM0.10 per egg.

[1] Average weight of a standard whole chicken is 1.8 kilogramme

FIGURE 1. *Trend of Subsidy Outlays, 2000 – 2022*



Note: Total subsidies exclude wage subsidy programme under the COVID-19 Fund
Source: Ministry of Finance, Malaysia

Research Findings on Fuel Subsidy Rationalisation in Malaysia

According to the World Bank, Malaysia needs to phase out broad-based subsidies and move towards targeted subsidies through a cash transfer mechanism to better support vulnerable groups. The mechanism is proposed to be applied gradually and reviewed periodically to avoid an abrupt subsidy removal that could lead to a sharp increase in inflation. The subsidy rationalisation aims to enhance efficiency in the economy and rebuild fiscal space while minimising the risk of economic shocks.

In the 2023 Article IV Consultation Report, IMF emphasised that energy subsidies in Malaysia are costly, regressive, inefficient and detrimental to the environment. IMF stated that subsidy rationalisation needs to be accompanied by a clear explanation that is well-defined and transparent to the rakyat. The article also suggested the broad-based subsidies to be replaced with a targeted cash transfer along with strengthening the social safety net particularly to poor households. The Government is advised to apply subsidy rationalisation gradually and clarify the exact sequencing of energy price increases as well as exact price-setting mechanism to avoid public uproar.

Yingzhu Li et.al., (2017) asserted that the elimination of petroleum and gas subsidies in Malaysia is expected to enhance economic efficiency and contribute up to 0.65% to the GDP growth. The rationalisation of fuel subsidies creates additional room for the Government's fiscal position. However, the subsidy removal could increase the price level that requires the Government's intervention through compensation policies. The study also suggested that Malaysia should repurpose the savings from fuel subsidies rationalisation to investment, particularly in education and healthcare sectors. Meanwhile, a mitigation plan must be established in light of the expected resistance from the public.

Saeed Solaymani et.al., (2014) suggested that in the short run, subsidy reform have an overall positive impact on Malaysia's real GDP, but adversely affect investment on sectors that use subsidies, mainly in the agricultural and energy sectors. The results also suggested that the reform policy will lead to an increase in poverty level with the biggest impact on the rural households, predominantly employed in the agricultural sector. Therefore, Malaysia must work towards a subsidy reform that specifically targets poor households, necessitating a better targeting mechanism.

Moving Forward

Learning from the COVID-19 pandemic experience, the social safety net proved to be a crucial form of social assistance in safeguarding the life and livelihood of the rakyat, particularly the vulnerable groups. During the pandemic, RM530 billion in stimulus packages were given, of which RM92.5 billion fiscal injection was for wage subsidies, reskilling and upskilling, food security and various other social assistance programmes. An enhanced social protection with proper planning will prepare the rakyat and the Government to be financially equipped in facing possible crises in the future. Hence, to minimise the impact of the subsidy rationalisation, the Government will enhance the social safety net programmes to incorporate various forms of support, particularly in terms of employment, healthcare, housing, energy, education and food assistance.

A gradual shift from a broad-based to a more targeted subsidies programmes is crucial. The shift can be effectively executed taking into consideration various factors, such as income level, geographic location, demographic and work status. Targeted mechanism can be implemented by improving the current cash assistance programme through consolidating the existing programmes currently undertaken by various agencies. The mechanism should also leverage on latest technology advancement and adopt digitalisation to minimise operational costs followed with close monitoring and assessment to ensure the intended results are achieved.

Efforts to rebuild and increase fiscal space would have to be driven by both higher revenue collection and efficient resources utilisation. The Government will continue to explore other sources of revenue and improve the current revenue collection that will strengthen fiscal position to ensure a more sustainable economic growth.

Conclusion

The magnitude of broad-based subsidies mainly for fuel, poses a significant risk to long-term fiscal sustainability. Considering its substantial impact, a specific approach needs to be formulated with the objective to mitigate income inequalities, minimise inefficiencies and at the same time curb leakages and wastages. Therefore, to ensure a fair and equitable income distribution while achieving a sustainable fiscal position, the reform is crucial to steer Malaysia towards higher growth trajectory in line with the aspirations of Ekonomi MADANI.

