

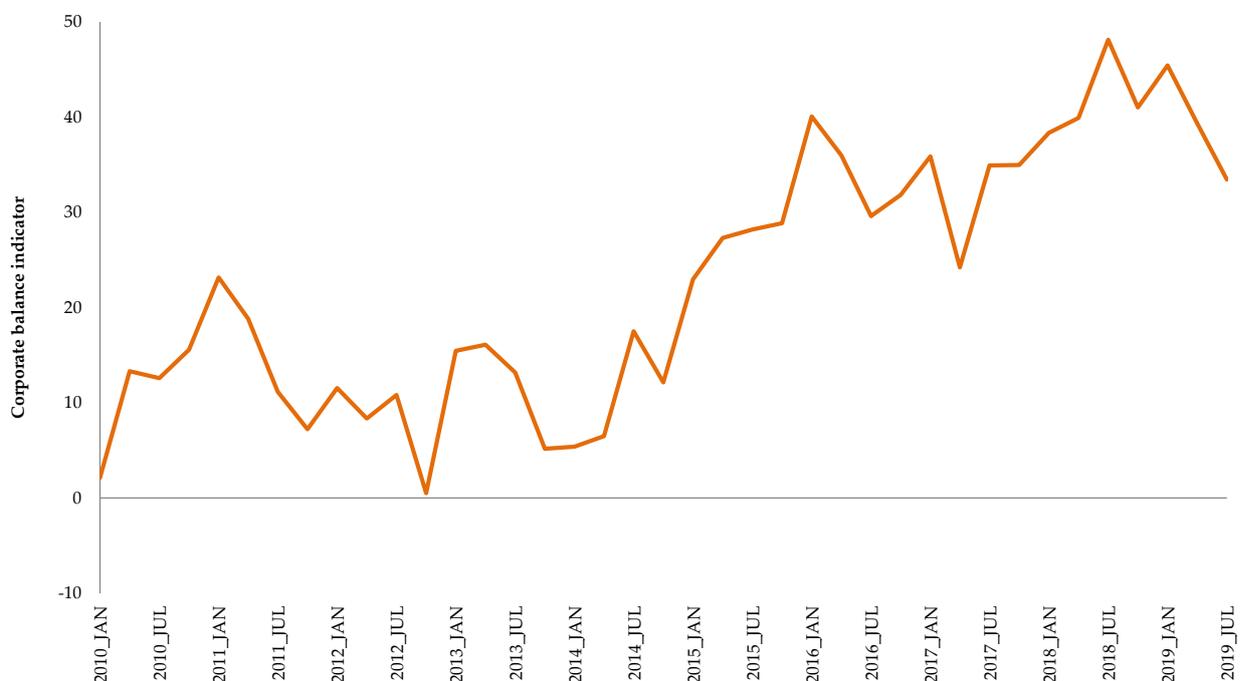


Results of the July 2019 IEER Quarterly Business Climate Survey

The Quarterly Business Climate Survey of IEER is based on the survey of 400 CEO respondents about their business situation and expectations. According to the records taken in July 2019 the level of business confidence in Hungary decreased slightly compared to April 2019.

In July 2019 the Quarterly Business Climate Index dropped from 39 points to 33 (see Figure 1).

Figure 1: Quarterly Business Climate Index, January 2010 – July 2019



Source: IEER 2019

Please note that the score in the figure is a balance indicator projected on a scale of 100. In all cases, the balance indicator shows the difference between the rate of companies providing positive and negative situation reports. The indicator therefore spans a scale from -100 to +100. -100 indicates that all of the surveyed companies assessed their situations to have been negative, while +100 indicates that all of the surveyed companies assessed their situations to have been positive.

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The Quarterly Business Climate Index was the highest for construction companies (+49 points), while for trading companies it was +43 points and for companies offering business services it was +35. Companies in the processing industry got the lowest score at +30 points. Trading companies experienced a 8

points increase quarter-on-quarter, while there was a 13 points decrease in case of companies in the processing industry compared to the previous quarter.

