Speech by YB Lim Guan Eng
Luncheon Address, Khazanah Megatrends Forum 2018

[Salutations]
Datuk Shahril Ridza Ridzuan, Managing Director of Khazanah Nasional,
Distinguished Speakers, Guests,
Ladies and Gentlemen,

1. A very good afternoon to all of you. I would like to thank Datuk Shahril and Khazanah Nasional for inviting me to address such a distinguished crowd here today.

2. The theme of this year's Khazanah Megatrends Forum, "On Balance: Recalibrating Markets, Firms, Society and People" is one that closely encapsulates the bulk of my efforts so far as Minister of Finance as we to recalibrate Malaysia's public finances.

3. I would like to share with you how the Ministry of Finance can provide a leading role in 3 areas, namely achieving fiscal sustainability, creating an "Entrepreneurial State" and raising the well-being of our *rakyat*.

Macro and Fiscal Prospects – A Storm is Coming; Is our Ship Seaworthy?

Ladies and gentlemen,

4. I understand that you have heard from earlier this morning that the global external conditions herald a coming storm. Is the Malaysian ship ready to weather such storms?

5. As investors' confidence wavers, we are seeing an outflow of funds from Emerging Markets back to safe havens in Developed Markets. But so far, Malaysia has been more resilient than others in facing the outflow.

6. The external macroeconomic impact to Malaysia has not been as severe as other Emerging Market countries, as evidenced by the performance of the Malaysian ringgit and the FBMKLCI. The ringgit has been one of the best

performing Emerging Market currencies – depreciating by about 3.0% against the US Dollar YTD as of end of September, as opposed to Philippine Peso depreciating 8.4%, Indonesian Rupiah depreciating 10.3%, Indian Rupee depreciating 13.8% and Turkish Lira depreciating 59.7%.

7. One of the main reasons for the Malaysian resilience is our current account in contrast to other countries that suffer from twin deficits. In 2017, Malaysian had a current account surplus of 3.0% of 2017 GDP and in the first half of 2018, the balance stood at 2.7% of GDP or RM18.9 billion. There have been some concerns about the weak 2Q18 current account surplus of only RM3.9 billion and the low August 2018 trade balance of RM1.6 billion. But these low surpluses in large part were caused by the tax holiday period after we abolished the GST, that in turn encouraged imports. Indeed August imports grew at a high rate of 11.2% YoY. With the reintroduction of the SST in September, import growth will moderate and improve the balances in the short term. Therefore, we expect the Malaysian current account to remain in surplus for this year and not suffer from twin deficit.

8. Meanwhile, the FBMKLCI remains steady (+0.6% YTD by end of September) as opposed to the MSCI Emerging Market Index which has fallen 7.7% in the same period. Looking at fixed income markets, while we cannot entirely escape the effects of a more hawkish US Fed, the 10-year Malaysian government bond yield has risen by only 16 basis points so far this year up to end of September, as opposed to more drastic moves in other markets – 69 basis points in India, 212 basis points in Indonesia, and at an staggering rate of 588 basis points in Turkey.

9. It isn't all just roses. There are thorns and the bulk of them happen to be in public finances. Yet whilst we have to deal with RM1,087 trillion worth of government debt and liabilities which stood at 80.3% of GDP, we do have options in dealing with it.

10. The good news is that there is still all of you – the corporate sector. Malaysian corporates has the capacity on its balance sheets to invest and pursue growth because Malaysian corporate debt, at least among the listed companies, is merely 20% of GDP. Indeed, the debt-to-EBITDA ratio of Malaysian public listed companies is about 2x, far lower than public listed

companies across the MSCI Developed Markets and Emerging Markets indices at 5-8x. So, we need all of you to invest and strive for an earnings growth higher than the 6.8% achieved by the FBMKLCI companies last year. I know there are headwinds, I understand that returns may have flattened, but the corporate sector has a prominent role in helping to keep the economy going.

11. Our long-term economic goal is to become a developed nation. Here, I want to highlight three key pillars upon which my Ministry will play a leading role – achieving fiscal sustainability, creating an entrepreneurial state, and most important of all improving the well-being of the *rakyat*.

Fiscal Sustainability – Short-term Fiscal Consolidation vs. Long-term Growth

12. As the Minister of Finance, I am in charge of ensuring the fiscal sustainability of the government. In the short-term we have to consolidate our fiscal position in order to address the excesses of the previous government. The first step is to lay bare the actual fiscal position of the nation – revenue, expenditure, liabilities. The whole truth, rather than bits and pieces of it. The last administration's penchant for opaque off-budget spending had made this difficult but we have managed to overcome that challenge. Off-budget spending will be a relic of the past, even more so after we transition to accrual accounting from cash accounting by 2021.

13. As we prepare for Budget 2019, the first Budget of the new government, we are putting in place some additional institutional checks-and-balances for government finances as part of the government's overall institutional reforms. In particular, the newly-formed Public Finance Committee ("PFC") is tasked to outline government medium-term fiscal plans to balance out needs for fiscal consolidation and need for the government to spend for future economic growth. We have also set up a Tax Reform Committee ("TRC") to make our nation's taxation system more efficient, neutral and progressive.