While subsidies can be used strategically to achieve various economic, social, and environmental goals, it is essential for the Government to strike a balance between distribution of resource and maximising economic benefit. In order to lessen the pressure on the Government's budget, a more effective and targeted subsidy rationalisation is crucial and timely. Subsidy rationalisation may create more fiscal space for spending on high-multiplier impact programmes and projects. Thus, a policy intervention supported by close engagement is required to smoothen the transition towards a gradual and targeted subsidy mechanism.

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Supplies and services, which accounts for 12.5% of OE, is anticipated to increase by 11.8% to RM38 billion. A significant portion of 83.2% is allocated for material supplies; cleaning and security services; repairs and maintenance; telecommunication and utilities as well as other services. In addition, retirement charges, which accounts for 10.7% of OE, is expected to remain stable at RM32.4 billion. Of this amount, RM26 billion or 80.1% comprises pension payments for around 971,000 pensioners, while the remainder is mainly for gratuity payments and cash awards in lieu of accumulated leave. The Government is considering to shift towards a defined contribution scheme to effectively manage pension obligations in the future, as pension commitments are expected to escalate further.

An allocation of RM15.6 billion is channelled for grants to Federal Statutory Bodies, primarily for operational expenses such as emoluments as well as supplies and services. The bulk of the grants is mainly for 20 public universities and nine teaching hospitals, accounting for 60.3% of the total grants. Meanwhile, RM8.7 billion is allocated for grants and transfers to state governments, with RM6.7 billion representing constitutional transfers under the Federal Constitution.

As the nation embarks on the second phase of the Twelfth Plan, the Government is committed to providing a substantial allocation to support the ongoing programmes and projects with high-multiplier impact to futher boost the economy. A sum of RM90 billion is budgeted for DE constituting 4.5% of GDP, among others for about 2,000 new projects with an estimated initial cash flow of RM8 billion in 2024. In terms of sectoral allocation, the economic sector remains to be the largest beneficiary, receiving 50.3% of DE, followed by social (31.5%), security (13.9%) and general administration (4.3%).

A sum of RM45.2 billion is provided for the economic sector to drive and support economic growth. However, the amount is lower compared to the RM55 billion allocated in 2023, which included payment for maturing 1MDB bond. The main subsectors within the economic sector are transport, trade and industry as well as environment. The transport subsector receives the largest share with RM19.1 billion or 21.3% of DE. Notable new projects in this subsector include the construction of additional lanes for PLUS highway from Yong Peng Utara to Sedenak Phase 2 as well as upgrading of road in Bandar Baru Tunjong, Kota Bharu, Kelantan and Sebayan to Kudat, Sabah. In addition, allocation is also provided in serving the financial commitments, mainly for strategic infrastructure projects such as Mass Rapid Transit (MRT), Light Railway Transit (LRT), East Coast Rail Link (ECRL), Sabah and Sarawak Pan Borneo highways and Jambatan Kedua Pulau Pinang.

In an effort to further boost industry capabilities, the trade and industry subsector is allocated RM3.6 billion or 4% of DE, mainly to support initiatives under the New Industrial Master Plan 2030. Meanwhile, the environment subsector is allocated RM3.3 billion, with a primary focus on the implementation of nationwide flood mitigation programme, which is valued at approximately RM11 billion.

The social sector will receive an allocation of RM28.3 billion or 31.5% of DE. The education and training subsector foresees an increase in allocation of 5.2% to RM14.3 billion, particularly to construct new schools and improve existing facilities. For 2024, 18 new schools have been approved with an estimated project value of approximately RM1.6 billion, including construction of Sekolah Menengah Kebangsaan Agama Jempol, Negeri Sembilan and Seri Damai School Complex, Kuala Lumpur. Meanwhile, the health subsector will receive RM6.1 billion for the construction and upgrade of health facilities as well as the procurement of healthcare equipment. New projects under this subsector include the construction of a pathology block in Raja Perempuan Zainab II Hospital, Kelantan and National Subfertility Centre, Selangor. As for the housing subsector, RM2 billion is allocated to construct the Government quarters and affordable housing for the rakyat, including under the Home Assistance Programmes.