Figure 2: Quarterly Business Climate Index by economic sectors, January 2010 – July 2019



Source: IEER 2019

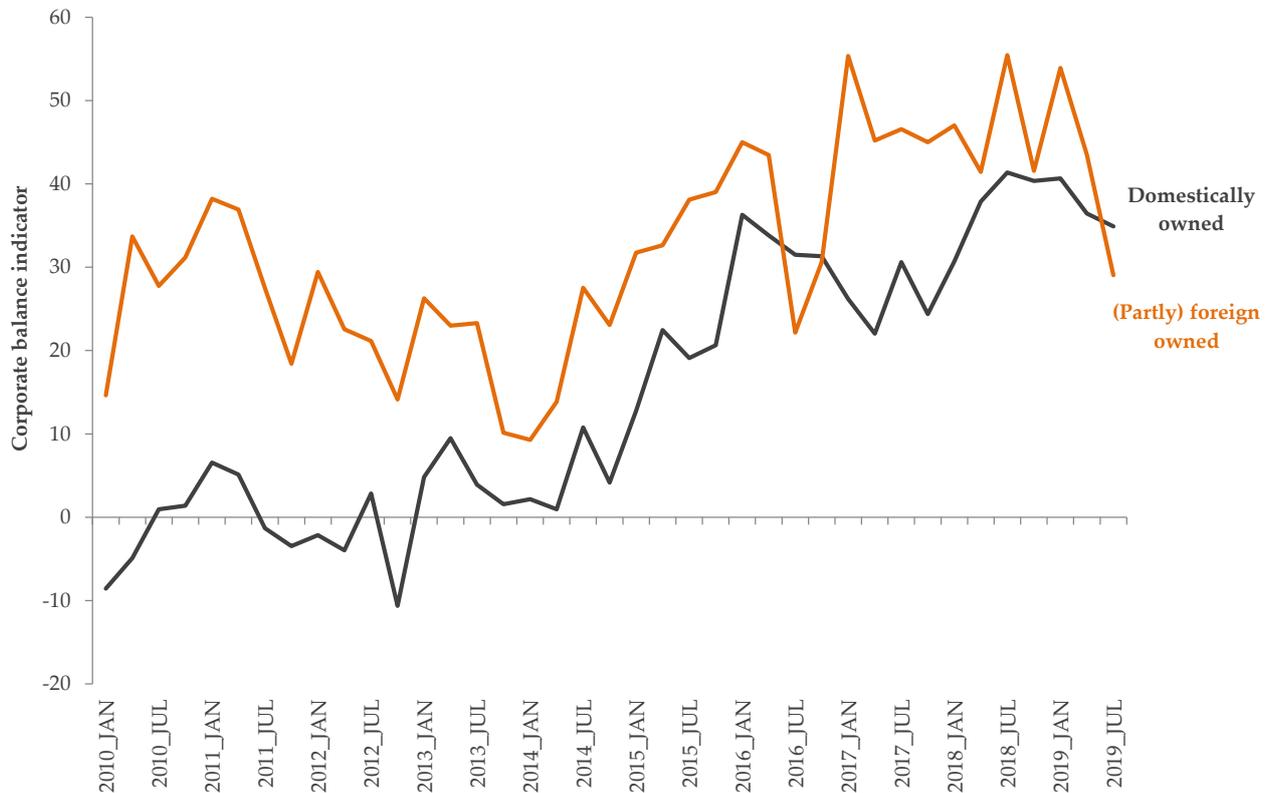
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Examining companies by ownership structure reveals that the Quarterly Business Climate Index is +35 points for domestically owned companies and +29 points for (partly) foreign owned enterprises. While domestically owned

companies lost 2 points quarter-on-quarter, (partly) foreign owned enterprises showed a 14 points decrease for this indicator.

