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Global Economics & Market Strategy

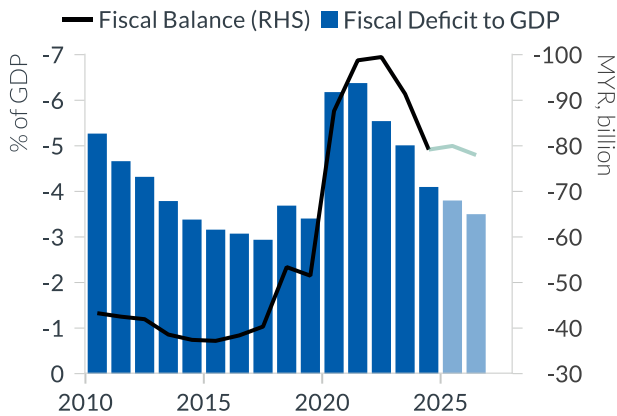
Budget 2026 Preview: Fiscal Sustainability and Inclusive Development

- ◆ In our view, Budget 2026 will focus on five key prongs: (1) fiscal sustainability, (2) economic stimulus and infrastructure development, (3) social welfare and inclusivity, (4) strengthening the business and investment climate, and (5) advancing Environmental, Social, and Governance (ESG) priorities.
- ◆ We forecast fiscal deficit target at 3.5% of GDP for 2026, potentially followed by 3.2% of GDP set for the following year. We expect MYR86 billion–MYR89 billion to be allocated for development expenditure. The central priority will be to strengthen regional mobility and promote more balanced development across states.
- ◆ Budget 2026 is poised to be a pivotal instrument in steering Malaysia towards sustained and inclusive growth amid a complex global environment. Anchored firmly within the framework of the 13th Malaysia Plan (13MP) and the MADANI Economy, it will serve to balance immediate fiscal prudence with long-term strategic investments.

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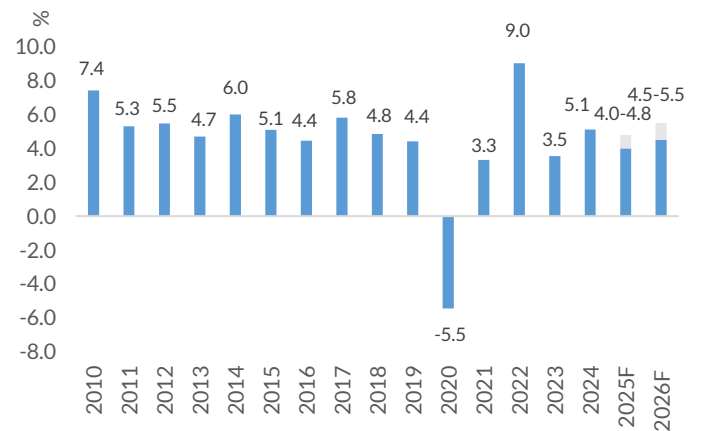
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Figure 1: The fiscal deficit target is to be set at 3.5% of GDP



Source: Macrobond, RHB Economics & Market Strategy.

Figure 2: We expect the GDP projected range to be at 4.5%-5.5%



Source: CEIC, RHB Economics & Market Strategy.

A Resilient Malaysia, Forged by A Strong Budget

In our view, Budget 2026 will focus on five key prongs: (1) fiscal sustainability, (2) economic stimulus and infrastructure development, (3) social welfare and inclusivity, (4) strengthening the business and investment climate, and (5) advancing Environmental, Social, and Governance (ESG) priorities.

We forecast Malaysia's GDP at 4.2% in 2025. Malaysia's economy is expected to maintain a firm footing through the second half of 2025, building on solid momentum established in the first half of the year. Real GDP growth registered at 4.4% in 1H25, reflecting robust consumer spending, healthy labour market dynamics, and continued investment activity. Despite external pressures, particularly in the form of global trade tensions and sector-specific tariffs, the domestic economy remains resilient. Growth into the next two years will be underpinned by steady domestic demand, wage growth, and the continuation of multi-year public and private sector projects. The broadening of the Sales and Services Tax (SST) is expected to have minimal impact on overall consumption and inflation, given its targeted scope on discretionary items and selected services.

