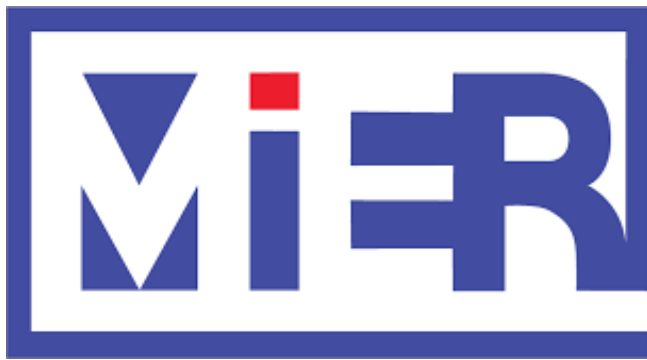




**MALAYSIAN INSTITUTE OF
ECONOMIC RESEARCH**

**BUDGET 2026:
MIER PRE-BUDGET
2026 DISCUSSION**

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A. Enhancing Macroeconomic Resilience

1. As an open economy, Malaysia may face external challenges, especially from slower global trade due to US tariffs, policy uncertainty, and ongoing or new geopolitical conflicts. Despite external risks, domestic demand—driven by private consumption and investment—will be the main driver of growth. While external trade is expected to slow, it will still support the economy.

Budget 2026 is an important chance to introduce policies that boost growth and keep Malaysia on track with RMK13 targets. It should include measures to drive the economy, strengthen resilience, and address key risks.

2. Proposals to catalyse economic growth:

I) Boost Private Consumption and Raise Employee Compensation

Private consumption can be stimulated by increasing employee compensation (COE) and providing more effective, targeted income transfers. Malaysia's COE is still low compared to peer countries, so steps should be taken to raise it.

Possible measures include:

- Expanding the progressive wage policy more quickly
- Starting efforts to reduce reliance on foreign workers, aligned with the RMK13 goal of lowering their share from 15% to 10% by 2030
- Encouraging mid-tier and large companies to raise wages based on workers' skills and qualifications
- Gradually increasing the minimum wage
- Improving wage negotiation mechanisms to ensure fair pay between employers and employees

The Budget should also continue income transfer programs, but make them more targeted and productive. These transfers should be linked to "exit strategies" that help households move out of the low-income group in the short to medium term, where appropriate.

II) Boost Private Investment and Tourism Value

Private investment can be strengthened by speeding up the conversion of approved investments into actual projects and encouraging more value creation.

Key steps include:

- Increasing the realization rate of approved investments and shortening the time from approval to implementation
- Fast-tracking investment projects by GLCs, GLICs (RM120 billion), and PPP/PFI projects (RM61 billion) under the 13th Malaysia Plan
- Introducing initiatives to encourage value creation across all sectors, as outlined in RMK13
- Maximising returns from tourism by improving its links with the domestic economy
- Enhancing Malaysia's investment ecosystem by cutting red tape, ensuring fair competition, and improving support services to make Malaysia more investor-friendly

Public spending could also be used to encourage private sector investment, including in non-traditional areas like rural infrastructure, schools, hospitals, and social impact projects.

III) Expand Exports and Maximise Trade Agreements

The budget should include clear measures to boost export value, especially for high-value **“Made by Malaysia”** products. It must help businesses navigate global trade challenges, such as U.S. tariff measures, and support efforts to diversify export markets.

Key actions include:

- Incentivising production and export of high-value Malaysian goods and services.
- Helping firms make better use of existing bilateral and regional trade agreements.
- Supporting initiatives to expand into new international markets.
- Encouraging export-oriented companies to strengthen domestic supply chains and increase local value-added content.

IV) Raise Enterprise-Level Productivity

While national labour productivity is improving (2.9% annually from 2021–2025 and projected 3.6% thereafter), more focus is needed at the **firm and industry** levels. The Malaysia Productivity Blueprint highlights the need to tackle productivity barriers unique to each sector.