The Government places a significant emphasis on preserving national security and safeguarding public safety. The security sector is allocated RM12.5 billion, with RM7.4 billion and RM5.1 billion are channelled for the defence and internal security subsectors, respectively. These allocations are for development projects, including the acquisition of new assets, upgrading of existing military and security equipment as well as construction and refurbishment of police stations, military camps and quarters for security personnel.

The general administration sector is allocated a budget of RM3.9 billion to facilitate continuous improvement in public service delivery. The allocation is mainly for projects to enhance ICT network systems as well as refurbishments and maintenance of Government buildings and facilities, such as civil servant quarters, court complexes and training institutions.

Federal Recoverable Loans

The total Federal Recoverable Loans[1] under the Development Fund as of 31 December 2022 amounted to RM41.5 billion or 2.3% of GDP. Of the total, loans to companies constitute the largest share amounting to RM27.4 billion or 66.1%, followed by state governments (RM9 billion; 21.7%), Federal Statutory Bodies (RM5 billion; 12%) as well as other organisations and cooperatives (RM87 million; 0.2%).

[1] The Federal Recoverable Loans is part of the Federal Government Financial Assets, which consist of loans facilities due from state governments, local governments, statutory bodies, companies, cooperatives and various organisations.

The loan disbursement through DE is estimated to register RM1.4 billion in 2023. State governments are the largest recipient at RM793 million or 57.2% of the total disbursement, followed by companies (RM348 million; 25.1%), Federal Statutory Bodies (RM235 million; 17%) and other organisations (RM9.5 million; 0.7%).

The Government is expected to receive loan repayments totalling RM700 million in 2023. The bulk of the repayment is anticipated from companies at RM400 million or 57.1% of the total, with Sabah Electricity Sdn. Bhd. being the biggest contributor. Meanwhile, loan repayments from state governments are estimated at RM242 million or 34.6%, with Sabah and Sarawak contributing RM154 million. The remaining balance is expected to be received from Federal Statutory Bodies at RM52 million or 7.4% and other organisations at RM6 million or 0.9%.

In 2024, the Federal Government continues to provide loans to state governments, Federal Statutory Bodies, companies and other organisations through DE with the aim of achieving the socioeconomic development agenda and improving the quality of life of the rakyat. The total loan disbursement is estimated at RM1 billion with the state governments continuing to be the biggest recipients amounting to RM750 million, followed by Federal Statutory Bodies (RM108 million), companies (RM144 million) and other organisations (RM8 million). Loans will primarily be utilised for programmes and initiatives related to water and electricity supply as well as sewerage treatment infrastructure.

Loan repayments in 2024 are estimated at RM800 million. Of the total, 62.4% or about RM500 million repayments are anticipated from companies. Loan repayment from state goverments are expected around RM230 million, while the balance of the loan repayments will be from Federal Statutory Bodies (RM62 million) and other organisations (RM11 million).

Conclusion

The Government public expenditure strategy is formulated to support domestic economic activities and improve public service delivery while ensuring fiscal discipline. In tandem with the Ekonomi MADANI framework, the fiscal stance will continue to emphasise on public expenditure efficiency and effectiveness as well as generating higher value for money while minimising leakages and wastages. This endeavour will be undertaken through fostering good governance and accountability on public finance. Overall, the Government remains committed to achieving sound fiscal position while promoting investments that will boost economic growth in the long term.