Looking ahead to 2026, economic activity is projected to strengthen further, with GDP growth forecasted at 4.7%. This outlook is supported by improving realisation of approved investments, higher capital deployment in strategic sectors, and the ongoing implementation of key national initiatives under the 13th Malaysia Plan (13MP), including the MADANI Economy Framework, the National Energy Transition Roadmap, and the New Industrial Master Plan 2030. Private consumption is set to remain a growth anchor, bolstered by sustained improvements in household incomes, including civil service wage adjustments and a tighter labour market. While global risks persist—most notably sectoral tariffs from the US on semiconductors and related exports—Malaysia's diversified domestic economy, particularly its services sector, is expected to cushion some of these external shocks. Nevertheless, export-oriented sectors such as electrical and electronics (E&E), crude materials, and machinery remain vulnerable. The proposed 100% US tariffs on foreign-made semiconductors introduce uncertainty. However, Malaysia's exposure is somewhat mitigated by the fact that a significant share of its chip exports to the US originates from American-owned firms operating within the country.

Inflationary pressures are expected to remain contained over the near term. Headline inflation is forecast at 1.6% in 2025, rising moderately to 2.3% in 2026. The catalysts for higher inflation in 2026 may stem from upside risks pertaining to (1) potential SST broadening for various industries as discussed below, (2) further tightening of RON95 subsidy retargeting and (3) upsides from improved demand conditions. However, these measures are expected to be implemented gradually and in a targeted manner, helping to dampen broader inflationary spillovers. Inflation averaged just 1.4% in the first half of 2025 but is projected to rise to 1.8% in the second half of 2025. Monetary policy is expected to remain supportive, with the Overnight Policy Rate (OPR) projected to remain unchanged at 2.75% for the remainder of 2025. Policy direction in 2026 is expected to remain data-dependent, influenced by the path of domestic demand and the evolution of external risks, particularly those stemming from the global trade environment.

Budget 2026, scheduled for release on 10 October 2025, will play a crucial enabling role in reinforcing Malaysia's economic resilience and positioning the country for medium-term growth. As the first budget under the 13MP and the fourth in the MADANI series, it will serve as a fiscal and policy anchor to navigate near-term challenges while laying the groundwork for sustainable, inclusive development. The budget is expected to focus on five key pillars: fiscal sustainability, economic stimulus and infrastructure development, social welfare and inclusivity, improving the business and investment climate, and advancing ESG priorities. It is likely to include measures to tackle cost-of-living pressures, strengthen support for micro, small and medium enterprises (MSMEs), enhance competitiveness through investment incentives, and accelerate the green transition. In essence, Budget 2026 is poised to act as both a stabiliser and a catalyst—providing targeted relief where needed, while driving strategic transformation to elevate Malaysia's economic potential over the long term.

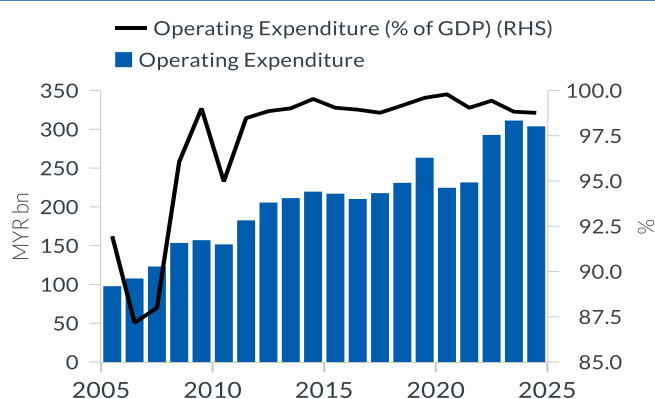
Specifically, the fiscal deficit target is likely to be set at 3.5% of GDP for 2026, followed by 3.2% of GDP for the subsequent year, to meet the midterm deficit targets. Under the Mid-Term Fiscal Framework (MTFF), the fiscal deficit is expected to continue consolidating, with the overall balance averaging 3.5% of GDP (2025-2027). Additionally, this forms part of the effort to reduce the fiscal deficit to below 3% of GDP by 2030, in line with the 13MP target. In addition, we expect MYR86 billion–MYR89 billion to be allocated for development expenditure in Budget 2026, in line with the 13th Malaysia Plan's (13MP) total allocation of MYR430 billion for 2026–2030. The central priority will be to strengthen regional mobility and promote more balanced development across states.

Prong 1: Fiscal Sustainability

The fiscal deficit target for 2026 is likely to be set at 3.5% of GDP, followed by a target of 3.2% of GDP for the subsequent year, in line with the midterm deficit targets. Under the Mid-Term Fiscal Framework (MTFF), the fiscal deficit is expected to consolidate further, with the overall balance averaging at 3.5% of GDP (2025-2027). Additionally, this forms part of the effort to reduce the fiscal deficit to below 3% of GDP by 2030, in line with the 13MP target.

