

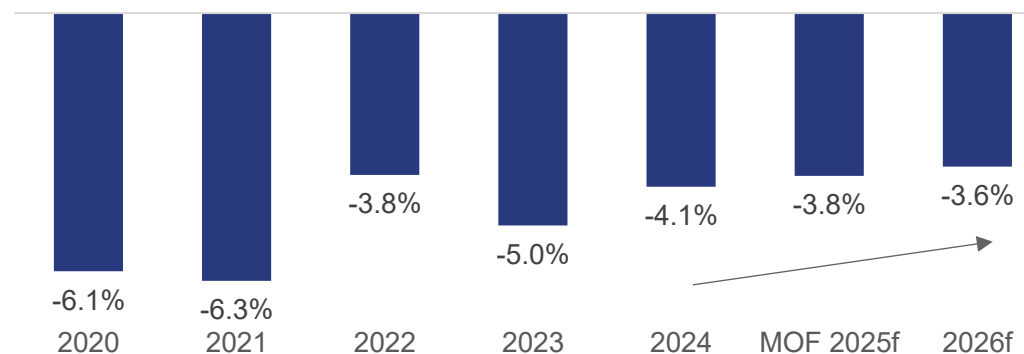
Pre-Budget 2026: Fiscal Consolidation Intact, Credibility on the Line

Malaysia Fiscal Balance: First Half Snapshot

	1H2024	1H2025
Revenue	139,081	147,624
Operating expenditure	157,104	155,336
Current balance	-18,023	-7,712
Gross development expenditure	33,935	33,288
Less: loan recoveries	393	540
Net development expenditure	33,542	32,748
Overall balance	-51,565	-40,460
Overall balance % of GDP	-5.5%	-4.2%

Source: MOF, CEIC, BMMB Economics

Fiscal Deficit % of GDP



Source: MOF, CEIC, BMMB Economics

Budget 2026 will be tabled on 10 October, the **first under RMK13** and a critical marker of the Government's fiscal trajectory. Unlike recent years where consolidation was largely aspirational, the numbers in **1H2025 show tangible progress**. The federal deficit narrowed meaningfully, with revenues boosted by improved tax collection and contained subsidy spending. Importantly, the deficit path expected to remain consistent with Putrajaya's target of **-3.8% of GDP in 2025**, stepping down from 4.1% in 2024 and 5.0% in 2023.

Macro conditions have also provided breathing space. GDP expanded **4.4% in 1H25**, while headline inflation cooled to multi-year lows near **1%** and unemployment steadied at **3%**. This mix of benign prices and steady demand has underpinned both fiscal collections and investor sentiment, reflected in a firmer ringgit, and stable domestic bond yields, with equity markets largely steady.

The backdrop sets a **constructive stage for Budget 2026**. The Government enters with credibility—fiscal anchors from the Fiscal Responsibility Act remain intact, new debt issuance is trending lower, and investor confidence has improved. But the margin for error is slim. Execution risks remain high, any revenue shortfall or commodity price shock could complicate the consolidation path.

Likely Budget Highlights – Relief, Targeting, and New Frontiers

Budget 2026 is expected to be **people-centric but fiscally mindful**. The Pre-Budget Statement signals continued focus on **cost-of-living support**, but with sharper targeting to avoid undermining consolidation efforts.

- **Targeted relief:** Existing cash aid programmes such as **STR and SARA** will be topped up, but delivery will lean more on digital rails (e-wallets, MyKad authentication). The emphasis is not just more transfers, but cleaner targeting to reduce leakages.
- **M40 focus:** Unlike previous years where the bulk of subsidies and aid were B40-oriented, this round is likely to extend relief measures to **middle-income households** who face persistent cost pressures (childcare, healthcare, housing). This shift has been flagged by policymakers and is consistent with market expectations that the M40 will feature more prominently.
- **Third sector.** For the first time under RMK13, the Government is explicitly recognising the role of the **third sector** (co-ops, NGOs, social enterprises) in delivering social programmes. Budget 2026 may allocate seed funding or matching grants, **or even pilot issuance of social/impact sukuk** to mobilise private capital alongside fiscal resources. The move opens space for financial institutions to participate in blended-finance frameworks, scaling up cooperatives and social enterprise to play a role in areas directly tied to cost-of-living concerns.
- **Growth levers:** Budget 2026 will align closely with the **MADANI agenda and RMK13 priorities**. We expect continued funding of transformation initiatives — the NIMP30, the National Energy Transition Roadmap, KL20 high-value digital economy push, and Visit Malaysia 2026. Infrastructure spending is likely to feature more, particularly in **Sabah and Sarawak**, where both states are positioned as sustainable energy and growth hubs, and may receive additional funding for connectivity, rural infrastructure, and green investments.
- **Governance reforms.** The Pre-budget statement re-emphasises the reform pipeline—procurement act, SOE governance, tax enforcement (tax identification number, e-invoicing), and the Global Minimum Tax. While **legislative bandwidth is constrained ahead of elections**, Budget 2026 will likely highlight these to reassure markets on structural reform intent.