The Budget should therefore:

- Provide incentives for firms to conduct productivity diagnostics and implement improvements.
- Support industry-level programmes that reactivate and expand productivity initiatives.
- Tailor measures to industry-specific needs to ensure sustainable productivity growth.

3. Proposals to Strengthen Resilience and Address Vulnerabilities

V) Build Fiscal Leverage

The government has made strong progress in improving its fiscal position. However, the debt service ratio remains high at 16%, and petroleum tax revenues are falling, reducing reliance on oil income — a positive long-term shift.

As global economic shocks become more frequent, Malaysia needs a stronger fiscal buffer to manage uncertainty and maintain economic stability. Moving toward a balanced or surplus budget would enhance confidence and resilience.

To further strengthen fiscal management, the Budget should include the following measures:

- **Broaden the tax base:** Introduce a fair and efficient tax system similar to the previous GST, but improved to avoid past weaknesses. It should have zero tax on essential goods and those used by lower-income groups. The current SST expansion is less effective, confusing, and inefficient.
- **Simplify investment incentives:** Review and streamline the many fiscal incentives to make them simpler, more transparent, and results-oriented.
- **Enforce fiscal responsibility:** Fully commit to the **Public Finance and Fiscal Responsibility Act 2025**, Audit Act, and Public Procurement Act to ensure transparency and accountability. Audit findings should lead to clear penalties and corrective actions. Funding for Ministries should be linked to implementation performance and outcome achievement.
- **Reform the civil service:** Address duplication of roles, outsource non-core functions, privatise where appropriate, and reassign staff according to national development priorities.
- **Improve expenditure efficiency:** Streamline overlapping functions in areas like youth, entrepreneurship, rural development, skills training, and socioeconomic programmes to reduce waste and improve coordination.
- **Transform the public sector:** Restructure and modernise the civil service to better align with Malaysia's current and future development needs.

VI) Strengthen the Current Account of the Balance of Payments

Close attention must be given to the current account balance, as Malaysia cannot afford to experience a twin deficit, even temporarily, without risking investor confidence and sovereign credit ratings.

Current weak performance is partly due to temporary factors—such as maintenance-related disruptions in commodity exports and higher imports linked to data centre investments—however, it also highlights underlying structural vulnerabilities that require policy attention.

The Budget should therefore include measures to strengthen the current account position by:

- Expanding exports, especially in high-value sectors.
- **Enhancing domestic linkages and supply chains** to reduce dependence on imported intermediate inputs.

- **Minimising leakages**, including managing outward remittances more effectively.
- **Sequencing large import projects** to better balance external payments.

These measures will help ensure a more sustainable and resilient external position for Malaysia.

B. Agriculture and Food Security

Laying the Foundation for Future Transformation

Budget 2026 will play a crucial role in laying the foundation for the **transformative agenda** outlined in the **13th Malaysia Plan (2026–2030)**. It also marks the mid-point alignment with key national policies, including the **National Agrofood Policy 2.0 (2021–2030)**, the **National Agri-Commodity Policy (2021–2030)**, the **New Industrial Master Plan (2021–2030)**, and the upcoming **National Food Security Blueprint (2026–2030)**.

The **agriculture sector**, with its multifunctional role, will continue to be a major contributor to **value creation, employment, export earnings, and rural development**, as well as to **food and nutrition security**. This contribution will be driven by integrated **supply and value chains**—covering inputs, production, processing, value-adding, and trade—both domestically and internationally.

Given the **dominance of the oil palm industry** (over 5 million hectares, exceeding other agricultural land uses combined), it will remain a key driver of growth in 2026. The sector is expected to lead in advancing **digital agriculture, circular economy practices**, and the **greening of value chains**. Further emphasis will be placed on **high-value innovations** such as nutraceuticals, renewable biomass energy, animal feed, and waste-to-wealth products.

In line with the 13th Malaysia Plan, efforts will also focus on **reducing greenhouse gas emissions, enhancing carbon sequestration, and participating in carbon credit trading**, including through **Bursa Malaysia’s Voluntary Carbon Exchange**.

The following are proposed measures for consideration under **Budget 2026**.

