2017 BUDGET PROPOSALS – THREE PRIORITIES

1.Competitiveness	• Design a competitive tax rate to sustain as well as spur more investment • Malaysia's regional peers are ahead of the curve
2. Management of foreign workers, minimum wages	• Predictable and consistent policy • More engagement with the industry players
3. Property sector	• Prevent an over-adjustment in the sector • Review of selective property-cooling measures

GATHERING EXTERNAL HEADWINDS THREATHEN TO DAMPEN MALAYSIA' ECONOMIC PROSPECTS

- **Multiple external and domestic headwinds** (global recession risk, slowing China economy, Brexit's induced uncertainties as well as the ringgit's volatility) pose great challenges to Malaysia's economic prospects.
- **Sustaining domestic demand** is paramount to counteract domestic economy from reeling external shocks.
- While measures to support consumer spending should continue, **strong private investment activity** needs to be sustained to create jobs.
- Must calibrate **short-to medium-term measures** to strengthen our economic and financial resilience.
- **Continued fiscal consolidation** whilst providing targeted fiscal support.
- With our export engine is under threat, **2017 Budget** should focus on the following thrusts:
  - i) Strengthening the nation's competitiveness for the next take-off
  - ii) Sustaining domestic demand
  - iii) Enhancing exports capacity
  - iv) Safeguarding domestic price and financial stability

ISSUE 1: REINFORCING COMPETITIVENESS IS KEY TO BOOST MALAYSIA'S GROWTH POTENTIAL

- The **sliding private investment growth trend** in recent quarters warrant concerns, raising the fear of losing momentum.
- A **competitive and transparent tax structure** is the key factor to sustain the viability of business and spur investment.
- While the private sector is supported by a host of fiscal and non-fiscal incentives, their effectiveness may not be as impactful compared to a competitive corporate income tax rate.
- The **trend now is to do away those "excessive discretion" of targeting incentives** as they are less transparent, invite corruption and rent-seeking and hence, discouraging investment across all industries.
- Malaysia is exposed to the **fierce competition for FDI within the region** and **equally competitive cost of doing business** in competing jurisdiction.
- Besides that, **political stability**, **economic stability** and **good governance** remained a strong catalyst to retain as well as attract investment.

PROPOSAL 1: FORWARD ANNOUCEMENT OF LOWER CORPORATE TAX RATE

- **Malaysia's corporate income tax rate of 24%** is **one of the highest in Asean** and hence, renders it less attractive and competitive to investors.
- Brunei Darussalam (20%), Cambodia (20%), Singapore (17%), Thailand (20%) and Vietnam (22%), Laos (24%), Myanmar (25%). Indonesia recently announced that it plans to lower the corporate income tax rate to 20% from 25% now, and will gradually reduce to around 17.5%.
- The implementation of GST should be compensated by a lower corporate income tax rate, a move to maintain a competitive cost of doing business.
- Lowering the tax rate: i) would **improve tax compliance** as businesses want a fair, understandable and reasonable tax policy; and ii) a **strategic way of tapping the underground economy** to participate in the mainstream,
- Faced with revenue constraints, we **propose a forward pronouncement of cutting the corporate income tax rate, say by 2% points per year starting from YA2018, taking the tax rate to 18% by 2020 from 24% currently.**

- We believe that the forward announcement of offering a competitive tax structure demonstrates the government's firm commitment towards making Malaysia a highly competitive and big investment potential destination in Asia and ASEAN in particular.
- A progressive tax reform will provide certainty and enable investors to plan ahead their investments along with the developments in TPPA, RCEP and China's "One Belt, One Road" initiative.