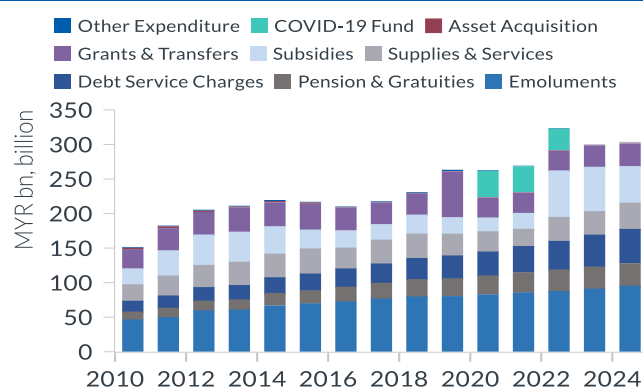
For Budget 2026, we expect no major new tax measures or subsidy rationalisation initiatives, as key reforms—such as the expansion of SST and the rationalisation of diesel and RON95 subsidies—have already been implemented or are on track for implementation. Instead, the emphasis will likely be on fine-tuning and refining existing policies to ensure smoother execution and maximise fiscal impact. However, in this prong, we expect to see further clarity on five key revenue initiatives: (1) potential expansion of the Sales & Service Tax (SST) scope, (2) increases or adjustments on tax of unhealthy consumables, (3) phased implementation of the carbon tax, (4) revised estimates of savings from the RON95 rationalisation, and (5) updates of e-Invoicing in Malaysia.

Figure 3: Operating expenditure (OE) trending above 90% of central government revenue



Source: Macrobond, RHB Economics & Market Strategy

Figure 4: Emoluments, subsidies, as well as grants & transfers are some of the major contributors to OE



Source: Macrobond, RHB Economics & Market Strategy

First, we do not rule out the possibility of further revisions to the Sales and Service Tax (SST), particularly the service tax rate for selected sectors. In this regard, the rate for food and beverage services, i.e. restaurants, as well as telecommunications services, may be raised from 6% to 8%. Such an adjustment would form part of the government’s broader strategy to strengthen revenue collection while continuing to exempt essential goods and services. Note that the recent SST expansion is projected to generate approximately MYR 5 billion in additional revenue over the six months starting in July. On an annualised basis, the target is to raise around MYR 10 billion. This additional revenue influx is expected to strengthen government finances by providing greater fiscal space to manage public expenditure and reduce the budget deficit. Thus, based on past annual revenue data from F&B services (2023: MYR228.7 billion)¹ and telecommunication services (2024: USD5.1 billion or MYR21.4 billion)². A potential broadening of the SST via F&B services and telecommunications to an 8% rate will translate to an additional MYR5.0 billion of government revenue on an annual basis.

Second, beyond the expansion of the SST, we expect increases or adjustments in taxes on unhealthy goods, such as sugary drinks, tobacco, and alcohol, as part of the government’s efforts to both discourage unhealthy consumption and raise revenue. The last change to the excise duty on alcohol took effect on 1 March 2016. Separately, a tax on sugar-sweetened beverages (SSBs) was proposed in 2014 and implemented in 2019, with an excise duty of MYR0.40 per litre for ready-to-drink drinks with high sugar content. Under the 13MP, a proposal has been made to expand pro-health taxation to include both tobacco and alcohol. A sugar tax was implemented in 2025, providing a precedent for a potential increase in tobacco tax. According to estimates, increasing the excise tax on cigarettes to MYR0.80 per stick, from the current MYR0.40, is expected to generate around MYR770 million in annual revenue.

¹ New Straits Times, [Malaysia's F&B sector: A key economic driver with rapid growth](#), April 2025

² RCR Wireless News, [5G is expected to represent 84% of total mobile subscriptions in Malaysia by 2029](#), April 2025

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Third, a carbon tax is also likely to be on the radar for Budget 2026. Malaysia has committed to introducing a carbon tax, effective in 2026, initially targeting high-emission and trade-exposed sectors, such as the iron, steel, and energy industries.³ The plan, which is part of Malaysia's broader climate strategy, also includes reducing carbon intensity by 45% by 2030 and achieving net-zero emissions by 2050. For Budget 2026, we expect further clarity on the carbon tax for the medium term, potentially with plans to introduce tax deductions for companies incurring expenses on Measurement, Reporting & Verification (MRV) activities and other carbon project-related work, applicable through to the end of 2026.