I) Reprioritising, Rationalising and Repurposing Agri-Support Services and Incentives

Under the **13th Malaysia Plan**, a key shift in agriculture and food security is the move from focusing on individual food items to a **“basket of food” approach**, recognising the **substitutability and complementarity** among food sources such as carbohydrates, proteins, fats, fibre, and micronutrients. This approach aims to ensure a balanced and nutritious diet by optimising what can be **produced locally** and what can be **sourced efficiently from abroad**, balancing **self-sufficiency** with **self-reliance**.

The **Self-Sufficiency Ratio (SSR)** targets set under the 13MP include:

- Rice: **80%** (main carbohydrate source)
- Beef and Buffalo: **50%**
- Fisheries: **90%**
- Poultry Meat: **140%**
- Poultry Eggs: **123%**
- Fruits: **83%**
- Vegetables: **79%**

To achieve these targets, **Budget 2026** should prioritise the **reprioritisation, rationalisation, and repurposing** of agricultural support services—covering **research, extension, credit, marketing, and incentives**—across the **public, private, and third sectors**.

In line with the Government's ongoing **subsidy rationalisation**, existing **inefficient or poorly targeted subsidies**—such as **blanket fertiliser** and **certified paddy seed subsidies**—should be reviewed and redesigned, especially in light of findings from **Auditor-General's Reports** and **Public Accounts Committee deliberations**. Support should instead be channelled toward **digital agriculture, precision farming, and green value chain initiatives**.

Additionally, a **comprehensive crop insurance scheme** should be developed, involving strong **state-level participation** and flexible implementation mechanisms to enhance risk management for farmers.

II) Promote Greater Private Sector Participation in Agro-Food Production

Given the evolving roles of the public and private sectors, there is a need to encourage greater private and third-sector participation in agro-food production through innovative partnership models. The Government should promote Public-Private Partnerships (PPP) and Public-Private-People Partnerships (PPPP), particularly those involving social enterprises, cooperatives, community organisations, and philanthropic entities.

Budget 2026 should provide targeted incentives and allocations to support transformative PPPP initiatives, especially in the interior regions of Sabah and Sarawak. These initiatives should integrate biodiversity conservation, agroforestry development, and circular economy practices to ensure sustainable and inclusive growth.

III) Accelerate the Growth of High-Growth, High-Value (HGHV) and Strategic Industries

In line with the three main thrusts of the 13th Malaysia Plan — *Raising the Ceiling, Raising the Floor, and Good Governance* — Budget 2026 should prioritise accelerating the growth of High-Growth, High-Value (HGHV) **and** strategic industries.

For the agriculture and food security sectors, this includes advancing the Green Economy (particularly the greening of agri-food value chains), the Blue Economy, and the Halal industry. These efforts also support initiatives to improve quality of life through responsible food production and consumption, wider adoption of digital agri-technology, and stronger resilience in food supply chains and trade networks.

IV) Support Farmers and Smallholders in Carbon Credit Monetisation

With the planned **introduction of a carbon tax in 2026**, Malaysia is poised to expand participation in **Bursa Malaysia's Voluntary Carbon Exchange (VCM)**. Farmers and smallholders can benefit from **carbon credit monetisation**, especially in key sectors such as **rice** and **oil palm**.

However, successful participation requires more than technology for **GHG reduction, carbon sequestration, and waste-to-energy initiatives**. It also depends on access to **innovative financing** and the ability to **Measure, Report, and Verify (MRV)** emissions accurately, supported by **third-party verification** before carbon credits can be issued and traded.

Therefore, the **Government should provide targeted financial support and incentives** to help farmers and smallholders meet these requirements and unlock new income streams through the Voluntary Carbon Market.

V) Support Counter-Trade for Food

Malaysia currently does not classify **palm oil** as a food product in most food security policy documents. This contrasts with international practice, as organisations such as the **FAO, World Bank, and UNCTAD** classify palm oil under “*Oils and Fats*.” Similarly, the **Department of Statistics Malaysia (DOSM)** includes “*Oils and Fats*” — and thus palm oil — in its **Household Expenditure Survey** under the food category.

