

24 July 2025

Prime Minister's Special Announcement

Reform deferred, populist push adds fiscal strain

SUMMARY

- The government latest measures are not a conventional fiscal stimulus but a **redistribution of recent macro gains** (stronger ringgit, stable inflation) to support domestic demand and ease cost-of-living pressures. While politically popular, they heighten the tension between near-term social spending and medium-term fiscal discipline.
- **Malaysia's Economy:** Targeted fiscal measures, including cash transfers and targeted fuel subsidies, are set to boost private consumption in 2H25, helping offset external trade risks due to high tariff impact, and reaffirmed our GDP growth target at 4.3% (2024: 5.1%).
- **Headline Inflation:** Fuel subsidy reform is finally set for rollout in 4Q25, but in a surprising twist, most consumers will enjoy cheaper RON95 petrol. Inflation is now expected to average 1.7% in 2025, down from our earlier forecast of 2.0%. Fiscal trade-offs loom as relief outweighs reform, with SST on fuels a possible offset.
- **Fiscal Outlook:** The new fiscal boost albeit smaller and delayed RON95 subsidy reform aims to support growth and ease living costs, but risk widening the fiscal deficit and raises debt. The new measures (RM2.8b or 0.14% of GDP) are modest but expected to push the 2025 fiscal deficit to 4.1% of GDP above the government's 3.8% target.
- **Debt Outlook:** Government debt is projected to reach RM1,330.6b or 65.9% of GDP by end-2025. This reflects slower growth in 2H25 and ongoing development spending. While the ceiling may be breached temporarily, prudent debt management, steady foreign bond inflows, and a stronger ringgit should help a stable medium-term debt profile.

OVERVIEW

- Prime Minister Dato' Seri Anwar Ibrahim's 23rd July address entitled "*Penghargaan Untuk Rakyat*" (Appreciation for the People) introduced additional cost-of-living measures totalling at least RM2.8b. While politically popular, these initiatives are not typical fiscal stimuli but rather a redistribution of fiscal gains from Malaysia's improving macro fundamentals. The rollout comes amid solid growth momentum, improved global competitiveness ranking, a resurgent ringgit, and benign inflation, aligning broadly with our GDP forecast of 2025 GDP at 4.3%, underpinned by resilient domestic demand and reform-led investor confidence despite uncertainties due to external headwinds from Trump's tariffs and geopolitical risks.
- In his address, the Prime Minister reaffirmed the government's commitment to inclusive growth under the *Ekonomi MADANI* framework. Existing MADANI welfare architecture (STR, SARA, Sejahtera MADANI) remains the delivery vehicle, while no new taxes or major off-budget items announced. At the same time, he underscored the importance of translating these gains into improvements in rakyat well-being. To further support domestic demand and ease cost-of-living pressures, the Prime Minister announced several new direct fiscal measures:

Table 1: Breakdown of Cost-of-living Measures

Measures	Description	Cost (RM billion)
SARA for All (RM100)	Cash aid for every adult Malaysian (22.0m people)	+2.0
STR + SARA Total	Enhanced cash transfers to B40, M40	15.0 (from 13.0)
Jualan Rahmah MADANI	Subsidised groceries across 600 state constituencies	+0.3
Toll Hike Freeze	Govt absorbs scheduled 2025 hike for 10 highways	+0.5
Targeted RON95 Fuel Subsidy	Future relief via RM1.99/litre RON95 (4Q25 rollout – est 18.0m people)	(2023-2024: 20.0b/year est.)

