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Viet Nam Institute for Economic and Policy Research, formerly known as Viet Nam Center for Economic and Policy Research was founded on July 7, 2008. On August 26, 2014, Viet Nam Institute for Economic and Policy Research was established on the foundation of Viet Nam Center for Economic and Policy Research, keeping the same abbreviation as VEPR. After 10 years of development, on February 12, 2018, VEPR was officially recognized as a Center of Excellence of Vietnam National University.

VEPR is an independent research organization under the University of Economics and Business, Vietnam National University, Hanoi. VEPR has continuously been growing and gaining reputation for thorough economic researches and timely policy discussions.

The main activities of VEPR include (i) provide quantitative and qualitative analysis of Viet Nam's economy issues and their impact on interest groups; (ii) organize workshops for policy dialogue which enable policy-makers, business leaders and civil society organizations to network, exchange then propose solutions to the current key policy's problems; (iii) organize advanced training courses on economics, finance and policy analysis.

One of the most popular publications of VEPR is the *Viet Nam Annual Economic Report,* published annually from 2009.

CONTACT US

Viet Nam Institute for Economic and Policy Research (VEPR)
University of Economics and Business, Viet Nam National University, Ha Noi

Address:	Room 707, E4 Building 144 Xuan Thuy strt, Cau Giay dist Ha Noi, Viet Nam
Tel:	(84-24) 3 754 7506 - 704/714
Fax:	(84-24) 3 754 9921
Email:	info@vepr.org.vn
Website:	www.vepr.org.vn

VIET NAM ANNUAL ECONOMIC REPORT
2020

Edited by Nguyen Duc Thanh & Pham The Anh

CONSOLIDATING THE BASE FOR FISCAL POLICY

ĐẠI HỌC QUỐC GIA HÀ NỘI
TRƯỜNG ĐẠI HỌC KINH TẾ

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AGENDA
LAUNCHING CONFERENCE
VIETNAM ANNUAL ECONOMIC REPORT 2020
CONSOLIDATING THE BASE FOR FISCAL POLICY

Time: 8:00 – 12:00, Wednesday, June 17, 2020
Venue: Sheraton Hotel, No. 11 Xuan Dieu Street, Quang An Dist., Hanoi

08:00 – 08:30	**Registration**
08:30 – 08:35	Welcome and Introduction
08:35 – 08:50	Opening Speeches Welcome Remarks by *Assoc. Prof. Pham Bao Son, Vice President, Vietnam National University – Ha Noi (VNU).* Openning Remarks by *Assoc. Prof. Nguyen Truc Le, Rector, VNU University of Economics and Business (VNU – UEB).* Congratulations Remarks by *Prof. Dr. Andreas Stoffers, Country Director of FNF Vietnam.*
08:50 – 09:30	Presentation on the contents of the Vietnam Annual Economic Report 2020 *Dr. Nguyen Duc Thanh – Chief Adviser, VEPR* *Assoc. Prof. Pham The Anh, Chief Economist, VEPR*
09:30 – 10:15	Comments from Experts *Dr. Can Van Luc, Chief Economist of BIDV, Director of BIDV Training and Research Institute* *Mr. Nguyen Van Phung, Head of Department, Large Taxpayers Department, General Department of Taxation* *Assoc. Prof. Vu Sy Cuong, Academy of Finance*
10:15 – 10:45	**Tea break**
10:45 – 11:55	Open discussion between the Report's Contributors and the Audience. *Chair: Assoc.Prof. Nguyen Anh Thu, Vice Rector VNU University of Economics and Business and President of VEPR*
11:55 – 12:00	Closing Statement by the Leader of VNU - UEB
12:00 – 13:00	Luncheon at the hotel

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HANOI, June 2020

CONSOLIDATING THE BASE FOR FISCAL POLICY

Vietnam Annual Economic Report 2020

CONSOLIDATING THE BASE FOR FISCAL POLICY

Contact:

VEPR

Viet Nam Institute for Economic and Policy Research (VEPR)

University of Economics and Business, Viet Nam National University, Ha Noi

Address:	Room 707, E4 Building, 144 Xuan Thuy street, Cau Giay district, Cau Giay, Viet Nam
Tel:	(84) 4 37547506 – ext: 704
Fax:	(84) 4 37549921
Email:	info@vepr.org.vn
Website:	www.vepr.org.vn

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ABOUT VEPR

VIET NAM INSTITUTE FOR ECONOMIC AND POLICY (VEPR), formerly known as Viet Nam Centre for Economic and Policy Research, was established on July 7, 2008 as a research centre under the University of Economics and Business, VNU. VEPR has legal status and is headquartered at the University of Economics and Business, Xuan Thuy, Cau Giay, Ha Noi.

VEPR considers its primary mission to be carrying out economic and policy research to assist in improving the decision-making quality of policy-making institutions, enterprises, and interest groups by providing insights into the social, political, and economic factors that drive the economic affairs of Viet Nam and the region. The main activities of VEPR include (i) providing quantitative and qualitative analysis of changing economic conditions in Viet Nam and assessing their impacts on various interest groups throughout the country, (ii) organizing policy dialogues among policy-makers, entrepreneurs, and other stakeholders to improve solutions to emerging issues, and (iii) conducting advanced training courses in economics, finance and policy analysis regularly and upon request.

Since 2018, VEPR has been awarded the status of the VNU Centre of Excellence by the President of the Viet Nam National University, Hanoi.

According to the *2019 Global Go To Think Tank Index Report* conducted by the University of Pennsylvania, VEPR was ranked 59th among top 107 think tanks in the Southest Asia and the Pacific.

CONTRIBUTORS

(Alphabetical order)

Assoc. Prof. Dr. Pham The Anh: MSc and PhD in Economics at The University of Manchester in 2003 and 2007 respectively. He is a senior lecturer in Macroeconomics at the National Economics University cum Chief Economist at Thang Long Securities Company; The head of macroeconomics at the National Economics University. Dr. Pham also takes charge of chief economist of VEPR now.

Ha Thi Diu: Bachelor of Economics at National Economics University and Researcher of Macroeconomic Research Team, VEPR.

Dr. Nguyen Tien Dung: PhD in Development Economics from Nagoya University (Japan); lecturer of the Faculty of International Business and Economics, University of Economics and Business, Viet Nam National Economics Uinversity, Ha Noi.

MSc. Nguyen Duc Hung: MSc in Development Economics of Vietnam Netherlands Programme, National Economics University; working for FPT

MSc. Nguyen Dieu Huyen: MSc in MSc Finance and Economic at University of Southampton, UK; Researcher of Macroeconomic Research Team.

MA. Pham Van Long: MA in the Master in Public Policy, major in Policy Analysis from Fulbright School of Public Policy and Management, Fulbright University Vietnam; researcher of the Microeconomic Research Team, VEPR.

MSc. Nguyen Hoang Oanh: MBA in CFVG and AIT, Thailand, and PhD in Economics at Vienna University of Economics and Business; lecture of National Economics University
Nguyen Quang Thai: BA with Distinction in Corporate Finance from National Economics University; yong Scientist Awards in ministerial level in 2012, Reseacher in Oxfam.

Dr. Nguyen Duc Thanh: PhD in Development Economics from the National Graduate Institute for Policy Studies (GRIPS), Tokyo, Japan, 2008. He was a member of the Economic Advisory Group for the Vietnamese Prime Minister (2011-2016) and president of VEPR (2008-2/2020). He is currently Chief Adviser of VEPR.

MA. Hoang Thi Chinh Thon: MA in the Master in Public Policy, major in Policy Analysis from Fulbright School of Public Policy and Management, Fulbright University Vietnam; lecture of National Economics University.

MA. Pham Thi Ngoc Quynh: MA in Public Management at University of Antwerp, Belgium, lecture of National Economics University.

BOARD OF ADVISORS AND COMMENTATORS

(Alphabetical order)

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Dr. Le Dang Doanh (Senior Economic Expert, Former President of Central Institute for Economic Management, member of the United Nations' Committee for Development Policy)

Dr. Le Hong Giang (Director of Foreign Exchange Fund, Tactical Global Management)

Assoc. Prof. Dr. Phi Manh Hong (Senior Lecturer at Faculty of Development Economics, University of Economics and Business, VNU)

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Dr. Vu Viet Ngoan (Head of Prime Minister's Economic Advisory Group (2016 to present), Former Chairman of National Financial Supervisory Commission of Viet Nam)

Dr. Le Hong Nhat (Senior Lecturer at University of Economics and Law, VNU - Ho Chi Minh City)

Mr. Nguyen Van Phung (Head of Deparment, Large Taxpayers Department, General Department of Taxation)

Assoc. Prof. Dr. Nguyen Hong Son (Deputy Director of the Central Economic Committee of the Communist Party of Viet Nam)

Assoc. Prof. Dr. Pham Bao Son (Vice President, Vietnam National University)

Prof. Dr. Sc. Nguyen Quang Thai (Standing Vice President cum General Secretary of Viet Nam Economic Association)

Dr. Vo Tri Thanh (Senior Economic Expert, Former Vice President, Central Institute for Economic Management)

Assoc. Prof. Dr. Nguyen Anh Thu (Vice Director, University of Economics and Business, VNU)

Mr. Truong Dinh Tuyen (Senior Economic Expert, Commissioner of National Council for Financial and Monetary Policy, Former Head of Prime Minister's Economic Advisory Group (2011-2016))

Dr. Dinh Quang Ty (Senior Research Fellow of Viet Nam Communist Party's Central Theoretical Council)

EDITING TEAM

Nguyen Duc Thanh	Nguyen Dieu Huyen
Pham The Anh	Pham Van Long
Ha Thi Diu	Dang Thi Bich Thao

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One of the most important contributions that must be mentioned is from the ***Board of Advisors and Commentators***, who have participated in many discussions, workshops, and seminars during different stages of the *Report*. Special thanks are due to Dr. Đinh Quang Ty, Assoc Prof. Dr. Phi Manh Hong, Dr. Can Van Luc, Assoc. Prof. Dr. Vu Sy Cuong, Assoc. Prof. Dr. Nguyen Anh Thu, Assoc. Prof. Dr. Nguyen Quoc Viet for their deep analyses and constructive feedback on each chapter of the *Report*.

We are grateful to the the Friedrich Naumann Foundation (FNF), Viet Nam for their generous support and fruitful cooperation in various aspects, especialy the sponsorship for the Conference launching this *Report* on June 2020.

We are greatly helped by VEPR staffs, especially the ***Editing Team***. Their enthusiasm, dedication, and persistence are an indispensable part of this Report.

We would like to express our gratitude to the members of the Department of Science and Technology at VNU in Ha Noi, and the Department for Research and International Relations at the University of Economics and Business for their enthusiastic support during the project.

Despite our efforts, we understand that there may be limitations and even errors in the *Report*. We sincerely hope to receive comments and contributions from the readers to improve our upcoming reports.

Ha Noi, Jun 17th, 2020

On behalf of the Contributors

Dr. Nguyen Duc Thanh and Assoc. Prof. Pham The Anh

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LIST OF ABBREVIATIONS

ADB	Asian Development Bank
ASEAN	Association of Southeast Asian Nations
ATAD	Anti–tax Avoidance Directive
BEPS	Base Erosion and Profit Shifting
BoJ	Bank of Japan
BRICS	Group of Brazil Russia India China and South Afica
CbC	Country – by – Country report
CFC rule	Controlled Foreign Corporation rule
CIT	Corporate Income Tax
CNY	Chinese Yuan
COVID-19	Corona Virus Disease -19
CPI	Consumer Price Index
EBITDA	Earnings Before Interest, Tax, Depreciation and Amortization
ECB	European Central Bank
EIA	U.S. Energy Information Administration
EU	The European Union
EUR	European Currency
EVFTA	EU-Vietnam Free Trade Agreement
FDI	Foreign Direct Investement
Fed	Federal Reserve System
FIA	Foreign Investment Agency
FRED	Federal Reserve Bank of St. Louis
FTA	Free Trade Agreement
GAAR	General Anti–Abuse Rule
GBP	The British Pound Sterling
GDP	Gross Domestic Product
GEP	Global Economic Prospects
GINI	GINI index
GSO	General Statistics Office of Vietnam
GTA	Germany Trade & Invest
IDR	Rupiah Indonesia
ILO	International Labour Organization
IMF	The International Monetary Fund

IPI	Industrial Production Index
JGB	Japanese Government Bond
JPY	Japanese Yen
M&A	Mergers– Acquisitions
MIC	Made in China 2025
NEER	Nominal Effective Exchange Rate
OBI	Open Budget Index
ODA	Official Development Assistance
OECD	Organization for Economic Co-operation and Development
PBoC	People's Bank of China
PCI	Provincial Competitiveness Index
PIT	Provincial Competitiveness Index
PMI	Purchasing Managers' Index
PPP	Purchasing Power Parity
PTA	Preferential Trade Agreement
qoq	Quarter on Quarter
QUAD	Group of USA, Australia, Japan and India
SBV	The State Bank of Vietnam
TCJA	Tax Cuts and Jobs Act
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
USD	US Dollar
USTR	United States Trade Representative
VAT	Value-Added Tax
VCCI	Vietnam Chamber of Commerce and Industry
VND	Vietnamese Currency
WB	World Bank
WDI	World Development Index
WEF	World Economic Forum
WEO	World Economic Outlook
WTI	West Texas Intermediate
WTO	World Trade Organization
yoy	Year On Year
Ytd	Year To Date

EXECUTIVE SUMMARY

Vietnam Annual Economic Report 2020 has been conducted in the context of a global economic slow down due to COVID-19, with which, Vietnam's economic growth in the first quarter of the year was slower than the same period last year. Due to the impacts of this pandemic, along with the increasing tensions among many countries around the world, trade flows, investment flows, and especially global supply chains are strongly diverting, making the global outlook more uncertain than ever. As Vietnam continues to deepen in international integration and is increasingly sensitive to external forces, our tax system could be eroded rapidly under the pressure of international competition. This year's report, titled "*Consolidating the Base for Fiscal Policy*", focuses on the Vietnamese tax system in both regional and global contexts, thereby pointing out opportunities and challenges to our fiscal system in supporting the sustainable development of the economy.

In the Report, the first two chapters give an overview of the current world economy and Vietnam's economy, the next four chapters deal with in-depth analyses of some aspects of the taxation system in Vietnam and provide several notices of the other taxation systems in ASEAN countries, thus, identify the new opportunities and challenges for the Vietnam's economy during and after this crisis. In particular, chapter 3 presents an overview of the structure and features of the taxation system in Vietnam and reports the performance of the budget revenue system in accordance with the international integration process, ever since the country's newly declared membership in WTO (2007 onward). Chapter 4 generally describes common macroeconomic standards of ASEAN countries to observe the difference between countries and the need to supervise all the tax incentives on the enterprise income tax across nations. Chapter 5 provides an estimation of the tax expenditure from the corporate income tax in Vietnam and gives an evaluation of the effect of tax exemption. Chapter 6 deals with an overview of the tax avoidance and evasion behaviors, and legal framework to regulate this kind of behavior in Vietnam. Finally, chapter 7 presents three scenarios for the Vietnamese economic outlook for 2020 and provides policy recommendations for short-term, medium-term and long-term development.

A REVIEW OF THE WORLD ECONOMY IN 2019

World economy was growing tardily during 2019 at the rate of 2,4% which was lower than the rate of 3% of 2018 (World Bank, 2020). This was the lowest growth rate since the Financial Crisis 2007-2008. The decline of investment and international trade is regarded as the primary factor leading to the sluggish growth rate in 2019. In particular, this decrease in investments and trade was due to the effect of U.S.-China trade war and the follow-up trade protectionism policies, economic and political tension in some emerging economies, tightened credit policies and the promotion of consuming domestic goods in China. Global FDI in 2019 fell 1,3% more in value than 2018. Global political tensions and lack of businesses confidence are responsible for the stagnation of investment. Particularly, the FDI dropped in all of the markets including mergers & acquisitions and greenfield investments.

The growth rate of international trade in 2019 was 1,4%, down from 4% in 2018. Several complex crises that led to this decline could be named: the U.S.-China trade war, different perspectives between nations in the G20 meeting, and the struggle of the WTO in the multilateral trade's adaptation. There was a likelihood of an expansion in trade protectionism. Although the U.S. and China have passed the first stage of a trade agreement, many conflicts between the two countries remain unsolved and the trade protectionism gives no signal of declining in the future. The Europe is internally tearing apart, conflicts between the largest economies are unsolved, along with ongoing regional and political clashes of disagreement, etc… These events continue to have negative effects on the global economy.

Trade protectionism signaled an upward trend in 2019. According to Global Trade Alert, in 2019, the number of trade discrimination measures has been increased by 429 while the number of these measures but with the focus on liberalization has been increased by only 101 (GTA, 2020). The total number of trade intervention measures regarding protectionism was 1050 in 2019, equivalent to that number in 2018, and was nearly 70% higher than the number in 2015, 2016, and 2017 which were all approximately 600. During 2017 - 2019, China and the U.S. were making 23% of the new trade protectionism measures each year whereas, in the previous years, this rate was about 12% (GTA, 2019).

The price of crude oil generally ranged from 50 to 60 USD/barrel during 2019 and significantly decreased at the beginning of 2020. The price of WTI, on average, reached 57 USD/barrel in 2019, which was lower than its average value in 2018. In the first quarter of 2019, oil price tended to slightly increase due to the effort of cutting the oil supply from the OPEC and Russia. In the second quarter, oil price varied because of the tension in the Middle East and the flood of the Midwest, causing the oil delivery industry to struggle. In September, the largest oil production infrastructure in Saudi Arabia was attacked by drones and this led to a decline in oil supply. The event that the U.S. assassinated general Qassem Soleimani of Iran worsened the interruption of oil demand and potentially made the price much higher at the end of the year. Economic sanctions acted on Venezuela by the U.S. were damaging the oil exporting industry of these two nations, forcing higher oil prices. However, the upward pressure on oil prices was reduced because the U.S. increased the oil production.

Other than the damages from the COVID-19 pandemic, the global economy in 2020 continues to suffer from many difficulties such as geopolitical tension or unpredictable moves in terms of trade conflict between the United States and other partnership countries, especially the tension between the U.S. and China (which is likely to escalate after the pandemic). These shocks will affect the growth of international trade, weaken economic activities, disturb the global value chain and the FDI flows from pivotal countries, and, thus, affect global economic growth. In this economic hardship, UNCTAD (2020b) forecasted in March that global FDI could decrease by 30-40% during 2020-2021 due to the contraction of and investment cross-border M&A. The tendency for an acceleration of new trade protectionism measures along with a gradual loss of trust in globalization after the crisis could lead to a further fall of investment in many countries. This means the capital in the developing countries could flow back to the developed countries.

For the international financial market and assets market, the negative effect of COVID-19 has caused the central banks to stay defensive, with the main aim is to protect the economy instead of focusing on growth in the meantime. In 2020, there will be more aid and stimulus packages to support enterprises and individuals. Negative interest rates could be more popular worldwide in 2020 due to the sloppy economic outlook.

Despite the gloomy economic prospect caused by COVID-19, this could be a time for a restructure of the economy with new possible directions. Social distancing and remote working could bring about new motivations for growth.

AN ASSESSMENT OF THE VIETNAMESE ECONOMY IN 2019

While the world economy decelerated, Vietnam's economic growth in 2019 still reached an impressive rate of 7.02%. The most notable point in 2019 is that the General Statistics Office recalculates GDP, with which the scale of the economy increased by 25%. However, according to the GSO announcement, this new calculation method would only be applied since 2021. The main contributors to growth are the industrial & construction sectors (50.4%) and the service sector (45%). PMI has the 49th month at over 50 points, marking the continuous expansion of the manufacturing sector. On investment, the FDI sector is still the fastest growing sector in all aspects (production value, exports, and job creation). In 2019, the number of employees working in industrial enterprises increased by 2.8%, higher than the previous year (2.6%). In particular, labor in non-state enterprises increased by 1.4%, while labor in the FDI sector increased by 4.3%. The country had 138.1 thousand newly established enterprises, up 5.2% compared to 2018. The average registered capital per newly established enterprise reached 12.5 billion dong, 11.2% higher than the previous year. Meanwhile, the total number of temporarily suspended enterprises decreased to only 72.4 thousand.

Compared to 2018, the retail and commodity retail services of 2019 are much improved in both value and quantity. The total value is estimated at 4,940.4 trillion VND, up 11.8%. In particular, the retail volume (excluding price factor) increased to 9.2%. Total social investment capital at current prices in 2019 is estimated to increase by 10.2% over the previous year. Of which, capital from the state-owned sector (accounting for 31% of the total capital) increased by 2.6% over the previous year, the non-state sector (accounting for 46%) increased by 17.3%; the FDI sector (accounting for 23%) increased by 7.9%. The private sector has shown an increasingly important role in the structure of social investment capital. In general, state investment has been gradually narrowed along with the process of restructuring state-owned enterprises since 2015. Total disbursed FDI increased by 6.7% over the same period in 2018. The amount of newly and additionally registered capital figs in 2019 continues to fall. There are 3883 newly granted FDI projects, an increase of 27.5% compared to 2018. The processing and manufacturing industry is still the sector attracting the most FDI capital with the total registered capital accounting for 72.2% of total newly registered capital. Korea is the leading investment partner in 2019 with a total registered capital of 3.66 billion USD.

By the end of the year, the trade balance had a surplus of about 9.9 billion USD, nearly 2 times the surplus of 2018. Total exports and imports respectively increased by 8.1% and 6.3% compared to 2018. Similar to previous years, exports from FDI enterprises increased by 4.2%. FDI sector still accounted for the largest proportion of export, but the share has decreased to 68.8% of total exports. Exports from the domestic sector have significantly improved, increased by 17.7% (yoy). For the whole year of 2019, the FDI sector had a trade surplus of 35.85 billion USD, while the domestic sector had a trade deficit of 25.91 billion USD. Crude oil export continued to decline, reaching only 2.02 billion USD. The US continues to be Vietnam's largest export market with a turnover of 60.7 billion USD, up 27.8% compared to 2018. China is still the largest import market with a turnover of 75.3 billion USD, increasing by 14.9%.

In 2019, the average CPI increased by 2.79% (yoy), lower than the increase of 3.54% in 2018, and still below the 4% threshold set by the Government. The major contributor to the increase of CPI in 2019 is the sharp increase in the price of food. Interbank interest rates increased at the end of the calendar year and traditional New Year when the capital demand of enterprises and consumer demand increased. In 2019, deposit rates of commercial banks remained relatively stable at 5% p.a for the first nine months of the year and only slightly decreased at the end of the year due to the SBV's lowering of policy rates. Meanwhile, lending rates remained high, around 7-9%. The money supply in 2019 increased by 12.10%, still high compared to other countries in the region. Deposit growth in 2019 reached 12.5%, higher than in 2018. Credit growth was only 12.10% - the lowest in the last five years. The VND / USD exchange rate was relatively stable in 2019.

Budget revenue is still not sufficient to offset the budget expenditure. The budget deficit of 2019 is estimated to be 209.5 trillion VND, equivalent to 3.4% of GDP, lower than the estimate approved by the National Assembly at the beginning of the year (3.6%). The budget deficit in 2019 increased compared to 2018 due to increasing recurrent expenditure. The structure of budget expenditure did not improve, as spending on development investment only accounted for a small proportion (below 30%).

In general, Vietnam's economy in 2019 continued to fulfill the socio-economic targets set by the National Assembly. GDP growth for the whole year reached 7.02 %. The annual average inflation was 2.79%, lower than the target (4%). International trade and investment are growing. The money market, capital market, and exchange rates are stable and under control. The budget deficit and public debt also showed certain improvements. However, the aforementioned successes are based on a macroeconomic foundation that is still uncertain and carries many potential risks. Firstly, economic growth, exports, and employment are increasingly dependent on the FDI sector and a few FDI enterprises. Secondly, the private business sector has not grown and is still subject to many barriers from the domestic institutional and business environment. Thirdly, the monetary policy space is gradually narrowed by increasing inflationary pressures as well as by the exchange rate commitments. And finally, fiscal policy does not create positive changes in the structure of budget revenues, while high public debt, budget deficits, and state assets are increasingly declining. This means that Vietnam is lacking fiscal buffer to cope with external shocks.

Given these outstanding issues, the Government and ministries need to continue to focus on cutting unnecessary business conditions, to improve the business environment and to overcome domestic shortcomings. The Commission for the Management of State Capital at Enterprises (CMSC) should set the central task of reducing the focal point of management, removing obstacles to promote the equitization of SOEs. Second, monetary policy needs to adapt promptly to economic fluctuations. The top priority is flexible exchange rate management, to absorb the impact of external shocks. Interest rates should be kept stable to facilitate businesses' access to the capital market. Third, at a longer-term level, Vietnam needs to gradually build a fiscal buffer, first through streamlining the state hierarchy and cutting down on recurrent spending.

CHARACTERISTICS OF THE BUDGET REVENUES OF VIETNAM IN THE INTERNATIONAL INTEGRATION PROCESS

As a transforming economy, Vietnam now is taking robust steps to change the ideology of economic management and operation. The Government has made increasingly tight commitments in opening markets and developing the private sector. Taxation is one of many fields that have witnessed a major reform since the opening of the economy and the implementation of Doi Moi (renovation) in Vietnam. In general, Vietnam's current tax system is comparable to that of other nations with conventional market economies. However, have the tax policies in Vietnam been able to ensure fairness, and, if yes, to what extent? Has the tax system succeeded in regulating the revenues substantially? Are the tax administration procedures conducted transparently enough? What is the further guidance needed to improve the tax system?... These are very important and foundational questions that need to be addressed with respect to our current taxation system. Chapter 3 of the report will answer these questions one by one.

The Law on State Budget promulgated by the National Assembly in 2015 regulates that all the sources of revenue in Vietnam must follow certain common regulations at the central level. Local authorities are not allowed to propose taxes and fees by themselves. All the tax revenues, especially taxes, charges, and fees, are entitled to official legal documents guiding the implementation so that local systems can consistently be enforced nationwide. The relative scale of the state budget with respect to GDP tends to decrease. On average, during the period of 2006-2019, the state budget revenue accounted for approximately 25.16% of GDP. The instability in the share of total state budget revenue to GDP primarily occurred during 2010-2019. Similarly, the tax revenues declined from 22.2% GDP (2006) to 17.8% GDP (2019). Over the past few years, the growth rate of total revenues tends to reduce. Compared to the period of 2006-2011 when the average growth rate per person reached 17.4%/year, the period of 2012-2019 witnessed a downward trend to only 7.2%/year.

In terms of tax structure, the proportion of indirect tax in the total tax revenue has increased substantially up to more than 60% while the direct tax accounts for less than 40% (despite a high increase in the absolute value). This led to a decrease in the progressive property of Vietnam's taxation system. In comparison with other nations of the ASEAN-5 and OECD, the percentage of tax revenue to GDP in Vietnam was lower than that of OECD countries but higher than that of ASEAN-5 countries. The share of direct tax in Vietnam was much lower than OECD but ranked second among the ASEAN-5. By contrast, the share of indirect tax to GDP in Vietnam was higher than that of the OECD nations and ranked number two in the ASEAN-5 group. Furthermore, the proportion of fees and charges in the total state budget revenue and total tax revenue substantially decreased during 2009-2011 but tended to grow again during 2012-2019. In the last three years, revenues gained from fees and charges increased robustly with respect to the absolute value. The average growth rate in fee and charge revenues in the 2012-2019 period was about 21%/year. The capital revenue dropped during 2011-2015 and leaned to an increase again soon. Revenues gained from non-refundable ODA only took 1.15% of non-tax revenue in 2019. This result showed that Vietnam's current budget revenue closely depends on indirect tax, especially Value-Added Tax while this tax is highly regressive. Fees and charges are creating a burden on residents. Every proposal on increasing consumption tax, fees, charges needs to be taken into careful consideration due to its influence on the fairness in consumption. Particularly, the Draft Law amending and supplementing a number of articles of the Law on Value-Added Tax, the Law on Fees and Charges are brought to the discussion and adjustment in the future.

Statistics about the number of taxpayers who pay income tax and statistics about the number of enterprises paying corporate income tax are not publicly displayed. Nevertheless, according to the General Statistics Office of Vietnam (GSO, 2020), by December 31st of 2018, there had been 714.8 thousand enterprises that were operating, growing at 9.2% compared to the same period in 2017. In particular, 610.6 thousand enterprises were able to generate revenue (accounting for 85.4%). The proportion of profitable businesses account for 44.1% of total enterprises in 2018, equivalent to about 269.3 thousand enterprises. Despite an increasing number of enterprises and businesses that generate revenue, the share of businesses that made profits was constantly decreasing during the 2016-2018 period. Intuitively, this decline means that there is a decrease in the amount of corporate income tax payable, therefore, negatively influenced the tax revenue. Moreover, the informal sector still remains at large (about 30% GDP of Vietnam in 2017). One of the biggest barriers that prevent them from focusing on upgrading to the enterprise position is that they are required to pay informal fees along with formal fees (up to 40% of the profit).