Comparison of corporate income tax rate (%)

Country	YA 2008	YA 2012	YA 2016
Malaysia	26%	25%	24%
Indonesia	30%	25%	25%
Singapore	18%	17%	17%
Thailand	30%	23%	20%
Vietnam	28%	25%	20%
Asia average	27.99	22.89	21.97
Europe average	21.95	20.42	20.48
EU average	23.17	22.51	22.09
World average	26.1	24.4	23.63

Source: KPMG

PROPOSAL 2: PREFERENTIAL TAX RATE FOR SME (CONT'D)

- SMEs must be **financially strong and competitive enough** to withstand head-on competition from foreign parties in the ASEAN Economic Community (AEC) market place and also the forthcoming TTPA.
- SMEs should continue to **enjoy preferential tax rate given their relatively high compliance costs** (absence of the economic of scale), higher business costs and higher risk of failure.
- Currently, the first-tier tax rate is 19% for the first RM500,000 and 24% for the balance of chargeable income.
- To ensure that tax and non-tax policies do not place SMEs at a competitive disadvantage, for example through relatively high effective tax rates, it is proposed that:

  i) **Reduce the first-tier tax rate in stages by 2% per year** w.e.f YA2017 from 19% to 13% in YA2019;

  ii) **Raise the threshold level of chargeable income** for the first-tier tax rate to **RM1.0-2.0 million** from the present RM500,000; and

  iii) **Review the eligibility of paid–up capital of "Special Classes" of SME**. The current "Special Classes" of SMEs refer to companies resident in Malaysia, which has a paid-up capital in respect of ordinary shares of RM2.5mil and less. In order to have a wider reach impact, the government should consider to **raise the paid-up capital to RM3.5-5.0 million and less.**

PROPOSAL 2: PREFERENTIAL TAX RATE FOR SME (CONT'D)

iv) **A corporate income tax rebate of 30%, up to a maximum relief of RM30,00**0 be given to help SMEs to deal with rising business costs and the much needed cash flow to support their business activities and growth. Ultimately, a gradual reduction in corporate income tax rate and preferential tax rate treatment will sharpen the cost structure of SMEs, giving them the competitive edge to expand in the global marketplace.

The table below illustrates the calculation of a corporate income tax rebate of 30%, up to a maximum relief of RM30,000.

		Current	Proposed Rebate	Combination*
Taxable income		RM 2 mil	RM 2 mil	RM 2 mil
Gross Tax	19% for 1st RM500K	RM 95,000	RM 95,000	RM 85,000
	24% on Balance	RM360,000	RM360,000	RM360,000
Gross Tax payable		RM455,000	RM455,000	RM445,000
Rebate of 30%, up to max RM30k		-	30,000	30,000
Net Tax payable		RM 455,000	RM 425,000	RM415,000
Effective tax rate		22.75%	21.25%	20.75%

** Incorporating proposed preferential tax rate of 17% during YA2017 and corporate tax rebate.*

ISSUE 2A: A HOLISTIC APPROACH TO TACKLE FOREIGN WORKERS

- Over the period of 2000-2014, the number of registered foreigners working in the country grew by **7% per annum from about 810,000 in 2000 to 2.14 million in 2015**.
- As of 31 March 2016, the number has dipped to 1.993 million as some have found Malaysia no longer attractive as an employment destination. The reasons cited were the falling ringgit, the expiration of the workers' contracts, the unwillingness to renew their employment contract as well as health issues.
- Foreigners **dominated the manufacturing sector** (36.1%), agriculture (23.5%), construction (19.9%) and services (13.0%). The share of foreign workers to Malaysia's workforce had increased from 8.4% in 2000 to 14.9% in 2014. These figures do not include the growing number of illegal foreign immigrants into Malaysia and are considered part of the local workforce.
- The Malaysian Trades Union Congress has estimated that there are seven million foreign workers in total, including illegals. Such large numbers make up 22.6% of total population and 49.6% of total labour force in 2015.
- **Foreign workers' issues need immediate attention**. With migrant workers have becoming a permanent feature of Malaysia's socio-economic landscape, their influx should not be viewed lightly as there are national interest, social, community as well as security implications if the numbers and whereabouts of foreign workers are not contained, regulated and monitored.
- The **formulation of foreign workers employment policy** must **meet a sustainable balance** between managing the socio-economic spillovers and supporting the industry's needs whilst moving towards reduce the dependency of low-skilled workers.

