Malaysia's Carbon Tax: From Policy Signal to Portfolio Risk

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Malaysia's planned carbon tax marks a significant step in the country's evolving climate policy framework. The government has signalled that carbon pricing could be introduced from 2026, initially targeting iron, steel and energy sectors. This will be supported by the forthcoming Climate Change Bill (RUUPIN), which will provide the legal and regulatory foundation for the mechanism. While the final design of the policy, including the carbon tax rate, sector coverage and compliance thresholds have yet to be announced, the direction of the path is becoming increasingly clear as Malaysia aligns with global decarbonisation trends and the European Union's Carbon Adjustment Mechanism (EU CBAM).

Carbon pricing effectively introduces an additional cost factor for carbon-intensive industries, which may place gradual pressure on margins and profitability over time. Viewed positively, it could create valuation differentiation across companies depending on emissions intensity, decarbonisation readiness and their ability to manage transition risks. While details are fluid, we performed a scenario analysis for the potential carbon tax impact to financials in exhibit 2 and 3, where we find that at RM15/tonne, majority of companies will be affected in profitability by at least 5% or more.

In our view, the introduction of carbon pricing should be viewed not only as a compliance requirement but also as an emerging signal of transition risk that will increasingly need to be incorporated into portfolio analysis. As the policy framework evolves, companies will need stronger emissions governance, improved data management and clearer decarbonisation strategies to manage potential cost pressures and regulatory expectations.

Malaysia's planned carbon tax marks an important turning point in the country's climate policy framework. The government has signalled its intention to introduce carbon pricing beginning in 2026, supported by the forthcoming Climate Change Bill (RUUPIN) that will provide the legal and regulatory foundation for the mechanism. While the final design of the policy, including the carbon tax rate, sector coverage and compliance thresholds have yet to be announced, the direction of policy is becoming increasingly clear: carbon pricing will form a central component of Malaysia's strategy to manage climate transition risks and align with global decarbonisation trends and the EU CBAM.

Carbon pricing effectively introduces an additional cost factor into the operating structure of carbon-intensive industries, which could place pressure on margins and profitability over time. At the same time, the policy creates valuation differentiation across companies depending on their emissions intensity, decarbonisation readiness and ability to manage transition risks. Firms with strong emissions management strategies may be a benefit and better access to sustainability-linked financing and potentially lower cost of capital.

In this context, the carbon tax should be viewed not only as a compliance obligation but also as an emerging signal of transition risk that may increasingly influence capital allocation decisions across portfolios. In addition, the adherence to EU CBAM standards could also keep our exports competitive through continued market access.

Carbon Tax Policy Framework. Malaysia's carbon tax policy is progressing through a staged legislative process. The government first signalled the introduction of carbon pricing during Budget 2025, with enabling legislation expected to be introduced under the Climate Change Bill. Current policy discussions indicate that the carbon tax could take effect in 2026 starting with iron, steel and energy sectors. This fiscal measure builds upon Malaysia's National Sustainability Reporting Framework (NSRF), which was officially launched in September 2024. While the carbon tax is pending, mandatory sustainability disclosures have already commenced as of January 1, 2025, for large-cap Main Market issuers. The phased adoption of ISSB Standards (IFRS S1: General Requirements for Disclosure of Sustainability-related Financial Information and IFRS S2: Climate-related Disclosure) will expand to all other Main Market companies this year (2026), with ACE Market and large non-listed entities (revenue > RM2 b) following suit by 2027.

The first phase of the carbon tax is expected to focus on direct emissions, commonly referred to as Scope 1 emissions. These emissions arise directly from operational activities such as fuel combustion and industrial processes. Policymakers have indicated that early implementation may target carbon-intensive sectors, particularly iron and steel production and energy generation, as these industries account for a large share of industrial emissions and therefore provide significant leverage for emissions reduction policies.

Companies subject to the carbon tax will likely be required to implement robust Measurement, Reporting and Verification (MRV) systems. These MRV systems are expected to align with internationally recognised frameworks such as the Greenhouse Gas Protocol for accounting and align with the IFRS S2 (Climate-related Disclosures) standards now mandated under Malaysia's NSRF. Such alignment ensures that emissions data is prepared with the reasonable assurance required by regulators to accurately verify carbon liabilities and by investors to assess climate-related financial risks."