One of the factors that greatly affect the tax revenue in Vietnam is tax incentives, especially ones applied to the corporate income tax. Many multinational corporations that invested in Vietnam could be imposed with a 10% tax which was as low as half the general tax rate of 20%. The special enterprise phenomenon is when multinational corporations utilize the incentive policies related to corporate income tax in order to avoid tax. This has been popular for a long time but been recently governed closely since 2010. Legal documents on the tax incentives were publicly announced but other information about this matter has yet been recorded, especially the revenue loss in the state budget due to tax incentive has not been recorded and publicly reported. All the analyses of advantages and fees on tax incentives were not performed thoroughly and in detail either.

Along with the information technology innovations in tax management, many major tax reforms in Vietnam over the past few years have emphasized a strong determination to construct a fair and transparent taxation system. Vietnam has made progress in the dissemination of state budget information. In 2019, the country advanced by 14 levels in the Open Budget Index table and ranked

77th among the total of 117 nations chosen for the ranking. This result has assured many certain improvements achieved from the disclosure of state budget information recently. On the other hand, more necessary works are yet to be done. Statistical sets about the state budget published domestically and internationally are not similar in terms of the tax structure. Revenues that are not gained from the state budget are not publicly shown although these accounts are collected following the legal documents such as the Oil Price Stabilization Fund, the Fund for Prevention and control of tobacco harms, the Environmental Protection Fund, etc. The management of tax incentives in Vietnam has caused controversy over its transparency. Due to the mechanism of self-declaration and self-payment of taxes, with the “self-responsibility” mechanism, companies enjoying tax incentives have never been collected, even at the local scale. Other information about enterprises and individuals paying their taxes is not accessible. According to the Law on Tax Administration (Law 78/2006/QH11), individuals and organizations must provide sufficient and necessary information for tax authorities. This piece of information will be kept confidential and only provided for inspection or policy purposes upon request of public authorities. In the coming time, Vietnam needs to encourage the disclosure and transparency of data on state budget revenues and expenditures, including the data on the taxpayers, tax expenditure, especially data on tax incentives in the annual state budget report and ensure the disclosure of this information at a suitable and early time, so as to be in accord with international best practices.

TAX INCENTIVES COMPETITION AMONG ASEAN COUNTRIES: A CASE OF CORPORATE INCOME TAX

Using tax incentives became policy norms in ASEAN countries to encourage domestic investment as well as attract foreign investment. ASEAN countries tend to compete with each other rather than cooperate to promote economic growth, putting concerns on fiscal costs on the side-lines. This is further reinforced by large divergences among ASEAN countries in terms of economic development, macroeconomic policies, and governance. Practices of tax incentives along with large reductions of effective tax rates with incentives are implemented by their own ways, leading ASEAN's tax incentive system to be more complex. Therefore, it is increasingly difficult to discuss among these countries to bring about a mutual agreement in the practice of tax incentives and the level of transparency of providing tax incentives. Chapter 4 investigates these countries’ tax incentives practices, especially via corporate income tax (CIT) by summarizing all of the rules in the legal framework on tax incentives with the featured offers including tax exemptions, tax holiday, preferential tax rates, tax deduction, transfer losses forward and some other tax incentives.

In legal terms, incentives are often stipulated in tax laws and laws on attracting foreign investment. The tax policy in general and the tax incentives in particular are always changed and updated to meet the socio-economic development context of a country. In ASEAN, the tax incentives are also up to date, following the trend of enhancing incentives. In general, the average of the CIT rate in ASEAN countries tends to decrease in the last decade. In 2010, the average of CIT rate in ASEAN countries was 25.1%. Over the next five years, the figure reduced dramatically to 22,6% in 2015. There was then a steady fall in 2020 with only 21,7%. Singapore offers the lowest CIT rate at 17 percent of the taxable income.

Activities and sectors that enjoyed tax exemptions in ASEAN countries are relatively diverse. Lao PDR, Myanmar and Indonesia are three countries that provide tax-exempt for reinvesting activities. In Vietnam and Cambodia, economic activities in the agricultural sector will be exempted from tax. The CIT exemption only granted to approved services projects in Malaysia. Meanwhile, Singapore and Brunei Darussalam offer tax exemptions for SMEs. Tax holiday in ASEAN countries officially lasts from 5 to 20 years depending on the law. The average length of tax holiday in ASEAN countries is about 12 years. Brunei Darussalam and Indonesia are countries with a higher tax holiday period among ASEAN countries. In addition, businesses in ASEAN countries can enjoy at least 50% and up to 100% of tax reduction. Cambodia, Thailand and Indonesia provide the most attractive preferential tax rate among ASEAN countries. Businesses in ASEAN countries are allowed to deduct all reasonable expenses related to production and business activities. Some countries offer an extra tax deduction to activities related to SMEs, training, R&D, export and expanding oversea such as Cambodia, Malaysia, Singapore and Thailand. Vietnam and the Philippines offer an additional deduction for labour expenses. In Malaysia and Singapore, any unutilized tax losses can be carried forward indefinitely and offset against future trading profits. Indonesia provides an extension of tax losses carry-forward for up to ten years. Vietnam, Thailand, Cambodia and Myanmar provide a maximum of five years of losses transfer. While the Philippines offers up to six years of losses transfer, operating losses of businesses in Lao PDR will be deducted for three years. Governments also offer other incentives such as tax credit, investment allowances and depreciation. In the context of Covid-19 pandemic, governments of ASEAN countries had issued some supportive policies to recover business activities, including tax incentive policies. The policies focus mainly on delaying tax payments (Vietnam), tax holidays (Cambodia, Lao PDR and Malaysia) and tax reduction (Indonesia and Singapore).

One of the criticisms often levelled against tax incentives in developing countries is that they are redundant, the same investments would have been undertaken even if no incentives. The lowering of CIT rates is often used as a tool by a government to improve the country’s attractiveness to foreign investors. Tax incentives seem to be effective in attracting investment in

Cambodia and Malaysia. In countries like Indonesia and Myanmar, the relationship among tax incentives and FDI is still widely discussed by experts, they consider to what extent tax incentives are effective to increase investment. Despite generous tax incentives given by the government, the relationship among tax incentives and FDI is limited, even not improved in countries like Brunei Darussalam and the Philippines.

To reduce harmful tax practices and avoid the races to the bottom, ASEAN countries should be restructuring their tax incentives system, enchanhing tranparency on tax incentives and to ward forming a regional mechanisms on tax incentives. At first, the system of tax incentives, especially the incentives for the CIT should be restructuring. Tax law would be most preferable to contain provisions on tax incentives, including eligibility requirements. Redundant and excess incentives need to be removed. As mentioned above, the same investment would have been undertaken even without tax incentives. Therefore, it is not necessary to provide continuous tax incentives. Instead, more important things that ASEAN countries need to do to attract investment are improving the business investment environment, enhancing the quality of infrastructure and especially improving the quality of human resources in the context of rising labour costs. The governments should aim at two objectives: broadening the tax base and harmonizing tax systems among ASEAN members. Tax incentives need to be made public to all investors. Incentives via a separate agreement between the government and investors should be used with caution. In the case of use, the entire content needs to be public. Eligibility requirements for granting tax incentives should be clearly defined and readily verifiable. Failure to do so, it creates unnecessary uncertainty for investors. On the other hand, ASEAN countries should improve tax transparency by publishing tax expenditure in the annual budget. The annual tax expenditure report should include not only the total tax expenditure estimates but also the estimates for each activity. To end and avoid the race to the bottom when offering tax incentives, a minimum tax standard for ASEAN countries should be seriously considered and discussed. This requires ASEAN countries to vigorously reform their tax systems, especially tax laws as mentioned above. The initial cost may be large, but it avoids the heavy and long-term losses of harmful tax practices. Tax revenues will be improved, the ASEAN governments will have more resources to address the inequality issues and ensure that no one is left behind.

VIETNAM TAX EXPENDITURES: THE CASE OF CORPORATE INCOME TAX

Tax expenditure has not been comprehensively recognized in Vietnam and in developing countries. By contrary, in developed countries, tax expenditure has been observed and been publicly available since the 1970s. Tax expenditure, tax evasion, and tax avoidance are the three components of budget losses which policymakers, activists and analysts pay a close attention.

Overall, tax expenditures are tax incentives for a specific group of taxpayers which are outside the bechmark tax system. Thanks to these treatments or incentives, the aforementioned group can be applied a lower tax rate than the general tax rate or have a lower taxable income than the one the benchmark tax system. In another word, tax expenditure is the tax revenue loss due to the application of special terms or mechanisms.

Theoretically, there are three methods to estimate the tax expenditure including revenue foregone, revenue gain, and outlay equivalence. In practice, there are also three widely applied methods to estimate the tax expenditure, including: micro-stimulation model, computable general equilibrium (CGE) model, and conventional accounting or "head count" approach. Due to the data in Viet Nam, the research team employed the method of revenue foregone combining with conventional accounting to estimate the tax expenditures for corporate income tax in 2012, 2014, and 2016. Furthermore, the research team also applied the computable general equilibrium (CGE) model to assess the impacts of the tax expenditure abolition.

The tax expenditure estimate for corporate income tax, based on Vietnam Enterprise Census (VES), was a remarkable number and sharply increased in 2016. The figure was equal to 7% of the total state budget revenues, 30% of corporate income tax revenue, 5% of the total state budget expenditures, and even higher than health expenditure. In 2016, the tax expenditure estimate for corporate income reached nearly 86 trillion VND. That rising by 40% and 50% compared with the figure in 2014 and 2012 respectively. The tax expenditure has two components research team calculated that tax expenditure due to tax reduction was nearly doubled from 34 trillion VND in 2012 and 2014 to VND 64 trillion VND in 2016. The effective tax rate was about 70% of the general tax rate of corporate income tax. In 2012, the general tax rate was 25%, while the effective tax rate was 18.4%. The figures in 2014 were 22% and 16.8%, respectively, and the ones in 2016 were 20% and 13.6%, respectively.

The highest tax expenditure group is foreign-invested and industry (especially manufacturing). To specify, The proportion of foriegn-invested enterprises was about 3% of total positive profit enterprises, but the proportion of tax expenditure of this group was nearly a half (2016). The effective tax rate of manufacturing enterprises was about one fifth of the general tax rate. The proportion of tax expenditure of large foreign-invested (equity is more than 100 VND billion) enterprises in industry sector accounted to 41% of total tax expenditure, although the number of this group was only 1% of total positive profit enterprises (about 1.6 thousand enterprises). And the effective tax rate of this group was 8%. And 90% of enterprises of this group is located in zones which are industrial, export processing, economic, and hi-tech zones or parks.

Using the method of revenue gain combining with the computable general equilibrium (CGE) model, the study shows that if the tax expenditure for corporate income tax are removed, the budget revenues might increase by 20%. However, the simulation results also indicate that the removal of tax expenditure might exert both positive and negative impacts on the economy, which depends greatly on the government response. If the government uses this incremental budget revenue to allocate into development projects or to tackle the poverty, that might improve the social welfare and the economic growth. If the majority of the revenue generating from the tax expenditure abolition is allocated into current expenditures, it might not improve the economic growth. If the increase of the value-added tax rate alters the tax expenditure abolition, the household income and consumption might plummet.

Furthermore, the simulation analysis also illustrate that the elimination of tax expenditure for corporate income tax will have adverse effect on the high-income household groups, whom receive the remarkable amount of benefit of tax incentives. If the government uses this incremental budget revenue to allocate into development projects or to tackle the poverty, the abolition might bring significant benefits to low-income households. Thus then the tax expenditure abolition might not have adverse effect on the poverty rate and the GINI index. The regression function of welfare effects of tax expenditure abolition also shows that the least affected households are low-income, female-headed, rural, and self-employed head households.

Finally, although producing astonishing numbers, these calculations also have significant limitations. The Vietnam Enterprise Census data only provides gross accounting profits and the total tax payment of each enterprise. Meanwhile, there is a major difference between tax accounting and ordinary accounting. Moreover, an enterprise can execute many projects in different industries, while tax incentives are often applied for industry. The lack of access to the profit and tax payment by activity is an remarkable problem. Hence, to ensure the accuracy of tax expenditure estimates and contribute to right policy recommendations, the access to tax profile of all enterprises should be the first priority in the following researches.

TAX AVOIDANCE AND EVASION IN VIETNAM: THE CASE OF CORPORATE INCOME TAX

Corporate income tax avoidance and evasion is a global phenomenon that takes place particularly in multinational companies. Tax avoidance is either legal or semi legal acts, exploiting gaps in customs and tax regulations to reduce payable taxes. Tax evasion is illegal acts so that tax liabilities are not required.

There are many channels of tax evasion and avoidance, including: transfer mispricing; strategic location of intellectual properties; international debt shifting; tax treaty shopping; tax deferral; or corporate inversions, etc.

Industry 4.0 or the digital economy produces new business models that reduce the physical presence of businesses, while increase the importance and mobility of intangible assets and increase the integration of the value chain, therefore creating great challenges for the international tax system.

Countries around the world are making great efforts to prevent tax avoidance and tax evasion with a series of tax system reforms. These policies can be divided into two groups: (i) policies towards tightening regulations and; (ii) policies to increase tax transparency.

In Vietnam, tax violations in recent years have occurred not only in corporate income tax but also in other taxes. The businesses with tax violations are not only multinational but also state owned and private. The act of tax fraud is becoming more and more complex, the scope is wider, the scale is bigger and the tricks are increasingly sophisticated.

Vietnam has been making positive changes related to tax laws to integrate more deeply into the regional and global economy, improve the fair competition environment and avoid tax losses. Among them, the most significant is the reduction and simplification of administrative procedures, the issuance of Decree 20/2017/NĐ-CP and the approval of the Law on Tax Administration (amended) 2019, and the signing tax treaties with countries in the region and around the world.

One of the most important findings of this study is that tax policy (through statutory tax rates or tax incentives) plays an important role in influencing tax avoidance and evasion behaviors. The greater the tax burden, the greater the degree of profit shifting. In particular, the response of enterprises in the FDI and non-SOE sectors to the changes in tax policy is much larger than that of SOEs.

Multinational companies have more opportunities, and thus committee more in tax avoidance and evasion, than domestic businesses. Other things being equal, the declared profitability (ROA and ROE) of FDI enterprises tends to be much lower than that of domestic enterprises, regardless of their strength in terms of international market access, technology, or lower capital intensity than SOEs.

On average, in the period of 20103 - 2017, the estimated tax revenue loss due to tax avoidance and evasion each year ranges from 13.3 to 20.7 trillion dong, equivalent to 6.4 - 9.9% of the total corporate income tax revenue. These figures are about 3-4 times larger than the number of detected annually by regulatory agencies. In particular, the estimated annual tax revenue loss from the FDI sector can reach 8.0 - 9.0 trillion dong (4.0 - 4.5% of CIT revenue), while the corresponding number of the non-state sector is up to 10.5 trillion dong (5% of CIT revenue).

Vietnam should continue to maintain and improve existing policies, and study and develop new policies that are widely applied and recommended by developed countries and international organizations. Such policies may include: gradually tightening the ceiling of tax deductible interest expenses of associated companies; regulations aimed at preventing tax base erosion and thin capital; abolish excessive tax incentives; enhance information exchange with other countries, improve database for tax administration purposes; implement tax administration regulations for e-commerce, digital-based business, and other services performed by suppliers in foreign countries without permanent establishments in Vietnam; incorporate issues of tax competition, tax incentives, and tax avoidance and evasion to ASEAN's agenda to raise awareness and initiate regional discussions on these topics.

VIETNAM'S ECONOMIC PROSPECT IN 2020 AND POLICY IMPLICATIONS

In addition to the medium-term policies that incorporate the proposed policy views in the thematic chapters of the Report, Chapter 7 provides three forecast scenarios for Vietnam's macroeconomic perspective for the year. 2020 and some detailed discussions of short-term policies are in place today.

Vietnam's economic outlook in 2020 and beyond depends on the ability to control the disease, both domestically and globally. Vietnam's economy is facing many opportunities and well as challenges. Factors that can support growth for the rest of the year include: (i) Free Trade Agreement and Investment Protection between Vietnam and the European Union (EVFTA and IPA)) has been completed and approved, and will take effect from August 1, 2020; (ii) Progress of disbursement and construction of key public investment projects is accelerating; (iii) Costs of raw materials and fuels remain low due to the declining global demand and production; (iv) Opportunity to receive the flows of investment, as foreign investors attempt to disperse risks from the US-China trade war, while taking advantage of FTAs, cheap labor, tax incentives, and lax environmental management in Vietnam; (v) Inflation rate is moderate, creating favorable conditions for the implementation of macroeconomic policies to support growth.

Nevertheless, Vietnam is also facing many risks and challenges in an unstable global economic landscape. The risk of a second wave of COVID-19 infection with the possibility of further blockade measures and supply chain disruption is still present in many major economies around the world. In addition, geopolitical conflicts between large countries can cause a largely open economy like Vietnam to suffer regardless of the victory in favor of either side. In addition, the domestic macroeconomic condition is still weak, not much improved compared to previous years with chronic problems such as: high fiscal deficit, low budget for development investment; insufficiently improved health of the banking - financial system; the heavy dependence of growth on the FDI sector; labor force is high in quantity but low in quality; low efficiency of public investment and widespread corruption; the delayed equitization process of SOEs; inadequacies regarding institutional and business environment. These shortcomings, if not improved soon, will not only hinder short-term recovery, but also adversely affect the stability of Vietnam's economy in the long term

Taking into consideration the positive as well as the negative factors affecting the Vietnamese economy today, we make forecasts of growth and inflation under different scenarios regarding different possibilities of disease control. With the removal of the social distancing earlier than expected (from the end of April compared to the expected end of May before), we update the Vietnam's economic growth to be higher than the previous forecast. The most optimistic scenario is based on the assumption that the disease was completely controlled domestically by the end of April and the economic activity gradually returned to normal. Meanwhile, the world has begun to relax blockade measures since the beginning of June, helping Vietnam's goods export industry grow well in the second half of the year. However, economic activities in the field of tourism, accommodation and passenger transport are still reserved and only gradually recover. The worst impact of COVID – 19 will be in the second quarter. With this optimistic scenario, Vietnam's economic growth is forecast to reach about 5.3% in 2020. With neutral and pessimistic scenarios, epidemics (in many important economic and financial centers around the world) is presumed to recur and countries must extend the blockade period to the second half of the third quarter, even the fourth quarter of 2020. The impact of COVID – 19 on agriculture, forestry & fishery, manufacturing sector and service sector will be more serious. Economic growth in 2020 might be only 3.9% in the neutral scenario, or just 1.7% in the pessimistic scenario.

Finally, Chapter 7 summarizes the medium-term policy implications analyzed in the in-depth study chapters of the Report.

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Vietnam Annual Economic Report 2020

Consolidating the Base for Fiscal Policy

Ha Noi, Jun 17, 2020

Good Policy, Sound Economy

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Looking back on the 12-year journey

of

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Dr. Tu Thuy Anh
Assoc. Prof. Dr. Pham The Anh
Ms. Jessica Atherton
Dr. Lucy Cameron
Mr. Shasi Kant Prasad Chaudhary
Mr. Nguyen Huu Chi
Assoc. Prof.Dr. Vu Sy Cuong
Mr. Tran Manh Cuong
Dr. Pham Van Dai
Dr. Vu Pham Hai Dang
MA. Vu Hoang Dat
MA. Hoang Xuan Diem
Ms. Ha Thi Diu
Dr. Laure Pasquier Doumer
Dr. Tran Viet Dung
Dr. Nguyen Tien Dung
Dr. Nguyen Binh Duong
Dr. Yamauchi Futoshi
Dr. Le Hong Giang

PhD. st. Nguyen Khac Giang
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Dr. Quach Mach Hao
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Nguyen Duc Hieu
Assoc. Prof. Dr. Ha Van Hoi
Dr. Nguyen Thi Minh Hue
Dr. Nguyen Quoc Hung
Dr. Nguyen Manh Hung
MA. Pham Thi Huong
Dr. Vu Thanh Huong
Dr. Ken Itakura
MA. Pham Bao Khanh
Assoc. Prof. Dr. Nguyen Viet Khoi
MSc. Bui Ha Linh
Ms. Bui Thi Thuy Linh
PhD. st. Vu Minh Long

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MA. Pham Van Long
Dr. Edmund Malensky
Dr. Nguyen Thi Minh
Mr. Dinh Tuan Minh
MA. Pham Tra My
MA. Nguyen Thi Linh Nga
MA. Nguyen Thu Nga
PhD. st. Nguyen Hong Ngoc
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Dr. Pham Sy Thanh
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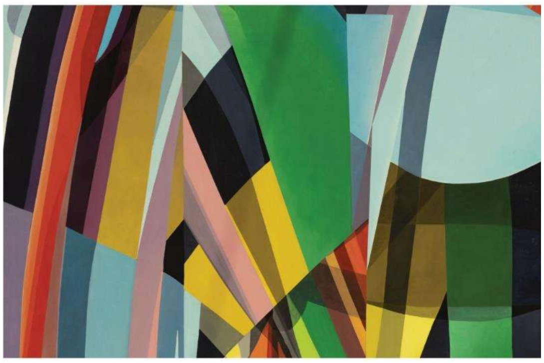
The Context of VAER 2020

- The Vietnam Economic Annual Report 2020, titled "Consolidating the Base for Fiscal Policy" was conducted in the context of strong shifts in trade flows, investment flows, and especially global supply chains, making the global outlook more uncertain than ever. As Vietnam continues to deepen in international integration and is increasingly sensitive to external forces, our tax system could be eroded rapidly under the pressure of international competition. What are the opportunities and challenges to our fiscal system in supporting the sustainable development of the economy in this new situation?

VIET NAM ANNUAL ECONOMIC REPORT
2020

Edited by:
Nguyen Duc Thanh & Pham The Anh

CONSOLIDATING THE BASE
FOR FISCAL POLICY



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VEPR Contributors of VAER 2020

1. Assoc. Prof. Dr. Pham The Anh
2. Ha Thi Diu
3. Dr. Nguyen Tien Dung
4. MA. Nguyen Duc Hung
5. MSc. Nguyen Dieu Huyen
6. MA. Pham Van Long
7. Dr. Nguyen Hoang Oanh
8. Nguyen Quang Thai
9. Dr. Nguyen Duc Thanh
10. MA. Hoang Thi Chinh Thon
11. MA. Pham Thi Ngoc Quynh

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Overview of the World Economy 2019

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Outline

- General remarks
- U.S. economy
- EU economies
- Japanese economy
- Chinese economy
- BRICS economies
- ASEAN economies
- U.S. – China trade war, global trends in international trade and investment
- The world commodities' prices
- World economic outlook 2020

VEPR General Remarks

Global economic growth rate decrease to 2.4% in 2019, lower than 2018 (3%) (World Bank, 2020) due to:

- Weakened international trade and global investment flows
- Trade tension between the US and other countries, especially US – China trade war
- Macroeconomic tensions in some emerging economies
- China's stricter credit policies and expanded domestic consumption policies

VEPR The U.S. Economy

Growth Rate Below Projected Target

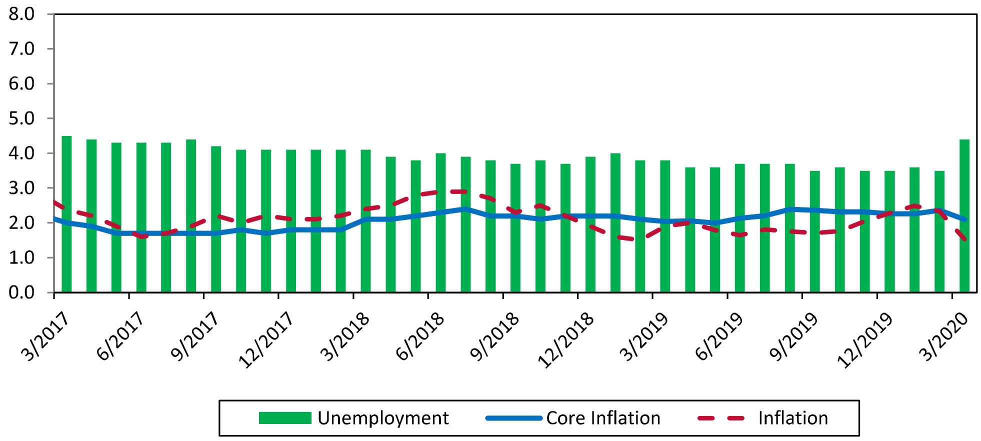
- Growth rate: 2.3% in 2019, much lower than the targeted 3%.
- Trade deficit decreased by 1,7%, in comparison to last year, reached 616.8 billion USD (2,9% GDP). The main reason is attributed to the decline in imports from China.
- Fed terminated monetary policy normalization due to concerns on the slowing down of the global economy and the doubt of the market on the U.S. economic growth. Within 2019, Fed decreased policy rate 3 times in July, September and November.

VEPR

The US Economy
Growth Rate Below Projected Target

- Number of new jobs showed an upward trend since February. The unemployment rate fluctuated under 4% within the year.
- Fiscal deficit reached 1 trillion USD in 2019 and the budget deficit was 1.02 trillion USD, increased 17.1% (yoy) (CBO, 2020)

US's Inflation and unemployment rate , 2017-2020 (%, yoy)



Source: Bureau of Labor Statistics of US (2020), CEIC (2020)

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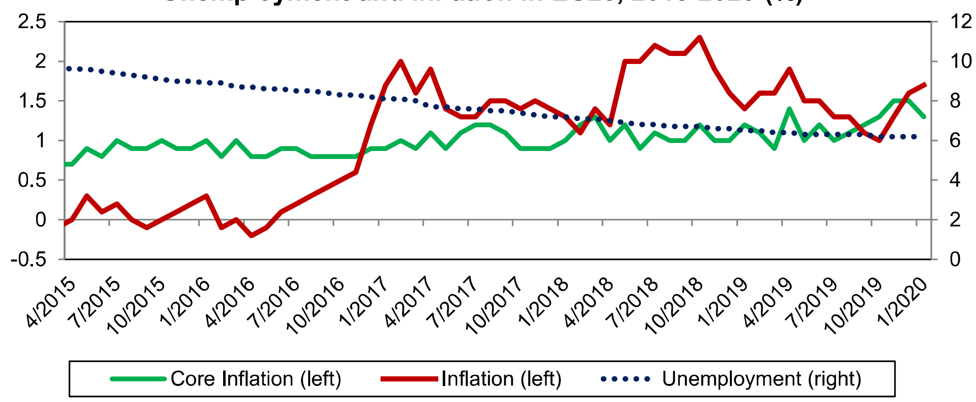
The EU
Weak Economic Growth

- GDP growth in EA19 is estimated to be 1,2% in 2019, the growth rate in EU28 was 1,4% (eurostat, 2020) due to uncertainty around Brexit and the weakening German economy (a result of the decline in German manufacturing sector associating with the drop in demand from Asian market)
- Improved employment in EU28. The unemployment rate gradually declined from 6.5% in Jan to 6.2% in Dec 2019.
- Core inflation fluctuated within 1.1% and 1.5% during the year.

Unemployment and inflation in EU28, 2015-2020 (%)



Source: OECD (2020)

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The UK
Facing multiple challenges

- The UK GDP growth decreased sharply from 2% in Q1 2019 to 1% in Q4 2019.
- Domestic manufacturing weakened, due to delay of investment as the hesitation of Brexit within 2019 deteriorated business confidence.
- Monetary policy was cautious and flexible. Interest rate was kept unchanged at 0.75% for the whole year.

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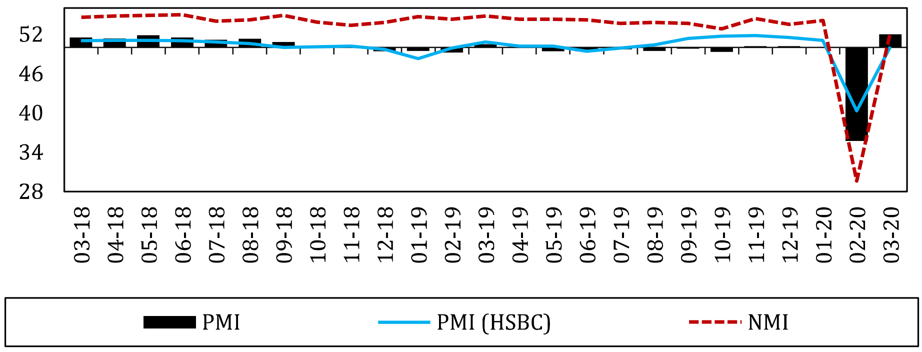
Japan
Lack of motivation for growth

- Growth rate reached 0.97% in Q1, 0.86% in Q2, 1.75% in Q3, and -0.7% in Q4. Annual growth stood at 0,7% (OECD,2020).
  - Stagnation in international trade, as a result of the escalation in US – China trade war
  - Japan – Korea trade tension
  - Japan retail sale index increased sharply in Q3 before dropping in Q4 due to the increase of consumption tax.
  - Shortage of labour supply
- Olympic 2020 was expected to be a "nudge" for the Japanese economy. COVID-19 and the delay of the Olympic 2020 neutralized this motivation.

