REFSA Notes

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REFSA'S PRE-BUDGET 2026 STATEMENT - THE DENOMINATOR MATTERS MORE

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REFSA'S PRE-BUDGET 2026 STATEMENT - THE DENOMINATOR MATTERS MORE

Malaysia's fiscal managers deserve some credit. Over the years, Putrajaya's budgets have largely adhered to economic orthodoxy—loosening the purse strings when growth falters and tightening them when the economy hums. Countercyclicality, in other words, is not the problem. The trouble lies deeper: not in what the money is spent on, but rather what is being deprioritised.

WHEN AUSTERITY TARGETS THE FUTURE

During the heady growth years from 2011 to 2019, development expenditure—the part of the budget meant to build the future—was repeatedly sacrificed at the altar of fiscal prudence. Its share of GDP and of total spending shrank markedly, as charts from government data show. Capital investment in the essentials of long-term growth—education, health, trade and industry, energy, and public utilities—all took a hit.

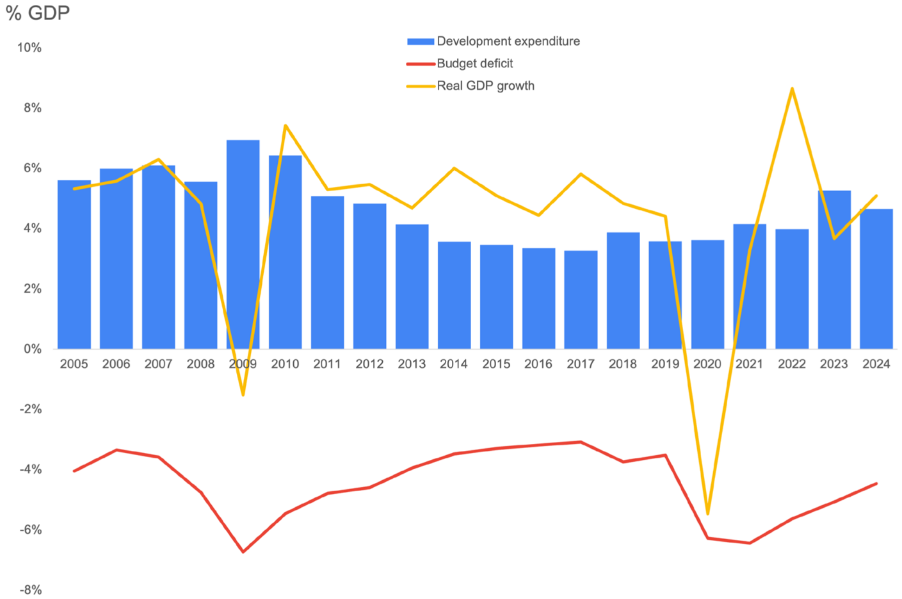

Chart 1: While budget expenses are textbook countercyclical, but development bears the brunt
Source: data.gov.my, belanjawan.mof.gov.my, REFSA analysis