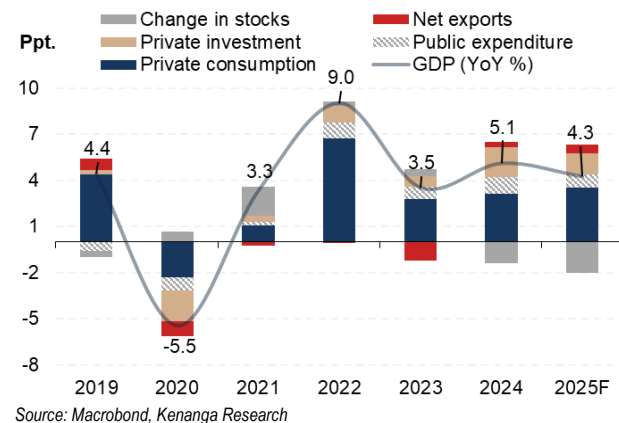
Source: MoF, Kenanga Research

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GROWTH OUTLOOK: MODEST FISCAL PUSH TO ANCHOR GROWTH

- Targeted fiscal measures are expected to lift private consumption and cushion external headwinds in 2H25, though trade risks remain
 - A boost to private consumption.** The RM2.0b one-off Sumbangan Asas Rahmah (SARA) cash transfer to all adults, alongside the Sumbangan Tunai Rahmah (STR) allocations (RM15.0b from RM13.0b), *Jualan Rahmah Madani* (RM0.6b from RM0.3b) and a freeze on toll hikes (RM0.5b), should deliver a short-term boost to private consumption in 2H25. The SARA programme alone is set to benefit over 22.0m Malaysians, front-loading spending potential around the Malaysia Day holiday period and year-end festive season. We expect spillover into stronger household spending in F&B, retail, and essential goods, partially offsetting export drag if trade tensions escalate. We forecast private consumption growth to expand by 5.8% in 2025 (2024: 5.1%), supported by the impact of these new measures, coupled with steady labour market conditions and rising household income.
 - Growth outlook intact.** Overall, we maintain our 2025 GDP growth forecast at 4.3% (2024: 5.1%), anticipating moderate 2H25 growth, but will be underpinned by fiscal support and lower policy rates. While the near-term fiscal impulse is mildly expansionary and supportive of overall growth, we remain cautious on persistent external headwinds, particularly from elevated US tariffs.

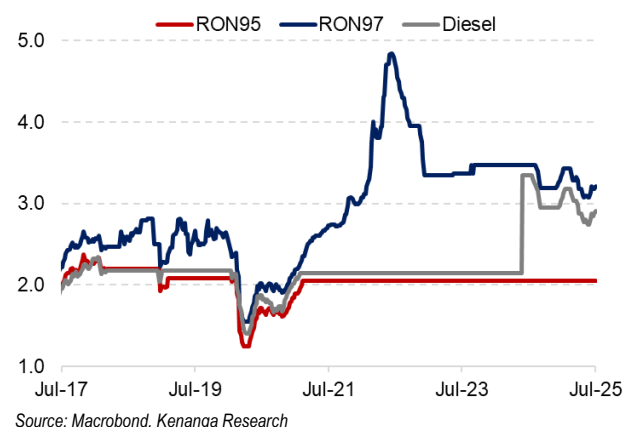
Graph 1: GDP Growth Trend (demand side)



INFLATION OUTLOOK: A CALIBRATED DETOUR

- Headline inflation is expected to rise modestly in 4Q25, but the impact may be softer than initially projected. This is primarily because a majority of around 18.0m Malaysians are expected to benefit from the lower RON95 petrol price of RM1.99 per litre (from RM2.05).
- In our latest monthly inflation update published yesterday, we reaffirmed 2025 forecast of 2.0%, which assumed targeted fuel subsidy reforms would commence in August. The government has now delayed implementation to 4Q25, with final details expected by end-September. Combined with further reduction in subsidised RON95 prices, the inflation impact will likely be smaller than previously assumed.
- The reform, long delayed and politically fraught, is designed to recalibrate Malaysia's unsustainable fuel subsidy model. Rather than a blanket removal, the government is pursuing a more targeted approach. The top 5–10% of income earners, those presumably with the financial capacity to absorb market prices, will be excluded, while low- and middle-income groups remain shielded and may benefit from cheaper fuel.
- To implement this, **the government is expected to float RON95 at market price. For eligible recipients, it plans to expand on the existing IC-linked identification system, developed for diesel rationalisation.** A more sophisticated, tech-enabled mechanism is expected, though the earlier all-in-one registry (PADU) appears sidelined. The aim is to minimise both inclusion errors and exclusion errors, long-standing flaws of universal subsidy schemes.
- For 3Q25, we forecast headline inflation to range between 1.5% and 1.8%, rising slightly **to 2.2% and 2.6% in 4Q25 due to** staggered and partial implementation of fuel reforms. On balance, this **brings our new full-year inflation forecast to 1.7%, 30 basis points (bps) downward revision**, and below the 10-year average of 1.9%.