China
Growth Deceleration

- Economic growth reached 6.1% in 2019, (the lowest level since 1990) due to (i) US – China trade war, (ii) decline of the stock market and monetary market, (iii) unstable real estate market, (iv) high pressure on public debt and (v) NPLs from SOEs.
- PMI fluctuated around 50 for the whole year => Chinese manufacturing sector did not respond strongly with “Made in China 2025” .In the beginning of 2020, COVID-19 significantly hurt the manufacturing sector.

PMI and NMI Indexes of China

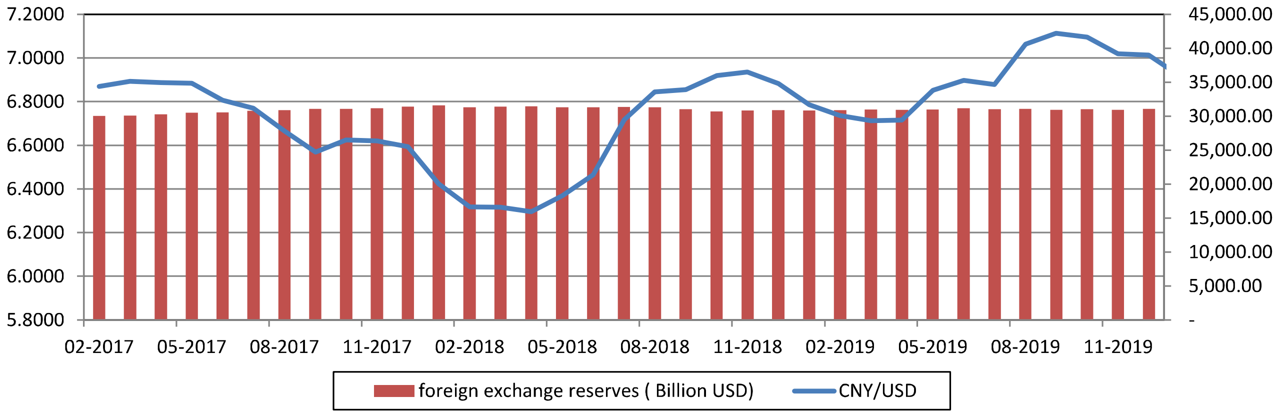


Source: AAStock (2020)

China
Growth Deceleration

- The Chinese government supported economic growth by fiscal stimulus and quantitative easing.
- As Fed decreased policy rate 3 times within 2019, CNY showed an overall upward trend against USD => hindrance for export.

Exchange rate and foreign exchange reserves of China

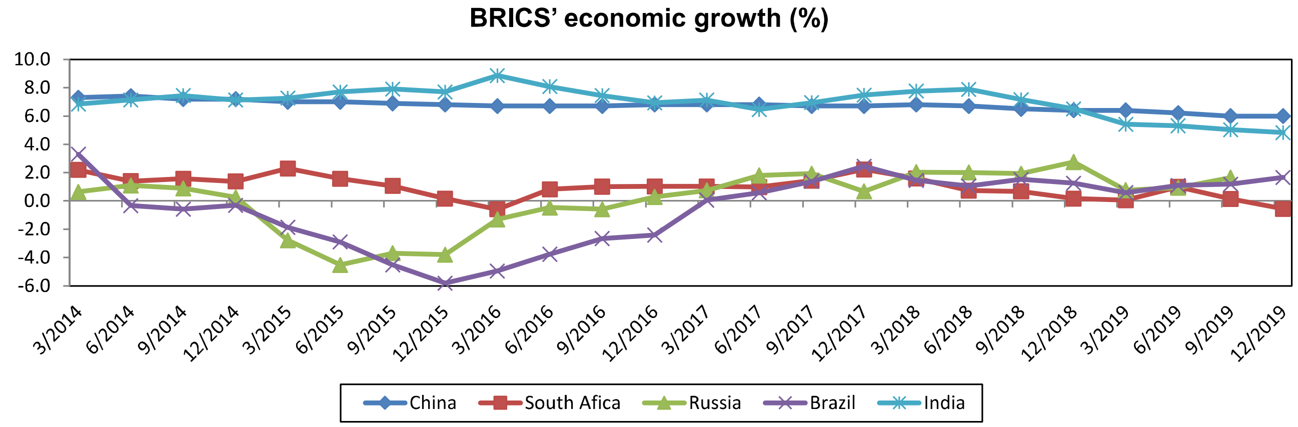


Source: FRED (2019)

BRICS economies

Continuous Divergent in Growth

- Chinese economic growth keeps decelerating in 5 years. Brazillian growth rate substantially improved from 0.59% in Q1/2019 to 1.66% in Q4/2019, partly due to the recovery of the mining sector after Amazon fire. Indian economy experienced a drop in growth.
- In India, controversial policy reforms led to religious tension, bankruptcies, unemployment and personal financial difficulties. Indian economic growth dropped to 4.8 – 5.4% in quarters of 2019.

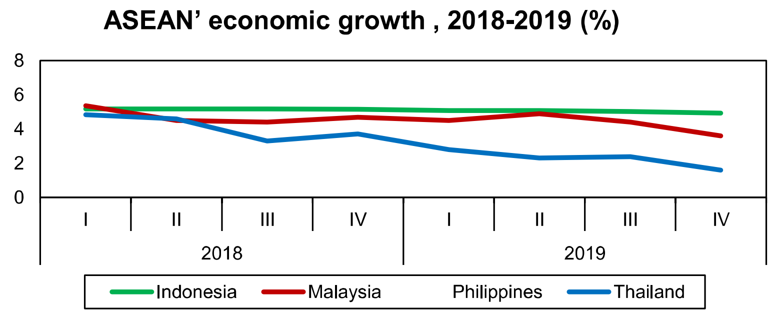


Source: OECD (2019)

ASEAN economies

Challenges from Investment Flows

- As US – China trade tension and Japan – Korea relation deteriorated, international landscape has become uncertain. ASEAN-4 economies experienced moderate growth in 2019.
- The outburst of COVID-19 brings about both opportunities and challenges, and deepened existing frictions in international relation. Existing problems within each ASEAN nation such as public debt, fiscal deficit, or the overdependence on foreign investment could resonate with the pandemic, causing economic difficulties.

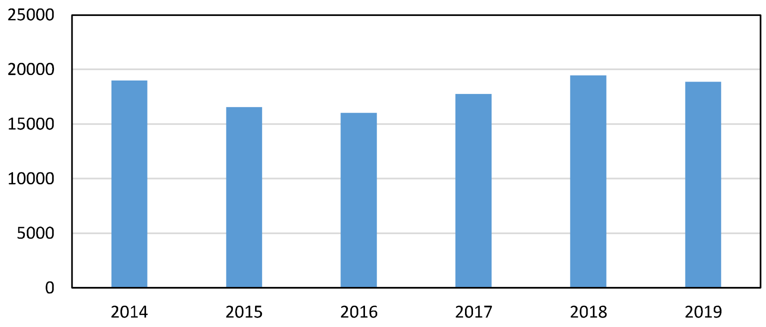


Source; OECD (2019)

US – China trade war, global trends in international trade and investment

- Global export value reached 18,889 billion USD in 2019, decreased by 2.9% in comparison to that in 2018 due to (i) US – China trade war (ii) Japan – Korea trade tension, (iii) Brexit and (iv) the growing trend in trade protectionism.
- Asia, Europe and North America are the most dynamic regions for international trade, accounted for approximately 90% global trade value.

Global Exports in the period of 2014-2019 (billion USD)



Source : WTO Data Portal (2020)

US – China Trade War

- Is just a symptom of conflicts at deeper level regarding:
  - The rising influence of China as a new superpower
  - Problems with respect to human rights, intellectual property, technology transfer

=> Trade war would not truly end without these problems being solved. It is expected that trade war could be prolonged for years, with unexpected twists and turns.

- According to Global Trade Alert (GTA), within 2019, the number of discriminating measures in international trade increased by 429, while the number of liberating measures increased by just 101 (GTA, 2020)
  - During 2017 – 2019, China and US were responsible for 23% of trade protective measures per year, while in the period before that, the figure was just 12%. (GTA, 2019)

VEPR Global FDI Flows

- Global FDI value in 2019 is estimated to be 1,394 billion USD, slightly decreased by 1,3% (yoy) due to:
  - Escalation of US – China trade war
  - The U.S's TCJA encouraged offshore profit to flow back to the U.S
- FDI flows to developed economies decreased by 6% (yoy), is estimated to be 643 billion USD
- FDI flows to emerging economies accounted for more than 50% of global FDI in 2019, remained stable at 695 billion USD. In which FDI to Asia, accounted for appox. 30% of global FDI, decreased by 6%.
- Total cross-border M&A value decreased by 40% (yoy), reached 490 billion USD.
- Total value of greenfield investment dropped sharply to 784 billion USD, decreased by 22% (yoy)=> gloomy prospect for global investment

Good Policy, Sound Economy

VEPR Global Capital Flows

FDI inflows, cross-border M&A and Greenfield investment by region, 2018 – 2019 (USD Bil)

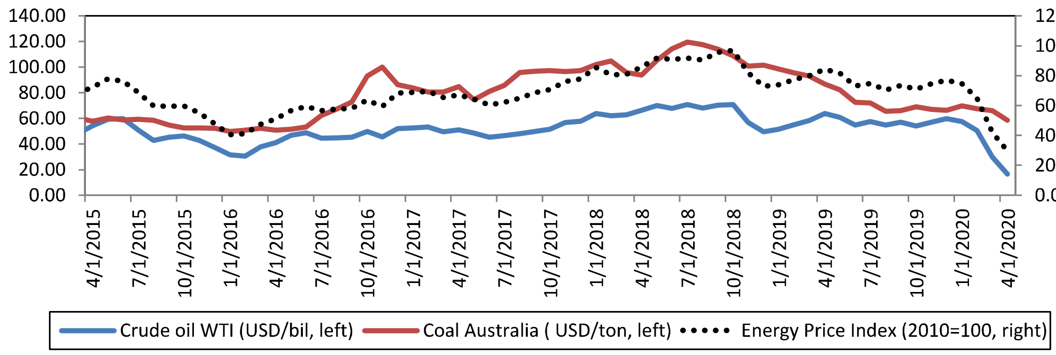
Region	FDI inflows			M&A			Greenfield investment		
	2018	2019	Growth rate (%)	2018	2019	Growth rate (%)	2018	2019	Growth rate (%)
World	1413	1394	-1	816	490	-40	999	784	-22
Developed Economies	683	643	-6	698	411	-40	375	329	-12
EU	357	305	-15	362	158	-56	203	182	-10
North America	297	298	0	224	180	-19	123	109	-11
Developing Economies	696	695	0	124	77	-38	573	411	-28
Africa	47	49	3	2	5	238	76	62	-19
Latin America and the Caribbean	146	170	16	39	22	-44	78	103	32
Developing Asia	501	473	-6	84	49	-41	418	246	-41
Transition Economies	34	57	65	3	1	-46	51	44	-14

Source : UNCTAD (2019)

VEPR The World Commodity Prices

- Crude oil price fluctuated around 50 - 60 USD/ barrel in 2019 and decreased sharply in 2020 .Within 2019:
  - OPEC and Russia's attempts to reduce production
  - Tensions in Middle East nations and flood in Midwest
  - The largest oil production hub in Saudi Arabia was attacked
  - The assassination of Iranian general Qassem Soleimani
- The increase in oil supply from the U.S countered the upward pressure caused by the above events on oil price.

Energy prices and energy price index, 2015-2020



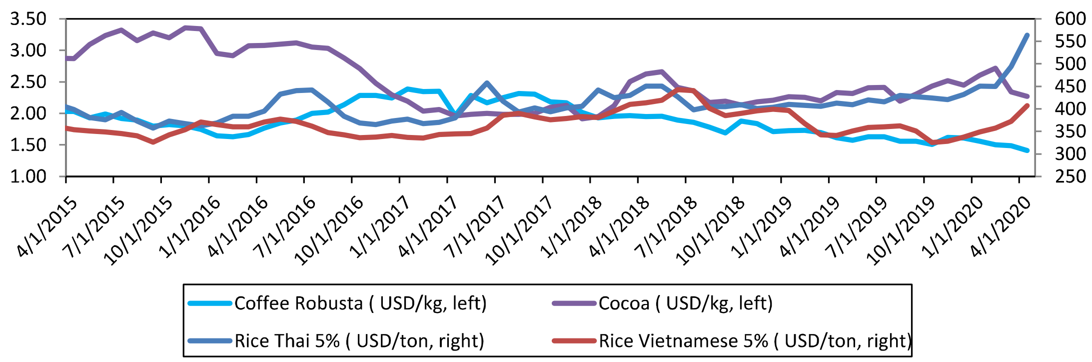
Source: EIA(2020), WB (2020)

Good Policy, Sound Economy

VEPR The World Commodity Prices

- Australian coal price showed downward trend due to: (i) China prioritization of domestic consumption for coal, (ii) decline in demand from the U.S and European nations, (iii) the availability of other types of renewable energy.
- Cocoa price and Thai rice price followed an upward trend, while Vietnamese rice and Robusta coffee experienced a drop in price.

Prices of some agricultural products in global market, 2015-2020



Source : WB (2020)

VEPR

Global Economic Outlook for 2020

- Global trade prospect:
  - International trade and investment flows are expected to be more uncertain due to : (i) geopolitical risks, uncertainty from U.S – China trade war, (ii) the rise of protectionism and erosion of the multilateral trade system, (iii) the reform/restructure of some major economies, including China and other powers, (iv) reconstruction of world order (New Cold War).
  - UNCTAD (2020b), Global FDI could decrease by 30 – 40% in 2020-2021, as the decline of investment and cross-border M&A could be further deteriorated.
  - According to WTO (2020), global trade volume could decrease by between 13% and 32% in 2020, since COVID-19 caused great disturbance on international trade and global socio-economic landscape.

Good Policy, Sound Economy

VEPR

Global Economic Outlook for 2020

- In the best scenario, WTO expect international trade to decrease by 12.9% (yoy) :
  - North America: decrease 17.1% in export value and 14.5% in import value;
  - Central and North America: drop 12.9% in export value and 22.2% in import;
  - European nations: decrease 12.2% in export value and 10.3% in import;
  - Asian nations: decrease 13.5% in export value and 11.8% in import value.
- In a worse scenario, WTO expect international trade to decrease by 31.9% (yoy) :
  - North America: decrease 40.9% in export value and 33.8% in import value;
  - Central and North America: drop 31.3% in export and 43.8% in import;
  - European nations: decrease 32.8% in export value and 28.9% in import;
  - Asian nations: decrease 36.2% in export value and 31.5% in import value.

- **Outlook on international finance:** The negative impact of COVID-19 has put central banks on the defense mode, with which the main goal is to protect the economy instead of promoting growth.
  - In 2020, there might be more stimulus packages all over the world
  - Negative interest rate could be more prevalent in 2020

Global Economic Outlook for 2020

- Crude oil price is unlikely to recover in 2020 as global economic slow down significantly hurt demand for oil.
- Initial changes in global supply chains: The trend of moving away from China due to the increase of costs and risks → Reshape the global supply chain (decentralized instead of centralized?) → This process would probably last for the next decade.
- Formation of a new world order? (clash of civilizations or the possibility of a New Cold War) → Partly depends on the results of the US Presidential election in November 2020.

→ At any possibility, expectation is high regarding strategic moves of India and the ASEAN → Vietnam is in a spiral of intense changes and conflicts in the future.

Overview of the Vietnamese Economy 2019

VEPR

Outline

- Production and Growth
- Demand Side
- Inflation and Monetary Policy
- Asset Markets
- National Budget and Public Debt
- Policy Implications and Recommendations for 2020

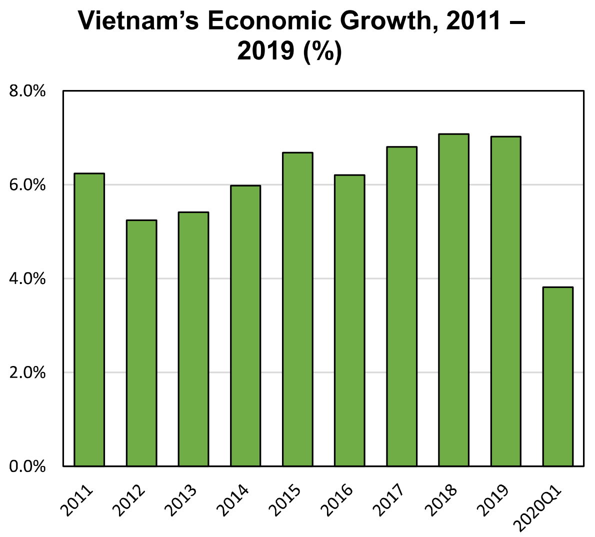
VEPR

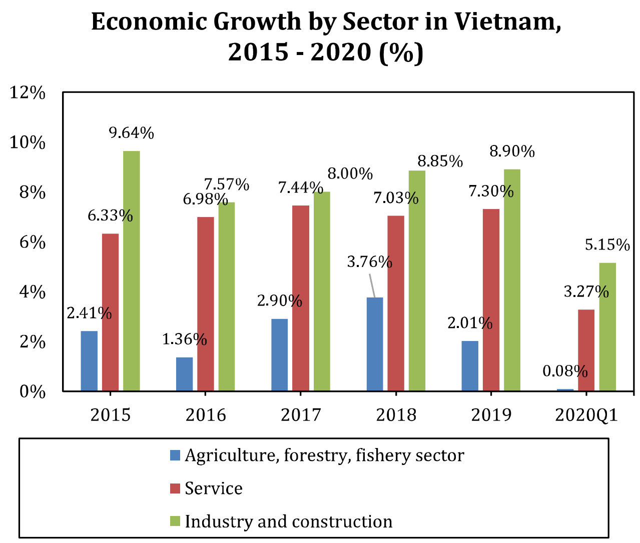
Production and Growth

- Growth in Sectors and Industries
- Employment in Enterprises
- Operation of Enterprises

VEPR Growth in Sectors and Industries

- Actual GDP growth stood at 7.02% in 2019, exceeded target (6.6%-6.8%).
- Main contributors to economic growth were Industry and Construction sector (50.4%), and Service sector (45%).





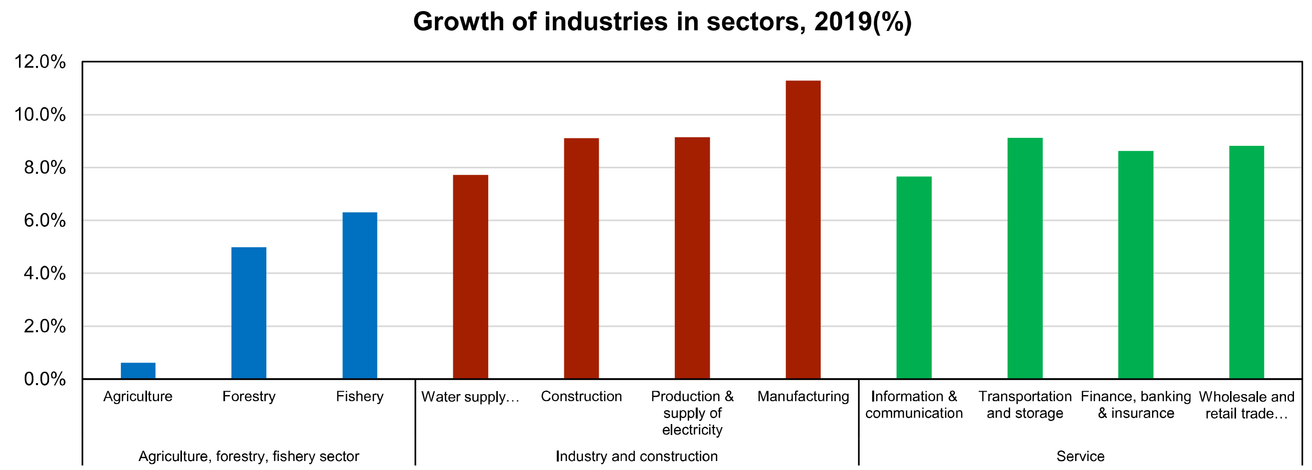
Source: GSO (2020)

VEPR Growth in Sectors and Industries

- Recalculation of GDP results in a 25% higher figure. Nevertheless, new calculating method only takes place since 2021.
  - (i) Addition of 76 thousand enterprises;
  - (ii) Additional information from administrative entities inquiries;
  - (iii) Update of national accounts 2008,
  - (iv) Updates on economic divisions and (v) Updates on economic structure.
- Concerns on the recalculation of GDP:
  - (i) The recalculation pushed GDP 25% higher, while the main reason is the new 76 thousand enterprises.
  - (ii) Would budget revenue increase in tandem with GDP?
  - (iii) Would other economic indicators such as public debt ratio and government debt be levitated?

Growth in Sectors and Industries

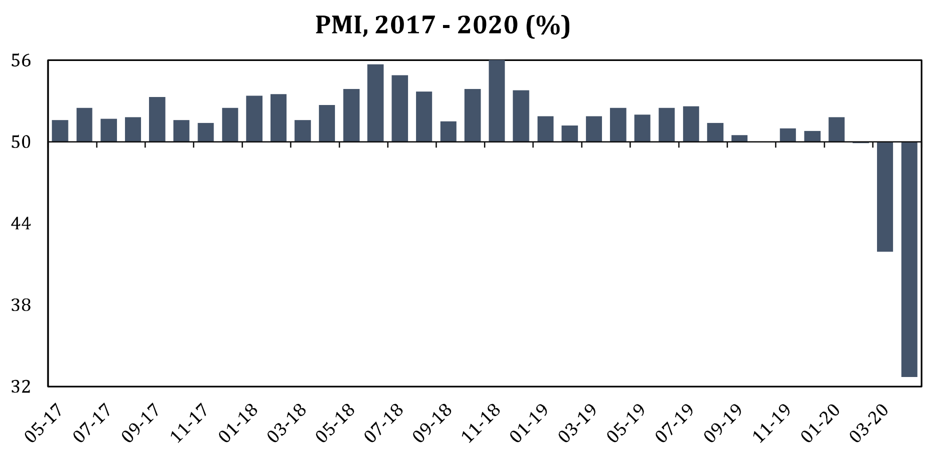
- Industries experienced optimistic growth, such as manufacturing and processing (11.29%, yoy)
- Accomodation and catering increased by 6.71% yoy, as international arrivals increased by 16.2% (yoy) (Vietnam National Administration of Tourism, 2020).



Source: GSO (2020)

Growth in Sectors and Industries

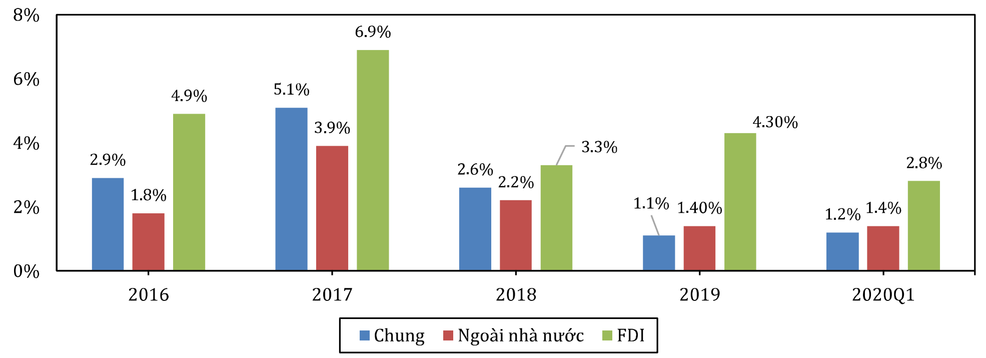
- PMI remained above 50 for the whole year, the manufacturing sector has been expanding for 49 consecutive months by the end of 2019. => Optimistic prospect for the manufacturing sector and the economy, before COVID-19 happened in the beginning of 2020.



Source: HSBC, Nikkei (2020)

VEPR Employment in Enterprises

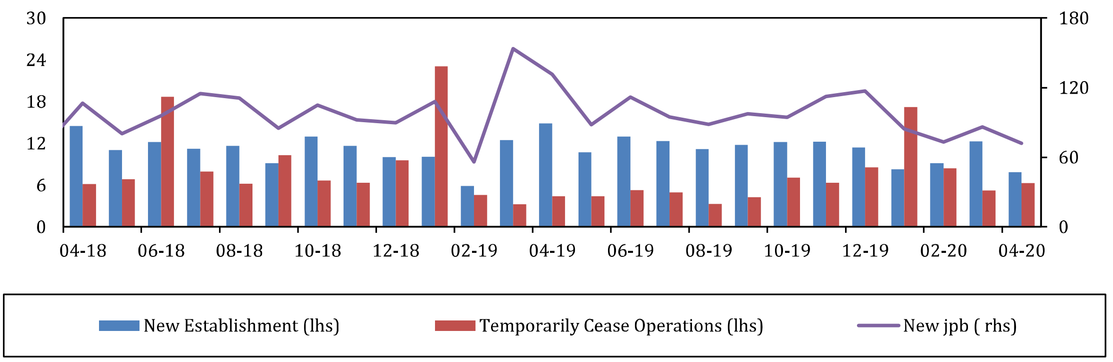
- Number of employees working in industrial enterprises increased by 2.8% in 2019, higher than that in 2018 (2.6%).
- Labor growth in the FDI sector stood at 4.3% in 2019, higher than that in 2018 => manufacturing activities was better in 2019 than in 2018, despite the slow down of global trade in 2019.



Source: GSO (2020)

VEPR Operation of Enterprises

- In 2019, there were 138.1 thousand newly established enterprises, increased by 5.2% (yoy). The total value of registered capital and total number of registered labors increased by 17.1% and 13.3%, respectively.
- In 2019, there were 46.8 thousand enterprises not operating within the registered venue, increased by 43.4% (yoy) => concerns regarding corporate tax duty.



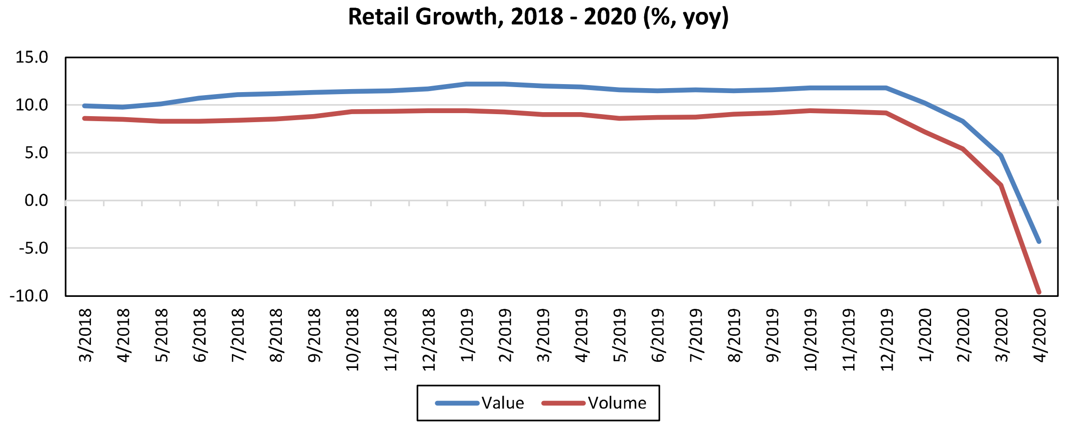
Source: GSO (2020)

VEPR Demand Side

- Retail Revenue
- Total Social Investment
- International Trade
- FDI

VEPR Retail Revenue

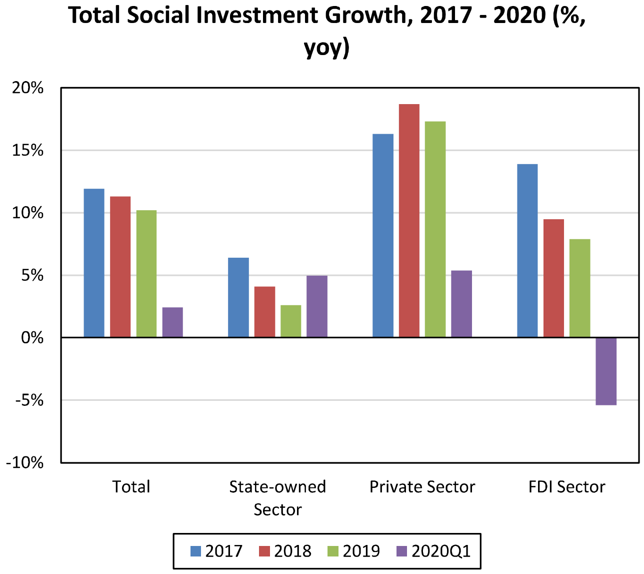
- Total retail sale in 2019 increased by 11.8% (yoy), retail volume (excluding price factor) increased by 9.2% (yoy).
- Stationary and education appliances increased by 14.4% (yoy) ; food increased by 13.2% (yoy); household appliances, tools and equipments increased by 11.3% (yoy); textile & garment increased by 10.9% (yoy); transportation vehicles increased by 7.8% (yoy). Tourism revenue increased by 12.1% (yoy).