Figure 3: Quarterly Business Climate Index by ownership structure, January 2010 – July 2019



Source: IEER 2019

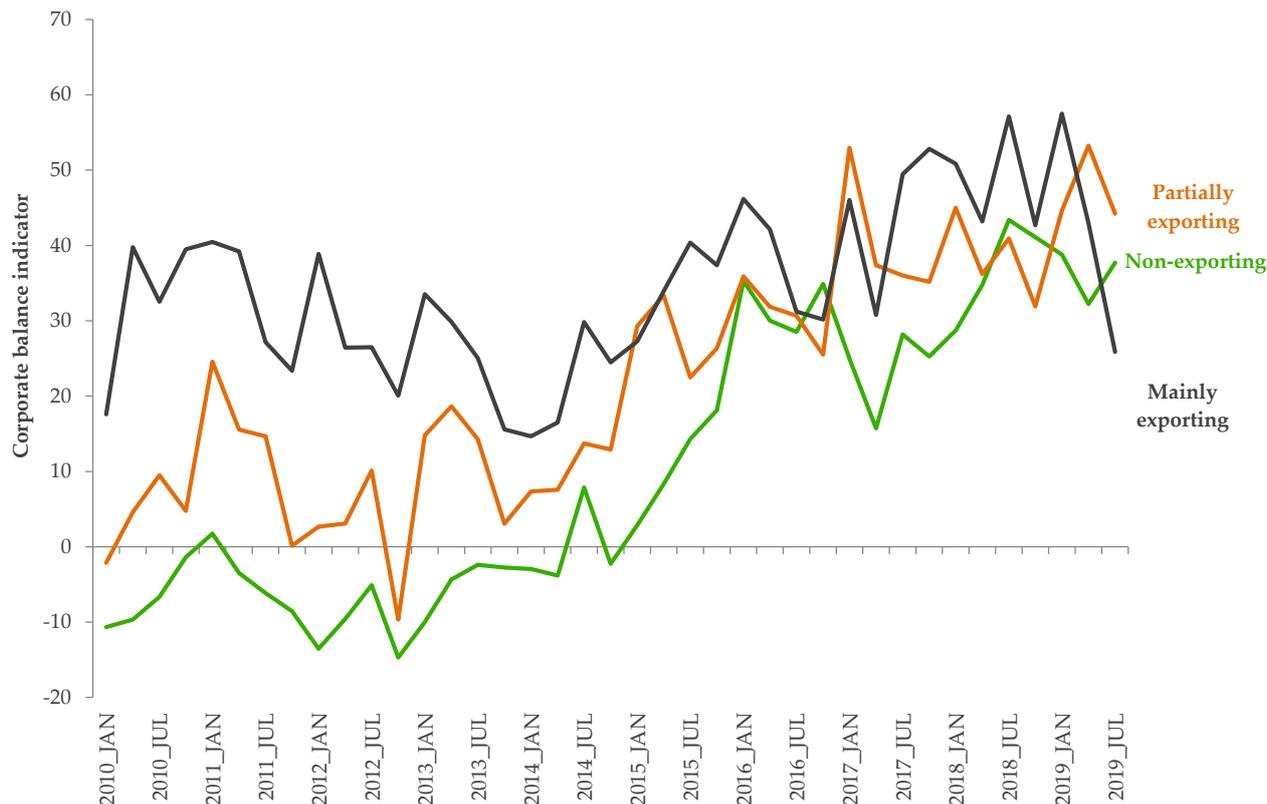
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With regard to exports, the value of the Quarterly Business Climate Index was the lowest for mainly exporting companies (+26 points), while it was +44 points for partially exporting and +38 for non-exporting enterprises. Compared to the previous quarter,

mainly exporting companies lost 17 points each, whereas the same indicator decreased by 9 points among partially exporting enterprises. The non-exporting enterprises experienced a 5 points increase.

Figure 4: Quarterly Business Climate Index by export activity, January 2010 – July 2019



Source: IEER 2019

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The Quarterly Business Climate Index has ten components such as:

- current/expected business situation;
- current/expected profitability;
- expected investment activity;
- current stock orders;
- production levels of the previous half-year/expected production levels;
- expected change in staff members;
- expected capacity utilisation.

As far as sub-indicators are concerned, CEOs were far more optimistic about their expected level of investments, current stock orders, whereas their opinion on the current and expected profitability, production levels of the previous half and expectations regarding expected production levels are considerably more pessimistic than in April 2019.

Year-on-year outlook regarding all indicators – expect the expected level of investments and

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expected headcount – companies have more pessimistic expectations than in July 2018.

According to data recorded in July, large companies and small and medium sized enterprises assessed their situations similarly.