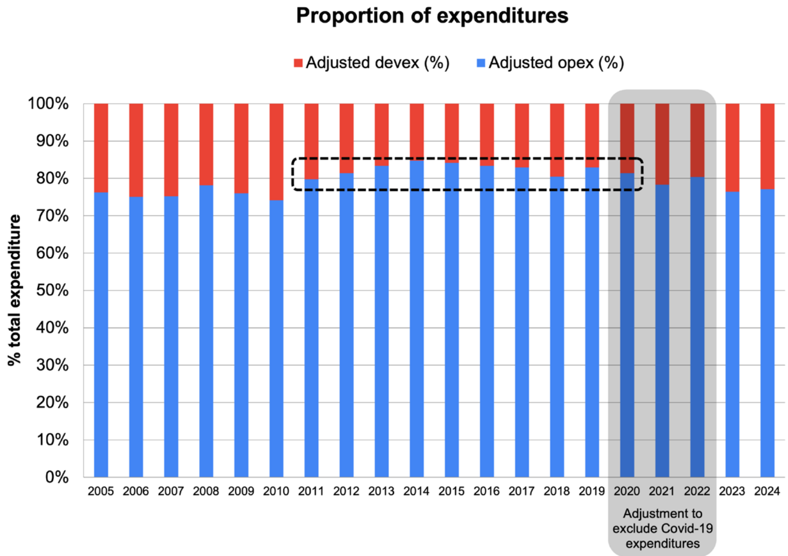

Chart 2: Development expenditure started declining in 2011 and dipped below 20% of total spending from 2012 until 2020
Source: data.gov.my, belanjawan.mof.gov.my, REFSA analysis

THE COST OF CUTTING TOMORROW'S GROWTH

Delving deeper, the contraction in development spending hit Malaysia where it hurts most: education, health, industry, and energy. These are not mere line items—they are the very levers of productivity and innovation.

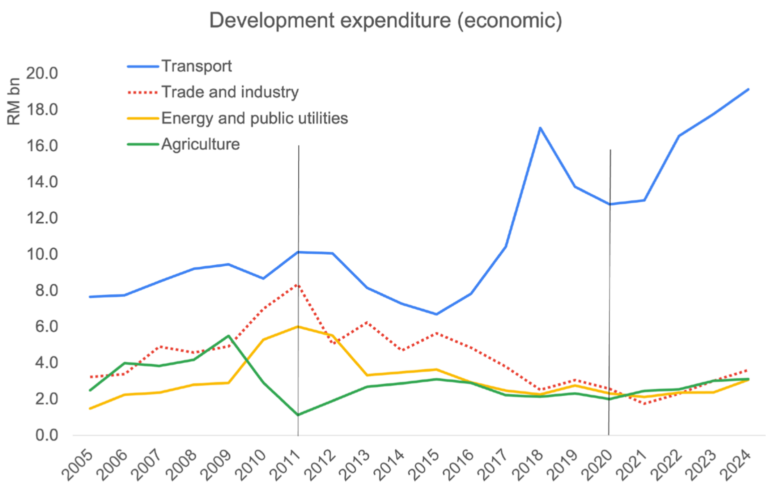

Chart 3a: Absolute Decline in Spending for Trade & Industry and Energy & Public Utilities
Source: data.gov.my, belanjawan.mof.gov.my, REFSA analysis

Development expenditure (social)

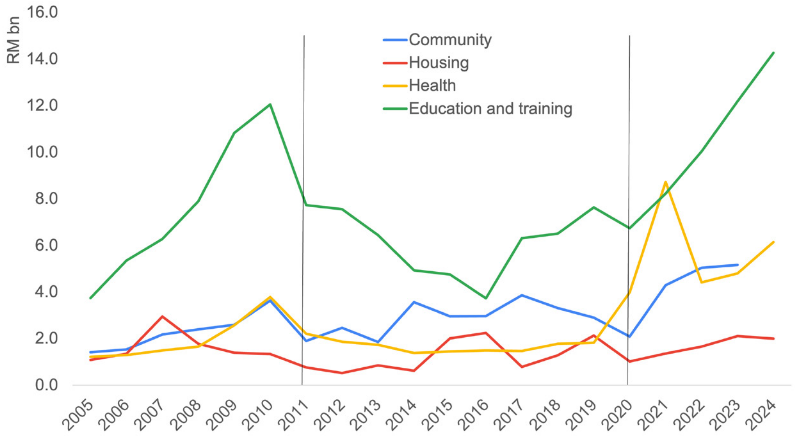

Chart 3b: Absolute declines in spending for education and training and health
Source: data.gov.my, belanjawan.mof.gov.my, REFSA analysis

The cuts have left wounds that will take time to heal. Malaysia's research-and-development (R&D) spending, at a meagre 0.95% of GDP in 2020, lags behind Thailand's 1.2% and Singapore's 2.2%. Even worse, the private sector's share of R&D funding plunged from 64.5% in 2010 to 34.2% in 2020, according to the National Survey of Research and Development conducted by Malaysia's Science, Technology and Innovation Center (MASTIC). In short, the country's capacity to innovate has withered just as its regional rivals double down on technology-led growth.