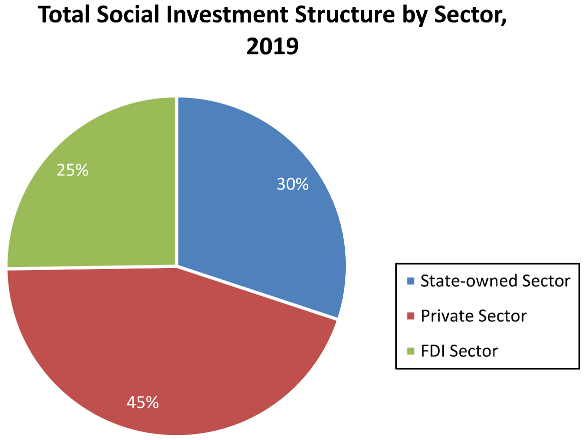
Source: GSO (2020)

Total Investment

- Total Social investment carried out at 2019's current price increased by 10.2% (yoy). The private sector and FDI are expected to outweigh the public sector.



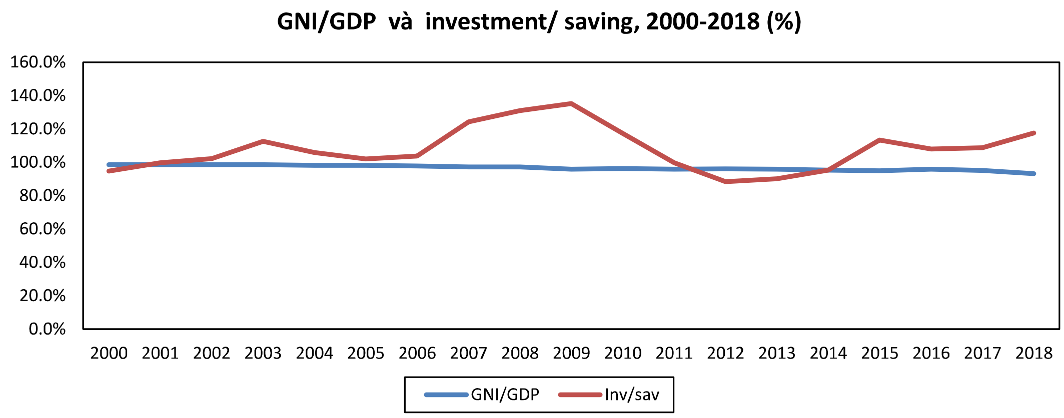
Source: GSO (2020)



Source: Author's calculation from GSO (2019)

Total Investment

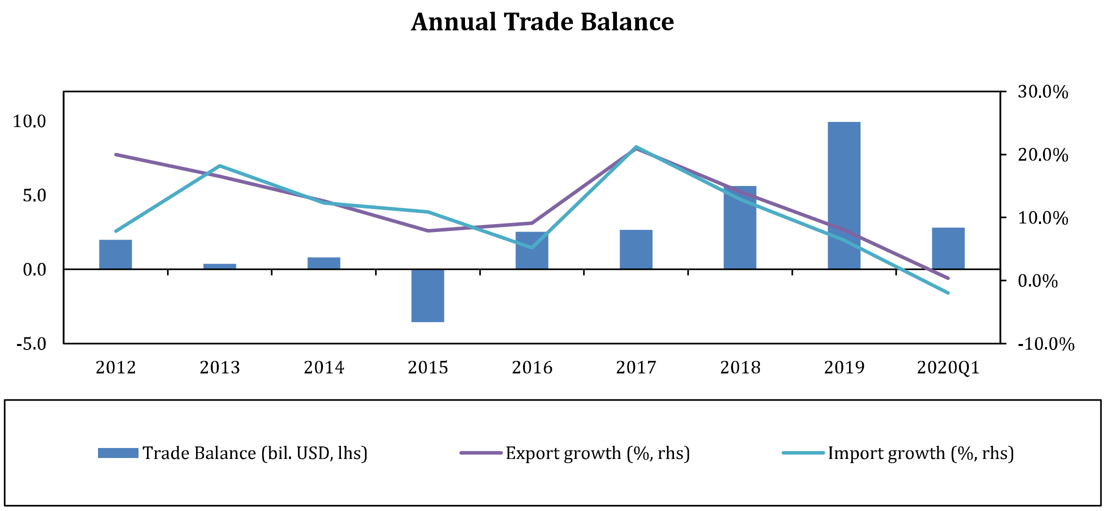
- GNI/GDP ratio follows a downward trend, from 98.6% (in 2000) to 93% in 2018 (ADB) => ownership-related payments for foreign investor increased.
- Investment/saving ratio exceeded 100% recently => foreign borrowing and interest payment are expected to rise, in order to maintain investment and growth.



Source : ADB (2020)

VEPR International Trade

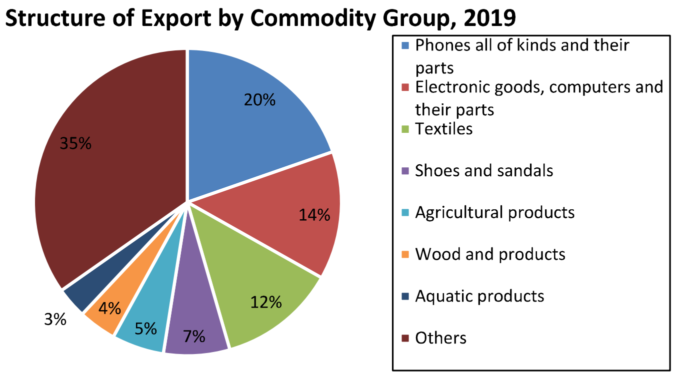
- Trade surplus reached 9.9 billion USD, nearly doubled 5.6 billion USD in 2018 => support SBV to maintain a stable USD/VND and increase foreign reserve
- Exports from FDI sector still contributed the largest part (68.8%), but the weight decrease in comparison to last year.

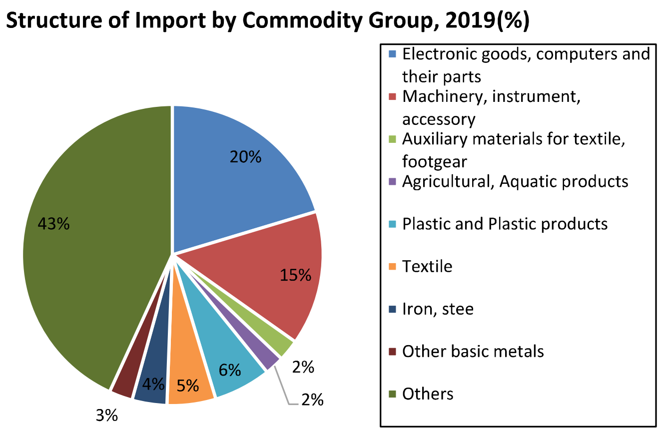


Source: GSO (2020)

VEPR International Trade

- There were 32 items that reached export turnover of 1 billion USD, accounted for 92.9% total export turnover. The U.S was the largest export market of Vietnam, with export turnover reached 60.7 billion USD, increased by 27.8% (yoy)
- Capital goods for manufacturing and processing industries reached 144.12 billion USD, accounted for 90.6% total import turnover. China was the largest import market of Vietnam, with import turnover reached 75.3 billion USD, increased by 14.9%

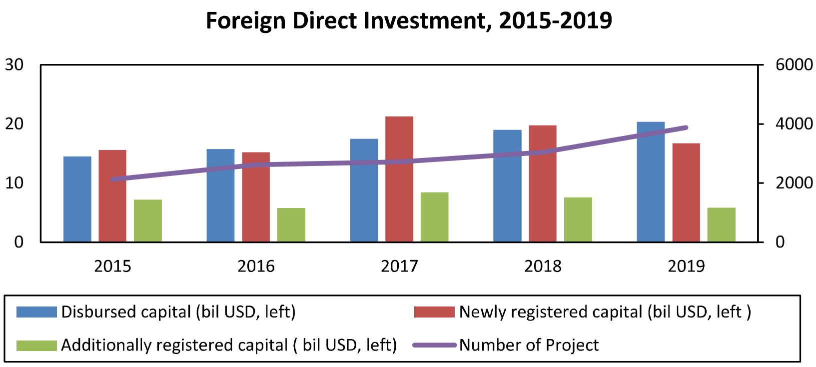




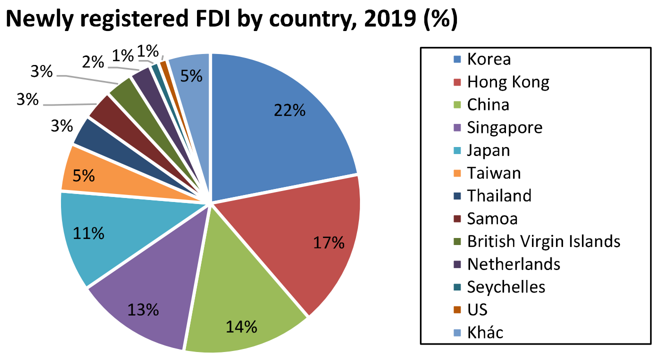
Source: GSO (2020)

VEPR Foreign Direct Investment

- Total disbursed FDI value stood at 20.4 billion USD in 2019, increased by 6.7% (yoy) mainly because of registered investment from the previous years.
- Korea is the top investor in 2019, with total registered investment stood at 3.66 billion USD



Source: Author's calculation based on GSO data (2019)



Source: GSO (2019)

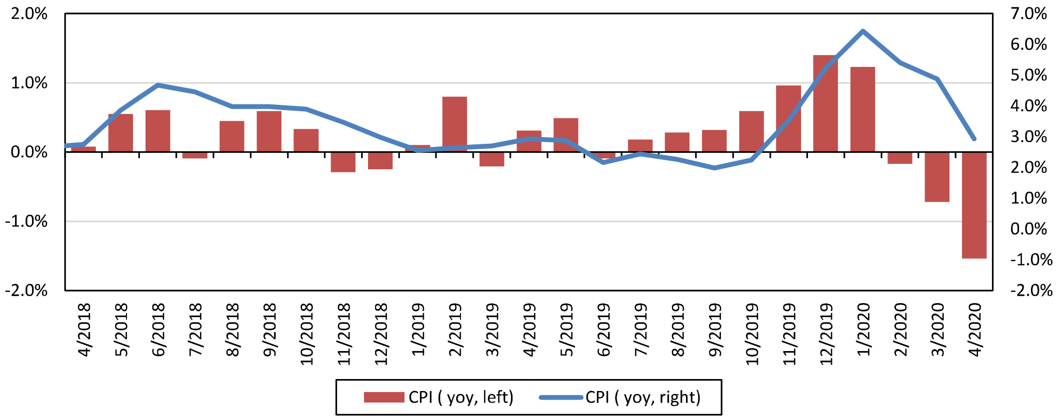
VEPR Inflation and Monetary Policies

- CPI
- Interest rate and Credit
- Exchange rate

VEPR Consumer Price Index

- Average CPI in 2019 increased by 2.79% (yoy), lower than the increase of 3.54% in 2018, and still below the 4% threshold set by the Government. Food and foodstuffs have contributed greatly to the increase of CPI due to the impact of African swine cholera.
- In 2020, the goal of controlling inflation below 4.0% can be achieved if food prices in the rest of the year are well controlled.

Consumer Price Index, 2018 – 2020 (%, yoy)

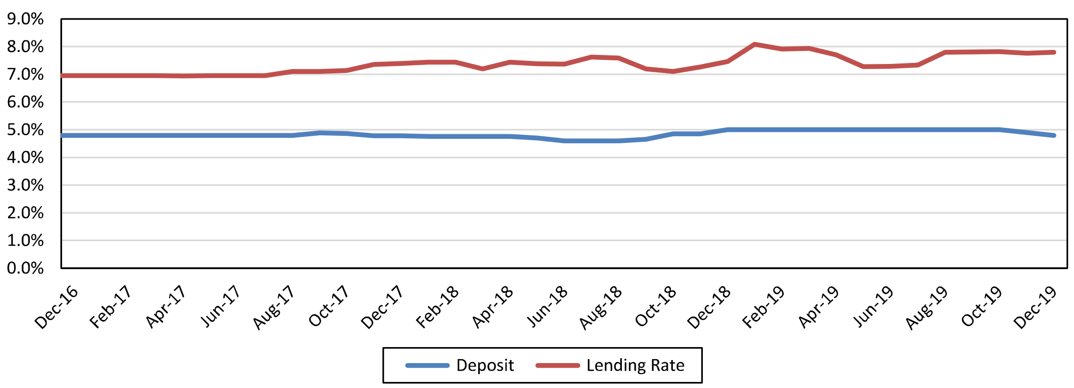


Source: GSO (2020)

VEPR Interest Rate and Credit

- In 2019, interbank interest rates followed a downward trend. Deposit rates of commercial banks remained relatively stable at 5% / year, while lending rates remained high, around 7-9%.
- In November, the SBV decided to lower the policy rate to 0.25%. In general, the current interest rate level in Vietnam is still high, the decrease of 0.25% has not really had much impact on business activities.

Deposit and Lending Rate, 2016 – 2019 (%)

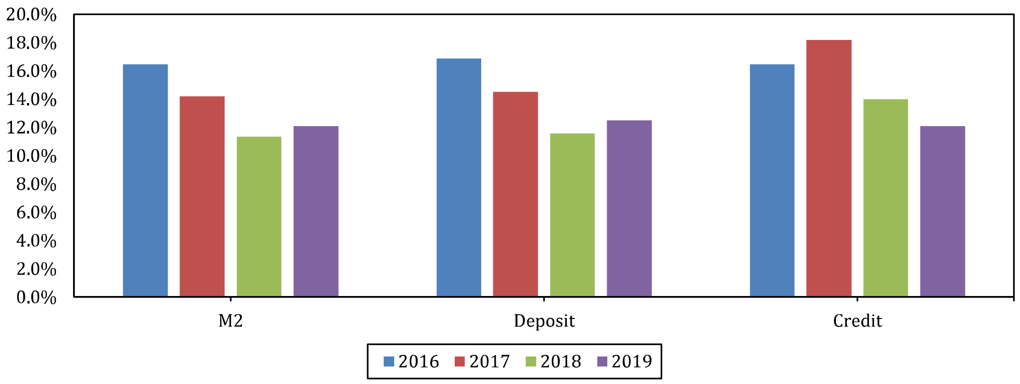


Source: IMF (2019)

Interest Rate and Credit

- The money supply in 2019 increased by 12.10%, currently at a high level compared to other countries in the region. The M2 / GDP ratio has reached over 175%, much higher than previous years such as 2018 (170%) => SBV needs to be more cautious with the money supply growth, considering inflation and property price bubbles.

Growth of M2, Mobilization and Credit (%, yoy, ytd), 2016 – 2019

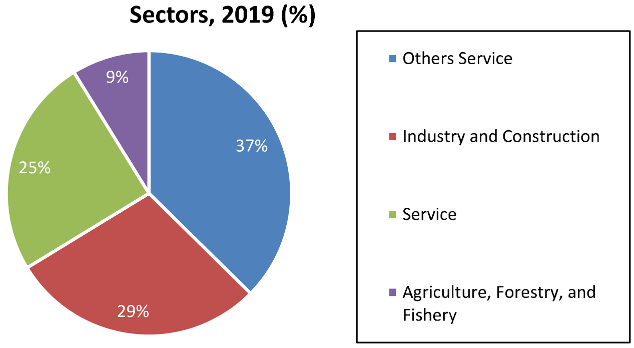


Source: SBV (2019)

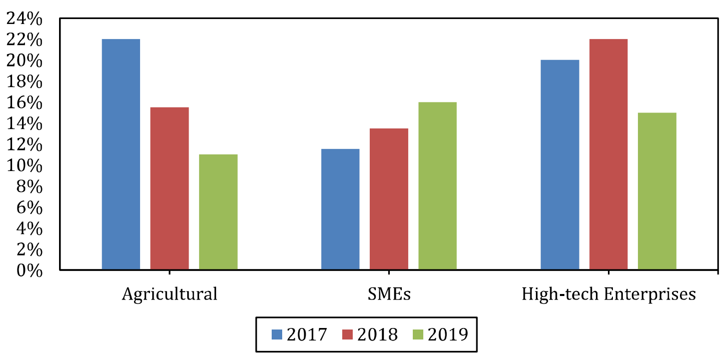
Interest Rate and Credit

- Credit growth in 2019 was only 12.10% - the lowest level in five years.
- Credit outstanding in the commercial sector accounted for the highest proportion (22.5%) of the total outstanding loans of the economy in the fourth-class industries. Credit growth for prioritize small and medium enterprises and enterprises in the agricultural sector.

The Proportion of Credit Balance by Economic Sectors, 2019 (%)



Credit Growth by High Priority Economic Sectors, 2017-2019

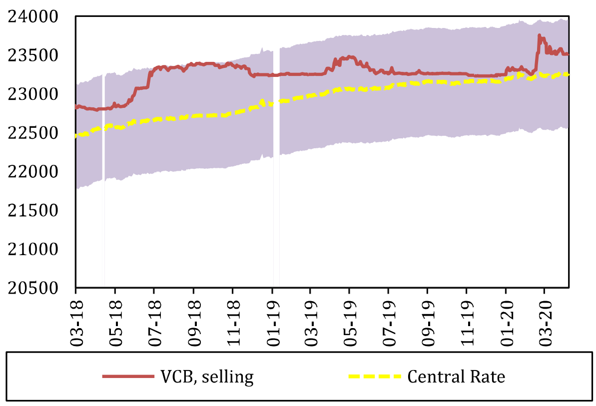


Source: SBV (2019)

VEPR Exchange Rate

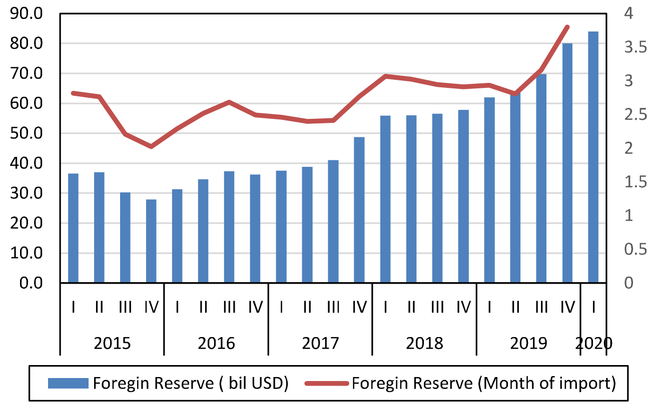
- VND/USD exchange rate was maintained stably in 2019, ending at 23,155 VND/USD, up more than 1% compared to the end of 2018.
- By the end of Q4 2019, foreign exchange reserves reached nearly 80 billion USD - the highest level ever. This is the foreign exchange reserves equivalent to more than three months of import in accordance with international standards to ensure macroeconomic stability.

Nominal Exchange Rate (VND/USD)



Source: VEPR compilation (2020)

Foreign Exchange Reserve, 2015 – 2019



Source : CEIC (2019)

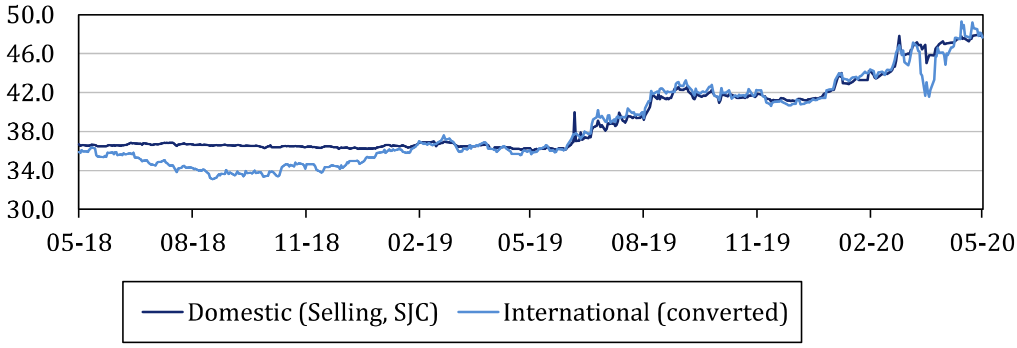
VEPR Asset Markets

- Gold Market
- Stock Market
- Real Estate Market

VEPR Gold Market

- In 2019, the domestic gold price closely followed the fluctuations of the world.
- In 2020, gold price is expected to remain high due to:
  - COVID-19 pandemic
  - Monetary easing and budget deficits in a number of countries around the world
  - Tension between the U.S and China, Iran, North Korea

Gold Price, 2017 – 2019 (million VND/tael

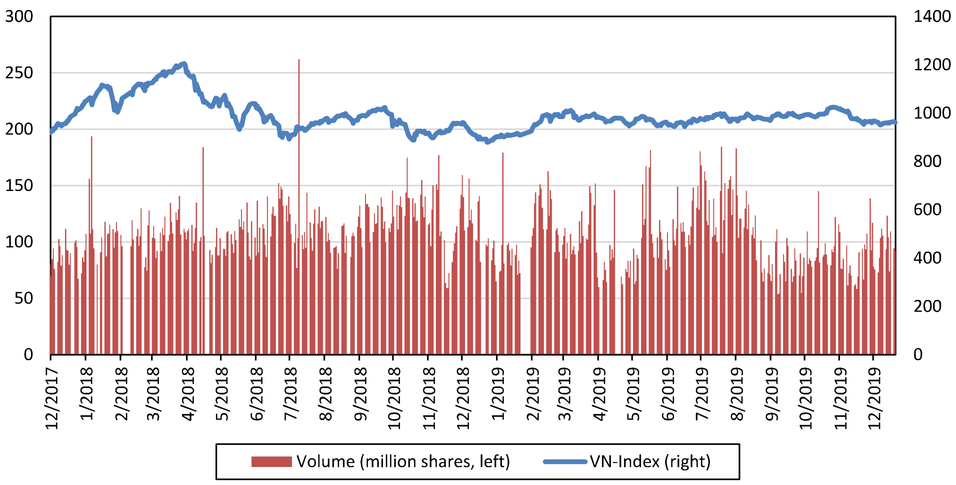


Source: SJC (2020)

VEPR Stock Market

- Vietnam's stock market increased by 7.76% in 2019, lower than the increase in 2018. The market opened the first session of the year with the VN-index at 891.75 points, ending the year at 960.99 points.

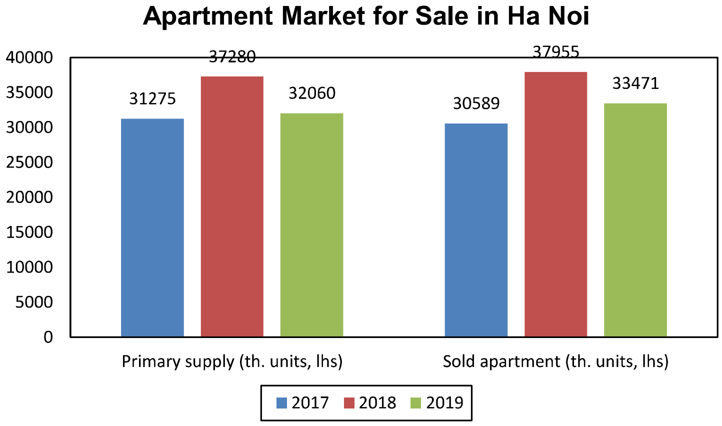
VN – Index, 2017 – 2019

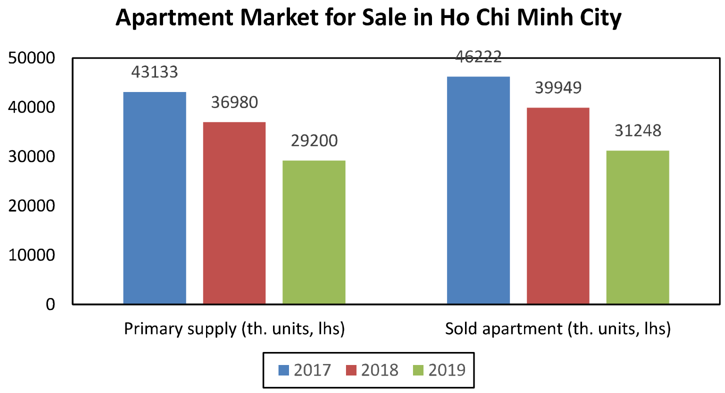


Source: VNDIRECT (2019)

VEPR Real Estate Market

- Supply decreased in both Hanoi and HCMC markets in 2019, especially in Hanoi.
- Apartment supply in Hanoi decreased 8.2% (yoy), reaching only 32,060 units. HCMC also opened to sell more than 29,000 units.

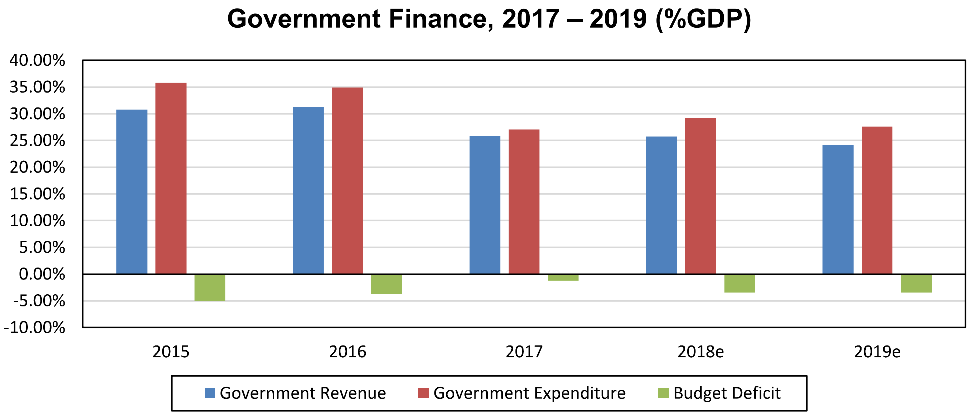




Source: JLL (2020)

VEPR State Budget and Public Debt

- According to the Ministry of Finance's first estimate, the total state budget revenue in 2019 exceeded yearly projection by 3.26%, while the total state budget expenditure exceeded 2.05%. Budget revenue is still not sufficient to offset the budget expenditure.
- The budget deficit in 2019 is estimated to be about 209.5 trillion VND, equivalent to 3.4% of GDP.

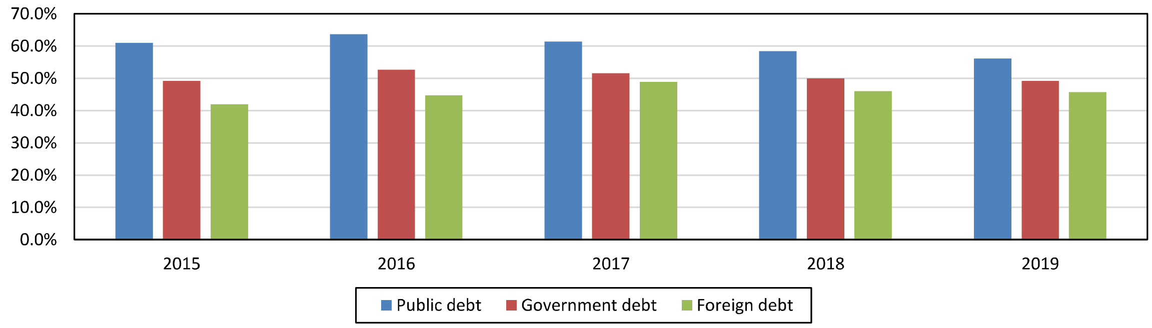


Source: MOF (2019)

VEPR State Budget and Public Debt

- It is estimated that the budget revenue to GDP ratio will drop sharply in 2019, to about 24.1%.
- The ratio of public debt to GDP continues to decline in 2019, to 56.1% due to high economic growth and slow progress in public investment disbursement.
- In order to meet the projected expenditures in 2020, the Government proposed the National Assembly to lend more than 495,000 billion VND.
- (Ministry of Finance, 2020) Vietnam is currently planning to borrow USD 1 billion from abroad in 2020 to offset the budget deficit caused by COVID-19.