PROPOSAL 2A: MAPPING A COMPREHENSIVE AND SUSTAINABLE POLICY

- The most urgently needed policy reform is to **develop a comprehensive foreign manpower system** for managing the inflow and utilisation of foreign workers to augment domestic workforce.
- A sudden steep hike in foreign worker levy on an ad-hoc basis, especially during a soft economic environment would be burdensome to industries.
- We propose the following measures:

  i) **Accessible to reliable and accurate database of foreign workers**. The relevant ministries and agencies must maintain a reliable and accurate database as well as detailed information on the availability of foreign workers. The database must be made accessible to local employers and employment agencies. Such information is not readily available due to highly sensitive nature of the data

  ii) **Foreign worker levy**. Faced with the current weakening economic conditions and soft demand, the **current levy structure should be reviewed and lowered for a period of 1-2 years, starting this year**.

  iii) The recalibration of foreign worker levies **must be progressively implemented within a specific time-frame on a pre-announced schedule**. The fixed schedule of levy structure not only provides a certainty to industries and also allows sufficient time for businesses and industries to adjust. While the fixed schedule is designated to provide the industry with more certainty, the Government must also **exercises flexibility to review, defer or modify the levy structure during the ups and downs of business cycles and economic conditions.**

MAPPING A COMPREHENSIVE AND SUSTAINABLE POLICY (CONT'D)

iv. Design **an efficient, simpler, transparent and cost effective policy tool** to allocate as well as manage the demand for foreign workers.

v. The **dependency ceilings**, which specify the hiring ratio of foreign to local workers, varying by sector and to what extent the shortage of local workers.

vi. The foreign manpower system should **incorporate source country restrictions to promote better integration** among foreign workers whilst **minimizing over-concentration risk**. Although the share of Indonesian workers to total foreign workers had been reducing significantly throughout the period 2000-2015, their presence remain substantial at 39.2% in 2015 (74.8% in 2000), followed by Nepalese (23.6% vs. 0.1% in 2000), Bangladeshi (13.2% vs. 19.6% in 2000), Myanmar (6.8% vs. 0.4% in 2000), India (6.5% vs. 2.3% in 2000) and Pakistanis (3.4% vs. 0.4% in 2000).

vii. The **hiring and re-hiring, application and approval mechanism** must be **transparent, consistent, accountable as well as efficiently run**. This helps to contain the tendency of irresponsible employers resorting to illegal channels to hire illegal foreign workers.

viii. The **enforcement agencies (police and Immigration department)** must be **strengthened and accountable** to carry out the task of managing foreign workers both legal and illegals.

PROPOSAL 2A: MAPPING A COMPREHENSIVE AND SUSTAINABLE POLICY (CONT'D)

viii. The **rehiring programme should be opened to all undocumented foreign workers** and must be made more efficient to assist manufacturers. The **processing charges for the rehiring exercise are too costly**.

ix. The **freezing of foreign workers must be lifted** for **ALL SECTORS** and not confined to the four sectors (manufacturing, construction, plantation and furniture-making industries). This is to prevent the frozen sectors from poaching foreign workers from the non-frozen sectors, and hence curtailing the hiring of illegal workers.

x. The **replacement of foreign workers**, whose permits have expired and successfully repatriated must be reviewed with a view of being accorded the priority of obtaining a speedy approval for the replacement of workers. This helps to minimise disruption to the companies' operation and production.

xi. The government should make **good use of the foreign workers' levies** it collected and rechannelled back to industries via **skilled labour enhancement program and automation grants** to help businesses and industries go through the transition process of reducing the dependency on unskilled workers.

xii. Actively engage with the stakeholders (industry, SMEs and employers) on the formulation of foreign workers employment policy. Prior consultations and the provision of a **lead timeline** would provide the breathing space for industries to fully prepared for the adjustment.