There are strong arguments, including those by **MIER**, that Malaysia should recognise **edible palm oil and palm-based products** as food. Palm oil is widely used in **cooking**

and food processing—such as in cakes, biscuits, margarine, chocolate, ice cream, creamer, and instant noodles—both domestically and internationally.

Reclassifying palm oil as food would have significant implications. Malaysia would effectively become a **net exporter of food**, allowing a new national narrative such as “*We Feed the World*” or “*We Feed the Future*.” With palm oil’s dominant role in land use, trade, and R&D, Malaysia is already a **global leader** in this sector. This move would also strengthen **food diplomacy**, support **counter-trade arrangements** for food imports, and enhance **national food security**.

Accordingly, **Budget 2026** should introduce **incentives to facilitate counter-trade initiatives** using palm oil and its products, especially to support **Sabah and Sarawak**, where geographical challenges affect food access. These measures should aim to strengthen **food availability, accessibility, utilization, stability, sustainability, and local agency**.

Additionally, there should be a **review and rationalisation of the windfall profits tax** on palm oil exports to ensure fair and efficient outcomes that support the industry’s contribution to national food security.

VI) Improve Coherence Between Federal and State Budgets

The **Department of Statistics Malaysia (DOSM)** is advancing the **democratisation of agricultural data** by publishing comprehensive value chain reports for key commodities such as **paddy, fruits, vegetables, livestock, fisheries, and oil palm**. These datasets, available at **national, state, and district levels**, will enable more coordinated **top-down and bottom-up planning**.

As **land and water resources**—critical to agriculture and food production—fall under **state jurisdiction**, it is essential to strengthen alignment between **federal and state planning and budgeting**. Greater **coherence and complementarity** between the **national Budget 2026** and individual **state budgets** (to be tabled subsequently) will ensure more effective implementation of agricultural and food security initiatives.

C. Securing Growth How defence modernization powers Malaysia's economy

Regional security today is marked by great power competition, contested maritime zones, cyber intrusions, and the rise of hybrid warfare. Hence for any developing country, peace and security are the bedrock of national progress. Defence and security are not merely instruments of protection, but essential elements of **national power** that underpin sovereignty, economic resilience, and international standing. As Malaysia looks ahead, Budget 2026 is set to play a pivotal role in reinforcing this foundation by modernising the Malaysian Armed Forces (MAF) into a Future Force that is both credible and sustainable.

I) Modernising the MAF

Beyond bolstering national security, the modernisation push is expected to stimulate Malaysia's defence industry. Collaboration with local universities, Research Centre, Financial Institution and International Stakeholders should focus on developing drones, radar, communications systems, and artificial intelligence applications. Mandatory technology-transfer agreements in foreign procurements are also on the table, ensuring that investments generate long-term economic returns.

II) Financing Models

To avoid fiscal strain, the government may consider sustainable financing models such as multi-year allocation schemes for major procurements to avoid annual fiscal strain, leasing models for selected assets, and establishing a Strategic Defence Fund to support long-term mega projects. These measures will ensure that modern asset acquisition can proceed without placing excessive pressure on the national fiscal position.

Budget 2026 must mark the beginning of a transformation of the MAF into a credible Future Force, flexible, technology-driven, rapid in response, and adaptable to emerging threats. This modernisation will not only secure the nation's defence but also position the defence industry as a new engine of economic growth. Through this strategy, Malaysia will be able to safeguard sovereignty and strengthen its standing as a respected regional player in maintaining peace and stability in Southeast Asia.

D. Productive Social Protection

Against the backdrop of demographic transition and economic structural weaknesses, the 2026 budget must be consistent with the long-term RMK13 goal of increasing productivity growth while enhancing people's standard of living. The budget approach should be centred on productive social protection. Malaysia has become an ageing nation, with more than 7% of the population aged 65 and over.