Although the policy framework is now taking shape, several key parameters remain pending. The government has not yet announced the final carbon tax rate, the precise sectors to be covered in the first phase, or the emissions thresholds above which firms will be taxed. These details are expected to be clarified once the Climate Change Bill is tabled and supporting regulations are issued by the Ministry of Finance. The Bill was last reported to be scheduled for its first reading by March 2026. (Link)

Regional Context. Malaysia's carbon pricing policy is developed alongside broader regional efforts to introduce market-based climate mechanisms. Singapore is seen as a prominent regional benchmark, having been the first country in Southeast Asia to introduce a carbon tax. The tax officially commenced on 1 January 2019, initially set at a transition rate of SGD5 per tonne of carbon dioxide equivalent (tCO_2e) to allow businesses time to adapt. In 2024, the tax was increased to SGD25 per tCO_2e Singapore's carbon price is set to increase from SGD25 per tCO_2e to SGD45 per tCO_2e in 2026, and an eventual target of SGD 50-80 per tCO_2e by 2030.

Although Malaysia has not yet announced a formal price trajectory, policy discussions suggest that the country could adopt a gradually increasing carbon price pathway. During a recent Kenanga-hosted webinar, Mr. Ray Lim, co-founder of Carbon Next and a carbon tax and decarbonisation strategist, indicated potential price levels beginning around RM15 per tCO2e and rising toward RM100 per tonne over the longer term.

Malaysia is also exploring the possibility of complementing the carbon tax with a broader emissions trading framework. Discussions have indicated the potential for a pilot Emissions Trading System between 2025 and 2027, which could eventually evolve into a more comprehensive carbon market. Over time, Malaysia may adopt a hybrid carbon pricing architecture that combines carbon taxes, emissions trading mechanisms and voluntary carbon markets. Such an approach would align Malaysia with evolving global practices in carbon pricing and provide greater flexibility for industries to manage emissions costs.

Macroeconomic Implications. Carbon pricing has implications that extend beyond environmental policy and into the broader macroeconomic landscape. By placing a monetary cost on carbon emissions, the policy effectively embeds environmental externalities into production decisions. This creates an incentive for firms to improve energy efficiency, adopt cleaner technologies and reduce emissions intensity over time.

Furthermore, carbon pricing also reshapes market behaviour by shifting capital toward lower-carbon assets and technologies. As carbon costs increase, investments in renewable energy, energy efficiency and low-carbon industrial processes become more economically attractive. Additionally, carbon tax revenues could provide governments with new fiscal resources to support climate mitigation initiatives and renewable energy development, ensuring broader economic transition strategies remain aligned with the National Energy Transition Roadmap (NETR).

Industry Readiness and Corporate Compliance. The effectiveness of a carbon pricing framework depends heavily on the availability of reliable emissions data. For this reason, regulators typically require companies to implement structured MRV processes that track emissions at the operational level. These systems involve collecting activity data related to direct fuel combustion and industrial process inputs at the operational level. Companies must then apply appropriate emission factors to calculate their total Scope 1 carbon emissions, which are subsequently verified through independent third-party assurance. Emission factors represent the calculated ratio of greenhouse gas emissions released per unit of activity, such as the amount of CO_2 produced per gigajoule of energy consumed.

While many large publicly listed companies have already disclosed sustainability information under Bursa Malaysia's Listing Requirements for Sustainability Reporting, we find the level of detail and assurance varies significantly across firms. Smaller companies often face challenges in developing emissions data management systems due to limited resources and technical expertise. The introduction of NSRF which mandates alignment with IFRS S2, is expected to drive improved quality of these disclosures. The IFRS S2 requires a more disciplined approach to quantifying climate-related financial risks, moving beyond qualitative narratives toward 'investor-grade' data

The introduction of a carbon tax therefore places greater emphasis on corporate climate governance and data management capabilities. Firms that fail to establish credible MRV systems may face regulatory risks, reputational concerns and potential difficulties in accessing sustainable financing opportunities. At the same time, financial regulators in Malaysia have introduced complementary frameworks, such as Bank Negara Malaysia's Climate Change and Principle-based Taxonomy and the Securities Commission's Sustainable and Responsible Investment taxonomy that increasingly link climate performance with capital allocation decisions.