ISSUE 2B : MINIMUM WAGE POLICY

- We support the implementation of a minimum wage policy to ensure a fair wage for the country's lowest paid workers and commensurate with the improvement in productivity growth.
- There remains **outstanding definition issues** concerning **what constitute basic wages**. Allowances or other incentive payments that were already borne by employers are not included as a part of minimum wages calculation, unlike in Hong Kong where the computation of "minimum wages" may include earnings, travelling allowances, commission, attendance allowances, overtime payment, tips and service charges.
- Under the Minimum Wages Order (MWO) 2016, there is no provision for negotiations and restructuring of wages, i.e. any allowances now being paid by employers, which is not part of the minimum wage cannot be incorporated to make up to the new minimum wage of RM1,000 per month.
- The **lack of representation from chambers of commerce** in the National Wage Consultative Council (NWCC) and its technical committee has denied having their voices heard and gathering of constructive feedback from the chamber's members and industries.

PROPOSAL 2B: FINE-TUNING OF MINIMUM WAGE POLICY

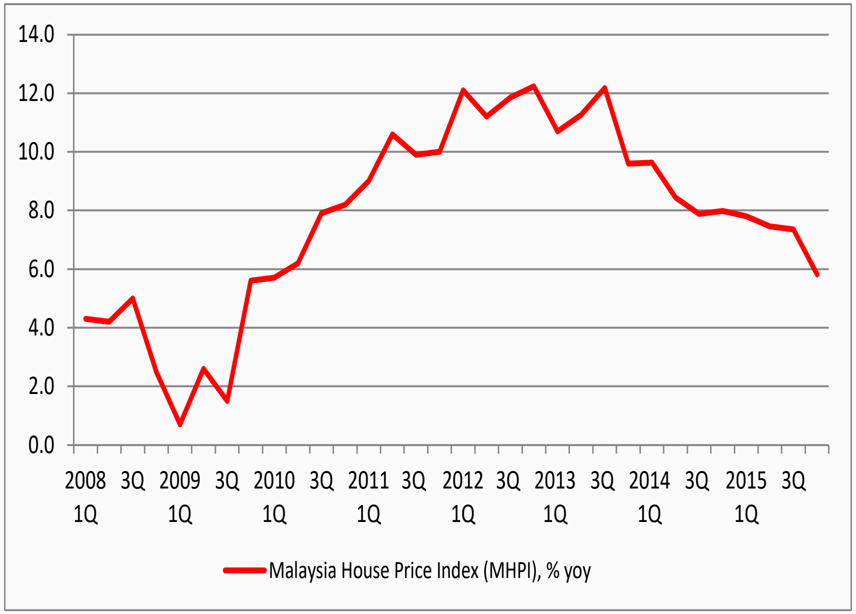
- Our proposals are as follow:
  1. i) **Review the definition of minimum wage** as **total take home pay** as opposed to **basic pay.** This is to ensure a fair treatment of compensation for local workers as foreign workers currently are enjoying more allowances such as transportation and accommodation.
  2. ii) Being one of the major chambers of commerce in Malaysia that has more than 100,000 direct and indirect members comprising Malaysian companies, individuals and trade associations, **ACCCIM once again urge the Government to appoint ACCCIM as a working member/representative in the National Wages Consultative Council (NWCC) and the relevant technical committees**. We believe that ACCCIM's representation in the NWCC would provide a useful platform to bring forward the views and suggestions from the SME and business community.
  3. iii) Minimum wage is not a mean to improve the income and well-being of workers. It is through the enhancement of skill sets, job knowledge and higher productivity growth that would enhance the worker's ability to command high salary and income. It is therefore, proposed that minimum wage **be applied only to unskilled workers**.
  4. iv) Continued to push for **a productivity-linked wage system** through a credible and transparent productivity measurement benchmarking, going by industry and region.