An exception to this is the production levels of the previous half and the expectations regarding expected production levels: the assessment of the small and medium sized enterprises is more positive than the evaluation of the large companies.

Tax Digitalisation

We live in a world where digitalisation is affecting each and every aspect of our lives including how our economy and society are organized and functioning. In Information Technology terms, “Digitization” is defined as converting physical information from analog to digital form whereas “Digitalisation” is converting a business model to digital operations. The information is digitized and the processes are digitalized. Digital transformation of a business is achieved through these two methods. Globalization along with digitization has led to unparalleled growth of information and data. In addition, projects of the Organisation for Economic Co-operation and Development’s (OECD) such as Base Erosion and Profit Shifting (BEPS), Automatic Exchange of Information (AEOI), Common Reporting Standard (CRS), the exchange of tax rulings within the European Union (EU) and taxpayer demand for public tax transparency, have presented additional challenges. “Tax Digitalisation” is the way through which tax administrations can effectively analyze all the information and can provide better services and become more efficient. Digitalisation of tax should not mean only converting paper forms into PDFs to upload on a government website, but it must be revolutionary, considering how taxpayers complete their filings, what is taxed, and how the authority can manoeuvre powerful data channels to complete and audit taxes without a filing being made. Thus, with incorporation of digital world in tax system, various issues of handling the large scale information and data as well as transparency can be settled at ease.

Tax challenges of the digital economy

The digital economy is a metamorphic process achieved by continuous progression in information and communications technology (ICT) that has strengthened the technology and made it relatively cheaper, transforming business processes and bracing innovation across various sectors of the economy, comprising traditional industries. In addition to the pros, there are various challenges caused by the digitalisation. The first finding regarding the tax challenges of the digital economy agreed by all G20 and OECD Centre for Tax Policy and Administration countries, under the Base Erosion and Profit Shifting (BEPS) Project was that the “Digitalisation” has become pandemic that makes it difficult to separate the digital world from the economy, including taxation system¹. Due to this, it

became evident that digital economy has the potential to aggravate the risks of BEPS for tax purposes viz mobility, data reliability, network effects, and the expansion of multi-sided business models. The second major finding was that the digital economy has raised several challenges for policy makers of tax which are classified in three categories under the name “broader tax challenges” that are related to the issues of taxing rights on income generated by cross border trade among the participant countries². These challenges are as follows:

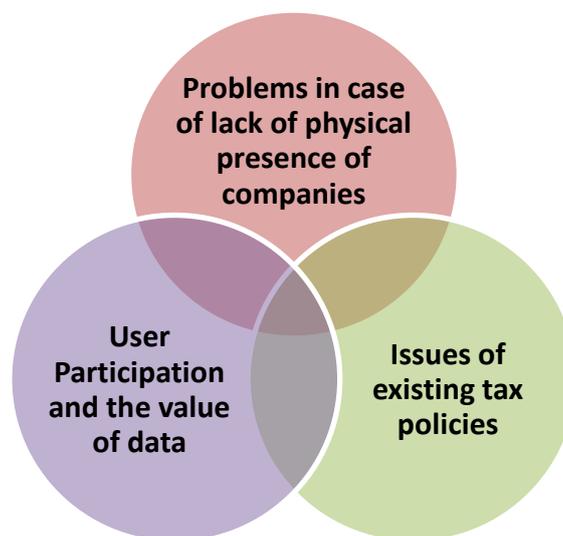
- The various problems that are faced in the collection of Value Added Tax (VAT)/ Goods And Services Tax (GST) in the destination country, where goods and services are procured by consumers from overseas based suppliers which lacks the physical presence whether

¹ OECD. (2019). Addressing the Tax Challenges of the Digital Economy. Available at <https://bit.ly/2XLoF2a>

² Pascal Saint-Amans. (2017). Tax challenges, disruption and the digital economy. <https://bit.ly/2jZ2FfQ>

- direct or indirect, in the consumer's jurisdiction.
- The businesses that are earning by sale in a country where their physical presence is less significant in the past, thereby challenging the relevance of existing rules that determine tax liabilities based on physical presence of the business at the time of framing tax policies.
 - The businesses that are utilizing the contribution of users in their value chain for digital products and services through collection and monitoring of data, which raises the concern of attribution and validation of contribution made by users.