FIGURE 3.1. *Total Expenditure by Sector*

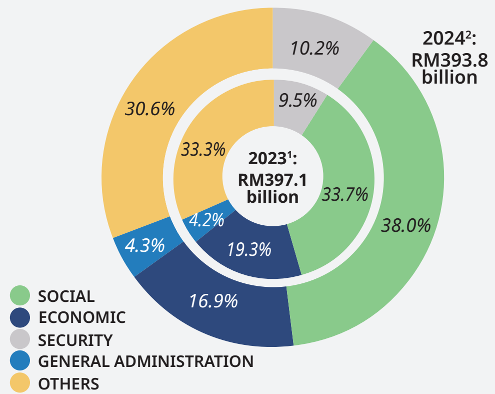


FIGURE 3.2. *Total Expenditure by Ministry and Agency*

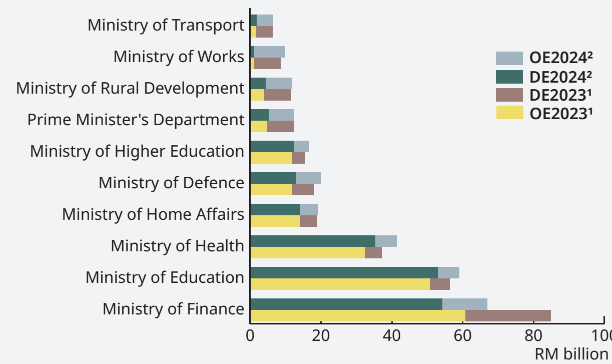


FIGURE 3.3. *Operating Expenditure by Component*

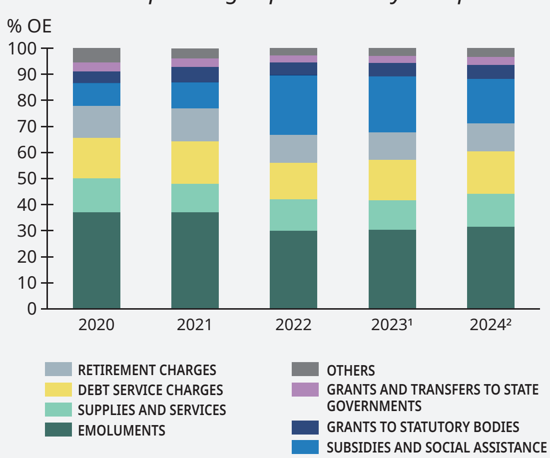


FIGURE 3.4. *Operating Expenditure by Sector*

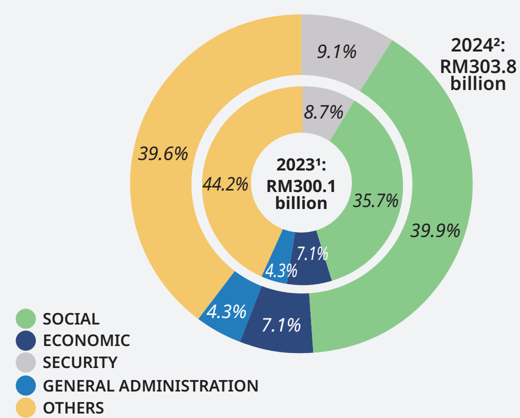


FIGURE 3.5. *Development Expenditure by Sector*

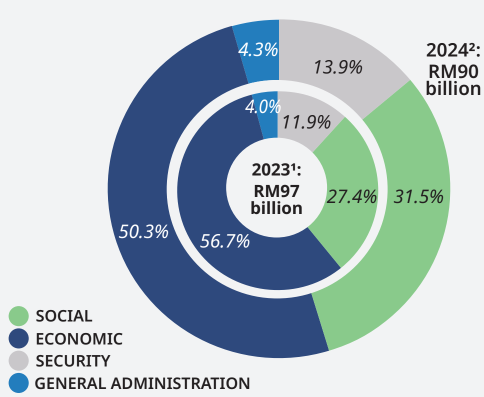
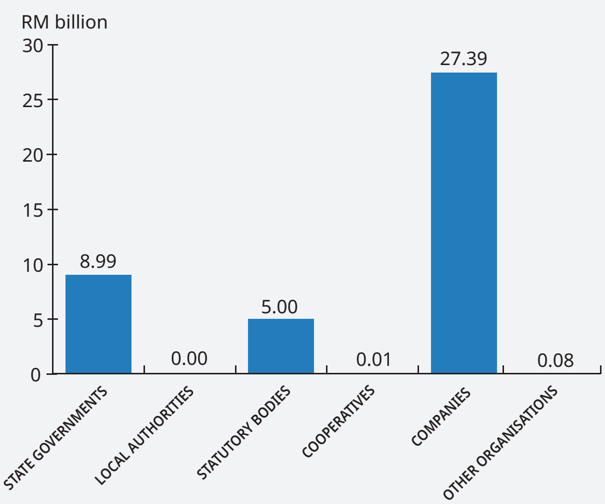


FIGURE 3.6. *Federal Recoverable Loans by Debtor*[3]



[1] Revised estimate
[2] Budget estimate, excluding Budget 2024 measures
[3] Total outstanding as at end-2022
Source: Ministry of Finance, Malaysia