Public, Government and External Debt, (% GDP), 2015 – 2019



Source: MOF (2019)

Good Policy, Sound Economy

VEPR Evaluation on Vietnam Economy 2019

- GDP growth in 2019 reached 7.02 (%). The annual average inflation was 2.79%, lower than the target of 4%. International trade and investment are growing. The money market, capital and exchange rates are stable and under control. The budget deficit and public debt also showed certain improvements. However, the economy still has many potential risks :
  - Economic growth, exports or employment are increasingly dependent on the FDI sector and a few FDI businesses
  - Vietnam is on the U.S.'s watch list for currency manipulation
  - The risk of demand-pulled inflation and exchange rate is low, while the risk of inflation due to supply disruption (food) increases significantly.
  - Foreign exchange reserves are adequate to ensure the minimum safety requirements in only short term
  - Budget revenue also relies on short-term revenue sources such as asset sales, while revenue from international trade declines rapidly due to FTAs

Policy Implications

- Vietnam should be careful not to become a backyard for China and South Korea to export to the US
- It is necessary to review the tax or land preferential policies for FDI in order to create a more equal environment for domestic enterprises.
- The government needs to be very careful with the decision to increase new debt to pay off old debt or/and offset expenditures, given that GDP would be recalculated from 2020, which may lead to public debt ceiling being lifted.
- Vietnam should focus on the fiscal, monetary and exchange rate policies to face the instability of the global economy:
    (1) Flexible exchange rate
    (2) Stable interest rate
    (3) Reduce leverage and improve the health of the banking system
    (4) Gradually build fiscal buffer by reducing recurrent expenditures

Good Policy, Sound Economy

Characteristics of the Budget Revenues of Vietnam in the International Integration Process

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Outline

- Scale of Budget Revenues
- Structure of Budget Revenues
- Taxable Individuals and Organizations
- Informal Sector
- Tax Incentives
- Tax Avoidances
- Fair Tax Monitoring
- Budget Transparency and Information Access
- Conclusions and Policy Recommendations

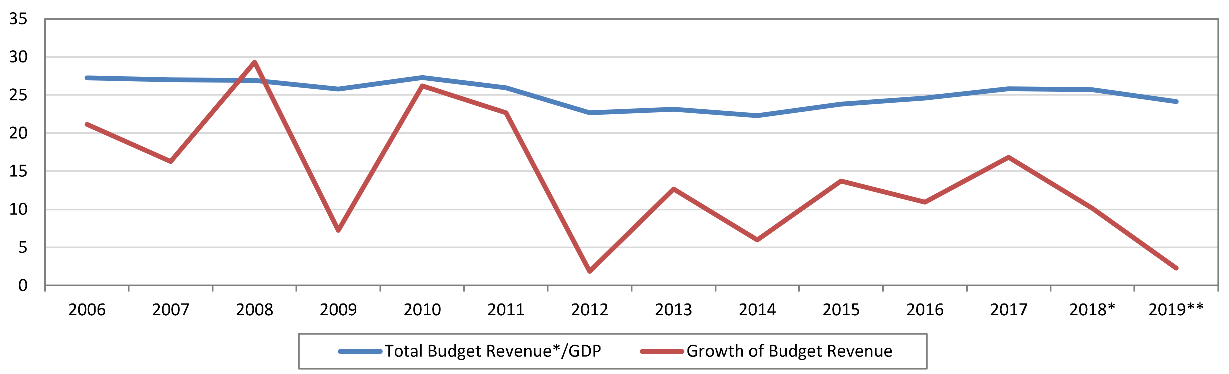
Good Policy, Sound Economy

Scale of Budget Revenue

Total Budget Revenue

- The total budget revenue of Vietnam accounted for 25,16% of the average GDP during 2006-2019. The ratio of budget revenue to GDP dropped sharply from 2010 to 2014, increased again over the next two years and witnessed a significant decrease in the period 2017-2019.
- The growth rate of budget revenue during this period made 12,2% per year and appeared to be slower in three recent years.

Total of Budget Revenue, 2006-2019 (%)

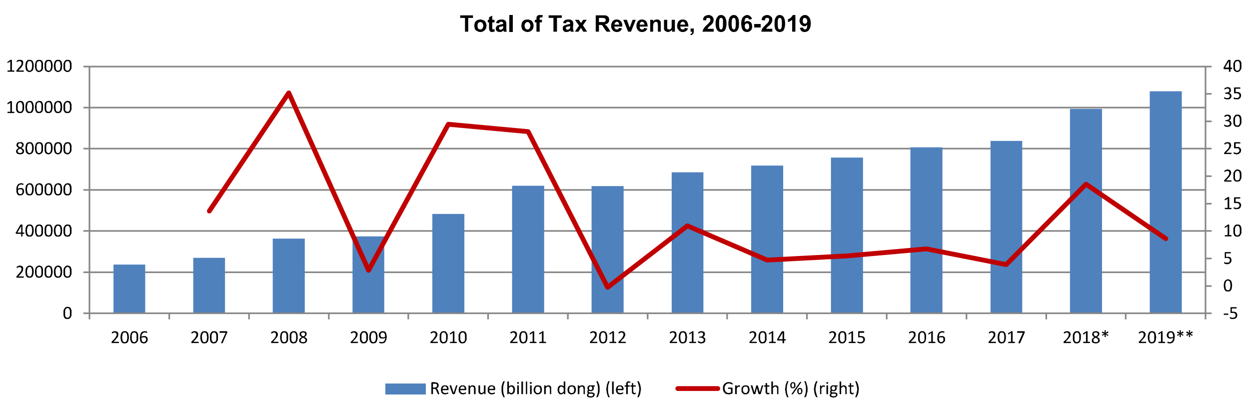


Note: The total state budget revenue does not include revenue from transfers, * The 2018 data is the second estimate, ** The 2019 data is the first estimate.

Source: Author's calculation from the Ministry of Finance (2007-2020)

Scale of Budget Revenue
Revenue from Tax

- On average, during 2006-2019, the portion of budget revenue gained from tax accounted for 78% of the total budget revenue. The tax revenue constantly increased at the average rate of 11,45% per year during this time.
- In recent years, the growth rate of tax revenue tended to decrease. During 2006-2011, the average annual growth rate was 17,4% and then down to 7,2% during 2012-2019.

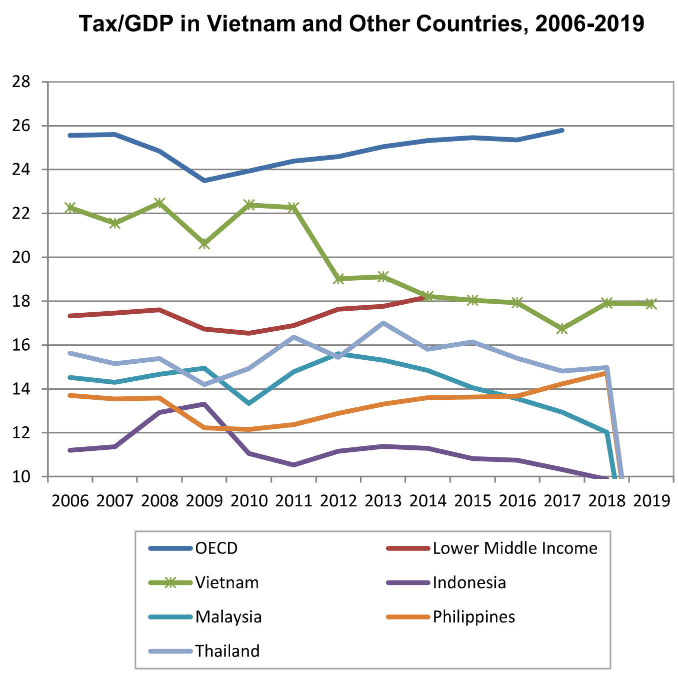


Note: * The 2018 data is the second estimate, ** The 2019 data is the first estimate.

Source: Author's calculation from the Ministry of Finance (2007-2020)

Scale of Budget Revenue
Revenue from Tax (cont.)

- Tax revenue (% of GDP) in Vietnam dropped from 22,2% (2006) to 17,8% (2019)
- Globally, the tax-to-GDP ratio of Vietnam has been lower than that of the OECD countries but comparable to middle-income countries since 2014.
- During 2006-2019, the share of tax revenue in GDP in Vietnam was higher than five ASEAN countries including Malaysia, Thailand, Indonesia, and the Philippines.



Source: Author's calculation from the WDI (2020)

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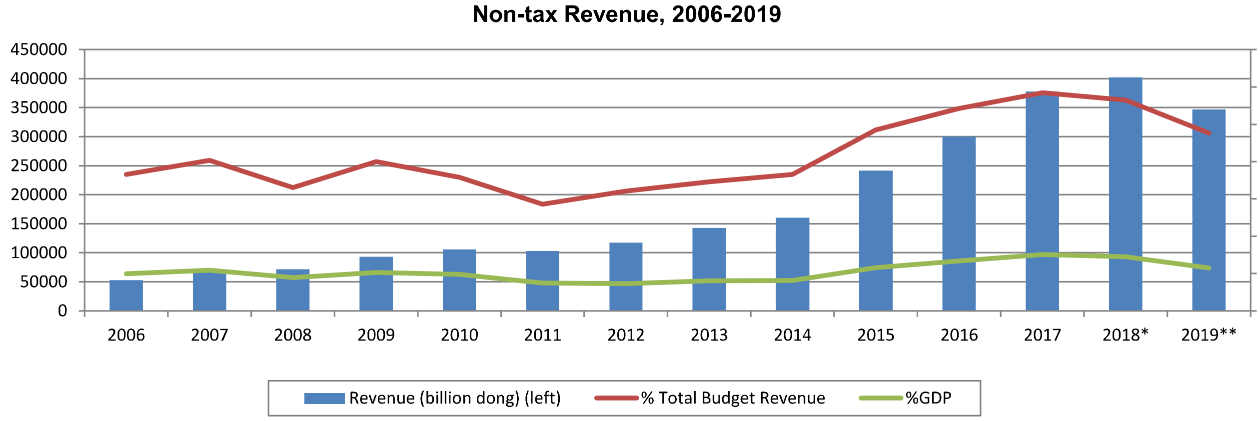
Scale of Budget Revenue

Non-tax Revenue

- The proportion of non-tax revenue increased from 18% (2006) to 29,2% (2017), then slightly decreased in 2018 and 2019 but remained relatively high, 28,2% and 23,8% of the budget revenue, respectively.
- During 2006-2019, on average, non-tax revenue accounted for about 20,8% of the total revenue. Non-tax revenue was 5,2% of the GDP.



Note: * The 2018 data is the second estimate, ** The 2019 data is the first estimate.

Source: Author's calculation from the Ministry of Finance (2007-2020)

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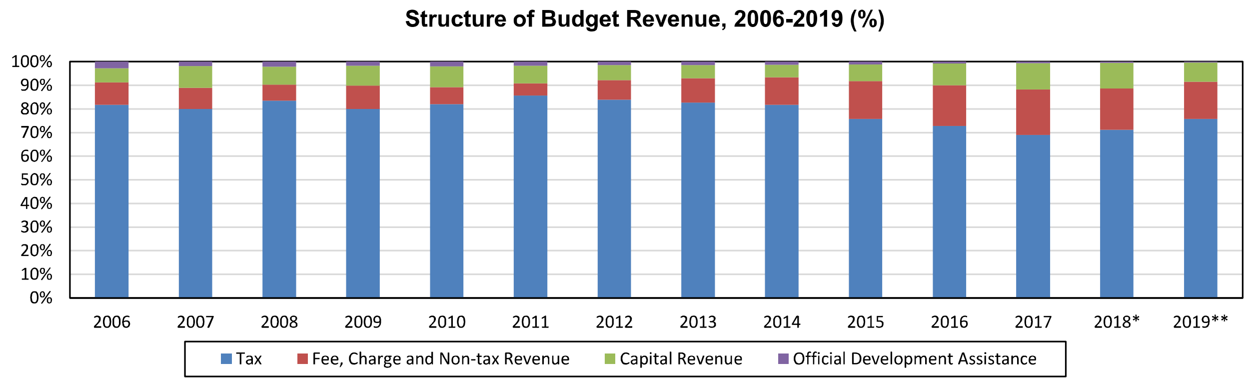
Structure of Budget Revenue

- During 2012-2017, portion of tax revenue constantly decreased from 84% (2012) to 64,8% (2017). However, the trend during 2018-2019 signaled a coming escalation.
- Fee, charge, non-tax, and capital revenue were rising while revenue gained from Official Development Assistance was declining significantly over the past few years.



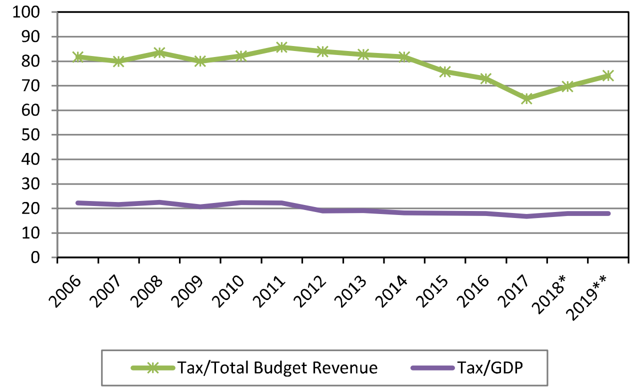
Note: The total state budget revenue does not include revenue from transfers, * The 2018 data is the second estimate, ** The 2019 data is the first estimate.

Source: Author's calculation from the Ministry of Finance (2007-2020)

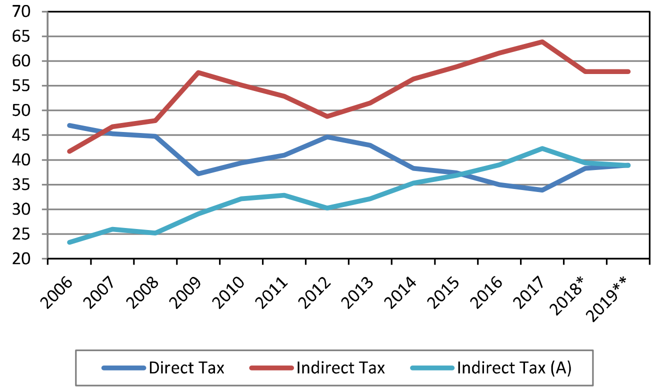
Structure of Budget Revenue
Structure of Tax Revenue

■ In 2006, direct tax and indirect tax accounted for nearly 50% and 40%, respectively. Up until 2019, the direct tax was down to 38,9% while indirect tax surged to 57,8% despite the exemption of excise, export, and import taxes.

Share of Tax on Revenue and GDP, 2006-2019 (%)



Structure of Tax Revenue, 2006-2019 (%)



Note: * The 2018 data is the second estimate, ** The 2019 data is the first estimate. (A) Only VAT and Environmental Protection Tax.

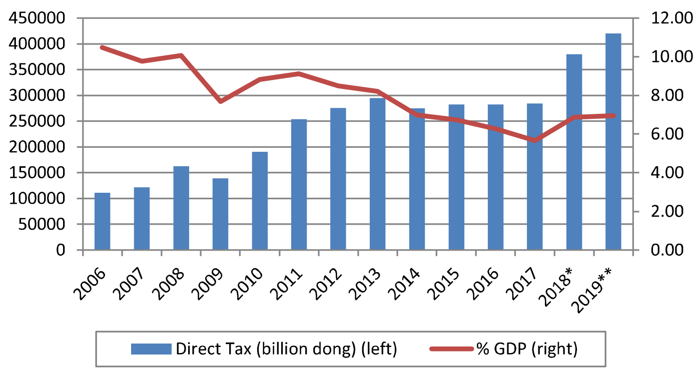
Source: Author's calculation from the Ministry of Finance (2007-2020)

Structure of Budget Revenue
Direct Tax

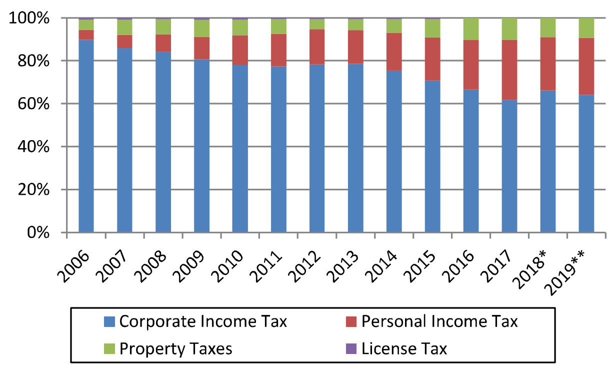
■ The share of direct tax to total tax revenue was falling during 2012-2017. The direct tax to GDP ratio dropped from 10% (2006) to 5,67% (2017). However, the Ministry of Finance's estimated data shows that the direct tax strongly increased with respect to its portion and absolute value in 2018 and 2019.

■ Corporate income tax accounted for the most percentage in the direct tax structure despite the declining tendency regarding its rate.

Direct Tax, 2006-2019



Structure of Direct Tax, 2006-2019



Note: * The 2018 data is the second estimate, ** The 2019 data is the first estimate.

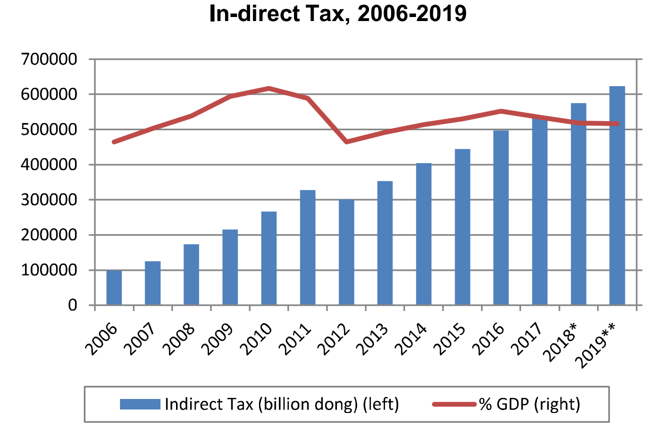
Source: Author's calculation from the Ministry of Finance (2007-2020)

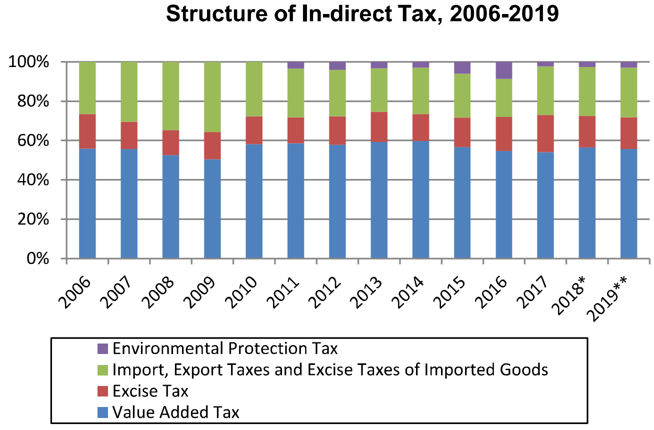
VEPR Structure of Budget Revenue

In-direct Tax

■ The percentage of indirect tax in total tax revenue was gradually higher and over 60% in 2016 which accounted for 11% of the GDP.

■ Value-Added Tax has become the largest source of revenue compared to any other kinds of indirect taxes. The VAT's share ranged from 50% to 60% of the total indirect tax during 2006-2019.





Note: * The 2018 data is the second estimate, ** The 2019 data is the first estimate.

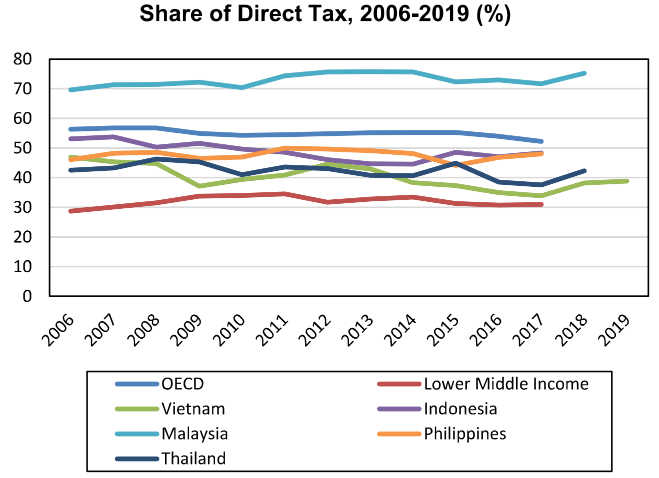
Source: Author's calculation from the Ministry of Finance (2007-2020)

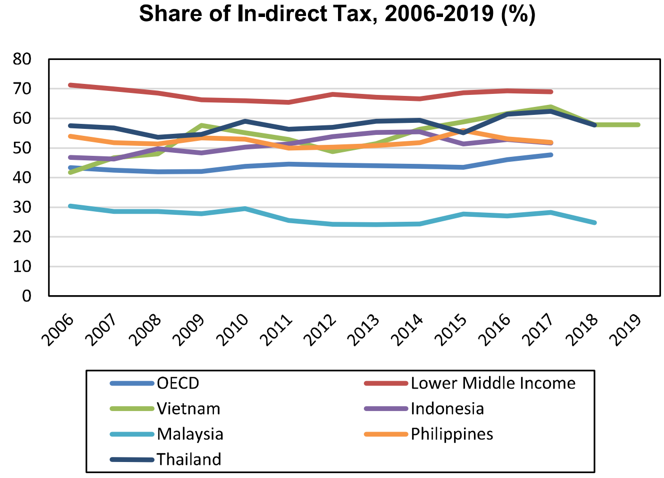
VEPR Structure of Budget Revenue

Share of Direct and In-direct Tax

■ Globally, during 2006-2019, the share of direct tax on the total in Vietnam was lower compared to OECD countries, the Philippines, Indonesia, and Malaysia.

■ Indirect tax's share was, on average, lower than the lower-middle-income countries but similar to Thailand and higher than the others.





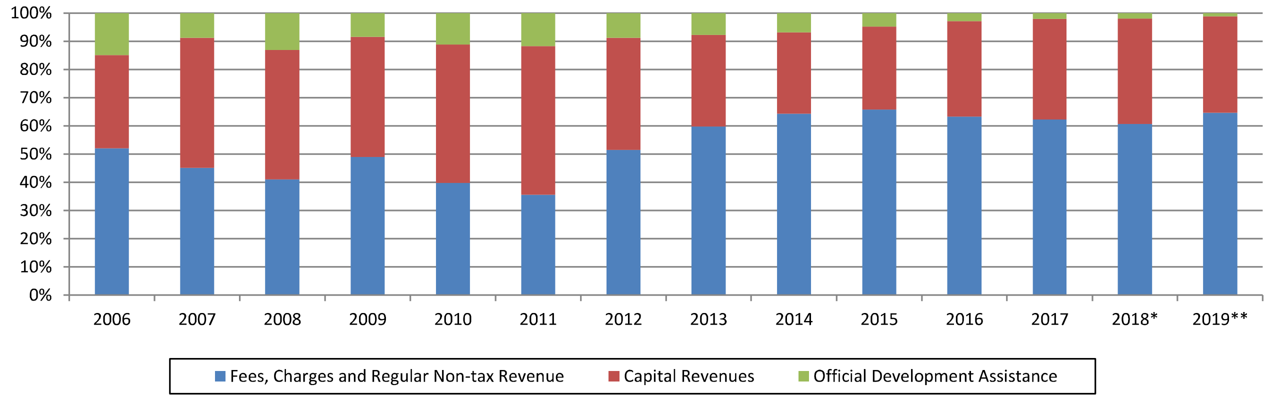
Source: Author's calculation from the WDI (2020)

VEPR Structure of Budget Revenue

Structure of Non-tax Revenue

- Fees, charges, and regular non-tax revenue accounted for the largest portion in the total non-tax revenue, about 54% on average during 2006-2019.
- Capital revenues strongly shrank during 2011-2015 but tended to increase back. Official Development Assistance only made 1,15% of the total non-tax revenue in 2019.

Structure of Non-tax Revenue, 2006-2019 (%)



Note: * The 2018 data is the second estimate, ** The 2019 data is the first estimate.

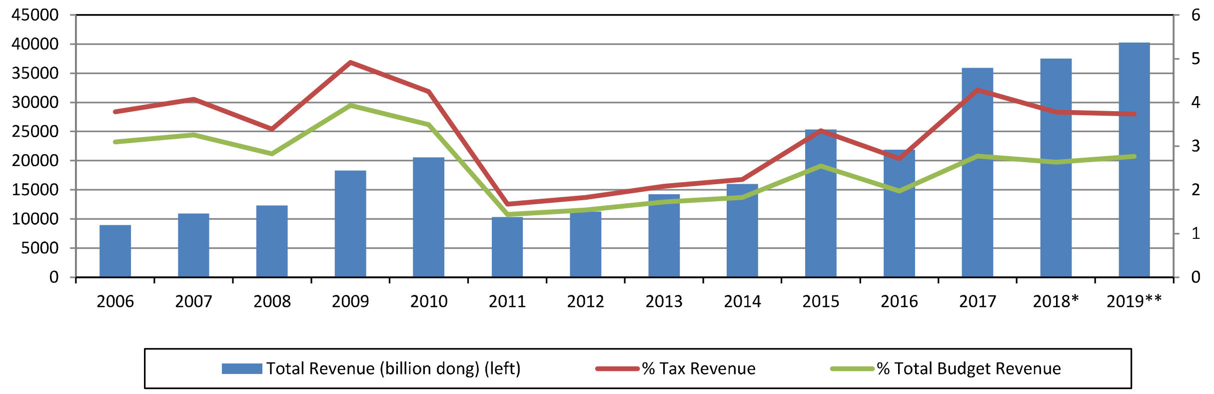
Source: Author's calculation from the Ministry of Finance (2007-2020)

VEPR Structure of Budget Revenue

Fees and Charges Revenue

- Fees are divided into 13 fields and 89 types.
- Charges are divided into 5 fields and 64 types.
- The share of fees and charges in the total budget revenue and total tax revenue significantly decreased during 2009-2011, followed by a steady increase during 2012-2019. Over the past three years, revenues from fees and charges escalated to the absolute value.

Fees and Charges Revenue, 2006-2019 (%)

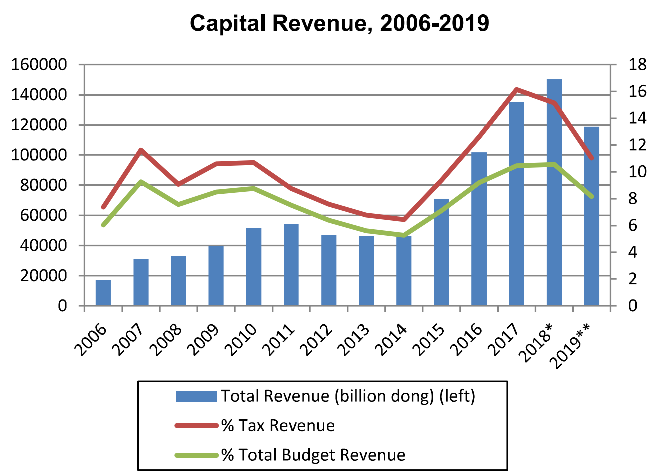


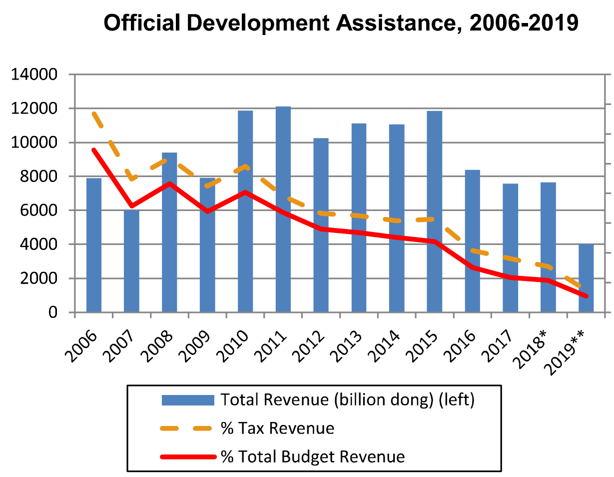
Note: * The 2018 data is the second estimate, ** The 2019 data is the first estimate.

Source: Author's calculation based on the data of the Ministry of Finance (2007-2020)

Structure of Budget Revenue
Capital Revenue and ODA

- Capital revenues included revenues from domestic and foreign loan principals, the interest of these loans, and state-owned capital contributions.
- Official Development Assistance declined in both proportion and revenue.