Fourth, we expect clarity on subsidy savings and potential new developments on Malaysia's RON95 rationalisation programme. Note that the government will introduce the BUDI95 targeted petrol subsidy on 30 September 2025, allowing eligible Malaysians aged 16 and above with a valid driving licence to purchase up to 300 litres of RON95 per month at RM1.99 per litre using their MyKad. The subsidy applies only to citizens; foreigners and foreign-registered vehicles will pay the market rate (currently MYR2.60 per litre). The monthly cap is intended for personal use, with ride-hailing drivers able to apply for additional allocations. **With current oil price estimates at USD 75 per barrel, the subsidy rationalisation is projected by officials to save MYR 2.5–4.0 billion annually.** These funds will be redirected to social support programmes, including Sumbangan Tunai Rahmah (STR), Sumbangan Asas Rahmah (SARA), education aid, and other cash assistance schemes. **In addition, commercial vehicles will continue to operate under the existing fleet card system.** Implementation will be phased, starting with the police and military (27 September) and STR recipients (28 September), before the nationwide rollout on 30 September.

Although the current RON95 subsidy retargeting is implemented through a usage cap applicable to all income groups, further refinements cannot be ruled out. At this junction, the subsidy is to be given to all Malaysians, regardless of income levels. However, we do not discount the possibility of future refinements to limit subsidy to certain income groups (see Figure 5). Several factors are under consideration, as noted by officials earlier on, including household income and size, number of vehicles, dependents, and regional differences in the cost of living. Households owning luxury cars or high-value assets may also be disqualified from receiving the subsidy. The projected savings—up to MYR 4 billion—are lower than earlier estimates of MYR 8 billion, which assumed rationalisation targeting foreigners and the ultra-wealthy. The reduced savings may also reflect lower oil retail prices, with the RON95 price having been adjusted from MYR 2.05 to MYR 1.99 per litre, resulting in additional subsidy disbursements.

Fifth and last, regarding the enhancement of tax administration and compliance, the full effects of the e-invoicing system are set to be extended to all taxpayers by the end of 2026 and will become evident next year. The implementation of e-Invoicing in Malaysia will extend through 2025 and 2026, covering a wider range of businesses based on their annual turnover. From 1 January 2025, taxpayers with an annual turnover between MYR25 million and MYR100 million will be required to adopt the system, followed by those with turnover between RM5 million and RM25 million starting 1 July 2025. In 2026, the rollout will continue with businesses earning between RM1 million and RM5 million from 1 January, before extending to the smallest entities with a turnover of up to RM1 million on 1 July 2026. This phased approach ensures a gradual and structured transition, moving from medium-sized enterprises in 2025 to smaller businesses by mid-2026.

³ S&P Global, [Malaysia sets 2026 carbon tax, reaffirms decarbonization goals in Budget 2025](#), Oct 2024

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Figure 5: Potential Criteria for Future RON95 Subsidy Rationalisation

Criterion	What is known / proposed	Notes / Status
Citizenship / Residency	Must be a Malaysian citizen (MyKad holder) to access subsidised RON95. Non-citizens will not be eligible.	Proposed verification via MyKad at petrol pumps.
Income / Disposable Income / Net Household Income	Use of income data (gross / net disposable income) to define eligibility. The top ~15% (T15) income group is likely excluded. At least 85% of Malaysians are expected to remain eligible under the subsidy.	Still being refined. "T15" definition not yet completely fixed.
Household size, dependents, number of cars, employment status	Factors under study include household size, number of vehicles owned, whether both spouses work, and the number of dependents/children in school/university.	These help assess of living burden. It has not yet been confirmed how heavily each will weigh.
Asset ownership/luxury items	Ownership of luxury vehicles, expensive property could disqualify or reduce eligibility.	Meant to exclude high-asset / higher net-worth individuals.
Cost of Living / Geographic Differentiation	Use the Cost of Living Index (IKSH) and Basic Expenditure for Decent Living (PAKW) by DOSM. Location of residence may matter.	Especially relevant, given that living costs differ widely across states.
Use of Central Database (PADU) and MyKad Verification	PADU (Central Database Hub) data will be utilised – it contains profiles that include income, education, socioeconomics, number of vehicles, assistance received, and other relevant details. MyKad scanning at pump points for verification.	This is core to the front-end implementation method.
Exclusions / Who Pays Full Price	Those ineligible (non-citizens, or purchases above 300 litres) will pay the unsubsidised market rate.	Subsidised price expected around RM1.99 / litre for eligible citizens (scheduled to start on 30 September 2025)

Source: Media Sources, RHB Economics & Market Strategy.

Prong 2: Economic Stimulus and Infrastructure Development

We expect MYR86 billion–MYR89 billion to be allocated for development expenditure in Budget 2026, in line with the 13th Malaysia Plan's (13MP) total allocation of RM430 billion for 2026–2030. As laid out in the 13MP, the overarching aim is to deliver a balanced, inclusive, and resilient growth trajectory, with a strong emphasis on infrastructure-led stimulus. Budget 2026 will likely prioritise regional mobility and connectivity, as the government seeks to close development gaps between states and promote more equitable growth across Peninsular Malaysia, Sabah, and Sarawak.

