Revised Customs Duty: What to Expect?

By Qarrem Kassim

Summary

On the 17th March 2021, the Minister of Finance, Tengku Datuk Seri Zafrul announced that an additional customs duty tariff is set to be imposed on several items of trade, in accordance with the Customs Duty Act 1967 (CDA). An export tariff of 15% is to be imposed on the following items involving ferrous waste and scrap ie. remelting scrap ingots of iron or steel which previously enjoyed a 10% tariff rate according to the Customs Duties Order List 2017.

The following table illustrates the change to the customs duty rate:

Item Code	Description	Announced Export Tariff Revision
7204.10.00 00	Waste and Scrap of Cast Iron	15%
7204.29.00 00	Waste and Scrap of Alloy Steel – Others	15%
7204.30.00 00	Waste and Scrap of Tinned Iron or Steel	15%
7204.41.00 00	Turnings, Shavings, Chips, Milling Waste, Sawdust, Fillings, Trimmings and Stampings, Whether or Not in Bundles	15%
7204.49.00 00	Other Ferrous Waste	15%

Source: Perintah Duti Kastam 2017

Malaysia is ultimately a net importer of scrap ferrous metals, as local production is only able to satisfy about 30% of local ferrous metals requirements[1]. Therefore, this export duty is seen as a boon for local industries who would benefit from cheaper ferrous metals supplies domestically, deterring the needed volumes from being exported. In addition, the Ministry of International Trade and Industry (MITI) had likewise announced additional restrictions on the imports of ferrous metals (principally from China) that hampers Malaysia's production of the good domestically.

Impact of Revised Export Duties

The revised customs duty is expected to discourage the export of ferrous scrap metal ie. metals containing iron, effectively encouraging the supply of steel products within the Malaysian economy and discouraging its export. This would have a net positive effect on our domestic supply of steel as Malaysian companies grapple with the rising cost of steel products following the partial lifting on Movement Control Order (MCO) restrictions during the second half of 2020.

The decision to keep import tariffs of ferrous scrap waste at 0% is meant to keep the supply-side afloat while supporting lower domestic prices for key users of steel, such as automobile producers and construction players. Amid the expansionary fiscal policy in the budget 2021 and various COVID-19 stimulus packages, steel prices are likely to face upward inflationary pressure as near-term demand increases while supply remains sticky.

According to the Construction Industry Development Board (CIDB), the inadequate global supply of iron ore is among one of the key reasons the price of steel bars has increased. In addition, local iron ore mines are unable to operate at full capacity due to several natural disasters which we have yet to fully recover from and restrictions caused by the pandemic[2].

Based on CIDB records, building prices in Malaysia has shown general price stability throughout 2020 except for steel bars and ferrous metals, which reached RM2,890/Metric Ton (MT) in January 2021 as opposed to RM2,435/MT in January 2020. For reference, the lowest price of ferrous metals was RM2,278/MT in May 2020.

[1] Malaysia imposes 15% ferrous scrap export duties to protect local industry, March 2021, S&P Global
[2] Steel: Depleting iron ore supply among reasons for price increase — CIDB, January 2021, The Edge Markets

As other nations likewise adopt expansionary fiscal policies, global demand-side competition for ferrous products has increased substantially, compounded domestically with lockdown-induced measures that made it more difficult for factories to operate at full capacity to increase the production of ferrous metals internally, leading to greater difficulties in obtaining an adequate supply of the metal for domestic usage.

In addition, the increase in steel prices have likewise been partly influenced by an unstable industrial cash flow cycle, as suppliers raise prices after taking into account the risk of late payments by the contractor who are in turn at risk of late payment by their clients, resulting a damaging spiral of price uncertainty and inflation. (ibid)

Importantly, one must also consider that the higher export tariff for domestic producers is a prudent move to rejuvenate the domestic market for steel manufacturing amid fears of oversupply from China. This may have inspired MITI to also announce stricter measures and standards on issuing manufacturing licences for scrap processors, allowing only local scrap consumers to import such items and cutting out middle-men traders[3].

In addition, MITI is taking the side of local manufacturers who fear a plan by a Chinese State-Owned Enterprise, Wenan, in funding a 5 to 10 million tonne-per-year steel factory in Samalaju, Sarawak. This facility would mop up most if not all available scrap metal in Malaysia, with the ability to offer better prices for the same raw input due to its size, causing local steel producers to lose out. Despite the local producer-friendly announcement from the government, officially, the steel project itself for Wenan has not been called off, triggering some level of anxiety and fear among local steel manufacturers[4].

Despite the fear of steel dumping from China, the Chinese market has in recent times been on the upswing, switching from net steel exporters to net importers of the good, with the demand for finished steel products in China so strong that they are now starting to buy overseas steel. Therefore the 15% export duty on scrap ferrous metal is a positive sign that such raw inputs are encouraged to be utilized domestically rather than towards manufacturers in China, boosting local industry.