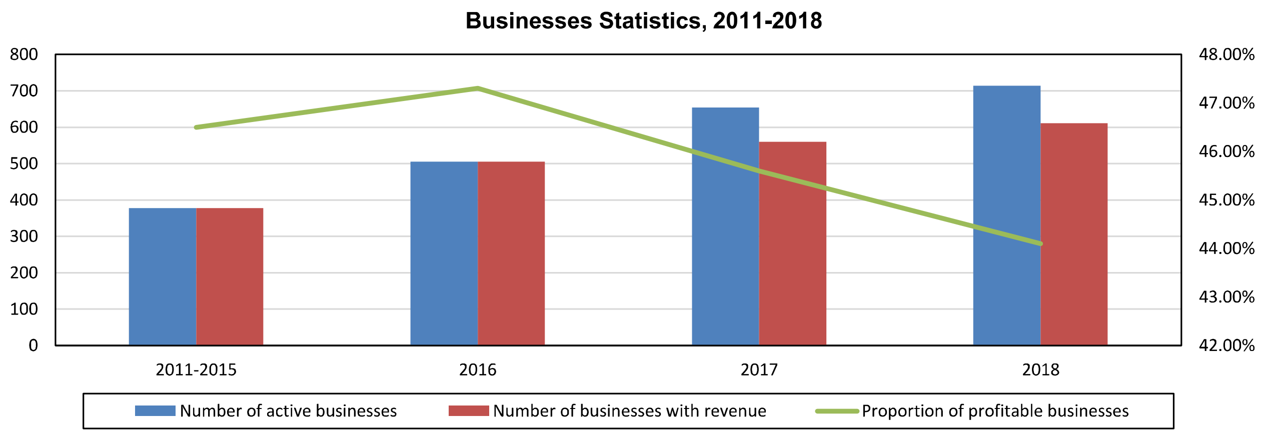


Note: * The 2018 data is the second estimate, ** The 2019 data is the first estimate.

Source: Author's calculation based on the data of the Ministry of Finance (2007-2020)

Individual and Organizational Taxpayers

- According to the General Department of Taxation, the number of personal income taxpayers was estimated at 8,1 million (2015).
- Up until 31/12/2018, the country has had 714,8 thousand enterprises currently operating. Specifically, 610,6 thousand enterprises generated revenues (85,4%). Enterprises that generated profits accounted for 44,1%. However, this rate fell perpetually during 2016-2018.



Sources: GSO (2020)

VEPR Informal Economic Sector

- Some estimations claimed that informal economic sectors accounted for 30% of Vietnam's GDP.
- The number of unregistered household businesses (informal businesses) was 4,9 million, making 60% of the total number of businesses in Vietnam.
- When an enterprise transfers to the formal sector, they could be burdened with relatively high formal and informal expenses. The cost of tax liability could be 39,4% of the profit (WB, 2018).
- According to PCI (2019), 63,4% of the surveyed enterprises were required to pay informal fees, increased slightly in comparison with 2018. This major barrier could prevent informal businesses from becoming formal.

VEPR Tax Incentives

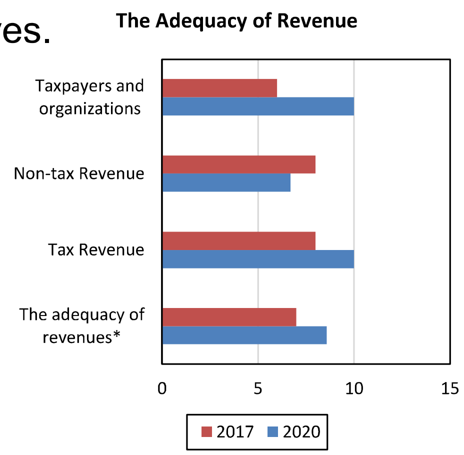
- After the Law on Corporate Income Tax issued in 2008 (amended in 2013), tax incentives were determined under this Law and its guiding documents.
- Legal framework allowed the government and localities to offer tax incentives for specials cases.
- The self-declaration mechanism causes diffculties in measuring the budget deficits caused by tax incentives.
- According to the Ministry of Finance (2018), in 2016, without the tax incentives (fees, charges, land/water rent), 64 thousand billion VND could have been added to the state budget revenue. This number is equivalent to 5.8% of the total budget revenue, 33% of the total current expenditure on education and training, and 84% of the current spending on healthcare.

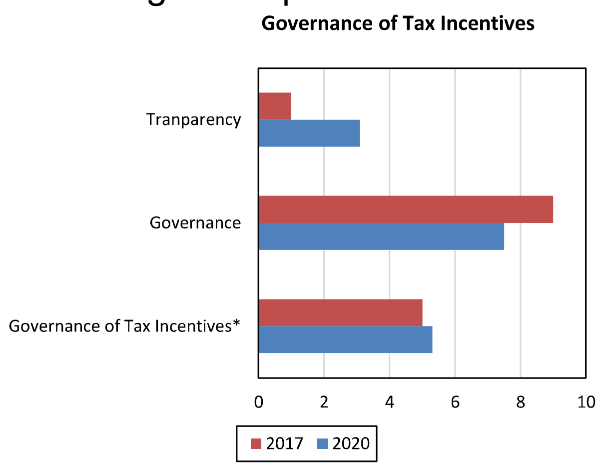
VEPR Tax Avoidance

- Since 2010, Vietnam has established positive policies to prevent tax avoidance. This fight against tax avoidance appears to be relatively successful since then.
- Despite many policies issued for this problem, tax avoidance has been very challenging to the tax authorities in Vietnam. Several major domestic firms find ways to reduce the amount of corporate income tax payable such as transfer pricing, implementation of specific projects eligible for tax incentives or even smuggling.
- In 2014, inspection results published by tax authorities in 2014 showed that 720 out of the 870 FDI enterprises have violated the tax law.
- Two expected measures to solve the problem of tax evasion will be more widely deployed in Vietnam in the upcoming time are consisted of digital payment and electronic billing.

VEPR Fair Tax Monitoring

- Vietnam's budget revenue was reviewed relatively well regarding its completeness. As evaluated by the Fair Tax Monitoring (FTM, 2020), the score on the adequacy of revenue sources has been improved compared to 2017's score.
- Particularly the index on governance slightly decreased compared to 2017 due to the ongoing problems related to monitoring the implementation of the tax incentives.





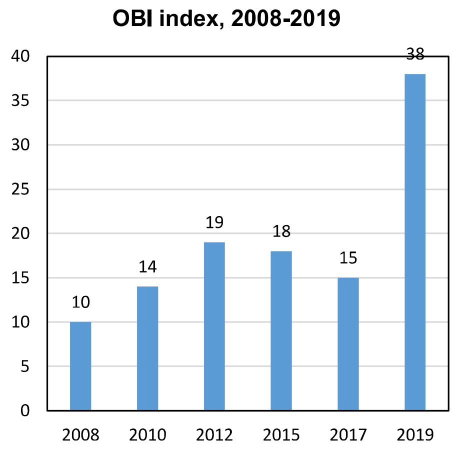
Note: * This index is calculated as the average of the component indexes in the FTM questionnaire.

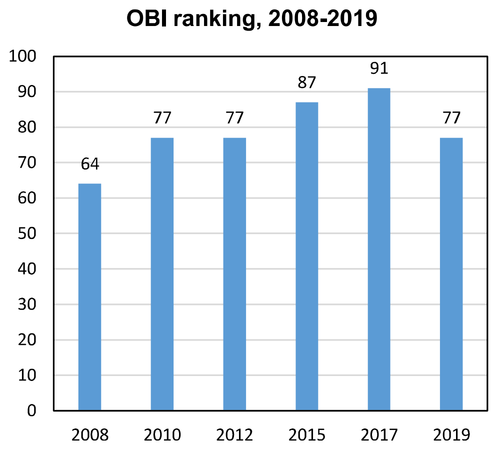
Source: Author's calculation based on the FTM data (2017, 2020)

Budget Transparency and Information Access

■ The Open Budget Index (OBI, 2017) – evaluated the Vietnam state budget transparency at the low level. However, in 2019, Vietnam witnessed an increase of 14 levels in the OBI, ranking 77th in the total of 117 ranked countries.

■ Statistics about the budget revenue are published at http://www.mof.gov.vn.





Source: IBP (2020)

Conclusions and Policy Recommendations

■ State budget revenue gained from tax accounted for the largest proportion. During 2006-2019, on average, this figure was about 78% of the total budget revenue.

■ The share of direct tax to the total tax revenue decreased drastically during 2012-2017 but tended to accelerate again in terms of both proportion and absolute value in 2018 and 2019. Corporate income tax made the largest percentage in the direct tax structure.

■ The proportion of indirect tax in the total tax revenue was gradually higher and over 60% in 2016 and made 11% of the GDP. Value-Added Tax generated the largest revenue among any types of indirect taxes.

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Conclusions and Policy Recommendations (cont.)

- The number of operating enterprises gradually raised time over time, but the rate of enterprises that could generate profits tended to curtail, which directly affect the tax revenue. Thereby, it is important to improve the investment environment and procedures more transparently, paving the way for enterprises to reduce unnecessary costs
- Some of the budget publication and expenditure of the government remains troublesome. The budget settlement is not punctually published. Statistics about the budget revenue have been lost due to the exclusion of tax exemption in Vietnam. The management of tax incentives in Vietnam is bringing about controversies over transparency.
- Vietnam needs to reinforce the publication activities and elucidate the statistics about the state budget revenue. Some responsibilities include the publication of the statistics about taxpayers, tax expenditure, especially the tax incentives in the annual budget reports, and assuring the publication to be punctual in line with international standards.

VEPR

Tax Incentives Competition among ASEAN Countries: A Case of Corporate Income Tax

Outline

- Comparative Overview of ASEAN countries' macro-economy
- Finance and budget systems in ASEAN Countries
- Foreign Direct Investment in ASEAN Countries
- Legal Framework on Corporate Income Tax Incentives
- Standard Corporate Income Tax in ASEAN Countries
- Tax Incentives in ASEAN Countries
- Tax Incentives and FDI
- Conclusions and Policy Recommendations

Overview of ASEAN Countries' Macro-economy

- ASEAN countries own a major diversity and difference regarding the macroeconomics, populations, economic scale, economic degree of openness, and good management. Singapore and Brunei are the two nations that possess the highest average income per person in the region but the smallest population with fewer than 6 million people.

Overview of ASEAN countries, 2018

Country	Population (million)	Labour forces, % population)	GDP (constant prices, billion USD)	GDP (PPP constant prices, billion USD)	GDP per capita (PPP)	Poverty rates
Singapore	5.64	61.96	328.44	508.00	90,091.42	n.a
Brunei	0.43	49.99	13.49	30.80	71,802.27	n.a
Malaysia	31.53	48.79	382.13	889.14	28,201.06	0.40
Thailand	69.43	56.04	441.68	1,173.67	16,904.70	9.90
Indonesia	267.66	49.59	1,146.84	3,106.46	11,605.86	9.80
Philippines	106.65	41.13	322.30	847.08	7,942.51	21.60
Vietnam	95.54	59.57	187.69	631.39	6,608.62	6.70
Laos	7.06	52.85	12.61	46.62	6,601.33	23.40
Myanmar	53.71	45.56	84.42	318.06	5,922.02	24.80
Campuchia	16.25	56.56	19.58	62.88	3,869.49	17.70

Note: poverty data: Myanmar (2017); Campuchia and Laos (2012); The Philippines and Malaysia (2015).

Source: World Development Indicators – (WB, 2020)

Financial and Tax Systems in ASEAN Countries

■ Public financial systems of several ASEAN countries are under huge pressure coming from public debt. The highest rate of public debt in ASEAN belongs to Singapore, Laos, Vietnam, and Malaysia. But Singapore managed to control its public debt while the state budget revenue reached a surplus of 3,7% in 2018.

Public Financial Indicators in ASEAN, 2007-2018, (% GDP)

Country	Debt data				Budget data		
	Public debt, 2007	Public debt, 2015	External Public debt, 2015	External Public debt, 2018	Expenditure 2018	Revenue 2018	Budget deficit, 2018
Singapore	86.3	104.7	n.a	n.a	14.0	17.7	3.7
Laos	62.5	61.9	46.5	51.0	20.9	16.2	-4.7
Vietnam	40.9	58.3	24.0	21.7	22.9	19.5	-3.5
Malaysia	39.9	57.4	n.a	n.a	22.7	19.4	-3.3
Thailand	35.1	42.7	5.6	7.1	21.4	21.4	0.1
Philippines	44.6	34.8	13.4	11.0	21.9	20.2	-1.6
Myanmar	62.5	34.3	21.9	19.2	21.8	18.8	-3.0
Campuchia	30.5	32.5	30.2	27.4	23.1	23.9	0.7
Indonesia	32.3	27.3	18.5	20.9	16.6	14.9	-1.8
Brunei	0.7	2.8	n.A	n.a	n.a	n.a	n.a

Note: Public debt is calculated from the WB's data (2020), other is calculated from the IMF's data (2020).

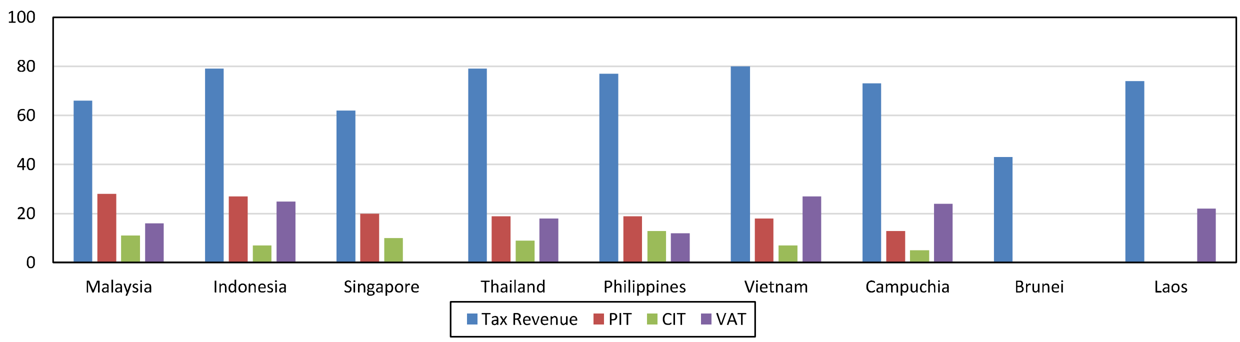
Source: Global Debt Database – IMF (2020); World Development Indicators - WB (2020)

Financial and Tax Systems in ASEAN Countries (cont.)

■ Budget revenue to GDP ratio maintains various among ASEAN countries, the lowest ratio is Indonesia's with 14,9% while the highest is Cambodia's with 23,4%.

■ Tax is the most important means for budget revenue in ASEAN countries. Some countries' budget revenue relies on corporate income tax such as Malaysia, Indonesia, Singapore, with this revenue rate accounting for more than 20% of the total budget revenue.

Structure of budget revenues in ASEAN countries, 2017



Note: Data from Cambodia and Malaysia in 2016, not available data for Myanmar since 2006.

Source: World Revenue Longitudinal Dataset (WoRLD) – (IMF, 2020b), and (Vietnamese Ministry of Finance, 2019)

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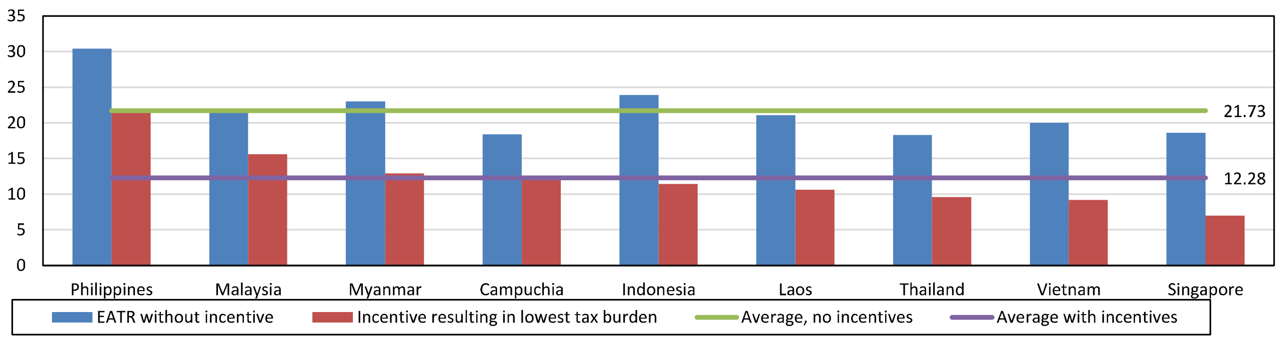
Financial and Tax Systems in ASEAN Countries (cont.)

■ One of the major matters in the tax system is that the tax incentives erode the tax base in ASEAN countries (OECE, 2019).

■ The average effective tax rate with tax incentives, on average, is less than 9.4 percentage points than the effective tax rate without tax incentives.

■Singapore and Indonesia are the two countries that have the highest difference between tax rates before and after being imposed with tax incentives, which is 11 percentage points.

Average effective tax rates (AETRs) with and without incentives (%)



Source: Verena & Katharina (2015)

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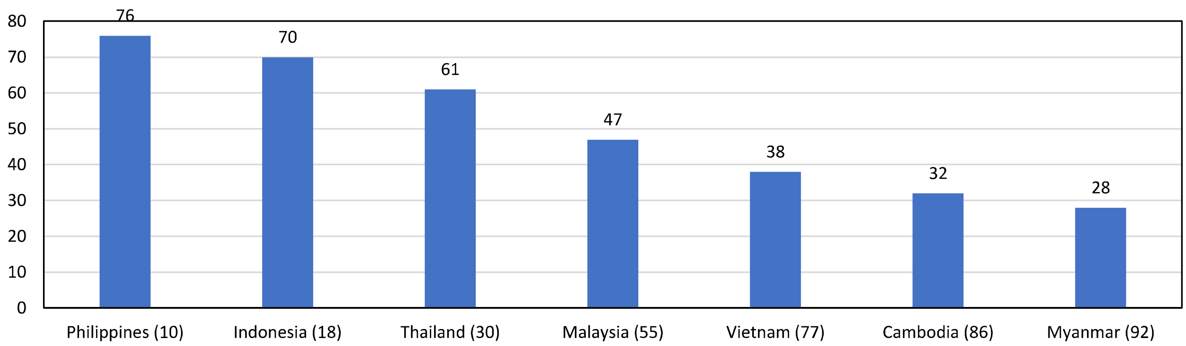
Financial and Tax Systems in ASEAN Countries (cont.)

■ The degree of budget transparency between the countries is highly various.

■ Among the ASEAN countries that have the Open Budget Index (OBI), the Philippines had the highest index (76/100), ranking 10th among the 117 evaluated countries.

■ Meanwhile, Myanmar had the lowest index (28/100) and ranked 92nd over 117 evaluated countries.

Open Budget Index (OBI) in ASEAN, 2019



Note: This index assesses budget transparency of 117 countries on a scale of 0 (not transparent) - 100 (very transparent)

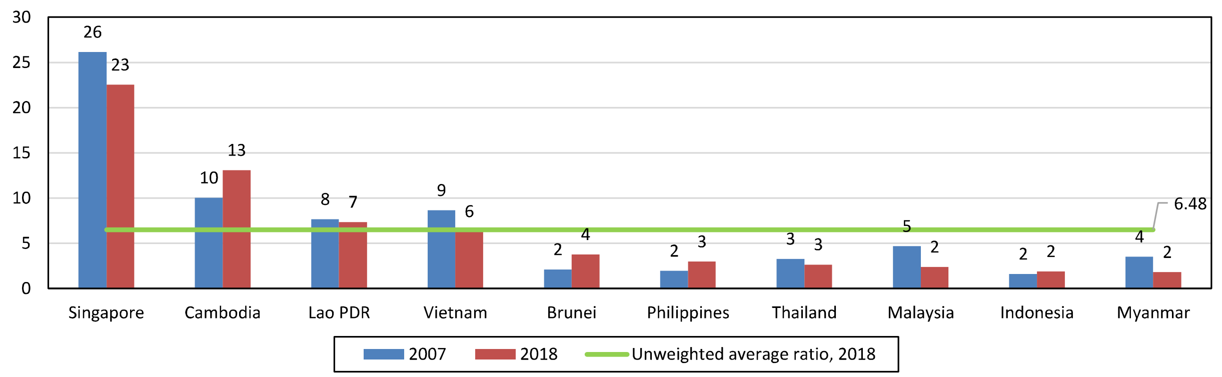
Source: IBP (2020)

Foreign Direct Investment in ASEAN Countries

■ The inflow FDI capital into ASEAN countries, on average, increased 5,2% during 2010-2018. Singapore has received 50% of the total FDI capital.

■ Cambodia also attracted a large amount of FDI inflow, with a rate of more than 13% of GDP in 2018. China owned the largest FDI capital in Cambodia in 2018. At the same time, China bore the primary investor of Laos, transferring 79% FDI capital to Laos in 2018.

Net FDI Inflows in ASEAN countries, 2007-2018 (% GDP)



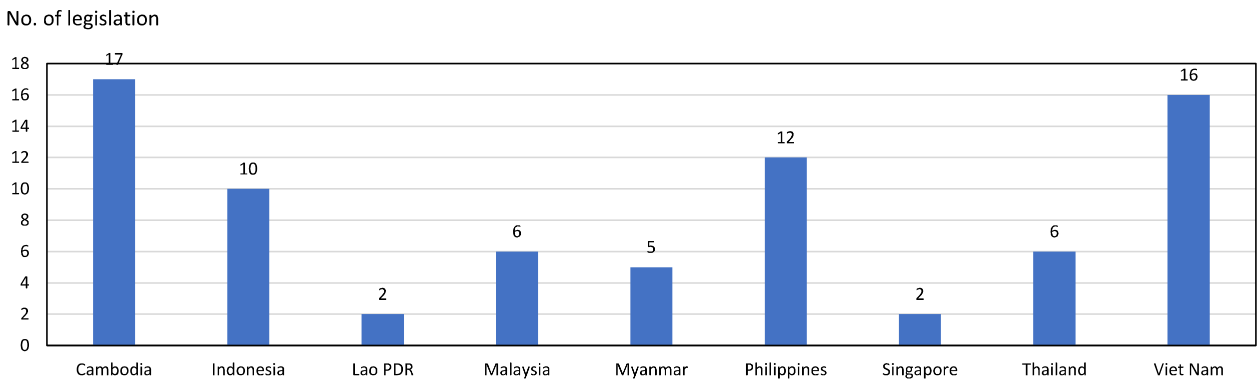
Source: WB (2020)

Legal Framework on Corporate Income Tax Incentives

■ Normally, tax incentives are determined in the Tax Law and Laws related to foreign investment.

■ Tax laws in general and, in particular, the Laws on tax incentives in particular are constantly amended to meet the needs of socio-economic development nationally. In ASEAN region, the Laws on tax incentives are updated to follow the trend of enhancing incentives.

Number of effective legal documents of CIT incentives in ASEAN, 2020



Note: In Laos and Singapore, only official laws are listed

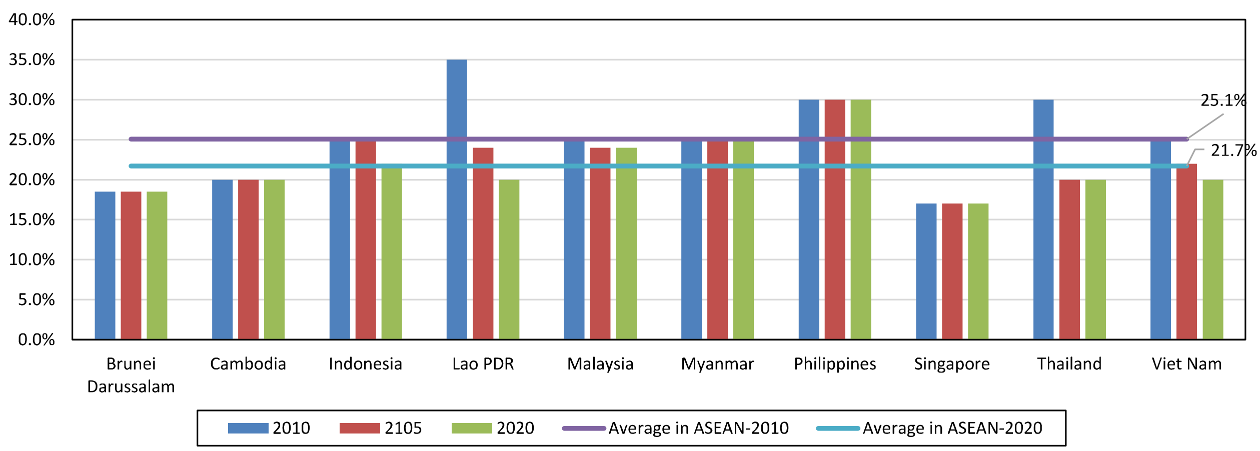
Source: The authors' review

Standard Corporate Income Tax in ASEAN Countries

■ ASEAN nations set their own standards corporate income tax: The highest tax rate is 30% belonged to the Philippines while the lowest is 17% in Singapore.

■ The average corporate income tax in the ASEAN countries tended to decline over the past decade, from 25,1% (2010) to 21,7% (2020).

Standard corporate income tax in ASEAN, by host country, 2020 (%)



Source: tradingeconomics.com

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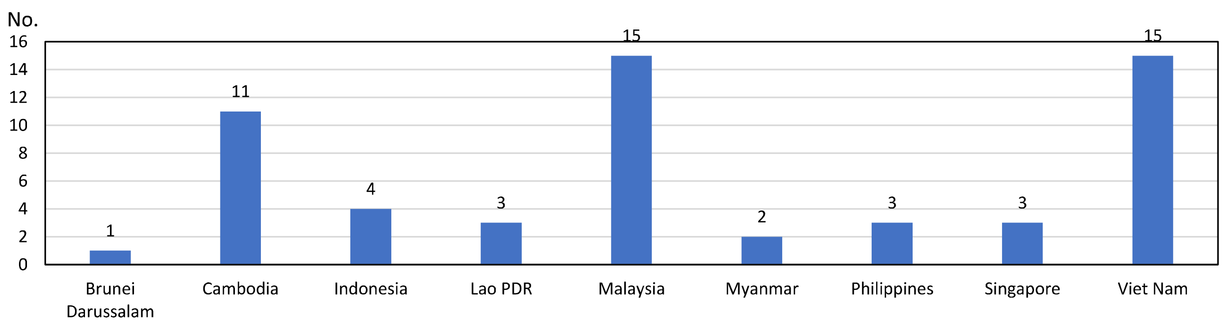
Tax Incentives in ASEAN Countries

Tax Exemptions

■ Depending on different priorities of the governments, they determine the eligible activities and fields for tax exemptions. Laos, Myanmar, and Indonesia provide tax exemptions for reinvesting activities. Vietnam and Cambodia enact the same policy to economic activities in the agriculture sectors. Malaysia does so for its approved service projects. Singapore and Brunei provide tax exemptions for small and medium enterprises.

Number of activities/sectors enjoyed CIT exempt in ASEAN, 2020



Note: There are differences among countries in the category of tax-exempt. For example: Vietnam and Cambodia classified by income source. Singapore, Indonesia, Lao PDR, Malaysia, Myanmar and the Philippine classified by business activities. Brunei classified by business scale.

Source: The authors' review and classifications

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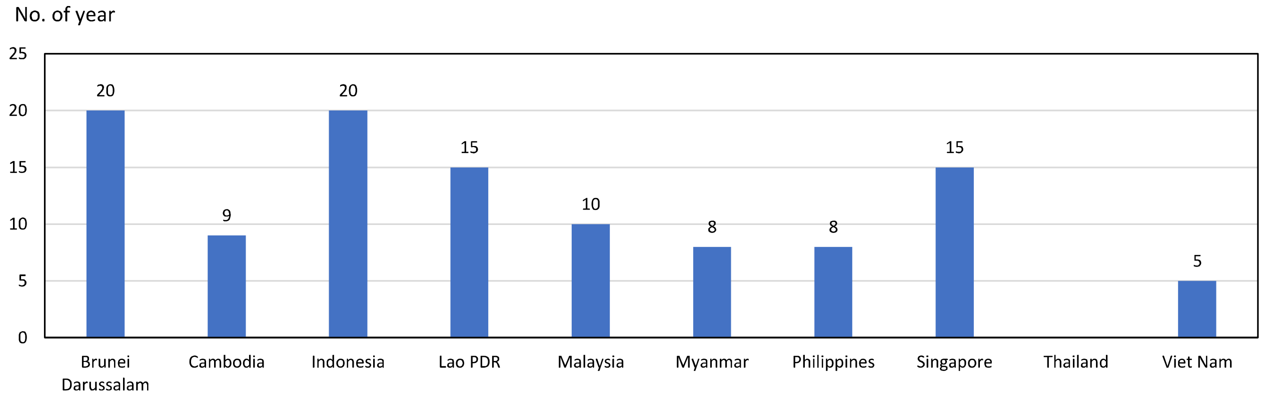
Tax Incentives in ASEAN Countries
Tax Holidays

- Tax holidays in ASEAN normally last from 5 to 20 years depending on the law by countries.
- The average length for the tax holidays in ASEAN is about 12 years.
- Brunei and Indonesia are the nations that provide the longest tax holiday period in the region, up to 20 years.

Maximum period of tax holidays in ASEAN, by host country, 2020 (No. of year)



Source: The authors' review

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Tax Incentives in ASEAN Countries
Tax Preferences

- While the tax exemption and tax holiday are limited to the group of beneficiaries, the tax preference is usually more open to other business activities.
- Enterprises in ASEAN countries can be imposed with a 50% to 100% reduction on corporate income tax.
- Cambodia, Thailand, Indonesia, and Malaysia are the four nations that provide the most attractive preferential tax rate, up to 100% of taxable income.