ISSUE 3: PROPERTY SECTOR CONTINUES TO CONSOLIDATE

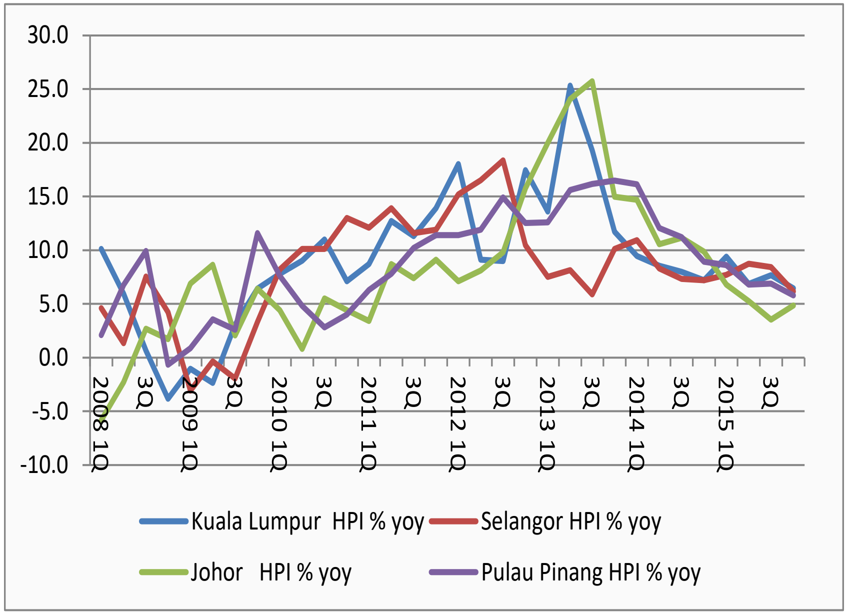
- A slate of **property-cooling and macro-prudential measures** (higher Real Property Gains Tax (RPGT), lower loans to value ratio (LTV), using net income (instead of gross income) in calculating debt service ratio for loan approvals) have had the **intended effects of curbing the nascent price bubbles** although these measures had **resulted in the softening of the property sector.**
- The **annual house price index** (HPI) continued its **slowing trend since 4Q2013** (+9.6% yoy) to 5.4% in 4Q2015, compared to an average growth of 11.4% in 4Q2011- 3Q2013. This almost matches the low of 5.6% growth posted in 4Q2009 during the period of 2008-09 Global Financial Crisis.
- MIER's Residential Property Index (RPI) crosses above the 100pt-threshold expansion mark of 111.2 for the first time in 1Q2016 after dipping below 100pt for five consecutive quarters since 4Q2014.
- According to the National Property Information Centre (NAPIC), **residential property sales value contracted 9.5% yoy in 1Q2016 while sales volume also declined 16.6% yoy,** marking the worst contraction since 4Q 2013.
- **Loan indicators for the residential property remained weak**. i) **Outstanding loan growth** extended its slowing trend; ii) **Housing loan applications** grew 7.1% in May, albeit exhibiting uneven trends; iii) **Approved housing loans** contracted 11.2% in May, but the rate of decline has narrowed from the steepest decline of 34.0% in Jan 2016. **Loan approval rate** for the purchase of residential property, which dropped to a record low of 38.3% in Jan 2016, **has increased gradually to 40.7% in May 2016.**