The growing elderly population, along with inadequate retirement plans, has resulted in many Malaysians falling into old age poverty. At the same time significant portion of Malaysians receive lower salaries. Approximately one-third of the labour force earns less than two-thirds of the national median wage, which is now RM3,000 per month, just RM300 more than the current minimum wage. Malaysia's percentage of skill-related underemployment has climbed significantly over the last decade, from around 10% among degree holders in 2010 to more than 30% by 2024. This highlights economic fundamental problems.

Increasing income and productivity. Therefore, the Budget should be tailored to increase people's income while resolving economic structural weaknesses. The primary strategy is to create meaningful employment opportunities through focused labour market intervention. Senior citizens, military veterans, and persons in informal employment are among the key target categories, with a two-pronged strategy aimed at producing a stream of income for the groups while also increasing overall productivity in the economy. Furthermore, the intended job creation should be aligned with the objective to lessen reliance on foreign workers.

Focus for Senior citizens:

- Provide opportunities for elderly workers to apply their skills without competing with younger employees.
- Incentives to support the care economy.
- Recognizing healthcare personnel.
- Incentives for family caregivers and civil society involvement in caring for seniors.

Military veterans:

- Intervention in the labour market by developing occupations that fit their skills, such as security staff, coaching, and disciplinary training.
- Maximize underutilized military assets to serve veterans.

Informal workers:

- Compulsory social protection coverage, notably for retirement and employment insurance.
- Opportunities for them to get into the formal sector.

Other marginalized groups:

- Women: Continue efforts to expand female labour participation, particularly among marginalized women such as single mothers.
- Undocumented children: providing access to education for undocumented children in order to increase future economic growth and reduce the possible cost to society if they grew up without education.

E. Urgent Infrastructure Construction for Sabah and Kelantan

The problem of reliable utility is an ongoing problem that are not only disservice to the population but also the main factor for stunted economic growth in both states. Provision of essential utilities like clean water and reliable electricity, particularly in rural areas is also crucial for enhancing quality of life in some of the poorest districts in Malaysia.

The government has committed to build infrastructure for both states in RMK13. However, these projects need to be **frontloaded** and prioritised in the government's budget for several reasons:

- More than ever, Sabah and Kelantan are prone to natural disasters especially flooding. Floods are damaging to the local economy as businesses and workers are not able to participate in economic activities. The damage and clean ups are also costly especially in areas where flooding happens frequently.
- Flash floods in major urban areas such as Penampang and Kota Kinabalu are especially damaging to the economy. Poor planning and unrestricted development has made certain areas prone to flooding even after short rain showers. Roads are constantly in need of repairs after flooding.
- Road and water infrastructure need to keep up as tourism industry grow. Hundreds of tourist travel to Kundasang from Kota Kinabalu everyday on poorly maintained trunk road. Five star hotels and golf resorts in the district of Tuaran are also popular but require travel on poor roads. Other districts with high tourism potential such as Kota Belud and Kudat are also limited by poor transport infrastructure. In Kelantan, tourists are known to fly into Kota Bahru to get to Pulau Perhentian.
- Large scale industries are unable to operate in an environment where electricity and water supplies are inconsistent.

G. Empowering Research

With rapid advancement of technology and innovation, it is even more important today for Malaysia to create its own technology. Rising monopolistic power and threat of being a captive customer are clear reasons for Malaysia to produce its own technology whenever possible. In order to be productive, the research agenda must have a few clear objectives:

Research output must be at least productive in the local context to reduce dependency on foreign technology and innovation. For example, there is no need to import drones for agriculture use of local research can produce similar products.

Differentiation between invention technology and innovation. Research into invention and technology takes time commitment which are rarely supported by the private sector. Innovation today, meanwhile is supported by private funding for commercial imperative. Therefore, the government needs to continue to commit to research in institutions such as universities, MARDI, SIRIM and others in order for Malaysia to continue to produce its own technology.

Scientists and researchers working in universities and government funded laboratories should be encouraged to train in business and finance in order to bridge the gap between technology (government orientation) and innovation (commercial orientation). The government may incentivise scientists by reviewing current intellectual property and profit sharing regimes.