Graph 2: Fuel Prices in Peninsular Malaysia



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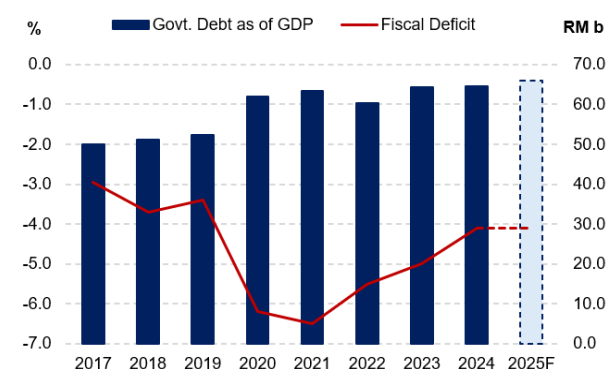
- **Core inflation, however, is expected to hold firm, at around 1.8%, reflecting resilient domestic demand and a tight labour market.** With GDP growth projected to hold above 4.0%, we see low probability for BNM to deliver another 25 bps OPR cut in the near term.
- **Our in-house view continues to advocate for a market-based fuel pricing mechanism, paired with targeted cash transfers** for vulnerable groups. For example, given that the current market price for RON95 hovers around RM2.50 per litre, the government could raise the subsidised price by RM0.10 per quarter. This would better align subsidies with fiscal capacity while protecting low-income households from global oil market swings.
- That said, the government appears to have opted for a politically calibrated approach, delaying reform and cutting the subsidised price further. To preserve fiscal space, **new revenue sources must be explored.** One possible option could be **extending Sales and Service Tax (SST) to premium fuel products such as RON97**, helping offset the subsidy bill and freeing funds for higher-impact, growth-enhancing investments that could lift productivity and, eventually, sovereign credit ratings.

FISCAL MANAGEMENT: DEFICIT PRESSURES MOUNT

• Small-scale fiscal boost and delayed subsidy reforms to support growth, but risk widening the deficit

- The newly announced direct fiscal measures, namely the RM2.0b one-off SARA cash aid, RM0.5b toll freeze, and RM0.3b extra allocation for *Jalan Rahmah Madani*, amounting to about RM2.8b, or 0.14% of GDP. Though relatively modest, these measures are likely to push the fiscal deficit beyond the government's 2025 target of 3.8% of GDP (2024: 4.1%), as we do not anticipate a budget surplus in the government's primary balance given the increase in its expenditures. Nonetheless, we maintain our deficit projection of 4.1% of GDP, assuming no offsetting revenue gains and factoring in the impact of slower GDP growth projection.

Graph 3: Govt Debt as of GDP and Fiscal Deficit



Source: Bloomberg, Kenanga Research

Note: The Govt Debt as of GDP in absolute terms (RM bil) and the scale is inverted on the right vertical axis

- Our projection also incorporates the government's commitment to continue fuel subsidies for most of the population under the targeted fuel subsidy rationalisation plan. While no full details have been announced, the net savings from the rationalisation are expected to be limited due to the decision to reduce the RON95 price to RM1.99/litre from the current RM2.05/litre, benefiting some 18.0m Malaysians.
- Consequently, federal debt is likely to increase by end-2025. While the fiscal injection supports short-term consumption and growth, it underscores the growing trade-off between social spending and medium-term fiscal consolidation.
- Although the expanded SST beginning in 3Q25 and the upcoming planned subsidy rationalisation likely in 4Q25 may ease fiscal pressure, we believe the government must proactively explore new and sustainable revenue sources. These include enhancing tax compliance, broadening the tax base and introducing alternative fiscal instruments to reduce reliance on volatile revenues.