PROPERTY SECTOR INDICATORS AT A GLANCE

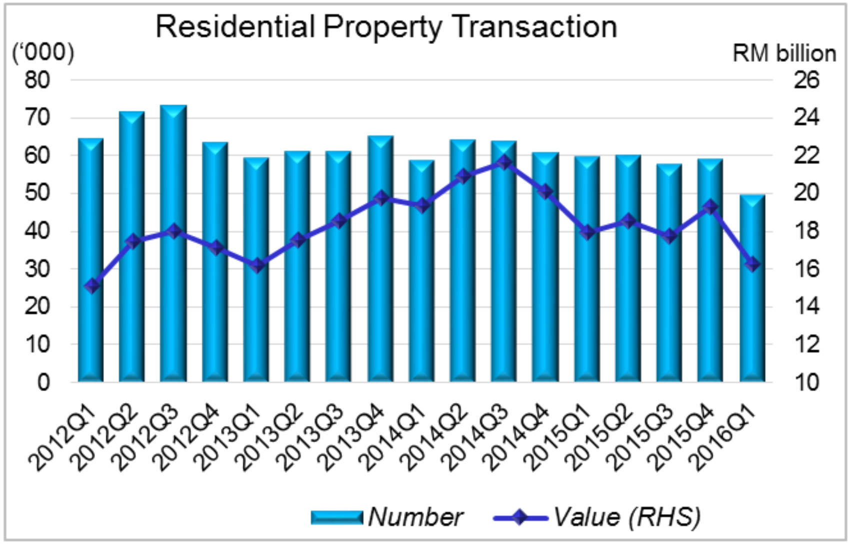
Property price index has been slowing since 3Q2013



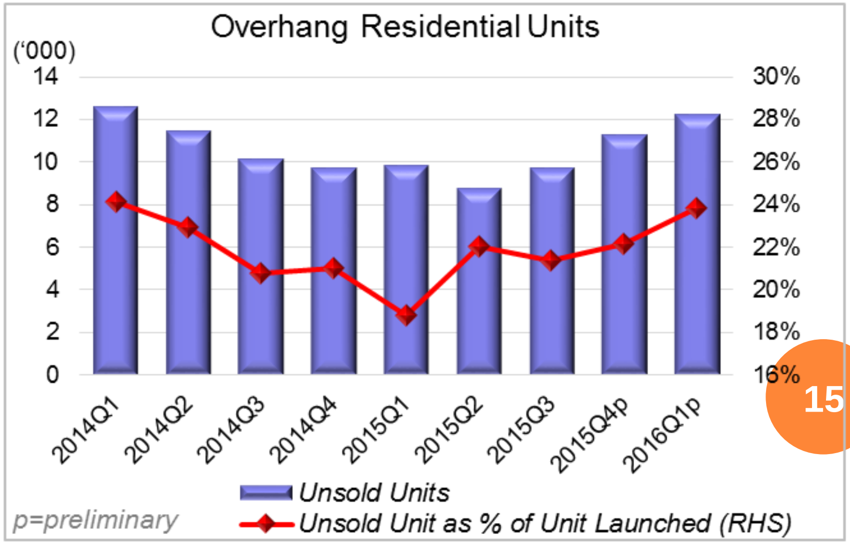
…across the major states



Both number and value of residential property transactions contracted sharply in 1Q2016



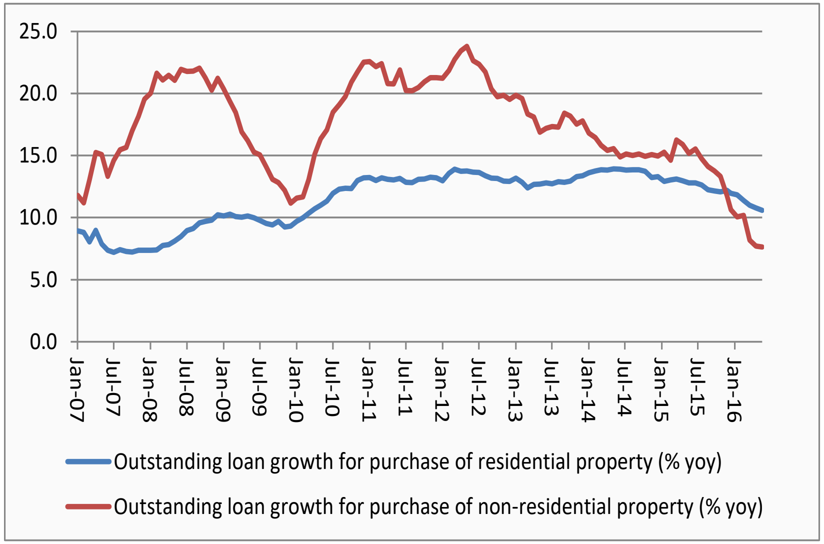
Number of overhang residential units rose for three consecutive quarters