To its credit, the government has recently reversed part of the slide. Post-pandemic budgets have seen notable increases in allocations for transport, education, and health. But the gains remain uneven. Investment in trade and industry—the backbone of Malaysia's industrial upgrading—remains anaemic. A consequence sees the share of domestic investments in Malaysia's electrical and electronics (E&E) sector shrivelling to a mere 4.5% of total E&E investments in 2024 (17.9% in 2012). So while Malaysia is known globally as an E&E powerhouse, garnering a significant share of the nation's exports, it masks the little value add that the sector actually brings, contributing a paltry 7% to its GDP.

IT'S TIME TO WALK THE PLAN

Malaysia unveiled lofty yet appropriate targets under its MADANI economic framework, targeting quality, sustainable growth with balanced distributions, premised on increased economic complexity. This has been followed through with flagship programmes such as the **New Industrial Master Plan (NIMP), National Energy Transition Roadmap (NETR) and National Semiconductor Strategy (NSS)**. These however require fiscal bullets for sustained green, industrial and R&D spending, and coherent execution.

Subsidy rationalisation, though politically fraught, offers an opportunity to shift resources towards these strategic sectors. Every ringgit saved from untargeted subsidies could fund Malaysia's transition to higher-value production and better-paid jobs. Yet the balancing act is delicate. The government faces the twin pressures of **rising debt-service costs** and a **public-debt ratio nearing 65% of GDP**.

FISCAL RESPONSIBILITY IS A VALUE, NOT A GROWTH CONSTRAINT

Preoccupation with debt reduction alone, however, misses the forest for the trees. Fiscal sustainability depends as much on growing the **denominator**—GDP—as on trimming the numerator. With limited fiscal room, Malaysia must invest smarter, not just spend less. The current administration is rightly insisting that each ringgit of public money should come with clear cost-benefit assessments, measurable outcomes, and transparent reporting—principles enshrined in the new **Fiscal Responsibility Act (FRA)**. While the FRA is certainly a powerful lever for reform, it should not become a barrier to growth. Overzealous adherence to dogmatic targets may result in missed opportunities and sacrifices the agileness that is required to navigate the new economic paradigm.

Raising long-term debt to finance mission-driven strategic investments—in R&D, technology, green infrastructure, and industrial upgrading—should not be taboo.

Public institutional knowhow in planning and implementing industrial policy, especially in technology related sectors, is also paramount. When well-executed, such investments expand productive capacity, increase economic complexity and ultimately ease debt burdens by lifting growth and tax revenues.

After years of underinvestment, Malaysia risks stagnating in a middle-income purgatory: tepid growth, modest wages, and an eroding technological edge. Reversing this trend requires restoring faith in the state's role as strategic investor and catalyst for innovation.

In short, fiscal discipline should not mean fiscal timidity. Budget 2026 offers the chance to build an economy that grows faster, pays better, and owes less—not by cutting ambition, but by financing it wisely.

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ABOUT REFSA

Research for Social Advancement (REFSA) is a progressive, non-profit think tank that promotes social advancement in Malaysia. Since its inception, REFSA has been at the forefront of policy discussions and debates in the important political and socio-economic issues of the nation. Today, our aspiration hasn't changed - we want to power the movement for a just, inclusive and multi-ethnic society.

REFSA NOTES

REFSA Notes is a collection of thoughts, reflections, and ideas from our research team. They aim to provide the groundwork for further discussions, commentary, research agendas, and policy recommendations.

Valuable comments and editorial assistance were provided by Tan E Hun.

Tan E Hun is Executive Director of REFSA.

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