• Limited fiscal buffers likely as the government frontloads borrowings

- **Debt headroom:** As of July 2025, Federal Government debt is estimated at RM1.32t. Statutory debt, which includes Malaysia Government Securities, Government Investment Issue, and Malaysia Islamic Treasury Bills, is estimated at 64.0% of GDP, leaving a margin of 1.0% or RM35.7b before reaching the statutory debt ceiling of 65.0%. Maturity risk remains low, with Malaysia Treasury Bills at RM2.0b, well below the RM10.0b cap, while offshore debt at RM27.9b, staying within the RM35.0b limit.
- **Government debt** is projected to reach RM1.33t or 65.9% of GDP in 2025, reflecting a more cautious outlook compared to the Ministry of Finance's 64.0% estimate. This forecast is primarily driven by expectations of slower 2H25 GDP growth dragging down nominal GDP and, in turn, raising the debt-to-GDP ratio. The higher debt level also reflects rising financing needs tied to ongoing fiscal support measures and development spending. A temporary breach of the 65.0% ceiling is possible, but we expect the government to manage this through a mix of fiscal discipline, revenue mobilisation, and prudent debt issuance. Continued investor confidence, supported by a stable

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domestic bond market and a stronger ringgit outlook, will be crucial in managing debt sustainability over the medium term.

- **Bond Outlook:** Foreign portfolio inflows are expected to continue, albeit more gradually, supported by improved sentiment, a stronger ringgit, and Malaysia's asset quality, which may boost demand for local bonds and lower yields. The recent OPR cut to 2.75% introduces a mild bull steepening bias, reflecting a more accommodative BNM stance. We revise our MGS 10-year yield forecasts to 3.30% (3Q25) from 3.53%, and 3.43% (4Q25) from 3.46%, anticipating softer front-end rates. On the supply side, gross issuance is slightly raised to RM166.5b, aligned with higher funding needs from the 4.1% fiscal deficit target. Rollover pressures should ease, with fewer MGS and GII maturities, with issuance likely to moderate in 2H25 after RM91.0b was raised in 1H25.

Table 2: Federal Government Debt Headroom

		latest	RM bil limit	balance
Offshore borrowing	1Q25	27.9	35.0	7.1
Malaysian Treasury Bills (MTB)	July-25	2.0	10.0	8.0
Statutory (MGS, MGII, MITB)	July-25	1,291.4	1,312.0	20.6
Statutory (% of GDP)	July-25	64.0%	65.0%	1.0%
Total:		1,321.3	1,357.0	35.7

Source: BNM, Macrobond, Kenanga Research

Appendix: Key Highlights from Prime Minister's speech

- Minimum wage raised to RM1,700 from RM1,500 to be fully implemented effective 1 August 2025
- GLICs and GLCs ensured 153,000 workers receive a living wage of at least RM3,100 per month
- Health Ministry expediting the hiring of over 4,000 new posts nationwide by end-2025
- The floor price for paddy purchases has been increased to RM1,500 in 2025
- Sejati MADANI channels up to RM100,000 to communities, empowering them to choose income-generating economic activities
- Kampung Angkat MADANI expanded from 40 to 200 villages in 2025.
- Sekolah Angkat MADANI ensures children receive quality education, targeting 1,000 adopted schools by end-2025.
- Every Malaysian citizen aged 18 and above will receive RM100 one-off via MyKad under the Sumbangan Asas Rahmah (SARA)
- Total STR and SARA allocations for 2025 increased to RM15.0b from RM13.0b costing additional RM2.0b and benefitting 22.0m people
- 15 September 2025 (Monday) is declared a public holiday in conjunction with Malaysia Day
- Toll rate hikes scheduled for 10 highways in 2025 are postponed, costing the government over RM500.0m
- Electricity tariff restructuring effective July 2025 saw 85.0% of domestic users enjoying bill reductions of up to 14.0%
- The RON95 petrol subsidy targeting mechanism will be announced by end-September 2025
- RON95 petrol price will be lowered to RM1.99 per litre from RM2.05

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