Figure 1: Three Challenges



In order to overcome these challenges various measures are being suggested in Annual Report, Addressing the Tax Challenges of the Digital Economy, which are being followed by some of the countries as found useful.

Need of digitalization of taxes necessary and impact of digitalization on international tax matters

Paying taxes involves a cumbersome process where one needs to fill up different types of forms and it is usually done with the help of an accountant. It is difficult, if not impossible, for people to handle their tax returns all by themselves as it requires complex calculations. Modern problems require modern solutions and digitization of taxes can change all aspects of taxation. A structured tax administration

could simplify this enormous problem. An automatic process which is user-friendly would make life easier for everyone. Digitalisation helps in improving process efficiency and data transparency. If the information is effectively analysed by tax administrators, they could offer more efficient services. Current tax system is out of date and full of loopholes. The biggest challenge that needs to be tackled is of BEPS. People and businesses evade taxes. Some companies shift their profits to low-tax environments or geographical locations.

The following problems could be cured through digital transformation of taxes:

- Greater demand for transparency

- Massive data piling up, which makes access to certain information difficult
- *Low compliance*: A huge gap in technology between how businesses operate and how public enterprises work. There are too many regulations on public sector and they lack digital skills.
- *Tax frauds*: People evade taxes because of poor administration of tax returns and filings.

Digital data could help in analysing economic trends and reading effects of policy changes on certain variables. There are certain benefits of tax payers like multiple payment methods and low probability of errors in filing of tax returns. Refunds would be faster and access to any information would be easier. Governments would benefit in terms of increased tax compliance, increased tax revenue, reduced operational costs, and improved audit efficiency. Digital transformation has a potential to push economic growth as well.

A joint and co-operative effort by OECD countries to counter BEPS has been made time and again. They published an action plan to ensure that the multinational companies with minimal physical presence in a country should be taxed where the economic activity is taking place and value is added. Once digitalisation is achieved, international tax concerns would be easier to deal with. This action plan would help in solving problem of allocation of taxing rights and problem of double taxation in two different countries. It also deals with the question of where the taxes should be paid and the amount of taxes to be paid. Enterprises are heavily involved in economic activity of a country without any significant physical presence in that country. Hence, a comprehensive plan, which covers

anti-BEPS laws and taxing rights, would help solve the problems of tax evasion.

Importance of an International Cooperation

International tax cooperation is necessary to strengthen the capacity of the ministries of finance and national tax authorities globally, especially in developing countries so as to achieve effective and efficient tax systems, with a vision to support the desired advances in public and private investment and combat tax evasion. United Nations has established a Committee of Experts on International Cooperation in Tax Matters as a subsidiary body of the Economic and Social Council that is responsible for reviewing and updating the United Nations Model Double Taxation Convention and the Manual for the negotiation of Bilateral Tax Treaties between developed and developing countries when required³. This Committee is responsible for providing a framework to enhance and promote international tax cooperation among different national tax authorities and assessing the ways by which various emerging issues could affect this cooperation. It will give special attention to the developing countries and countries whose economy is in transition, by making recommendations on capacity-building and the provision of technical assistance. Thus, **International tax cooperation has an important role in enhancing** intergovernmental consideration of tax issues that will further simplify the process of tax filing. In addition, tax evasion especially pertaining to the cross-border trade by the suppliers which have a very lesser physical presence in the consumer country for example Facebook, Instagram; international cooperation become necessary to channelize and keep a check.

³ ECOSOC Committee of Experts on International Cooperation in Tax Matters – 15th Session. 2017.

Conclusion

Digitalisation of tax which is emerging as a necessity in the upcoming days is therefore a revolution, associated with various advantages as well as difficulties which are needed to be considered and weighed accordingly. The global implementation of this policy by tax administrations has been initiated by many European countries that are still working on improving its efficiency and

affectivity. Digital transformation of tax administration and tax procedures will further cascade tax system reforms. This digitalisation once achieved, will make the complex task of filing returns easy and thus the goal of the transparency in tax collection and avoiding the tax evasion can be achieved. International trade will become easy with the digitalisation of tax and thus economic growth will shoot at global level.