The CIT rate and preference in ASEAN, by host country, 2020

Country	General CIT rate	CIT rate after preferencing (at the highest preferential level)
Brunei	18.5%	n.a
Campuchia	20%	0%
Indonesia	22%	0%
Laos	20%	5%
Malaysia	24%	0%
Myanmar	25%	12.5%
Philippines	30%	5%
Singapore	17%	5%
Thailand	20%	0%
Vietnam	20%	10%

Source: The authors' review

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Tax Incentives in ASEAN Countries

Tax Deductions

- Enterprises in the ASEAN region are allowed to deduct all reasonable expenses related to production and business activities.
- Some nations such as Cambodia, Malaysia, Singapore, and Thailand provide **additional tax deductions** on activities related to SMEs, training, R&D, exporting, and expanding oversea. Singapore offers up to **400%** tax deduction on certain eligible expenditures
- In Vietnam, tax deductions are applied to the additional charges for female laborers in companies focusing on the production, construction, or transportation, and for ethnic minority groups in all kinds of business.
- In the Philippines, in the first five years since the date of registration, a registered enterprise shall be allowed to have an additional deduction from taxable income equivalent to 50% of the wages of additional skilled and unskilled workers in the labor force.

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Tax Incentives in ASEAN Countries

Transfer Losses Forward

- Tax losses in Malaysia and Singapore could be transferred for unlimited time and compensated by the profit gained from future transactions.
- Indonesia allows an extension of tax losses carried forward for up to 10 years depending on field and business area.
- The other countries provide the 3-6 years of loss transferring time.

Transfer losses forward in ASEAN, by host country, 2020

Country	Maximum transfer period (years)
Brunei	n.a
Campuchia	5
Indonesia	10
Laos	3
Malaysia	Indefinitely
Myanmar	5
Philippines	6
Singapore	Indefinitely
Thailand	5
Vietnam	5

Source: The authors' review

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Tax Incentives in ASEAN Countries

Other Tax Incentives

- The governments provide several other tax incentives such as tax credits, investment subsidies, and depreciation
- In Singapore and Indonesia, incomes from other countries could avoid double taxation through foreign tax credit granted under treaties for the avoidance of double taxation
- Singapore provides an M&A assistance, allowing for removal of 25% value of the acquisition executed from 4/2015 to the end of 3/2020.
- In the Philippines, the companies that satisfy substantial conditions could have a 50% tax deduction of their reinvestment assistance. Malaysia also provides accelerated capital assistance for the enterprises.
- The accelerated depreciation method is applied in many countries. In Vietnam, the minimum time frame of depreciation of all types of fixed assets could be 5-6 years, even shorter, 2-3 years

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Tax Incentives and FDI

- Current studies point out the fact that the use of tax incentives as a tool to attract investment have shown little effect on ASEAN countries at the aggregate level (Oxfam, 2016; OECD, 2019)
- The relationship between tax incentives and FDI in nations could be divided into three groups:
  - Positive effect but risky: Cambodia, Malaysia, Singapore, Thailand, and Vietnam.
  - Unclear effect: Indonesia and Myanmar.
  - Limited effect: Brunei and the Philippines.
- The tax incentives can be more efficient if built on a strong overarching investment climate, including good quality infrastructure, availability of skills, macroeconomic stability, better protection and enforcement of intellectual property right (Oxfam, 2016; OECD, 2019).

Conclusions and Policy Recommendations

- Tax incentives have become more and more popular, especially ones that are related to the corporate income tax. But overuse of tax incentives could cause developing countries to “race-to-the-bottom”.
- Enterprises in the ASEAN region, tax incentives are provided at a high level and the actual amount of revenue forgone due to such incentives are huge
- The application of excessive tax incentives bears many limitations. Some examples are the high implementation and compliance costs, the potential of corruption, inequality extension, unfair investment environment, and revenue base erosion.
- The ASEAN countries need to restructure the tax incentives by limiting and removing unnecessary incentives. Transparency in the tax management requires strong reinforcement. Statistics about the tax expenditures in annual budget reports need to be published, moving towards to a formation of a regional common mechanism of tax incentives such as setting a shared minimum efficient tax rate.

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Vietnam Tax Expenditures: the Case of Corporate Income Tax

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VEPR Outline

- Introduction on Tax Expenditures
- CIT Expenditure Estimates for Viet Nam
- The Impacts of Eliminating Tax Expenditures
- Conclusions

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VEPR Definition of Tax Expenditure

- According to international practice, tax revenue losses are the amount of unearned due to: (i) Tax avoidance, (ii) Tax evasion, (iii) Tax expenditure (DFID, 2009).
  - Tax avoidance: Reducing the income tax paid by exploiting methods within the legal frameworks (Dyreng SD, Hanlon M, Maydew EL., 2008).
  - Tax evasion: Undertaking illegal methods to minimize the total income tax paid (Allingham and Sandmo, 1972).
  - Tax expenditures represent the amount of tax revenue foregone by offering tax incentives. Therefore, tax expenditures are illustrated by difference between the actual tax revenue and tax revenue according to benchmark tax system.

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Tax expenditures
Measures, purposes, and risks

- The diversification of tax expenditures:
  - Schick (2007), in OECD country members: tax reduction, tax subsidies and tax assistance
  - Tyson (2014): subsidies (deductions from the base), exemptions (exclusions from the base), rate relief (lower rates), credits (reductions in liability) and tax deferrals (postponing payments)

- Purposes
  - Improve the attractiveness of the investment environment
  - Attracting more foreign direct investment (FDI)

Risks
  - Tax base erosion
  - State budget loss due to tax incentives exceeding projected loss
  - Reducing resources for economic development and social welfare

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Tax expenditure estimate
Methodology and Models

Methodology

- Revenue forgone: Measures the reduction in tax revenue caused by a tax incentive after it has already taken effect.
- Revenue gains: Measures the additional tax revenue by removing tax incentives
- Outlay equivalence: Measures the sum of government spending needed in order to bring equivalent benefits in comparison to those when implementing tax incentives

Models

- Micro-stimulation model (OECD, 2010)
- Computable General Equilibrium model (CGE) (UNDP, 2018)
- Traditional accounting model (“head count” approach)

VEPR Tax Expenditure Estimate

- Tax incentives of CIT in Vietnam
- Tax incentives and tax expenditures
- Tax expenditure estimate in Vietnam
- Tax Expenditure in comparison with State Budget
- Classification by ownership
- Classification by economic sector and activity

VEPR Tax incentives of CIT

Legal framework

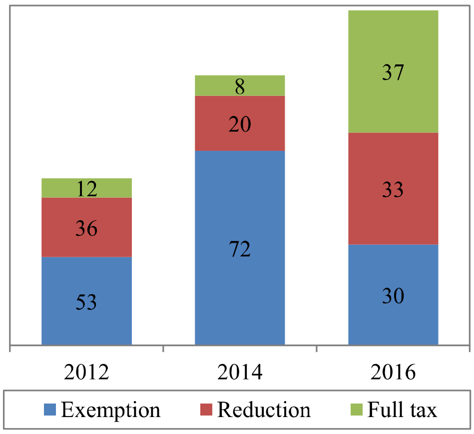
- Law on Corporate Income Tax 2008
- Law on Amended Corporate Income tax 2013
- Law 71/2014/QH13 amending and Supplementing a Number of Articles of the Laws on Taxes
- Decree 92/2013/NĐ-CP
- Decree 218/2013/NĐ-CP
- Decree 91/2014/NĐ-CP
- Decree 12/2015/NĐ-CP
- Circular 78/2014/TT-BTC
- Circular 96/2015/TT-BTC
- Circular 19/VBHN-BTC dated 20/7/2018

Forms of incentives

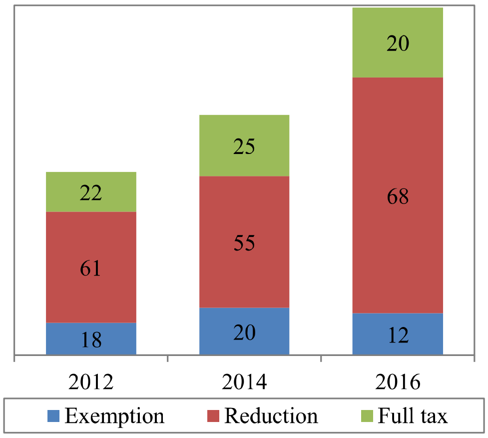
Forms	Content s
1. Tax exemption for some sources of income	Income from cultivation, husbandry, processing of agricultural products, aquatic products, salt harvested by cooperatives; income from transfer of emission reduction ...
2.Tax rate reduction	10% general tax rates in 15 years and 17% in 10 years (in comparison with general tax rate of 20% since January 1, 2016).
3. Tax holiday incentives	Exempting tax for 4 years and followed by a reduction up to 50% for the next 9 years or exempting in 2 years and reducing 50% for the next 4 years (depending on the projects' sector or location, including the project's expansion phases).
4. Loss transferring	Enterprises could forward losses to subsequent years. Time forward losses shall not exceed 5 years from the year following the year incurred.
5. Accelerated depreciation	Applying accelerated depreciation for fixed assets:The maximum rate shall not exceed twice the ordinary depreciation rate.
6. Other forms	Enterprises have significant number of woman; Enterprises employ substantial ethnic minority labour.

Source: Oxfam (2016).

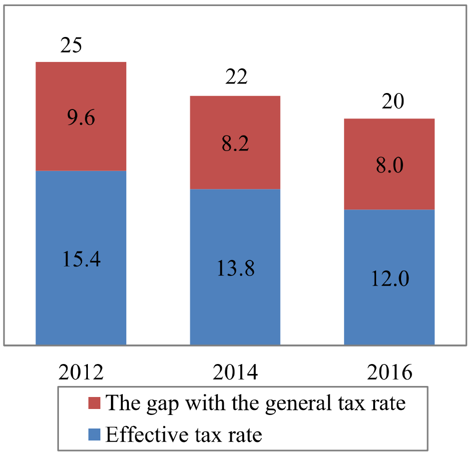
Tax Incentives and Tax Expenditures



The number of enterprises



The profit of enterprises



The effective tax rate

- Tax expenditure:
  - Tax-exempt expenditure:
    - Tax Exemptions
    - Zero tax rate
    - Tax Holiday
  - Tax-reduction expenditure: Preferential tax rate

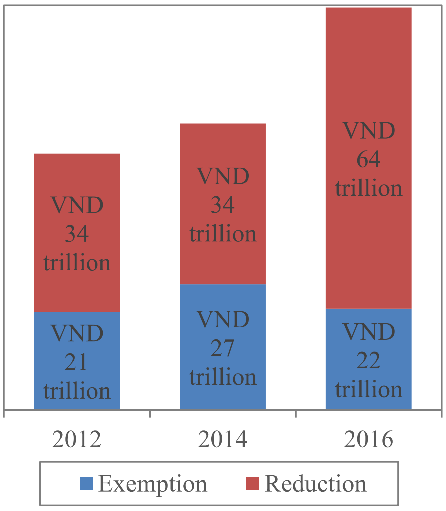
Tax Expenditure Estimate in Vietnam

- Methodology: Revenue foregone approach
- Tax expenditure:
  - The gap between the effective tax rate and the general tax rate
  - Tax base: the profit of all enterprises
- Effective tax rate and proportion of enterprises paying tax

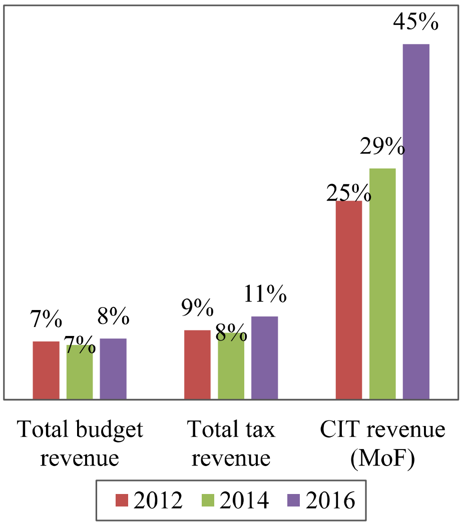
For a group of enterprises, the lower the actual tax rate, the greater the tax incentives they gained. The lower the share of tax payer in a group , the greater tax exemption that group gained.

- Data: 2012, 2014, and 2016 Vietnam Enterprise Survey

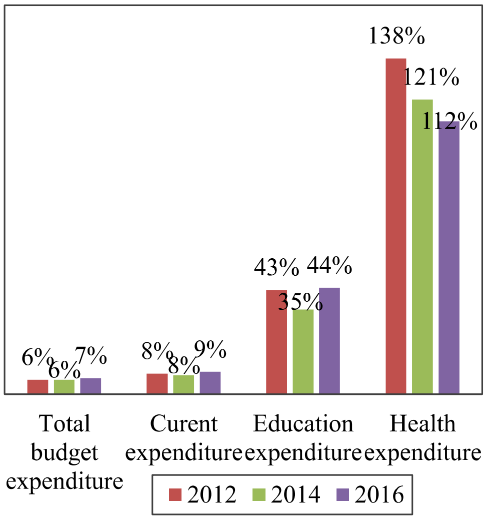
Tax Expenditure in comparison with State Budget



Tax expenditure



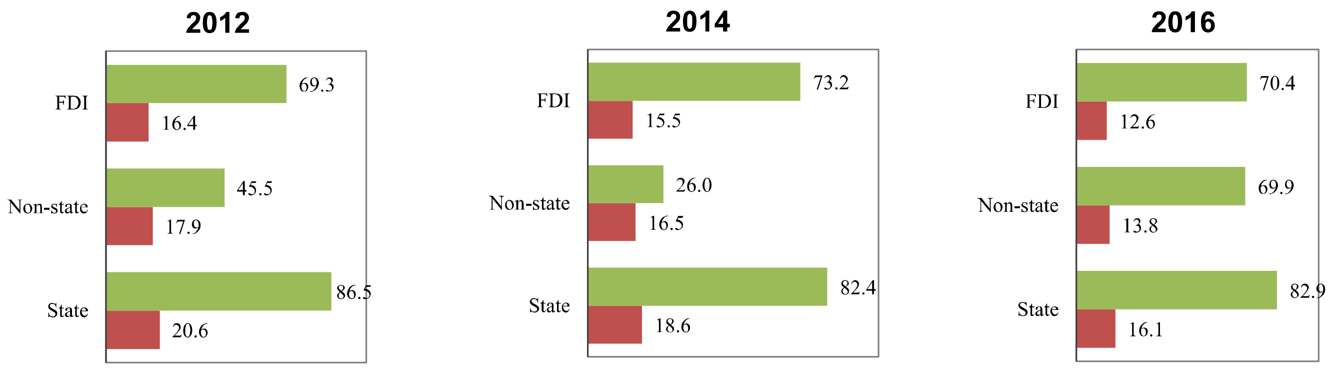
Compared with budget revenues



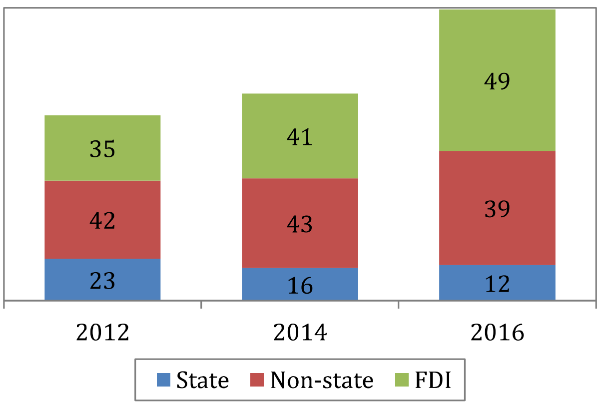
Compared with budget expenditures

- The tax expenditure estimated for corporate income tax, based on Vietnam Enterprise Census (VEC), was more than 1.5% of GDP.
- Meanwhile tax expenditures for all taxes in the Philippines was 1.49% of GDP (2011) and in Senegal was 3.9% of GDP (2012).

Classification by Ownership



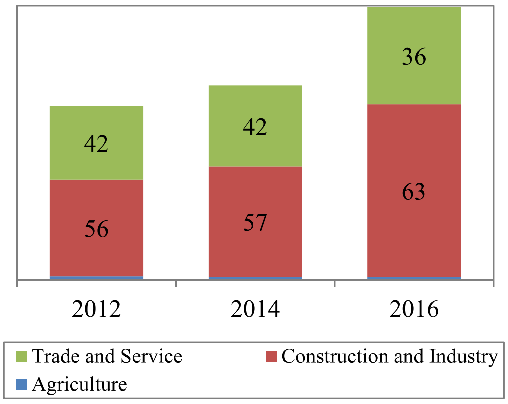
Effective tax rate and proportion of enterprises paying



Structure of tax expenditure

- The proportion of foriegn-invested enterprises was about 3% of total positive profit enterprises, while the figure of non-state enterprises was 96%.
- However the proportion of tax expenditure of FDI enterprises was nearly a half (2016). And the effective tax rate of this group was always the lowest rate, tax expenditure for FDI enterprises is 10 times higher than the non-state enterprises

VEPR Classification by Sector and Activity



Structure of tax expenditure by industry

Industry and construction sectors enjoy the most tax reduction over the years, the highest is 63% (2016).
+ In particular, the processing and manufacturing industry accounts for 56% of total tax expenditure (2016).
+ The most notable is the manufacturing of electronic products, computers and optical products.

	Economic activities	Number of Enterprise (%)	Tax Expenditure (%)	Effective Tax Rate (%)
3	Manufacturing	16.1	56.0	10.1
3.1	Manufacture of computer, electronic and optical products	0.3	24.7	3.0
3.2	Manufacture of food products	1.6	6.4	13.0
3.3	Manufacture of chemicals and chemical products	0.7	2.2	15.3
3.4	Manufacture of metals and fabricated metal products	3.2	3.5	13.0
7	Wholesale and retail trade; repair of motor vehicles, motorcycles and other motor vehicles	39.7	17.9	10.3
7.1	Wholesale (except motor vehicles, motorcycles and other motor vehicles)	26.3	13.4	12.3
7.2	Retail trade (except motor vehicles, motorcycles and other motor vehicles)	11.1	2.0	17.0
7.3	Sale and repair of motor vehicles, motorcycles and other motor vehicles	2.2	2.9	7.7

VEPR Assessing the Impacts
Using CGE model

- The CGE model
- Data
- The simulation analysis
  - Scenarios
  - Macro impacts
  - Household Consumption
- Micro-simulation analysis
  - The effects on poverty
  - The effects on income distribution
  - Regression analysis

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Computable General Equilibrium Model

- This study employs and a standard single-country CGE model to analyze the effect of tax incentives
  - The CGE model takes into account inter-industry linkages and the links between commodity and factor markets.
- The CGE model is a powerful tool to analyze the macroeconomic and distributional effects of tax policy changes.
- Our CGE model specifies 30 industries, 7 production factors, and 10 households.
- The model specifies physical capital (agricultural and non-agricultural capital) and five types of labor (managers and high-level professionals, medium-level professionals, staff and skilled workers, semi-skilled workers, and unskilled workers).
- Households are classified according to urban/rural area and five income groups.

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Computable General Equilibrium Model
Three sectors

- Households: Household income consist of labor incomes, capital incomes from self-employed activities, profits transferred from the corporate sector, government subsidies, and transfers from the rest of the world (remittances).
  - Households save a fixed proportion of income and spend the remaining on goods.
- The corporate sector: Income from capital and investment income from abroad. Businesses pay corporate income tax, transfer income to the government, transfer a portion of profits to households, and transfer profits abroad. The rest is savings.
- Government: Budget revenues include revenues from taxes and transfers from businesses and from foreign countries. The government spends on consumption, subsidies for households and saves for investment.

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Computable General Equilibrium Model
The types of taxes

- The CGE model takes into consideration following taxes:
  - Value-added tax
  - Indirect taxes
  - Import taxes
  - Personal income taxes
  - Corporate income taxes.
- The corporate income tax is imposed on the corporate income (excluding the capital incomes from self-activities).

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Data

- We makes use of different data sources to construct the benchmark dataset, including the 2012 Input-Output Table (IO 2012) constructed by the General Statistical Office (GSO), the 2012 Vietnam Household Living Standard Survey (VHLSS 2012).
- The 2012 VHLSS is used to allocate incomes to different types of labor and capital and different household groups.
  - We employ the daily wage rates and the number of working days calculated from the 2012 VHLSS to estimate industrial employment and labor incomes by types of labor.
  - The capital incomes from self-employed activities is estimated from the VHLSS, then these incomes are allocated to different household groups.

VEPR Data

- The information on profits, dividends, and other capital incomes from the 2012 VHLSS is used to estimate the value of profits transferred from the corporate sector to households and from the government to households.
- We use the information on household consumption from the 2012 IO and the share of household spending on each commodity calculated from the VHLSS to estimate household expenditure.
- Remittances, the net payments of investment incomes and foreign transfers to the government (official transfers) are collected from the balance of payments statistics
- Tax receipts for different types of taxes are taken from the input-output table and the official budget statistics.

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VEPR The Simulation Analysis

- In order to remove the tax expenditure, government must prevent all tax incentives, totally abolish the tax incentives
- Simulation analyses evaluate the medium-term effect of the abolition of tax expenditure of the corporate income tax: in all the simulations, production capital in each field was held stable whereas labor was to mobilize between the fields.
- Simulations are abide by neoclassical economics principles; therefore, investment was measured by the existent savings. Consumer Price Index was regarded as initial standard.

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The Simulation Analysis
Scenarios

Scenarios	Description
S1	Complete removal of corporate income tax (CIT) expenditures.
S2	Complete removal of CIT expenditures. (S1); the increase in budget revenues is used to raise government savings and consumption.
S3	Complete removal of CIT expenditures (S1); The increase in budget revenues is used to raise savings and subsidies for households.
S4	The government maintains the CIT expenditures, but raises VATs to obtain the same level of budget revenues as in the simulation S1.

The Simulation Analysis
Macro Impacts (%, change to baseline scenario)

	S1	S2	S3	S4
Gross output	0.09	-0.32	0.06	0.26
Real GDP	0.07	-0.02	0.07	0.02
Household consumption	-0.70	-0.86	-0.24	-4.03
Household income	-0.75	-0.90	-0.31	-4.10
Government consumption	0.00	21.72	0.00	0.00
Government revenues	19.71	19.31	19.70	19.71
Investment	6.44	1.36	5.24	10.63

- If the tax expenditure for CIT is removed, the budget revenues might increase by 20%.
- If the government uses this incremental budget revenue to allocate into development projects or to tackle the poverty, that might improve the social welfare and the economic growth.
- If the majority of the revenue generating from the tax expenditure abolition is allocated into current expenditures, it might not improve the economic growth.
- In simulation S4, raising the VAT to compensate for the revenue losses resulting from CIT exemptions exerts a strong negative effect on household welfare.

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The Simulation Analysis

Household consumption (%, change to baseline scenario)

	S1	S2	S3	S4
Rural households				
Group 1 (Poorest)	0.19	-0.49	1.06	-3.75
Group 2	0.20	-0.45	0.87	-3.69
Group 3	0.06	-0.46	0.65	-3.78
Group 4	-0.06	-0.39	0.39	-4.02
Group 5 (Richest)	-0.32	-0.44	0.00	-4.47
Urban households				
Group 1 (Poorest)	0.27	-0.49	1.25	-3.36
Group 2	0.20	-0.41	0.60	-3.49
Group 3	-0.05	-0.33	0.28	-3.81
Group 4	-0.54	-0.47	-0.22	-4.01
Group 5 (Richest)	-2.65	-2.17	-2.34	-4.31

- The tax expenditure abolition has a stronger negative effect on the high-income groups than the low-income ones.
- In S1 and S3 (the incremental budget revenue is allocated into development projects or to tackle the poverty), the consumption of the low-income groups might be increased. In another word, the poor obtains the benefit from the tax expenditure abolition.
- If the majority of the revenue generating from the tax expenditure abolition is allocated into current expenditures (S2), the poor might suffer.

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The Simulation Analysis

Household income (%, change to base-run scenario)

	S1	S2	S3	S4
Rural households				
Group 1 (Poorest)	0.18	-0.59	1.05	-3.98
Group 2	0.20	-0.50	0.86	-3.84
Group 3	0.05	-0.50	0.64	-3.89
Group 4	-0.05	-0.42	0.39	-3.99
Group 5 (Richest)	-0.31	-0.48	0.01	-4.29
Urban households				
Group 1 (Poorest)	0.25	-0.49	1.25	-3.67
Group 2	0.18	-0.42	0.59	-3.72
Group 3	-0.06	-0.34	0.28	-3.91
Group 4	-0.55	-0.46	-0.22	-4.14
Group 5 (Richest)	-2.64	-2.12	-2.34	-4.31

- Similar to the changes in household consumptions in the previous slide.
- Government's response to the increase of budget revenue due to tax expenditure might be to determine the effect on low-income households' income and consumption.
- In S4, both low-income and high-income households suffer from income and welfare losses due to a VAT increase instead of a tax expenditure removal.

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The Micro Simulation Analysis

- Micro-simulation analyses allow for impact evaluation of taxation policies in every household's level.
- In these analyses, we used the change in prices of production factors and commodities from CGE simulation to assure the effective impact of the taxation policies on every household.
- The analyses used the Vietnam Household Living Standard Survey (2012).

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The Micro Simulation Analysis
Poverty

	Base-run scenario	**Simulation S1** (Removing CIT expenditures)	**Simulation S4** (Raising VAT)
Poverty headcount ratio	15.0	15.0	15.9
Urban	3.0	3.1	3.5
Rural	20.1	20.1	21.2

- Complete removal of tax expenditures for CIT has no effect on the poverty headcount ratio in both urban and rural.
- Rising VAT to increase the budget revenue, instead of eliminating tax expenditures, increases poverty rate, especially in rural areas (increase by 1.2 percentage points).

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The Micro Simulation Analysis
Income Distribution

	Base-run scenario	Simulation S1 (Removing CIT expenditures)	Simulation S4 (Raising VAT)
GINI coefficient	0.414	0.411	0.413
Urban	0.389	0.384	0.389
Rural	0.38	0.379	0.378

- The removal of all tax expenditures for CIT improves the income distribution.
- With the complete abolition of tax expenditures for CIT as in S1, the Gini coefficient slightly falls from 0,414 in the baseline scenario to 0.411 in S1.
- Income distribution improves more in urban areas than in rural areas.

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The Micro Simulation Analysis
Regression

- Higher income groups are affected more negatively.
- Rural households are less affected than urban households.
- The households whose heads have job are less affected

	Simulation S1 (Removing CIT exemptions)	Simulation S4 (Raising VAT)
By Income Groups (The first quintile is the base)		
Second quintile	-0.029	-0.483***
Third quintile	-0.121**	-0.699***
Fourth quintile	-0.174***	-0.848***
Fifth quintile	-0.576***	-0.917***
Urban/Rural (Urban is the base)		
Rural households	0.339***	0.019
Geographical locations (North West is the base)		
North East	0.083	0.124*
Red River Delta	-0.136	0.194***
Northern Central Coast	0.026	0.196**
Southern Central Coast	-0.036	-0.179**
Central Highlands	0.016	-0.936***
South East	-0.048	-0.547***
Mekong Delta	-0.216***	-0.464***
Occupations of household heads (Unemployed is the base)		
Self-employed in agriculture	0.216**	-0.984***
Self-employed in non-agriculture	0.550***	-1.312***
Wage earners	0.783***	-0.695***
Educational attainment of household heads (No degree is the base)		
Heads with primary school degree	-0.017	-0.026
Heads with secondary school degree	-0.139**	0.027
Heads with tertiary school degree	-0.278***	-0.133**
Heads with college and university degrees or higher	-0.422***	-0.377***

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The Effects of Tax Policy - Regression Analysis

- Female-headed households are less affected.
- The impact of rising the value-added tax tends to increase according to household size.

	Simulation S1 (Removing CIT exemptions)	Simulation S4 (Raising VAT)
Gender of heads (Male is the base)		
Female	0.099	0.117**
Marriage Status of Heads (Married heads is the base)		
Single heads	-0.071	-0.220**
Others	0.101	-0.134**
Ethnic of heads (The Kinh is the base)		
Ethnic minorities	-0.087	0.188***
Household size (One-member household is the base)		0
2 members	-0.034	-0.448***
3 members	0.095	-0.864***
4 members	0.215	-1.126***
5 members	0.236*	-1.239***
6 members or more	0.212	-1.283***
Shares of female members	-0.207*	0.105
Shares of members aged less than 5	0.031	0.237*
Shares of members aged from 6 to 14	-0.526***	0.389***
Shares of members aged over 60	-0.095	1.419***
Constant	-0.535***	-1.105***
Number of observations	9104	9104
Adjusted R-squared	0.047	0.343

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Conclusions

Estimates of Tax Expenditure

- The tax expenditure estimated for corporate income tax, based on Vietnam Enterprise Survey (VES), is equivalent to 7% of the total state budget revenues, about 5% of the total state budget expenditures, and even higher than expenditure on health care.
- The group of enterprises with a high proportion of tax expenditure is foreign-invested and belong to the industrial sector (especially processing and manufacturing).
  - Tax expenditure of large foreign-invested enterprises (with more than 100 VND billion of equity) in industrial sector accounted for 41% of total tax expenditure, although the number of enterprises in this group was only 1% of total enterprises that generate profits (about 1.6 thousand enterprises).
  - The effective tax rate of this group was 8%, and 90% of enterprises in this group located in industrial zones.

