Govt sees up to RM11b revenue shortfall with oil at US$30 — experts

'Govt sees up to RM11b shortfall with US$30 oil'

To close the revenue gap, it may raise tax collection, cut spending or borrow more, say experts

BY MEENA LAKSHANA

KUALA LUMPUR: Putrajaya is expected to face a revenue shortfall of between RM5 billion and RM11 billion, based on the assumption that crude oil prices average at US$30 (RM127.50) per barrel (/bbl) this year, and that the government maintains its fiscal deficit target at 3.1% of gross domestic product (GDP), said economists.

RHB Research economist Peck Boon Soon said according to government estimates, every US$1 drop in oil prices will result in a RM300 million drop in government revenue.

"Assuming oil price of US$30 per barrel, they need to close the gap of about RM5.4 billion to maintain the 3.1% deficit target," he said, when contacted by *The Edge Financial Daily*, adding that Putrajaya is likely to maintain the target to avoid risking a possible credit rating downgrade.

However, Alliance DBS Research economist Manokaran Mottain thinks that if oil remains at US$30/bbl this year versus the US$48/bbl that was estimated in Budget 2016 last October, the fiscal shortfall could amount to about RM11 billion.

"We estimate that for every US$1 drop in Brent crude oil price, the government loses around RM600 million from its oil-related revenue. Therefore, assuming Brent crude oil averages US$30 per barrel throughout 2016, at real GDP growth of around 4.5%, Budget 2016 revenue could lose approximately RM11 billion and fiscal deficit to GDP ratio would deteriorate to 4%," he wrote in a note yesterday.

He said the government has three options to address the fiscal shortfall — raise tax collection, slash expenditure or raise its borrowings.

Given the dampened domestic business and consumer sentiments, Manokaran said any tax hike will likely be targeted and item specific, as broad-based hikes could be detrimental to the already-subdued domestic demand prospects.

"On the other hand, we believe the government could enhance tax collections though stringent enforcement," he said, such as strengthening border security to reduce goods smuggling.

"There is also the possibility that GST (goods and services tax) revenue could come in higher than the original estimation of RM39 billion," he added.

On spending cuts, Manokaran expects the targets to be non-essential expenses in operating expenditure, though he thinks civil servants' salaries, debt service charges, and grants to statutory bodies and state governments are unlikely to be cut.

The government may also look into reducing supplies and services allocations from five ministries — health, defence, education, home affairs and the prime minister's office.

"If the government targets a 10% cut on these allocations, it could save about RM2.5 billion," he added.

"We do not rule out the possibility of trimming education scholarships and the government encouraging students to pursue tertiary studies domestically," he added.

He said subsidy cuts may occur, but subsidies for essential goods and services would likely be maintained to ease the rising cost of living.

"Nevertheless, if the allocated subsidies were to be slashed by 10%, it could save the government up to RM2.6 billion," he added.

He said it is plausible for the government to use borrowings to fund the fiscal shortfall in the short term, but it will likely compromise the government's long-term fiscal commitments, resulting in future costs of higher debt servicing charges and difficulties in balancing its budget by 2020.

"In the 11MP (11th Malaysia Plan), the government targets to keep its total debt level at RM774 billion by 2020, equivalent to 43.5% of GDP," he said.

"As of [the] third quarter of 2015, total outstanding government debt amounted to RM623.3 billion (around 54% of GDP).

"Moreover, debt service charges as a proportion of government revenue have been gradually increasing in recent years (2016 estimate: 11.8% vs 2015 estimate: 11%)," he added.

Meanwhile, independent economist Lee Heng Guie said the government is likely to stick to its initial 3.1% fiscal deficit, as a higher fiscal deficit target would not go well with global rating agencies.

Lee said the government may provide short-term relief for businesses to ease cost burdens, such as deferring the implementation of the proposed increase in minimum wage, scheduled to be implemented in July.

"The other ways to earn revenue are: review Labuan's tax-free status, open up bidding for broadband that will help raise some assets, and propose voluntary cuts in EPF (Employees Provident Fund) contributions for employees [to free up more discretionary income among Malaysians]," he added.

Meanwhile, Deloitte Malaysia Country Tax Leader Yee Wing Peng said Putrajaya will likely raise sin taxes and legalise e-cigarettes, to boost its tax income for 2016 as it has "limited room" to raise corporate and personal income taxes.

While imposing duties in Labuan itself might not add much to revenue collection, he said withdrawing the island's duty-free status will help plug the flow of duty-free products into East Malaysia, which can be meaningful.

Malaysia hiked cigarette prices by over 40% last year, but further hikes "could well happen", he added, while "vape" or e-cigarettes may be regulated.

Brent crude oil price and fiscal sensitivity analysis

BRENT CRUDE OIL AVERAGE 2016 (US$/BBL)	FISCAL DEFICIT TO GDP RATIO (%)	REVENUE SHORTFALL (RM BIL)
20	-4.5	-17.2
25	-4.3	-14.1
30	-4.0	-11.0
35	-3.8	-8.0
40	-3.5	-4.9
48	-3.1	0.0
55	-2.8	4.3

*Assuming 4.5% real GDP growth in 2016
Source: AllianceDBS