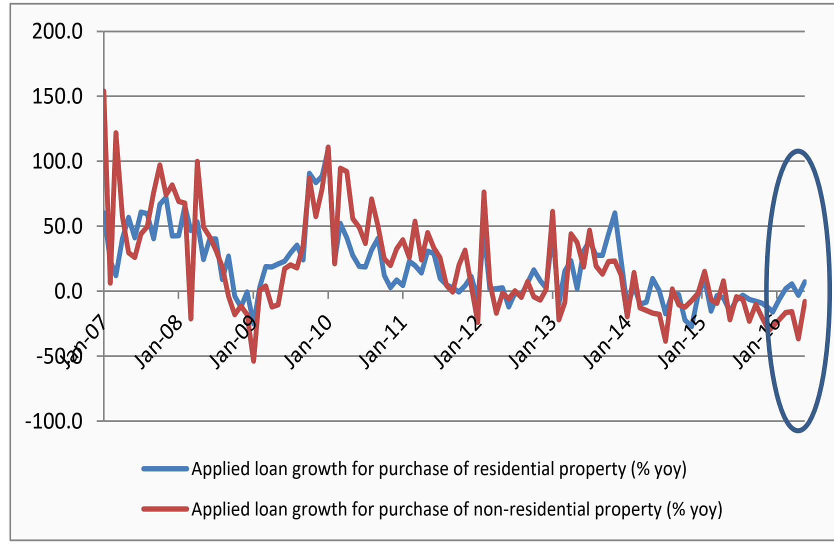


Source: NAPIC

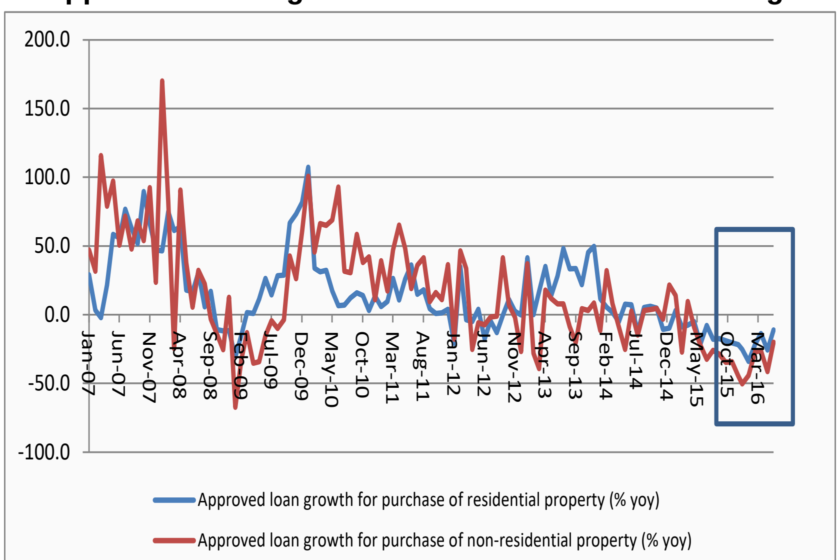
PROPERTY SECTOR INDICATORS AT A GLANCE

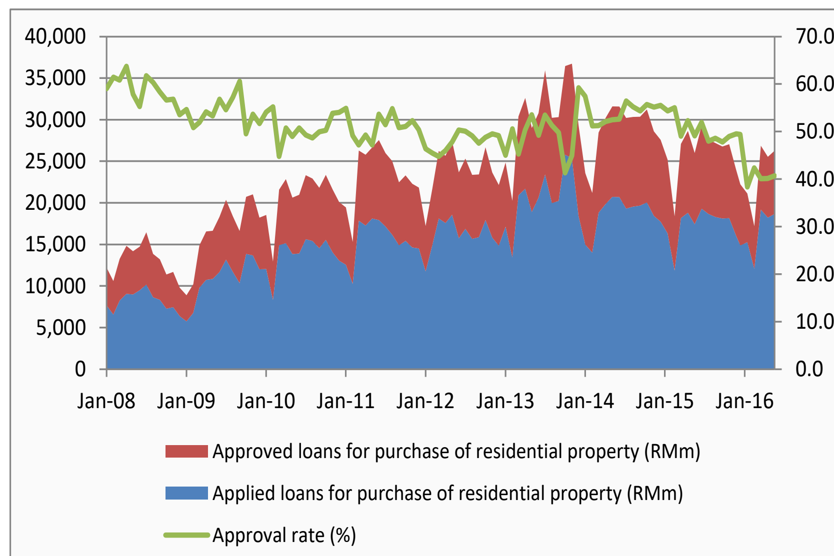
Outstanding loans growth for the purchase of residential property continued its slowing trend. Housing loan applications rebounded in May. It remains to be seen whether the rebound is sustainable





Approved housing loans contracted at a smaller magnitude in recent months. Loan approval rate has improved





Source: BNM

ISSUE 3: PROPERTY SECTOR CONTINUES TO CONSOLIDATE (CONT'D)

- The **property sector outlook is expected to remain challenging**. The sector will continue to consolidate with a weakening bias not only due to the on-going headwinds from the macro-prudential measures but also dampened by the prospects of weakening domestic economic growth, cautious buyer sentiment and "wait-and see" mode as well as the banks' more conservative lending stance given the current challenging economic environment.
- While the right time to adjust some of the measures is when the market equilibrium is a lot more certain and sustainable, but an **over-adjustment of the property sector must be avoided in a slowing economic climate**.
- A **prolonged economic slowdown** accompanied **by severe corrections in the property sector** would have **negative ramifications on the broader economy given its wide inter-and intra-linkages with the manufacturing, construction and financial services**.