Underpinning this expansion is the broader **Ekonomi MADANI** framework, which supports a five-year national investment plan of MYR611 billion, including contributions from government-linked companies (GLCs and GLICs) and public-private partnerships (PPPs). Infrastructure development, in particular, will be a key driver of domestic investment and employment. The planned MYR86 billion average annual development expenditure under the 13MP outpaces the MYR83 billion average under the 12MP, reflecting the government's intent to scale up infrastructure as a catalyst for growth. Core projects are expected to include highway upgrades, new rural roads, and enhanced air and rail connectivity. We expect Budget 2026 also to reveal plans for approximately 2,800 km of rural roads slated for construction or upgrade by 2030, aiming to boost access in underserved areas and contribute to both rural productivity and national logistics efficiency.

Major initiatives expected to be supported by Budget 2026 include continued works on the **Pan Borneo Highway and Trans Borneo Highway**, upgrades to the **PLUS Expressway in Johor and Penang**, and the **Central Spine Road** spanning **Pahang and Kelantan**. Flood mitigation will remain a fiscal priority, particularly in high-risk areas such as Johor, Pahang, Kedah, Sabah, and Perak. At the same time, Malaysia's development strategy is increasingly digital. Budget 2026 is likely to allocate funding for broadband expansion, smart city infrastructure, and digital innovation, reflecting the country's ambition to build a tech-savvy and future-ready economy.

The **digital economy agenda** will also feature prominently, with plans to expand 5G coverage to 98% in populated and industrial areas, while fostering the development of AI capabilities and promoting local innovation through the "Made by Malaysia" initiative. These efforts are aimed not only at improving Malaysia's technological competitiveness but also at attracting high-value foreign and domestic investment. As Malaysia advances with its infrastructure and digital modernisation drive, it will also be building economic resilience amid global uncertainties—laying the groundwork for a more inclusive, future-oriented economy that can sustain long-term growth across all regions.

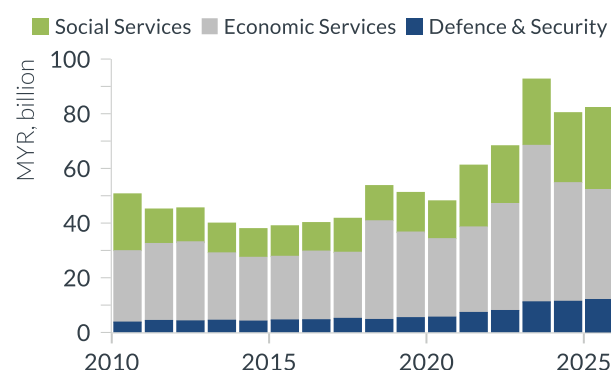
Figure 6: DE allocation to trend around MYR86 billion–MYR89 billion

	2021	2022	2023	2024	2025F	2026-2030*
Fiscal Deficit to GDP (%)	-6.4	-5.6	-5.0	-4.1	-3.8	< -3.0
Revenue (MYR bn)	233.8	294.4	315.0	324.6	339.7	1,820.6
Operating Expenditure (MYR bn)	231.5	292.7	311.3	321.5	335.0	1808.3
Gross Development Expenditure (MYR bn)	64.3	71.6	96.1	82.2	88.0	430.0

Source: *13MP Report, RHB Economics & Market Strategy.

Figure 7: Economic services segment receives the highest allocation over the years...

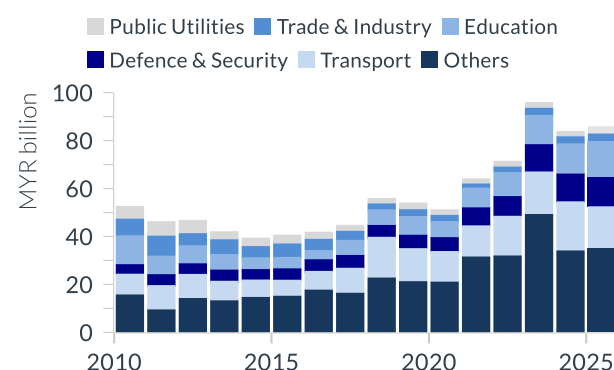
Malaysia Development Budget Allocation



Source: Macrobond, RHB Economics & Market Strategy

Figure 8: ...with main focus on the transport sub-sector

Development Budget Allocation for Major Sub-Sectors



Source: Macrobond, RHB Economics & Market Strategy

Prong 3: Social Welfare and Inclusivity

Reducing the costs of living and addressing social inequality would remain the top priorities in policy formulation. The budget is expected to feature measures aimed at improving social equity and supporting vulnerable populations. Potential focus areas include healthcare, education and social safety nets. Policies such as (1) affordable housing schemes, (2) subsidy programs for staple food items, (3) subsidies and fare discounts for low-income groups, as well as (4) cost-of-living assistance, are likely to be continued.