International trends

Changes in the production, consumption and employment situation in certain major international economies compared with peer expectations and the previous period.

		Period in review	Actual data	Expectations	Previous period
	Unemployment Rate	(Aug)	5.0%	5.0%	5.0%
Germany	Manufacturing Purchasing Managers Index	(Aug)	43.6	43.0	43.2
	IFO Business Climate Index ¹	(Aug)	94.3	95.1	95.8
France	INSEE Business Climate Index ²	(Aug)	105		105
	Unemployment Rate	(Aug)	3.7%	3.7%	3.7%
USA	CB Consumer Confidence Index	(Aug)	135.1	129.5	135.8
	Manufacturing Purchasing Managers Index	(Aug)	50.3	49.9	49.9
China	Manufacturing Purchasing Managers Index	(Aug)	49.5	49.7	49.7

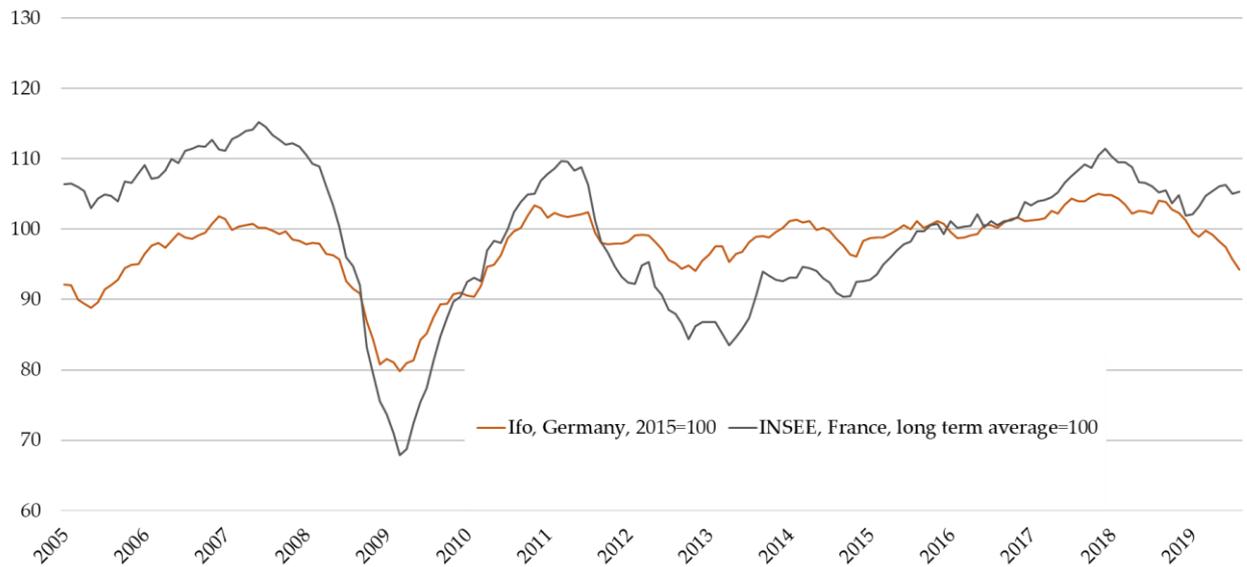
¹ <https://www.cesifo-group.de/ifoHome/facts/Survey-Results/Business-Climate/>

² <http://www.insee.fr/en/themes/indicateur.asp?id=105>

The rest of the data source: <http://worldeconomiccalendar.com>

In Germany, the IFO business climate index continues to decrease and its value was below the expectations in August. The manufacturing purchasing manager index (PMI) shows a slight increase while the unemployment rate stagnates at the same level. The French INSEE business climate index remained at the same level in August as in the previous month. In the United States, the CB consumer confidence index was higher than the expectations this month. The manufacturing PMI slightly increased as well. The unemployment rate continues to stagnate and performed as expected. The Chinese manufacturing PMI slightly decreased in August.

Business confidence in Germany and France,
based on the Ifo and INSEE business climate survey,
January 2005 - August 2019



Sources: www.ifo.de, www.insee.fr

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