- While core fundamental issues such as the affordability and over-supply in some segment of properties still linger, **a slow economic growth climate may be a good time to tweak some of the property-cooling measures to prevent the property sector from over-adjusting**. The risk of continued market consolidation could lead to a contraction if buyers' sentiments turn more bearish or the economy takes a turn for the worse.

PROPOSAL 3: FINE-TUNING OF PROPERTY MEASURES

- Housing demand and property prices are inevitably soft in an environment of weakening economic conditions, cautious consumer sentiment, rising unemployment rate and weak income growth.
- The **risk of continued property market consolidation** could **lead to a severe contraction** if **buyers' sentiments turn more bearish** or the economy takes a turn for the worse.
- As such, **selective fine-tuning of measures** in a challenging economic outlook would prevent the property sector from over-adjusting.

  i) Targeted fiscal incentives such as **lower the stamp or provide stamp duty relief** for the **property priced not exceeding RM500,000**;

  ii) **Re-introduce developer interest bearing scheme (DIBS)** for the **first-time house buyers (for owner-occupied)** and for the property priced below RM500,000;

  iii) With rising cost of living, housing affordability is an issue for the middle-income households to own a house. **Some leeway or flexibility should be given on the current stringent lending policy** for targeted groups, especially the first-home buyers or young families with a combined household income of RM10,000 and below to obtain home loan;

  iv) For **unsold property two years after completion**, **relax the rules and margin of loans** (e.g. 70% loan-to-value (LTV) for the third or more properties) to ease the glut of overhang properties.