



Aligning Budgetary Policy with National Planning: The 2026 Federal Budget and the 13th Malaysia Plan

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By Muhammed Abdul Khalid

SYNOPSIS

The Malaysia 2026 Budget – the first operation spending for the 13th Malaysia Plan (13MP) – undermines the 13MP objectives by continuing regressive fuel subsidies, while imposing austerity on critical sectors like healthcare. This fiscal misallocation, and unambitious inclusive growth targets, create a fundamental policy disconnect. Without bold reforms and greater social equity, the 13MP risks losing the public trust that is essential for its long-term success.

COMMENTARY

This brief argues that the 13MP's success is contingent upon bold fiscal reforms, particularly subsidy rationalisation. Yet, the plan's is fundamentally contradicted by its unambitious socio-economic goals for poverty reduction, inequality, and wage growth. The 2026 Budget confirms this gap, prioritising regressive fiscal reforms and inadequate progressive spending. This misalignment risks eroding public trust and undermining the much-needed political support for reforms.

Contradictions and Misalignments

The plan's vision is constrained by existing fiscal conditions – a persistent fiscal deficit, high debt and liabilities estimated at 86 per cent of GDP, and a minimal increase in development expenditure allocation. The total development allocation for the 13MP is RM430 billion – a mere RM15 billion increase compared to the 12MP (2021-2025) – a figure insufficient to address pressing underinvestment in critical sectors such as healthcare, education, and affordable housing. This translates to an average of only RM3 billion in additional development spending per year, or about 0.9 per cent yearly growth, which is way below the potential annual economic output of 4.5 per cent to 5.5 per cent.

Notably, the healthcare sector's allocation remains frozen at RM40 billion during the period, unchanged from the previous plan, despite documented challenges of overcrowding and understaffing. This stagnation, evidenced by a mere RM7 million or 0.1 per cent increase in health development expenditure in the recent budget, occurs alongside a broader trend of fiscal compression. Between 2024 and 2026, development expenditure is projected to reduce by 4 per cent, even as revenue and operating expenditures are projected to grow by 6 per cent and 5 per cent, respectively. In 2025 alone, development expenditure is anticipated to shrink by nearly 5 per cent, or approximately RM4 billion, compared to the previous year.

The logic seems straightforward. With fiscal deficit reduction being the primary macroeconomic target, and with development spending being almost entirely debt-financed, it becomes the most adjustable target for cuts. This is especially tempting when approximately three-quarters of government revenue is pre-committed to four major operating expenses: emoluments, pensions, debt service, and subsidies.

The government is grappling with a high and increasingly burdensome debt load. Debt service payments are projected to reach nearly RM60 billion next year, consuming nearly 17 per cent of federal government revenue – a significant increase from 9 per cent in 2009. The amount is equivalent to 72 per cent of the entire development expenditure budget. This escalating fixed cost is unsustainable; every ringgit spent on debt servicing is a ringgit not invested in schools, hospitals, or public transportation, thereby undermining long-term economic potential.

The 13MP's fiscal viability is contingent upon rationalising one of the largest and most inefficient components of operating expenditure: subsidies. The blanket subsidy model is both fiscally unsustainable and socially regressive.

Despite minor adjustments, such as excluding foreigners, the overall structure largely remains. Fuel subsidies are expected to cost the government RM11 billion in 2026 – 1.6 times higher than the entire allocated development spending on the healthcare sector! This spending is highly regressive; for every RM100 spent, the top 20 per cent of households receive an estimated RM42, while the bottom 20 per cent receive only RM4. This misallocation effectively uses scarce public resources to subsidise the wealthiest households, thereby exacerbating the very inequalities the 13MP aims to address.

Inconsistent Commitment to Reform

The government's commitment to reform appears inconsistent, creating policy uncertainty that undermines its credibility. After announcing intentions to eliminate fuel subsidies for high-income groups in the 2025 Budget, the government reversed course months later. It doubled down on the subsidy by making subsidised fuel six *sen* cheaper, effective from early October 2025. The recently announced 2026 Budget is silent on concrete steps for rationalising fuel subsidies.

This policy U-turn is compounded by other regressive fiscal practices. The continuation of a universal cash transfer of RM100 to all adult Malaysians –

regardless of income – a policy extended into 2026 at a cost of RM2.2 billion despite the negative fiscal balance, represents another poorly targeted expenditure. These funds could have been more effectively directed towards low-income families or invested in child nutrition and education programmes.

Similarly, the government's continued sugar subsidy directly contradicts its public health objectives amid a growing non-communicable disease crisis, clearly a misalignment between fiscal policy and public health goals.

Insufficiently Ambitious

Beyond inconsistent fiscal policies, the 13MP's own socio-economic targets lack the ambition necessary to foster inclusive growth. The plan aims to reduce the incidence of absolute poverty from 5.8 per cent to 4.7 per cent – a marginal improvement of just 1.1 percentage points over five years, which is also significantly lower than that of the previous plan.

Significantly, income inequality is not being treated with the seriousness it deserves, even though it remains one of Malaysia's most pressing challenges, made worse by the fact that lower-income groups continue to shoulder multiple taxes, including higher and expanded consumption taxes, which increased by 33 per cent between 2024 and 2026.

The target for the Gini coefficient, a measure of income inequality, is a marginal reduction from 0.388 to 0.386 over five years. This 1 per cent reduction over five years stands in stark contrast to the OECD average of 0.315. It is a mere symbolic improvement and far from achieving a fairer society, aligning Malaysia more closely with highly unequal economies, such as the United States, rather than with more equitable societies.

Concurrently, real wage growth is projected to lag economic expansion. Real wage growth is projected to grow by a modest 1-2 per cent annually during the 13MP period – lower than the 12MP's target – and below the economy's growth rate. In other words, workers are getting compensated less than the economic output.

Conclusion

The 13MP correctly identifies Malaysia's unsustainable fiscal trajectory. However, presenting subsidy reform as a purely fiscal exercise, without a parallel agenda to improve living standards and purchasing power, is a high-risk strategy. Securing public buy-in for painful reforms will be difficult without more aggressive and inclusive growth targets. The 2026 Budget, unfortunately, missed a key opportunity to set a credible tone.

For the 13MP to succeed, the government must adopt a three-pronged approach. First, it must accelerate the transition to targeted subsidies, implementing them gradually while concurrently expanding unconditional cash assistance and social protection programmes for lower-income groups. Second, the government must revisit the 13MP's socio-economic targets to establish more ambitious goals for

reducing poverty and inequality as well as promoting wage growth. Finally, it is critical to ensure the reinvestment of savings from reformed subsidies into development spending, mainly in healthcare, education, and affordable housing, to rebuild public trust.

The success of the 13MP ultimately hinges on the government's ability to align its fiscal consolidation agenda with meaningful economic inclusivity. Without this balanced approach, Malaysia risks achieving neither fiscal sustainability nor inclusive growth, rendering the aim of high-income nation status pointless. It is worth remembering that an unequal society is bad for growth and social and political stability, as history has repeatedly demonstrated. It would be far better if these lessons could be remembered, rather than re-learned.

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