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Sugar tax starts today

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Excise tax of 40 sen per litre is levied on sweetened beverages with more than 5g of sugar per 100ml

By SHAZNI ONG / Pic By MUHD AMIN NAHARUL

THE sugar tax finally begins today.

It was initially expected to begin on April 1 but postponed to today to allow manufacturers and the Customs Department time to prepare.

An excise tax of 40 sen per litre is levied on sweetened beverages with more than 5g of sugar or sugar-based sweetener per 100ml. This includes carbonated, flavoured and other non-alcoholic beverages.

Juice or vegetable-based drinks with over 12g of sugar per 100ml will also be taxed.

Finance Minister Lim Guan Eng announced the plan to introduce the tax during the tabling of the 2019 budget in November last year.

This follows a study conducted by the Ministry of Health (MoH) which found that nearly one in two Malaysians are overweight or obese.

The government has pushed the idea to impose a sugar tax as part of its efforts to promote a healthy lifestyle as Malaysia is reported to be the fattest country in South-East Asia with obesity and diabetes levels on the rise.

According to the World Health Organisation, 13.3% of Malaysians are obese and 38.5% overweight, in addition to the highest proportion of diabetics (14.9%).

In a report entitled "Tackling Obesity in Asean" released by the Economist Intelligence Unit in 2017, it was found that among the factors contributing to Malaysians' growing waistlines and health problems were rising incomes, shifting lifestyles and the lack of awareness about sugary drinks.

The MoH and other related bodies have welcomed the introduction of the tax as a move towards addressing national health issues and concerns.

With more than half of the population deemed as unhealthy, the cost of healthcare is enormous for the country, with estimates ranging between US$1 billion (RM4.15 billion) and US$2.1 billion based on a 2017 study by the Asia Roundtable on Food Innovation for Improved Nutrition.

This is a massive amount, considering the RM29 billion allocation for health under the 2019 budget.

Detractors and critics of the tax, however, opined that it would not be enough to make an impact, with reactions ranging from approval and concern to effectiveness and scepticism.

Similar tax is being imposed in other countries including the US (in certain cities), the UK, France, Mexico, Norway, Portugal, the United Arab Emirates, Saudi Arabia and South Africa.

Closer to home, Thailand, Brunei (both in 2017) and the Philippines (in 2018) are among the countries that have imposed the tax.

In April this year, Health Minister Datuk Seri Dr Dzulkefly Ahmad said the sugar tax is limited to manufacturers for the time being, and that there are no plans to extend it to eateries.

"We are now at the stage of educating consumers to drink less coloured, sugary drinks. That is the only way, at the moment, that we can discourage consumers from drinking these drinks," he said.

Meanwhile, in March, Prime Minister Tun Dr Mahathir Mohamad said there will be no new taxes except for the sugar tax.

He also said beginning next year, the government will use the revenue collected from this tax to provide free and healthy breakfast for all primary school children.

This article talks about Malaysia's government introducing sugar tax to fight the problem of obesity in the country. Ministry of Health's study found *"that nearly one in two Malaysians are overweight or obese."*

This concerns the government, as obesity is often associated with serious health risks, lowering productivity. Healthcare costs are huge - *"with estimates ranging between US$1 billion (RM4.15 billion) and US$2.1 billion."* These costs arise because sugar is a demerit good, which means, that when consumed it "can have a negative impact on the consumer[1]", hence, due to negative externality of consumption, market failure arises (Figure 1).