The government is expected to continue with subsidy rationalisation measures, particularly for RON95 petrol, to ensure assistance reaches those most in need while minimising fiscal leakages. This targeted approach reflects ongoing efforts to strike a balance between social protection and fiscal sustainability.

Housing affordability will remain a key priority under Budget 2026. Affordable housing schemes are expected to continue through state-linked initiatives and financing support targeted at B40 and M40 first-time homebuyers. The Rent-to-Own (RTO) scheme is also likely to be expanded under the 13MP to broaden homeownership opportunities, particularly for low-income households. In addition, tax relief measures are anticipated, including up to MYR7,000 for residential properties priced up to MYR500,000 and up to MYR5,000 for properties priced between MYR500,000 and MYR750,000. These reliefs may be claimed for three consecutive assessment years on sale and purchase agreements signed between 1 January 2025 and 31 December 2027. The Housing Credit Guarantee Scheme (SJKP) is also expected to continue, providing government-backed guarantees for first-time buyers who lack formal income proof or have irregular earnings, thereby enabling wider access to housing loans.

Targeted cash assistance and subsidies will remain central features of social support. Programmes such as Sumbangan Tunai Rahmah (STR) and Sumbangan Asas Rahmah (SARA), alongside continued subsidisation of public transport, are expected to receive higher allocations in 2026. Funding for STR and SARA, which supports lower-income households and senior citizens, could reach MYR16–17 billion, compared with MYR13 billion in Budget 2025 and the revised MYR15 billion following the Prime Minister’s special announcement. There is also the possibility of an additional SARA handout of MYR100 per eligible Malaysian, which would lift fiscal expenditure by a further MYR2.0 billion.

Civil servants are set to benefit from salary adjustments under the Public Service Remuneration System (SSPA), with the second phase scheduled for January 2026. Phase 1, which commenced in December 2024, saw implementers, managers, and professionals receive an 8% increase, while top management received a 4% increase. Under Phase 2, implementers, managers, and professionals will receive a 7% increase, and top management will receive a 3% increase. In August 2024, Putrajaya announced that civil servants in top management would receive a total 7% wage hike, while those classified as implementers, managers, and professionals would receive a total 15% increase under the new system.

Figure 9: Annual Allocation for Cash Assistance

Programme	Year	Total Allocation (MYR bil)
Bantuan Rakyat 1Malaysia (BR1M)	2012	1.8
	2013	3.0
	2014	4.6
	2015	5.9
	2016	5.9
Bantuan Sara Hidup (BSH)	2018	6.8
	2019	5.0
Bantuan Prihatin Nasional (BPN)	2020	10.0
Bantuan Prihatin Rakyat (BPR)	2021	8.1
Bantuan Keluarga Malaysia (BKM)	2022	8.2
Sumbangan Tunai Rahmah (STR) & Sumbangan Asas Rahmah (SARA)	2023	8.0
	2024	10.0
	2025	13.0
	2025 (revised)	15.0

Source: Media Sources, RHB Economics & Market Strategy.

Prong 4: Business and Investment Climate

Budget 2026 is expected to prioritise measures that enhance Malaysia's competitiveness, attract quality foreign direct investment (FDI), and strengthen support for micro, small, and medium enterprises (MSMEs). Policies aimed at fostering innovation, streamlining regulations, and improving the ease of doing business are likely to be introduced. The government is also expected to provide targeted incentives for priority sectors that drive growth and technological advancement, including renewable energy, digitalisation, electrical and electronics (E&E), advanced manufacturing, and agriculture.

In this regard, we highlight three key industries as critical focus areas for investors and financial stakeholders in the medium term: Rare Earth Elements (REE), E&E, and Islamic Finance Innovation. These sectors are not only highlighted in the 13MP but also present high-growth potential supported by policy frameworks, international collaboration, and substantial investment commitments.

Rare Earth: According to Malaysia's New Industrial Master Plan 2030, the country's valued rare earth elements resources are estimated at MYR747.2 billion (US\$175 billion), with the potential to attract MYR100 billion (US\$23 billion) worth of investments, creating 4,000 job opportunities.⁴ Budget 2026 may outline further plans to develop Malaysia's midstream and downstream processing capabilities to support rare earth upstream firms. Moreover, there has been engagement with foreign investors—countries like China have expressed interest in supplying technical and technology assistance, especially in downstream processing capabilities. Investors may then pay close attention to REE-rich states, such as Pahang, Terengganu, Kelantan and Perak, for rare earth mining and development.