14. All we are doing here is pulling back excesses of the past. What we are calling for is not austerity, but smarter spending. We have adopted a wider application of open tender for government procurements and projects

whereas previously, direct negotiations done by the previous administration had led to overspending. We are also more selective in making public investments. Furthermore, the government has successfully renegotiated the LRT3 project back in July when we cut the initial project cost by 47% (RM31.65 billion to RM16.63 billion) by tweaking the design specifications so that it meets a more realistic passenger demand projection. We have also shaved RM5.22 billion off the MRT2 total cost of RM56.93 billion recently by rationalising the above ground portion of the project. The RM5.22 billion savings represent 23% of the above ground portion of the cost. More savings will be gained when we retender out the underground segment soon.

15. If there are key areas of priority that require spending, we would be more than happy to spend – especially when it leads to long-term sustainable growth that improves the well-being of the *rakyat*. We are currently reviewing a large number of public-private partnership projects managed under UKAS. At the moment, 45 out of 67 PPP projects under review have been given the green lights to proceed, on the condition that it goes through open tender process benchmarked against international practices. This will not only generate additional economic growth, but also raise the quality of growth higher and leave no space for financial abuses that were prevalent in the past.

Entrepreneurial State – Private Sector Leads, Government Supports

Ladies and gentlemen,

16. Fiscal consolidation is a means towards fiscal sustainability. But sustainability requires a reasonable level of economic growth. This government understands that too much and too fast a consolidation may affect growth.

17. Amid challenges to public finance, this government believes the private sector must take the lead in steering the economy forward. However that does not mean the government cannot play a role. The government is committed to creating an environment where the private sector can thrive.

18. We need to pursue economic diversification. But this is easier said than done. For the private sector to pursue diversification, it almost certainly implies going beyond their core. This could be a different product, a different geography, a different industry, all of which are typically high risk endeavours for business. We must move away from the mentality of, “If you build it, they will come” or, in other words, if the government decides to promote a new sector, businesses will naturally move towards that sector. This is not true. Profits are hard-earned and, especially in a global economy, increasingly competitive.

19. That being said, it is also true that in this era of Industry 4.0, firms also need to evolve. They cannot just stand still, they must innovate or get left behind. The corporate lifespan of companies on the S&P 500 in the United States has decreased from 60 years in the 1950s to less than 20 today.

20. So then the question is, if the private sector is going to lead growth, and needs to innovate, how can the government supports the private sector in innovating for economic diversification? This needs to be a collaborative process. If there are ways in which the government can help either minimise the risks of innovation or improve the general business ecosystem in Malaysia, we will do it. This is an idea coined by UCL Professor Mariana Mazzucato, called the “Entrepreneurial State.”

21. A key finding in Mazzucato’s work is that, “…the private sector only finds the courage to invest after an entrepreneurial state has made the [initial] high-risk investments.” Indeed, as Dr. Ha-Joon Chang’s work has shown, the economic history of developed nations is also a history of government-led or government-driven initiatives – Nokia in Finland, the Internet and GPS in the US, cars in Japan, electronics in Korea – to boost the economic diversity of their nations.

22. We must focus on sectors and industries which are high value-added, externally oriented (to force companies to be globally competitive), in line with future megatrends such as demographics, climate change and Industry 4.0, and have important links with the rest of the Malaysian economy. We will not simply support a new industry just because it is new. While we do need to pursue economic diversification, not all diversification

makes sense. We will support a new industry only if it benefits Malaysia's economic future. Only then can we really move up the value chain and move towards a higher-income, higher-wage economy.

Societal Well-Being – Development and Growth encompass *Rakyat's* wellbeing

23. While it is important that we continue to drive Malaysia's economic growth, it must not be at all costs. At the end of the day, we must ask ourselves this question: how do we create as many opportunities – in as fair a way as possible – for every single Malaysian to better their lives?

24. Fairness does not necessarily imply absolute equality. Yet, that does not mean that anyone should not have the opportunities to pursue a fulfilling life for themselves and their families. The role of the government is to ensure that no one is penalised by their life circumstances. We are wholly committed to ensure that whatever opportunities and access greater economic growth and fiscal sustainability brings to Malaysia, those opportunities and access must be available to all Malaysians.

25. We are therefore committed to provide basic protection for all Malaysians via shared and affordable public services. These social welfare policies must be designed to empower Malaysians, especially the underprivileged B40 group, such that these policies become tools which will allow individuals to thrive and be rewarded.

26. We have already abolished the multi-stage GST tax and replaced it with a lighter single-stage SST tax. The GST is a particularly regressive taxation regime that burdens the lower income group excessively. We had to abolish it to avoid making the rich richer while leaving the poor living in extreme destitution. Indeed with the GST abolition, the government is lightening the people's tax burden by RM23 billion each year.

Conclusion

Ladies and gentlemen,

27. To close, I would like to just reiterate that while we are certainly facing some very challenging global external headwinds, Malaysia's economic fundamentals are robust and we can steer our way through these challenges. Of course, it is not all perfect – for one, our exports need to remain competitive to maintain our current account balance. We must also recalibrate public finances towards a path of long-term fiscal sustainability. Our current efforts at fiscal consolidation are focused on prudence – cutting out the excesses of the past while building a strong foundation for government finances to pursue smart and responsible fiscal policy moving forward.

28. We are not going to just pursue fiscal consolidation at all costs and we are definitely not in any austerity mode. Fiscal sustainability is but one of our aims to drive Malaysia's long-term development. We must also ensure that the government is supportive to a private sector-led economic growth, in what I like to think of as an "Entrepreneurial State."

29. That growth must be for all Malaysians. Ultimately, the welfare of the *rakyat* of Malaysia is the key objective of this government. Improving societal well-being is non-negotiable.

Thank you.