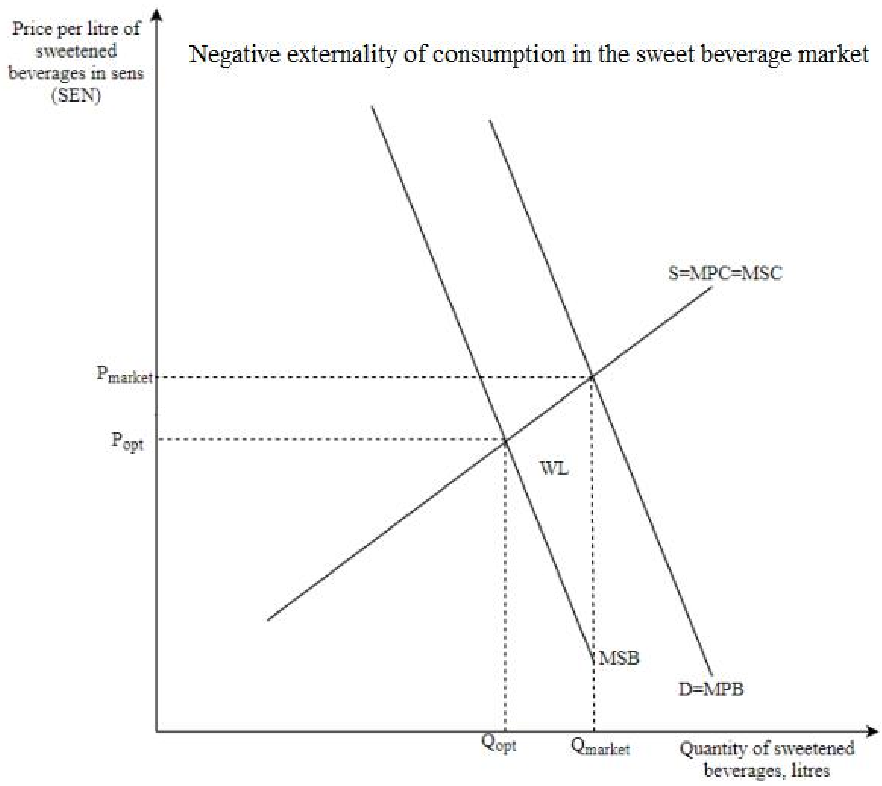

Figure 1

Demand in the market is determined by private buyers and thus D=MPB. The market equilibrium occurs at point (Q_{market};P_{market}), where MSC=MPC=MPB. However, this is not socially optimal, as private consumers don't account for the extra burden placed on society when consuming this good, therefore MPB>MSB, which leads to MSC>MSB at the market-determined equilibrium (Q_{market};P_{market}). Between Q_{market} and Q_{opt} MSC>MSB, which means, that the good is overconsumed and market failure arises. The associated welfare loss is denoted by the area WL.

[1] Pettinger, Tejvan. "Demerit Good Definition." Economics Help. Accessed March 23, 2020. https://www.economicshelp.org/blog/glossary/demerit-goods/

To combat this, a sugar tax was introduced- *"An excise tax of 40 sen per litre is levied on sweetened beverages with more than 5g of sugar or sugar-based sweetener per 100ml."* "An excise tax is an indirect tax placed on a selected number of goods[2]".

This tax increases the costs of production for the drinks, thus acting as an incentive for producers to produce less at the same price, which leads to a leftward shift of the S=MPC curve, while the MSC curve doesn't change (because only private prices increase), thus reducing the welfare loss (Figure 2).