Electronic & Electrical (E&E) and Digital Economy: As part of its "Ekonomi MADANI" vision, the government has set a target of elevating E&E exports from around MYR600 billion in 2024 to nearly MYR1 trillion by 2030, anchoring this ambition on major policy platforms such as the National Semiconductor Strategy (NSS) and the New Industrial Master Plan (NIMP) 2030. As such, we view Budget 2026 as an enabler to attract both foreign and domestic players into the E&E space. Concurrently, Malaysia aims to become a regional leader in AI. The National AI Action Plan 2030 supports AI literacy, innovation, and infrastructure, including the expansion of 5G nationwide and the implementation of a national cloud policy. With a goal of MYR1 trillion in E&E exports by 2030 and a strong push in semiconductors, the broader digital economy is expected to create 1.2 million jobs across manufacturing and digital services.

⁴ East Asia Forum, [Strategy and sustainability critical to Malaysia's rare earth ambitions](#), Aug 2025

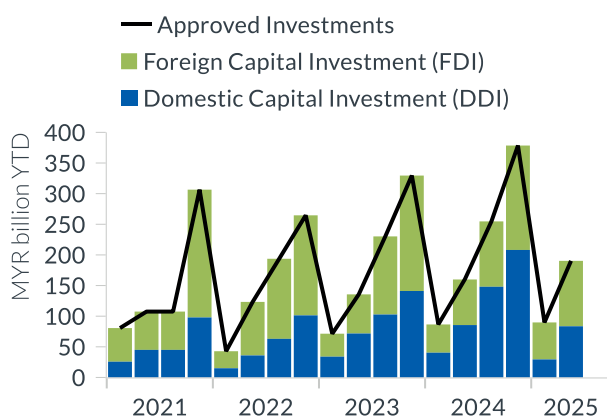
Islamic Finance: Budget 2026 will likely enhance Malaysia’s plan to solidify the nation's position as a global leader in this field. In Budget 2025, Malaysia earmarked MYR100 million for Islamic Finance to foster greater financial innovation. For the coming Budget, we will likely see more support for Malaysia to (1) expand cross-border ties, (2) grow markets for sukuk and other Shariah-compliant investments, and (3) promote ESG-linked Islamic finance, likely through the Malaysia International Islamic Financial Centre (MIFC).

Beyond the focus on the three key industries, other initiatives in Budget 2026 are expected to strengthen Malaysia’s investment appeal further. Potential updates or extensions to existing tax incentives, such as the Pioneer Status (PS) and Investment Tax Allowance (ITA), are likely to be introduced to encourage reinvestment and support industrial upgrading. These incentives will continue to be available to companies across various sectors, including manufacturing, agriculture, tourism, and other priority areas. Additionally, tailored tax packages may be developed specifically for the rare earth industry, aimed at attracting foreign partnerships and advancing Malaysia’s middle- and downstream capabilities. Complementing these fiscal measures, infrastructure enhancements and investment-friendly regulatory reforms are also expected to play a key role in boosting Malaysia’s competitiveness as a preferred investment destination.

Micro, small, and medium enterprises (MSMEs), which constitute 97% of all businesses, contribute 49% to employment and 39% to GDP, and will remain a central focus of government policy. Budget 2026 is likely to introduce a range of support measures aimed at enhancing the productivity and competitiveness of MSMEs. These could include grants, low-interest loans, capacity-building programs, and expanded digitalisation initiatives to help businesses adapt to the evolving economic landscape. The continuation of preferential tax rates for MSMEs, the expansion of micro-loan facilities, and increased support for startups and young entrepreneurs are also expected to be key features. Moreover, enhanced loan guarantees through the Business Financing Guarantee Scheme and soft loans provided by development financial institutions will help MSMEs navigate global trade uncertainties and mitigate the impact of external tariff pressures, particularly those arising from U.S. trade policies.