Sector Exposure to Carbon Pricing. The financial impact of carbon pricing will vary significantly across industries depending on emissions intensity, production technologies and energy consumption patterns. Industries with substantial process emissions are structurally more exposed to carbon costs. For example, the metals sector, including iron, steel and aluminium production generate significant emissions through chemical reactions inherent in the manufacturing process. Similarly, cement production produces emissions during the calcination of limestone, making decarbonisation particularly challenging.

By contrast, sectors such as power generation and transportation are primarily exposed through fuel combustion. In these industries, the financial impact of carbon pricing will depend largely on factors such as fuel mix, energy efficiency and regulatory mechanisms governing tariff structures. For instance, electricity generators that rely heavily on coal may face higher carbon costs, whereas companies with greater renewable energy penetration may experience lower exposure.

Scenario analysis presented during the webinar indicates that carbon pricing could lead to medium to very high earnings impacts for certain carbon-intensive sectors. Carbon prices above RM50 per tonne of emissions may begin to materially affect corporate profitability, especially for industries with high emissions intensity and limited short-term mitigation options.

Companies may mitigate these risks through several strategic approaches, including fuel switching, renewable energy procurement through power purchase agreements, operational efficiency improvements and product innovation that reduces emissions intensity.

Direct and Indirect Impact. Corporate exposure to carbon pricing arises through both direct and indirect channels. Direct exposure occurs when companies are taxed on their own operational emissions. For instance, an utility emitting approximately 200,000 tonnes of carbon dioxide annually could face carbon tax liabilities of around RM5.0m under a tax rate of RM25 per tonne, with the figures possibly increases over time. The illustration above is simplistic in that we have not assumed a taxable threshold (an emissions floor) which is a common feature for adoption in neighbouring countries where companies are only taxed on emissions exceeding a specific limit.

However, the actual financial impact will depend heavily on policy design. Mechanisms such as emissions trading systems, free emissions allocations or the use of carbon credits could reduce effective liabilities. Conversely, hybrid systems that combine carbon tax floors with emissions trading markets may increase the overall carbon price faced by companies.

EXHIBIT 1: Carbon Tax Sensitivity Scenario – Emissions and Tax Amount (FY24)

Sector	Company	Scope 1 GHG Emissions (tCO2e) FY 2024	Carbon Tax (RM/tonne CO2e) RM15	RM25	RM50	RM100
Oil & Gas	HIBISCUS[1]	6,668,835	-	-	-	-
	VELESTO[2]	62,264	933,960	1,556,600	3,113,200	6,226,400
	DAYANG[1]	31,602	474,030	790,050	1,580,100	3,160,200
	PCG[1]	6,690,000	-	-	-	-
Utilities	TENAGA[1]	38,750,000	581,250,000	968,750,000	1,937,500,000	3,875,000,000
	MALAKOFF[2]	19,063,308	285,949,620	476,582,700	953,165,400	1,906,330,800
	PGB[1]	6,074,946	91,124,190	151,873,650	303,747,300	607,494,600
	GAS MALAYSIA[2]	244,698	3,670,470	- 6,117,451	12,234,902	24,469,803
	YTLPOWER[1]	5,505,000	82,575,000	137,625,000	275,250,000	550,500,000
Building Material	ENGTEX[2]	10,207	153,105	255,175	510,350	1,020,700
	PMETAL[2]	1,793,600	26,904,000	44,840,000	89,680,000	179,360,000
	ULICORP[2]	34,866	522,990	871,650	1,743,300	3,486,600

Source: Companies

[1] Scope 1 (Malaysia Operations): Represents direct emissions specifically attributed to assets located within Malaysia.
[2] Scope 1 (Total/Global): Represents consolidated group emissions where a specific geographical breakdown for Malaysia was not disclosed by the issuer.