Budget 2026: Allocation Expected at RM430 Billion, Balancing Relief, Growth, and Fiscal Discipline

Revenue, Expenditure and Deficit Trajectory (2023–2026f)

	2023	2024	MOF 2025f	2026f
Revenue	314,959	324,618	339,706	352,000
% change	7.0%	3.1%	4.6%	3.6%
Operating expenditure	311,267	321,509	335,000	345,000
% change	6.3%	3.3%	4.2%	3.0%
Current balance	3,693	3,109	4,706	7,000
Gross development expenditure	95,084	82,275	84,679	85,000
% change	35.5%	-13.5%	2.9%	0.4%
Less: loan recoveries	1.0	1.7	1.3	1.3
Net development expenditure	95,082.7	82,273.0	84,677.7	84,998.7
% change	35.5%	-13.5%	2.9%	0.4%
Overall balance	(91,390.1)	(79,164.2)	(79,972.07)	(77,998.70)
Overall balance % of GDP	-5.0%	-4.1%	-3.8%	-3.6%

Source: MOF, CEIC, BMMB Economics

The **Budget 2026** allocation is expected to be around **RM430 billion**, reflecting the government's effort to consolidate while safeguarding growth and household support.

- **Expenditure mix.** Spending will balance between **targeted household relief** and **growth-oriented development**. Social protection remains a priority but will be increasingly digitalised and better targeted, while development expenditure is likely to focus on infrastructure, green transition, and digital economy initiatives consistent with RMK13.
- **Revenue drivers.** Fiscal consolidation will hinge on improved collection and compliance. Key measures include the full roll-out of **e-invoicing**, mandatory **Tax Identification Numbers (TINs)**, and potential adoption of the **Global Minimum Tax** in 2026. Together, these should strengthen the revenue base even as oil-related receipts moderate.
- **Fiscal balance.** With restrained expenditure growth and stronger tax administration, the government remains on track to achieve the **-3.8% of GDP deficit in 2025**, narrowing further to **-3.6% in 2026**. That said, the outlook remains sensitive to commodity prices and execution risks in tax reforms.

Positive Outlook Anchored by Domestic Demand, But Reform Pace Set to Moderate

While the government continues to signal commitment to **structural reforms** — from tax broadening to subsidy rationalisation — the pace is likely to **slow ahead of the general election cycle**. Instead, emphasis may be placed on **administrative reforms** such as e-invoicing, tax compliance, and digitalisation of government services, which are politically safer yet still supportive of fiscal credibility.

Growth: Positive but Measured Outlook

We remain **constructive on Malaysia's outlook**. Growth is projected to **moderate to 4.3% in 2025 before picking up to 4.5% in 2026**, supported by resilient domestic demand, policy-driven investments, and stronger development spending. Inflation is expected to stay **benign (1.6% in 2025; 2.0% in 2026)**, allowing monetary policy to remain accommodative at **2.75%**.

Overall, **Budget 2026 should reinforce stability and inclusivity while laying groundwork for long-term reforms**. The trajectory remains positive, but execution of fiscal and structural measures will be key to sustaining market confidence.

Revenue, Expenditure and Deficit Trajectory (2023–2026f)

Macroeconomic variable	2024 (A)	2025 (F)	2026 (F)
GDP growth	5.1%	4.3%	4.5%
Inflation rate	1.8%	1.6%	2.0%
Overnight Policy Rate (OPR)	3.00%	2.75%	2.75%
USDMYR end period	RM4.72	RM4.15 to RM4.20	RM4.10 – RM4.15

Source: MOF, CEIC, BMMB Economics