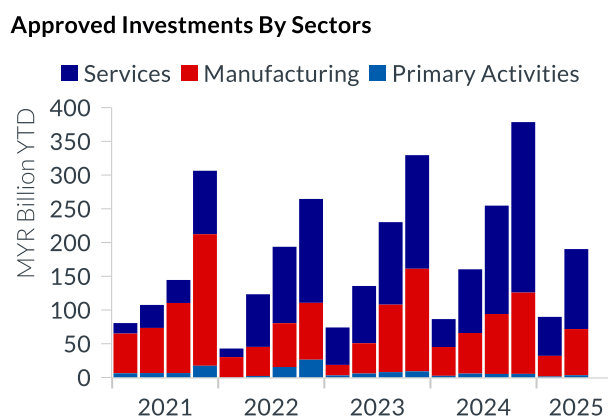
The tourism sector is poised to receive a significant boost through the Visit Malaysia 2026 campaign, with the government expected to allocate funding towards tourism infrastructure development, increased SME participation, and promotional activities. Drawing on lessons learned from previous campaigns such as Visit Malaysia 2020, this new initiative aims to create positive spillovers across the wider services sector. It is anticipated that this will strengthen Malaysia’s brand as a global tourism hub while supporting broader economic recovery efforts, particularly in the post-pandemic context.

Figure 10: Malaysia attracted MYR190.3 billion in approved investments in 1H25



Source: Macrobond, RHB Economics & Market Strategy

Figure 11: The approved investment projects are concentrated mainly in the services and manufacturing sectors



Source: Macrobond, RHB Economics & Market Strategy

Prong 5: Environmental, Social, and Governance (ESG) Priorities

Budget 2026 is expected to accelerate initiatives under the 13MP's green agenda, with a strong focus on renewable energy adoption, energy efficiency programmes, and the transition towards a low-carbon economy. A phased implementation of a carbon tax is likely to be introduced, initially targeting high-emission industries, such as iron and steel, as well as energy. This aligns with Malaysia's pledge to achieve net-zero greenhouse gas emissions by 2050 and its commitment under the Paris Agreement. Additionally, the government may expand incentives for solar, wind, and biomass projects to support its goal of increasing the share of renewable energy in the national energy mix to 31% by 2025 and 40% by 2035.

On the governance front, the government may strengthen ESG reporting requirements for publicly listed companies to improve transparency and accountability. Incentives for sustainable business practices are also expected, alongside support for SMEs to adopt ESG frameworks, ensuring that smaller enterprises are not left behind in the transition to a greener economy. These measures are consistent with 13MP goals of promoting responsible corporate governance, safeguarding investor confidence, and enhancing Malaysia's reputation as a sustainable investment destination.

To catalyse private sector participation, the government is likely to expand sustainable financing instruments such as green bonds, ESG-linked loans, and sukuk. Malaysia has been a regional leader in Islamic green finance, and Budget 2026 could further strengthen this role by encouraging long-term capital flows into renewable energy, environmental protection, and social development projects. Enhanced tax incentives and guarantees may also be introduced to mobilise private investment in sustainability-linked initiatives.

Allocations to the National Energy Transition Facility (NETF) are expected to continue in Budget 2026, supporting projects in renewable energy, energy efficiency, green mobility, and carbon capture technologies. This facility plays a critical role in bridging financing gaps for large-scale energy transition projects, complementing private sector efforts, and positioning Malaysia as a regional hub for clean energy investment.

Summary: A Bold Steer Towards Growth And Fiscal Resilience

In conclusion, Budget 2026 is poised to be a pivotal instrument in steering Malaysia towards sustained and inclusive growth amid a complex global environment. Anchored firmly within the framework of the 13MP and the MADANI Economy, it strikes a balance between immediate fiscal prudence and long-term strategic investments. With a likely budgetary deficit target of 3.5% of GDP in 2026, narrowing to 3.2% in 2027, the government is signalling its commitment to fiscal consolidation while maintaining the flexibility needed to support growth. The allocation of approximately MYR86 billion to MYR89 billion for development expenditure underlines a strong emphasis on infrastructure and regional connectivity, fostering more balanced development across the nation.

Economic growth is expected to strengthen to 4.7% in 2026, driven by robust domestic demand, increased capital investment, and the advancement of key initiatives spanning industrial modernisation, energy transition, and digital transformation. Despite persistent external headwinds, including sector-specific tariffs and global trade uncertainties, Malaysia's diversified economy and sound macroeconomic policies are poised to mitigate these impacts, thereby maintaining resilience and competitiveness. Inflation is projected to remain moderate, supported by measured policy adjustments and a prudent monetary stance, ensuring a stable environment for both consumers and businesses.

Budget 2026's multidimensional approach—emphasising fiscal sustainability, economic stimulus, social inclusivity, business climate enhancement, and ESG priorities—will act as both a stabiliser and catalyst. It aims to address immediate cost-of-living concerns, bolster MSMEs, attract investment through targeted incentives, and accelerate the transition to a green economy. This comprehensive strategy is designed not only to navigate near-term challenges but also to lay a robust foundation for Malaysia's medium- to long-term development goals, ultimately propelling the nation toward its vision of sustainable, inclusive prosperity by 2030.

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