EXHIBIT 2: Carbon Tax Sensitivity Scenario – EBITDA Impact (FY24)

Company	RM15	RM25	RM50	RM100
HIBISCUS	<5%	<5%	5–10%	5–10%
VELESTO	<5%	<5%	<5%	<5%
DAYANG	<5%	<5%	<5%	<5%
PCHEM	<5%	<5%	5–10%	5–10%
TENAGA	<5%	<5%	5–10%	5–10%
MALAKOF	>20%	>20%	>20%	>20%
PETGAS	<5%	<5%	5–10%	5–10%
GASMSIA	<5%	<5%	<5%	<5%
YTLPOWR	<5%	<5%	<5%	<5%
ENGTEX	<5%	<5%	<5%	<5%
PMETAL	<5%	<5%	<5%	<5%
ULICORP	<5%	<5%	<5%	<5%

Source: Companies

EXHIBIT 3: Carbon Tax Sensitivity Scenario – Profit After Tax Impact (FY24)

Company	RM15	RM25	RM50	RM100
HIBISCUS	5–10%	5–10%	5–10%	5–10%
VELESTO	<5%	<5%	<5%	<5%
DAYANG	<5%	<5%	<5%	<5%
PCHEM	10–20%	10–20%	10–20%	10–20%
TENAGA	>20%	>20%	>20%	>20%
MALAKOF	>20%	>20%	>20%	>20%
PETGAS	5–10%	5–10%	5–10%	5–10%
GASMSIA	<5%	<5%	<5%	<5%
YTLPOWR	<5%	<5%	5–10%	5–10%
ENGTEX	<5%	<5%	<5%	<5%
PMETAL	<5%	<5%	<5%	<5%
ULICORP	<5%	<5%	<5%	<5%

Source: Companies

- *EBITDA Impact - Operational efficiency deterioration*
- *PAT Impact - Bottom-line and valuation implications*

We have conducted an analysis of the affected companies under our coverage, quantifying their carbon emissions relating to domestic operations subject to the upcoming carbon tax. Domestic operations refer to direct emissions from assets located within Malaysia, while total (Global) reflects consolidated group emissions where a Malaysia-specific breakdown was not disclosed by the issuer. Our impact assessment is based on a fixed-rate carbon tax assumption applied to absolute FY24 emissions data, excluding potential tax-free thresholds or transitional credits. We have excluded companies such as Yinson, as their carbon footprint is predominantly generated through international offshore operations. Conversely, we have included Malakoff and Tenaga Nasional (TNB) in our scope, given their exposure as primary players in the Energy and Power Generation sector. Based on our scenario analysis using FY24 Scope 1 emissions, the earnings sensitivity to carbon pricing varies significantly across companies and sectors. At lower carbon price levels (RM15–RM25/tCO_2e), most companies experience relatively limited earnings impact, generally within the <5% to 10% range. As carbon prices rise to RM50/tCO_2e and RM100/tCO_2e, the impact becomes more pronounced for emissions-intensive companies, particularly within the utilities and energy segments. Companies with larger direct emissions bases see earnings pressures move into the 10%–20% and >20% impact bands under higher carbon price scenarios. At RM100, we expect 8% of companies in our sample could potentially be in losses. Meanwhile, companies with relatively smaller emissions footprints or lower direct exposure to fossil fuel combustion largely remain within the low impact band across the different scenarios. Overall, the analysis suggests that the financial implications of carbon pricing are primarily driven by absolute emission volumes and sector characteristics, with utilities and certain energy players emerging as the most sensitive to higher carbon tax levels. Once again, we caveat that the above exercise remains fluid given lack of clarity on implementation parameters including any carbon tax thresholds beyond which only will the tax be collected.

Indirect exposure arises through energy costs. Since Malaysia's electricity generation mix still includes coal and natural gas, carbon pricing applied to power producers may eventually be reflected in electricity tariffs if costs are passed through to consumers. In such scenarios, even companies with relatively low direct emissions could experience higher operating costs through increased electricity prices.

While companies may initially attempt to pass carbon costs on to consumers, we believe this approach is unlikely to be sustainable over the longer term. Persistent cost pass-through could weaken demand and reduce competitiveness, particularly in sectors exposed to global trade. Instead, companies will likely need to address emissions more structurally across their operations and value chains. Although decarbonisation initiatives may require higher upfront capex, such as investments in energy efficiency, cleaner technologies or fuel switching, we believe these investments could be more viable over time compared with repeatedly absorbing or passing through rising carbon tax liabilities.

Conclusion. Malaysia's planned carbon tax represents a significant development in the country's climate policy landscape. Although key details of the policy remain under discussion, the direction is increasingly evident. Carbon pricing will become an integral part of Malaysia's strategy to manage climate risks and align with international decarbonisation efforts.

Stock Ratings are defined as follows:

Stock Recommendations

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10%
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10%
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than -5%

******Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.***

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