Meanwhile, construction groups have also speculated that there is element of collusion among building material suppliers for steel and iron ore, sand, bitumen and cement[5]. Md Nasir Ibrahim, chairman of the Guild of Bumipetera Contractors Berhad claimed that there is an unofficial cartel among suppliers -wracked by losses from the lack of demand during the pandemic- who are controlling the domestic market price of materials to recoup lost revenue during the prior year.

Therefore, it is likely that the latest export tariff revision is more so consumer-driven by market players who intensively consume ferrous metals, concerned by the rising price of raw inputs. Particularly, small and medium sized players who were caught unaware by the pandemic, MCO restrictions and the sudden shortage of labour supply. This was particularly raised by the Master Builders Association of Malaysia (MBAM), who emphasized the damage caused to smaller stakeholders[6].

As MCO restrictions in 2020 tightened supply-side availability in ferrous metals for domestic players, it is rather prudent for the government to discourage the export of such metals for which in 2019 totalled USD376mil or RM1.58bil according to the latest World Trade Database figures available[7].

The breakdown schedule for 2019 is shown below:

Item Code	Product Description	Quantity Exported (KG)	Trade Value (USD '000)
7204.10.00 00	Waste and Scrap of Cast Iron	307,970,231	194,479
7204.29.00 00	Waste and Scrap of Alloy Steel – Others	142,098,401	53,480

[3] Malaysian ferrous scrap export tax looming, January 2021, Recycling Today
[4] Newsbreak: Policy revisions a boon for steel industry, January 2021, The Edge Markets
[5] After MCO, prices of materials have gone sky-high, complain builders, January 2021, Free Malaysia Today
[6] Government Urged to Intervene, Control Construction Material Prices, January 2021, Yahoo News
[7] Trade Statistics by Product (HS 6-digit), World Integrated Trade Solution, The World Bank Database

7204.30.00 00	Waste and Scrap of Tinned Iron or Steel	59,418,764	20,230
7204.41.00 00	Turnings, Shavings, Chips, Milling Waste, Sawdust, Fillings, Trimmings and Stampings, Whether or Not in Bundles	112,067,812	63,942
7204.49.00 00	Other Ferrous Waste	129,598,218	44,130
	Total	751,153,426	376,261

Source: World Integrated Trade Solution (WITS)

While the increase in export duty is a welcome move in keeping ferrous metal supplies within Malaysia's internal markets, the real impact to exports may not be as pronounced, this is because the export of ferrous metals comprises less than 0.002% of Malaysia's total exports for 2019. However, it will have a positive indirect impact on the cost of living as greater internal ferrous scrap supply encourage price stability in the sectors that use the metal intensively such as in construction and automobile production.

In other words, as the price of raw inputs for steel decrease domestically, the prices of final products that use these inputs intensively are reduced through market competition amid a general slowdown in per capita income due to MCO restrictions; thereby lessening the burden on the consumer. However, though the tariff may contribute to a lower input price in the short and longer-term, this may not necessarily translate into a substantial decrease in consumer prices if the government does not intervene in acting against market cartels, collusion and oligopolistic behaviour among ferrous metals producers as cited by industry groups described above, in addition to moves designed to protect domestic metals producers from foreign competition.

Key Takeaways and Recommendations

1. *Proper Messaging to the Grassroots*

It should be made aware that there is little to no negative consequence to the cost of living as the proposed increase in export tariffs are aimed to reduce price inflation in the cost of ferrous metals in the Malaysian economy. Rather, the negative impact would affect ferrous metal exporters who would be discouraged from exporting to markets overseas, encouraging its trade domestically.

In addition, the excise duty should be seen as a net positive for Malaysia's steel and ferrous metals industry, as domestic producers are able to rely on domestic inventories of ferrous scrap metal supplies as opposed to those same supplies being exported to Chinese markets, hence increasing the supply of ferrous scrap for Malaysian producers, bringing positive development to domestic employment and incomes.

2. *Clamping Down on Anti-Competitive Market Behaviour*

The government ought to clamp down on uncompetitive cartel-like behaviour among producers of ferrous metals and encourage price competition among local firms to bring down the price of steel, to the benefit of smaller stakeholders and help reduce input costs among many ferrous metals-dependent sectors such as in property development who will pass down the increased costs to the everyday property buyer culminating in housing inflation.

3. *Short-Term Government Price Controls Through Scrap Import Subsidies*

The government ought to intervene and control the price of basic construction materials in the short-term during this critical time as expansionary fiscal policy takes hold, so as to limit the inflationary market response to the increase in demand. Typically, an increase in fiscal spending on infrastructure works tends to produce a "crowding out" of resources in the market.

Therefore, a small, temporary subsidy in scrap metal imports would benefit producers in sourcing cheaper materials in the near term who can take advantage of the price differentials between the higher domestic steel price and the cost of ferrous scrap imports.