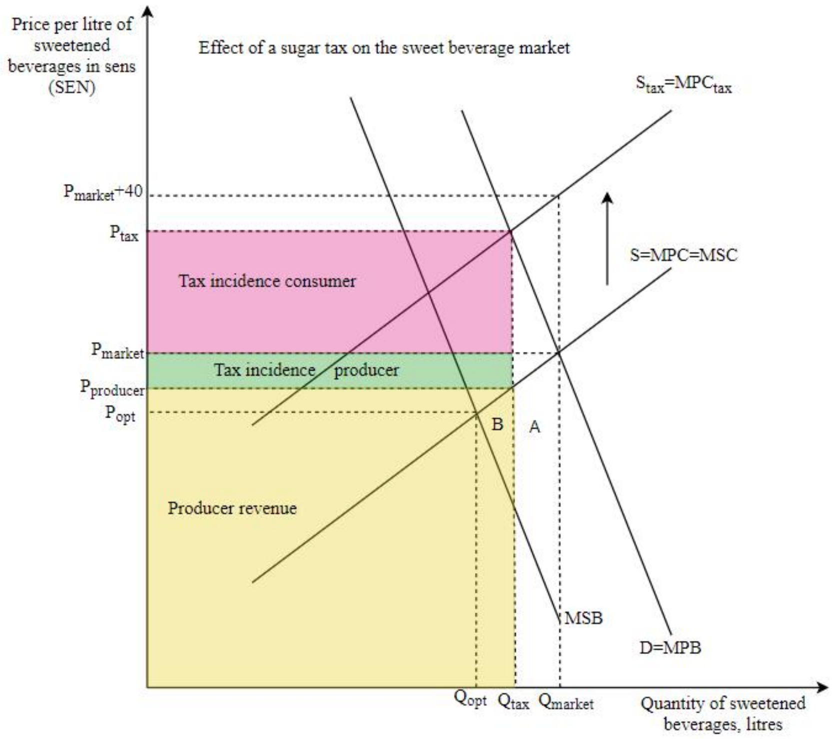

Figure 2

The tax causes extra private costs for the producers, which now want to produce less at the same price, thus S=MPC curve shifts to the left to $S_{tax}=MPC_{tax}$ curve. Producers want to pass all of the tax to the consumers so they set a price of $P_{market}+40$. However, at this price the good is oversupplied,thus the producers reduce price and a new market clearing point (Q_{tax};P_{tax}) forms, which decreases the welfare loss from area A+B to area B. After the changes, consumers pay a tax of $(P_{tax}-P_{market})*Q_{tax}$ while the producers pay a tax of $(P_{market}-P_{producer})*Q_{tax}$. Consumers are hurt relatively more by the tax than producers, because sugar drinks are an addictive good — demand for them is inelastic, thus producers are able to pass off most of the tax to the consumers by raising prices. After the tax, producers are also hurt, because producer revenue falls from $P_{market}*Q_{market}$ to $P_{producer}*Q_{tax}$ and consumers are also hurt, because they now are able to buy less ($Q_{tax}<Q_{market}$) at a higher price ($P_{tax}>P_{market}$).

[2] Finamore, David. "Government intervention - Indirect taxes" in *Economics: Supporting Every Learner across the IB Continuum,* edited by Christian Bryan, page 32. Harlow, Essex: Pearson Education Limited, 2014.

However, the sugar tax was not introduced suddenly, *"It was initially expected to begin on April 1 but postponed to today to allow manufacturers and the Customs Department time to prepare."*, thus producers had a chance to reallocate their resources and minimize losses. This could also further reduce negative externalities, because, to minimize losses, manufacturers are forced to switch to producing healthier products.

As for the winners, government would benefit from the tax revenue. In this case they have already decided how to use this money — *"the government will use the revenue collected from this tax to provide free and healthy breakfast for all primary school children"* — to further reduce obesity in Malaysia. Other possible winners in the situation include manufacturers and sellers of substitute goods, such as unsweetened teas, because to some people they would become the better choice, thus their share of the market would increase.

However, it is unclear whether the change this tax delivers will be significant. One could argue, that reducing the consumption of sugar drinks doesn't mean people will get healthier, it is possible, that they just consume more other unhealthy foods and still stay overweight and obese. Another concern is that the benefits from this tax would only work in the long-run, while in the short-run such tax would prove ineffective in reducing the market failure. This is so, because there is a time lag in reducing obesity, as it takes time for people to get healthier.

Nonetheless, even if the tax doesn't function in the short-run, it doesn't mean it shouldn't be implemented. In the long-run this tax could be extremely beneficial in reducing this market failure, which affects the whole Malaysian economy due to the fact, that a functioning labour force is an essential part of a thriving economy.

Word count: 746

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