Malaysia Budget 2021 – The pandemic budget

The Malaysian government announced an expansionary budget for 2021, aimed at providing sustained support for the economy. Financial support and fiscal reliefs are targeted at vulnerable populations and businesses to help them navigate the social, financial and economic fallout from COVID-19. In this investment note, we examine the potential investment implications for Malaysian financial markets from the measures proposed in Budget 2021.

Table 1: Malaysia Federal Government's revenue and expenditure

	2019 (RM billion)	2020 estimate (RM billion)	Budget 2021 (RM billion)
Revenue	264.4	227.3	236.9
Total expenditure[1]	317.5	314.7	322.5
Operating expenditure	263.3	226.7	236.5
Development expenditure	54.2	50.0	69.0
COVID-19 fund	-	38.0	17.0

Note: [1]Total expenditure = Operating expenditure +Development expenditure + COVID-19 Fund
Source: Maybank IB Research, 7 Nov 2020, "Malaysia Budget 2021: Nursing the economy back to health"

The Budget proposal will be debated in the parliament over the next two weeks before a vote. This time round, there is increased scrutiny on whether the Budget will pass or whether there will be any significant amendments to the proposal. In the past, passage of the Budget has typically been smooth. Uncertainty now stems from a fractious political make-up.

Impact on fixed income market & strategies

The government's assertive fiscal stance means that the planned budget deficit will only fall marginally from a targeted 6% of GDP in 2020 to 5.4% in 2021. The smaller deficit is based on an expected growth pick-up in 2021; official forecasts imply a nominal GDP growth of about 8.9%[2] year-on-year in 2021.

Due to the pandemic, the path of fiscal consolidation has been delayed. Prior to this, the government had targeted fiscal deficit of less than 3% of GDP in 2021. Nevertheless, fiscal slippage is unavoidable and reasonable considering the challenges posed by COVID-19 pandemic this year. As much as fiscal balances remain a key consideration for Malaysia's sovereign rating, we also believe that international rating agencies are likely to look at longer-term prospects of the country's public finances, including capability of generating sustainable revenue stream and governance standards, when making sovereign rating decisions.

The expansionary budget suggested less urgency for monetary easing, though rate cut may still be in the cards in 2021, depending on whether GDP growth in 2021 undershoots target. Even if there are no further cuts to the Overnight Policy Rate (OPR), we expect OPR to remain low for an extended period of time, thus supporting the local bond market.

Supply pressure remains a key concern for investors. Based on the official forecast of RM86.5 billion[3] in budget deficit, gross government bond supply for 2020 is less than previously expected. This is expected to provide some breathing space for the local bond market for the remainder of the year.

[2] Ministry of Finance, 6 November 2020
[3] Ministry of Finance, 6 November 2020

In 2021, bond supply is expected to remain elevated. Given the latest extension of the EPF withdrawal scheme (unemployed individual is allowed to withdraw RM500 per month from their EPF Account 1 and reduced EPF contribution (at 9% compared to 11% in normal times), demand for bonds from EPF is expected to remain below pre-Covid levels. As such, we are cautious on ultra-long duration government bonds in Malaysia.

That said, there is likely to be continuous investor demand on the shorter end of the yield curve due to high real yield valuations and monetary easing odds. Malaysia's 10-year real yield is one of the highest in the Emerging Markets, which explains the continued foreign inflow into the market. Foreign investors have remained net buyers of Malaysia bonds between April and October 2020, proving that attractive valuations are hard to ignore. We also do not discount possibility of more bond purchases by Bank Negara Malaysia in coming months.

Corporate bond issuance is also expected to increase in 2021 due to continuation of existing and new large infrastructure projects as well as strong economic recovery. Credit condition remains manageable, though downside risks persist on the back of resurgence of COVID-19 infections.

For now, we reiterate our neutral outlook on the local bond market. We maintain substantial holdings in selected corporate bonds to provide adequate income return to our bond funds. At the same time, a portion of the fund is invested in short-to-medium term government bonds for tactical positioning and liquidity purposes.

Impact on equities market

The Budget has a slight positive bias for the market given its expansionary stance and the non-materialization of measures that could have had negative impact on corporate earnings.

We have analysed the measures proposed in the Budget on various market sectors and summarized our views on their impact in Table 2.

To a large extent, local equities market will be influenced by global and local geopolitical development, progress on the control of COVID-19 pandemic and vaccine development. Economic recovery is uneven and as a result, performance of the equities market will unlikely be broad-based across all sectors. This necessitates an investment strategy where sector and stock selection are the keys to performances.

Notwithstanding the confluence of factors affecting the market, we continue to adopt a barbell strategy – staying with defensives to cushion the portfolio against market volatility while bottom-fishing to position well for an economic recovery. On a longer-term horizon, we remain focused on looking out for fundamentally sound stocks, particularly those that are beneficiaries of key investment themes vis-a-vis deglobalization, digitalisation, structural change to China's economy and climate change.

Table 2: Impact of Budget 2021 on Malaysian market sectors

Positive Impact	
Sectors	**Our views**
Gloves	• Financial impact from one-off contributions by glovemakers is far less negative than that of a windfall tax.
Construction	• RM15 billion will be allocated for transport infrastructure projects, and key projects like Rapid Transit System from Johor Bahru to Woodlands, Singapore and MRT3 are expected to be continued. • The KL-Singapore High Speed Rail project is expected to proceed subject to discussion with Singapore.
Technology	• Sizeable supply chain relocation incentives, as well as incentives for aerospace, electronics, medical devices and other high-tech segments.
Tobacco	• Legal tobacco volume may stabilize should enforcement against illicit trade be able to limit the amount of contraband cigarettes.

Neutral Impact	
Sectors	**Our views**
Property	• Measures are largely extension of current relief measures and unlikely to result in a big demand lift.
Telecommunication	• Although the government is granting RM1.5bn to 8m people in B40 to subscribe to internet services and buy new mobile phones, telecommunication companies will need to provide RM1.5bn worth of free data. Hence, the net impact is expected to be neutral. • Separately, the RM7.4bn to upgrade broadband services is not a new allocation as it is part of the RM21bn 5-year investments under Jendela.
Banking	• The continuation of targeted moratorium is basically an extension of the current measures and is unlikely to result in large changes from the existing condition. There is a risk, however, that the government will amend the Budget to approve an automatic blanket loan moratorium. Should that be the case, the impact may be less favourable on banks.
Healthcare	• Measures such as increase in tax relief for vaccination expenses and medical check-up is unlikely to result in large positive boost to earnings.

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