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Conclusions
Effect Analysis using CGE model

- Tax expenditures for CIT is quite high and have caused considerable fiscal losses.
- In terms of income distribution, high-income groups benefit the most from tax expenditures, and therefore, are strongly impacted by the elimination of tax expenditures.
- Low-income groups could benefit from eliminating tax expenditures as the government could use the additional budget to support a range of government sponsored programs.
- Failure to eliminate tax expenditures and inability to maintain budget revenues through increasing VAT taxes could create significant losses for all population groups.
- The government should carefully design and effectively implement tax incentives, especially in the context of very high budget deficits and a rapidly rising public debt.

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Limitations

- There is a crucial problem with the estimation based on Vietnam Enterprise Survey in this Chapter because of the inability to access the tax profile of all enterprises in Vietnam. There are two main following reasons:
  - This Survey is only provided the gross profit and the general tax code of enterprises instead of the profit and the tax code by activities.
  - There is a difference between the taxable profit and accounting profit.
- To ensure accuracy in following studies, the estimation of tax expenditure should be based on the tax profile of enterprises instead of surveys.

Tax avoidance and evasion in Vietnam:

The case of corporate income tax

Outline

- Definitions
- Literature review and international policy experiences
- Tax avoidance and evasion and legal framework in Vietnam
- Empirical analysis on tax avoidance and evasion: Evidence from firm level
- Conclusions and policy recommendations

The Conception of Tax Avoidance and Evasion

- Tax Avoidance
  - may be legal or semi legal;
  - exploiting gaps in customs and tax regulations to cut payable taxes.
  - is typically accomplished by structuring transactions so as to minimize tax liability.
- Tax Evasion
  - A form of enterprise committing illegal acts so as not to pay tax obligations.
  - Businesses often evade taxes by hiding taxable incomes or deliberately misrepresenting income sources.
  - It occurs when individuals/firms deliberately fail to comply with their tax obligations.

Main Channels of Tax Avoidance and Evasion

- Transfer Mispricing:
  - The transfer price in an internal transaction between the company's branches is mispriced in the direction of increasing the transfer price from a low taxed country to a high taxed country and vice versa.
- International Debt Shifting
  - A branch in a low-tax country lends money to a branch in a high-tax country.
- Strategic Location of Intellectual Properties:
  - Intellectual property rights are located in countries with low taxes;
  - The costs incurred in research and development (R&D) are usually borne by branches in high-tax countries.

Main Channels of Tax Avoidance and Evasion

- Tax treaty shopping:
  - Businesses set up branches in third countries to take advantage of bilateral tax treaties between the two countries.
- Tax deferral:
  - Profits from abroad transferred to the parent company are taxable;
  - Businesses tend to keep this profit overseas and postpone transfer to the parent company to avoid taxes.
- Corporate inversions:
  - The structure of the company was reversed in the direction of reversing the overseas branch into a parent company and the parent company becoming a branch.

Policies Against Tax Evasion and Avoidance

- Policies that aim to improves the tax system to tighten regulations.
  - controlled foreign corporation rule – CFC rule.
  - Conversion rule.
  - Provisions on intellectual property removal tax.
  - Regulations on interest that can be deductible –thin capitalization.
  - General Anti-Abuse Rule - GAAR.
- Policies that enhance tax transparency
  - Country-by-country report – CbC.
  - Tax transparency package (between EU country members).

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Tax Avoidance and Evasion in the Industrial 4.0

- Problems arise
  - the physical presence of the business decreases.
  - Mobility of intangible assets increases.
- Recent Solutions:
  - OECD: Digital tax
  - UK: Diverted profit taxes - DPT
  - Australia: Multinational Anti - Avoidance Law – MAAL
  - India: Equalisation Levy

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Tax Avoidance and Evasion in Vietnam

Structure of Budget Revenues in Vietnam , 2013-2019 (%)

	2013	2014	2015	2016	2017	2018*	2019*
Total Budget Revenue and Aid (trillion VND)	827	876	996	1080	1227	1254	1423
Revenue from taxes	82.8	81.8	75.9	75.2	75.7	81.5	77.7
In which.							
Corporate Income Tax	33.9	29	26.5	23.3	23.4	24.6	24.7
Personal Income Tax	6.9	6.7	7.5	8.4	8.5	9.2	9.7
Aids	1.35	1.27	1.22	0.75	0.66	0.64	0.21
Others	15.8	16.8	22.9	24.1	23.6	25.9	22.1

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Tax Avoidance and Evasion in Vietnam

- Tax fraud acts are complicated, the scope is wider, the scale is bigger and the tricks are increasingly sophisticated:
  - Corporate Income Tax:
    - The total number of violating enterprises was 642,423 the total tax collected was 35,922 bil. dong, the loss claim that not allowed for deduction was 185,002 bil. dong.
    - The number of violating enterprises increased sharply (31,759 in 2010, 103,211 in 2017, and 95,936 in 2018)
    - The loss reduction increased sharply (10,842 bil. dong in 2010, 40,915 bil. in 2018), significantly increasing the state budget revenue (by 1,783 dong bil. in 2010 and 7,145 bil. in 2018).

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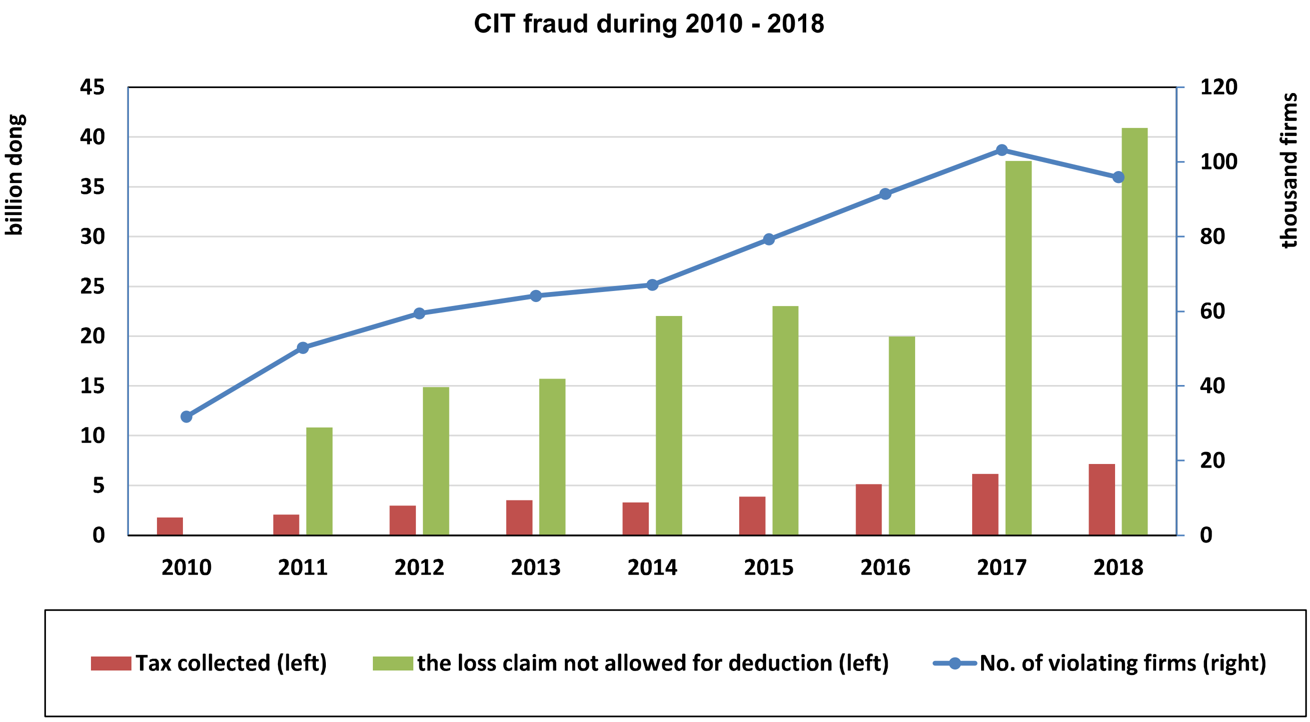
Tax Avoidance and Evasion in Vietnam



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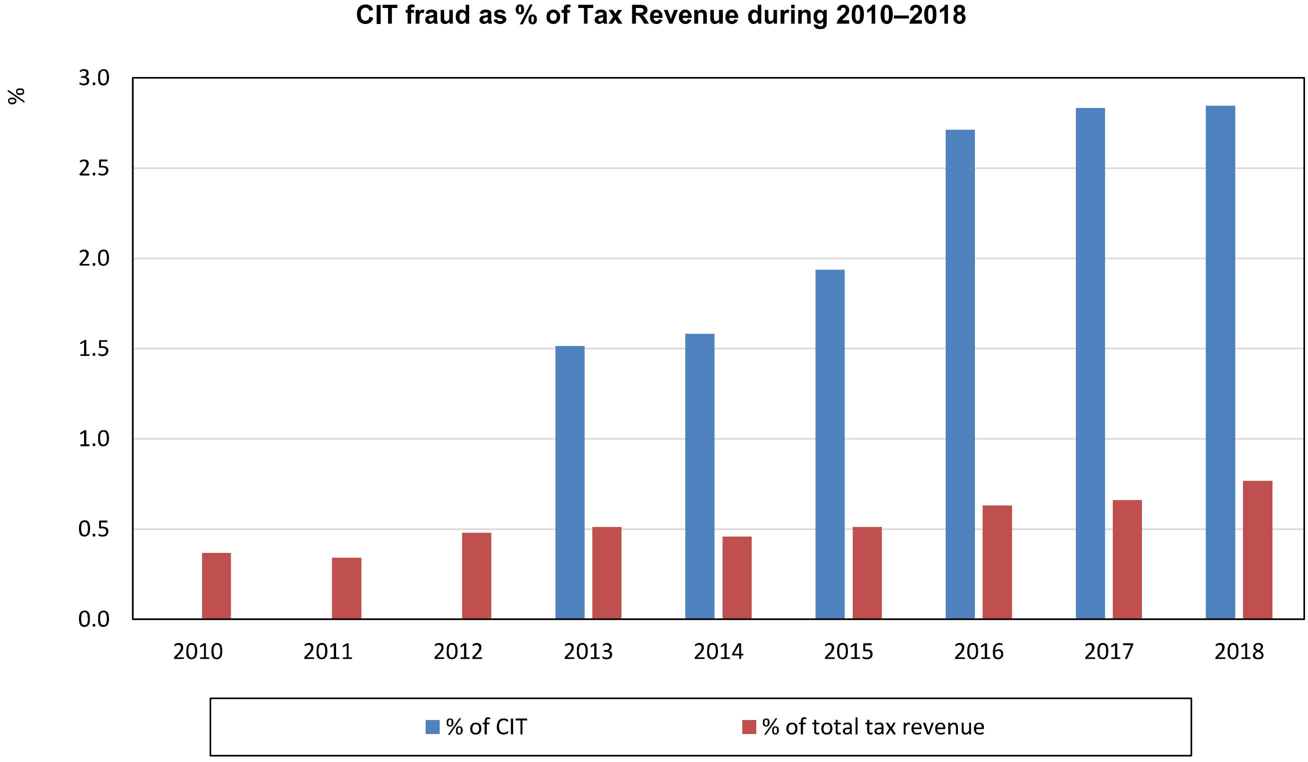
Tax Avoidance and Evasion in Vietnam



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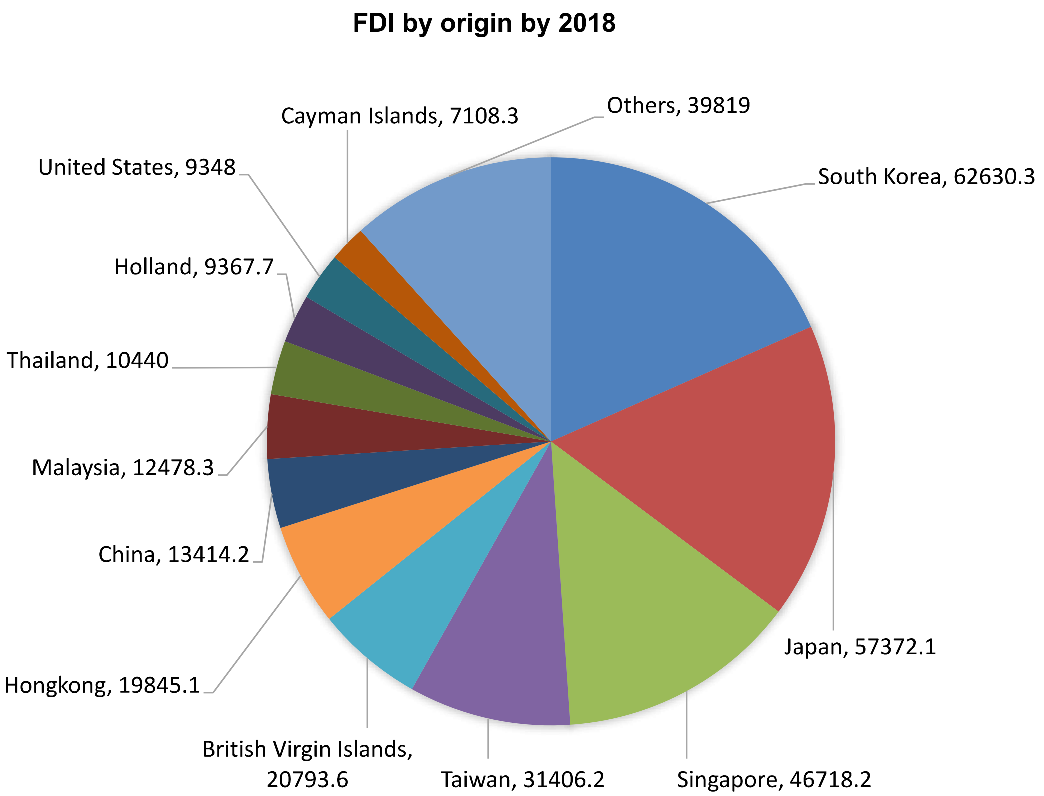
Tax Avoidance and Evasion in Vietnam



VEPR Tax Avoidance and Evasion in Vietnam

- Tax fraud acts are complicated, the scope is wider, the scale is bigger and the tricks are increasingly sophisticated:
  - Corporate Income Tax:
    - The proportion of businesses with losses was high (46.3% for FDI enterprises)
    - International and domestic price transfer is increasingly popular.
    - Tax debt is increasing, in which non-recoverable debts account for 42%.
    - Tax losses for e-commerce businesses

VEPR Decree 20/2017/NĐ-CP

- Decree 20/2017/NĐ-CP:
  - Aims:
    - Anti-transfer pricing for tax evasion purposes.
    - Reduce risks for businesses with related transactions.
    - Increase transparency.
  - Advantages:
    - Expand the scope of adjustment compared with the current regulations.
    - Consistent with the global tax policy framework.
  - Disadvantages:
    - The transfer pricing audit method (comparative basis).

VEPR Decree 20/2017/NĐ-CP

- Debate:
  - Article 8 Clause 3 relates to the deductible interest expense limit (Interest/EBITDA < 20%).
- MNCs almost have no response.
- The response mainly comes from the state conglomerates
  - Rely heavily on debt.
  - Have related transactions.
- Whether an enterprise is subject to the Decree 20 depends on two conditions simultaneously:
  - high leverage (debt/equity ratio, and thus the interest/EBITDA);
  - having affiliate transactions.
- How should the Decree 20 be amended?

VEPR The limit on interest/EBITDA ratio should not be raised

- Nearly 19% of SOEs had interest/EBITDA> 20%, much higher than those of the other two sectors.
- Only nearly 5.5% of FDI enterprises have interest/EBITDA> 20%; and less than 4% had this rate> 30% in 2013-2016

Proportion of firms with different interest/EBITDA ratios

	Proportion of Enterprises with Interest / EBITDA <= 10%			Proportion of Enterprises with Interest / EBITDA = (10%, 20%]			Proportion of Enterprises with Interest / EBITDA = (20%, 30%]			Proportion of Enterprises with Interest / EBITDA > 30%		
Year	FDI	SOEs	Non-State Enterprises	FDI	SOEs	Non-State Enterprises	FDI	SOEs	Non-State Enterprises	FDI	SOEs	Non-State Enterprises
2013	90.40%	70.90%	94.00%	3.60%	7.40%	0.90%	1.70%	5.10%	0.80%	4.20%	16.60%	4.40%
2014	90.80%	72.90%	94.90%	3.40%	7.30%	0.80%	1.90%	5.80%	0.70%	3.90%	14.00%	3.50%
2015	91.40%	75.70%	96.10%	3.30%	7.30%	0.70%	1.70%	4.70%	0.60%	3.60%	12.30%	2.60%
2016	92.10%	76.60%	89.80%	3.00%	7.00%	1.90%	1.60%	4.70%	1.60%	3.40%	11.80%	6.60%

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Discussion on Policy Impact of Decree 20

- Decree 20 affects SOEs the most and FDI the least.
- The ceiling of interest/EBITDA of 20% that is permitted to be tax deductible is quite low for the purpose of combating tax evasion of the FDI sector.
- It is necessary to maintain or even lower this ceiling.
- Businesses with associated transactions and large loans may be passive when Decree 20 is born.
- Borrowing and re-lending between the parent company and its subsidiaries are quite common among state conglomerates.

=> Interest expenses from contracts signed before the effective date of Decree 20 should be fully deducted.

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Discussion on Policy Impact of Decree 20

- The transfer term can be 5 years and only applies to businesses that are newly established/not yet generating revenue, or have large investments exceeding a certain number.
- Decree 20 should apply to all enterprises, domestic or MNCs, having cross-border transactions or not, and also the parent companies - subsidiaries with the same tax rate.
- Purpose: To avoid transferring profits from profitable companies to loss-making companies, transferring profits from 100% state-owned enterprises to equitized companies.
- As long as the lender is independent of the borrower, and independent of the parties to which the borrower has associated transactions, interest expenses should be fully deducted.
  - Anti transfer pricing via associated transactions.
  - Equality between businesses.
  - The erosion of tax bases and thin capital should be considered in another regulation.

VEPR Building a roadmap for fighting against tax base erosion and thin capital

- Plan a roadmap to completely eliminate loan interest deduction between associated companies.
- Even for independent loans, the tax deductible interest rate should be controlled at a certain level.
- Regulate the interest expenses that are tax deductible through the cap on debt/equity ratio.

VEPR Empirical Analysis

Methodology:

- Based on the ideas by Grubert and Mutti (1991) and Hines and Rice (1994):

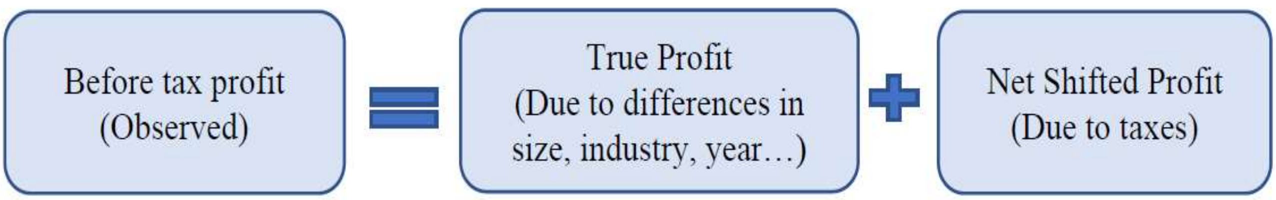

Figure 6.4: Theoretical Framework

  - True profit depends on size, industry, age,…
  - Shifted profit depends on tax factors.
- Analytical empirical framework, based on Huizinga and Laeven (2008), Beer and Loeprick (2014), Johansson (2017).

VEPR Empirical Analysis

- **Estimation Equation:**

$$Profitability_{it} = \alpha + \beta_1 \times \text{str}_{it} + \beta_2 \times d \times (\text{str} - \text{etr})_{it} + \gamma X_{ijt} + \delta_i + \sigma_t \epsilon_{it}$$

  - ✓ Profitability: ROA or ROE of firm *i* in year *t*
  - ✓ d = 1 for firms with positive profit and 0 otherwise
  - ✓ str: statutory tax rate
  - ✓ etr: effective tax rate
  - ✓ X_{ijt} is a vector of explanatory variables that reflect the firm characteristics (size, ownership, industry, expansion, ...)
  - ✓ δ_i and σ_t measure fixed effects

VEPR Empirical Analysis

- Data:
  - Annual enterprise census in the period of 2013 - 2017
  - Use the Interquartile Range (IQR) method to eliminate outliers. Specifically, sampling from Q1 - k * IQR to Q3 + k * IQR, with IQR = Q3 - Q1 and k = 2.

Main results:

- The higher the statutory tax rate, the lower the profit declared by businesses (tax evasion takes place in all types of businesses).;
  - With the same statutory tax rate, FDI and NNN reported lower profits than SOEs;
- The greater the tax incentive, the greater the profit declared by the businesses;
  - With the same tax incentives, FDI and NNN reported higher profits than SOEs;
- Simultaneous cut in statutory tax rates and preferential tax rates of 1 percentage point in recent years helps increase corporate income tax;

VEPR Empirical Analysis

Main results :

- The declared profitability of FDI is lower than that of SOEs and SOEs (due to the greater opportunity of tax evasion).;
- The bigger the asset, the lower the profitability;
- Firms that employ more workers or expand investments have a higher profitability;
- There are differences in profitability across industries. Mining, telecommunications, real estate finance and agriculture are the ones with higher profitability than other industries;
- Profitability tended to decrease in the period 2013–2015 and increased in the period 2016–2017;

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VEPR Empirical Analysis

Tax Revenue Loss by regions (Billion VND, ROA method)

Year	SOEs	FDI		Non-State Enterprises	Total	
		min	max		min	max
2013	1.144	4.309	8.841	9.267	14.721	19.252
2014	715	3.336	7.401	6.912	10.964	15.028
2015	740	3.818	8.595	8.538	13.095	17.873
2016	824	4.163	9.544	11.233	16.22	21.6
2017	1.017	5.213	11.673	16.871	23.101	29.56
Average	888	4.168	9.211	10.564	15.62	20.663

VEPR Empirical Analysis

Tax Revenue Loss (Billion VND, ROE method)

Năm	SOEs	FDI		Non-State Enterprises	Total	
		min	max		min	max
2013	1.038	1.683	7.278	9.426	12.148	17.743
2014	838	1.338	5.732	7.359	9.535	13.929
2015	869	1.693	9.008	9.701	12.263	19.579
2016	763	1.601	8.595	12.355	14.719	21.713
2017	996	1.987	9.656	15.038	18.021	25.69
Average	901	1.66	8.054	10.776	13.337	19.731

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VEPR Empirical Analysis

- The tax loss, both in value and as percent of CIT, has been on an upward trend since 2014;
- The tax loss is estimated at VND 15.6 - 20.7 trillion (7.5 - 9.9% of the annual CIT revenue) according to the ROA method, and 13.3 - 19.7 trillion VND (6.4 - 9.5% of CIT revenue) according to ROE method, approximately 3-4 times larger than the number of detected annually.
- Of which, the loss from FDI may be up to 8.0 - 9.0 trillion, equivalent to 4.0 - 4.5% of CIT revenue, while the loss from SOEs may be up to VND 10.5 trillion, around 5% of the annual CIT revenue.

Conclusions and Policy Recommendations

- Quickly study and apply measures to prevent tax avoidance and evasion currently being applied widely in advanced countries (ATAD, BEPS, TJN, ...). Strengthen tax administration.
- Decree 20 should be replaced by another decree in the spirit of the Tax Administration Law 2019.
- Study and implement regulations to prevent tax base erosion and capital thinning.
- Enhancing information exchange; requiring multinational corporations to have country-by-country reports - CbC reports; introducing tax regulations for digital-based activities,...
- Raising the issues of tax competition, tax incentives, and tax avoidance and evasion to ASEAN's agenda.

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Vietnam's Economic Prospect in 2020 and Policy Implications

VEPR Vietnam Economic Outlook 2020

- Vietnam's economic prospects in 2020 and beyond depend on the control of COVID-19, not only domestically but also globally.
- Currently, Vietnam is in a better position than many countries in the world thanks to the relatively early control of the epidemic.
- Meanwhile, the world economy is facing the risk of recession:
  - The COVID-19 pandemic is not completely under control and there is a risk of the second outburst;
  - Global FDI inflows have decreased in both M&A and greenfield investment;
  - The disruption of the global supply chain;
  - Budget deficit;
  - Tensions between the United States and allies with China are increasingly fierce; trade protectionism is increasing.

→ In the medium and long term, Vietnam needs to be aware of the possible shifts in the world economic order under the influence of the United States and other major powers, including extreme scenarios such as the formation of a new Cold War. The situation may depend greatly on the outcome of the US presidential election in November 2020

VEPR Vietnam Economic Outlook 2020

- Vietnam's economy faces many opportunities as well as challenges. Factors that are favorable for growth and in the near future include :
  - New-generation free trade agreements which have been effective and are about to take effect;
  - Increasing disbursement of public investment;
  - Raw material costs remain low;
  - Opportunity from investment flows, as investors attempt to: (i)disperse risks from US-China trade war, (ii) exploit the advantage of FTAs, (iii) exploit cheap labor, (iv) utilize tax incentives, and (v) exploit lax environmental management in Vietnam,…
  - Moderate inflation rate;
- Challenges and risks :
  - The risk of 2nd outbreak of COVID-19 infection is accompanied by risks of aggregate blockade and supply chain disruption;
  - The fiscal deficit increased due to a fall in revenues while the cost of disease prevention increased;
  - Fall into a spiral of geopolitical tensions between major countries.
  - Macro-economic foundation has not been improved in comparison to previous countries

VEPR Vietnam Economic Outlook 2020

- The most optimistic scenario (Scenario 1) is based on the assumption that domestic epidemics were completely controlled by the end of April and that economic activity gradually returned to normal. Meanwhile, the world has begun to relax blockade measures since the beginning of June, helping Vietnam's goods export industry grow well in the second half of the year.
- In neutral scenario (Scenario 2) or pessimistic (Scenario 3), epidemics in many important economic and financial centers around the world are assumed to re-emerge, and countries have to extend blockade measures to the later half of the third quarter, even the fourth quarter of 2020, with different levels of complexity.

GDP growth (%)			**Average Inflation rate (%)**
Optimistic	Neutral	Pessimistic	
5.3	3.9	1.7	3.5 – 4.0

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VEPR Policy Recommendations

Policies to support growth in the short term:

- Continue to tightly control epidemics domestically and gradually open to the outside world in a closely supervised manner;
- Promoting public investment in the second half of the year can offset the temporary difficulties of many manufacturing industries. However, public investment must be in the right place, avoiding waste of resources.
- Reducing recurrent expenditure (consumption) by at least 10% to devote resources to addressing the consequences of the epidemic.
- Improve infrastructure and institutional factors to attract investment flows;
- Continue to implement different policies to improve macro-economic conditions

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Policy Recommendations

Policies towards a transparent, fair and effective tax system, which support sustainable growth in the long term :

- Developing a transparent budget system, comply with international standards in accounting, publishing and budget monitoring;
- Undertaking a comprehensive tax system reform instead of fragmented changes;
- Review and restructure the tax incentive system;
- Strengthening the legal framework for tax administration, getting closer to international standards for increasing transparency and combating tax evasion and avoidance;
- Researching and applying anti tax evasion and tax avoidance measures, which are currently applied in advanced countries around the world;
- Conduct research to implement regulations to prevent tax base erosion and prevent thin capitalisation;
- Database needs to be improved for tax administration purposes;
- Add issues of tax competition, tax incentives, and tax avoidance and evasion to ASEAN's agenda

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Thank you for your attention

Contact:

Vietnam Institute for Economic and Policy Research,
University of Economics and Bussiness, National University Hanoi
R.707, E4 Building, 144, Xuan Thuy, Cau Giay
Email: info@vepr.org.vn
Tel: 04.37547506 ext 714/ 0975608677
Fax: 04.37549921

CHAPTER 7
VIETNAM ECONOMIC PROSPECT IN 2020 AND POLICY IMPLICATIONS

Pham The Anh and Nguyen Dieu Huyen

VIETNAM ECONOMIC OUTLOOK 2020

The world economy slowed down in 2019 due to the weakening of investment flows and international trade, the result of an increasing wave of trade protectionism surrounding the US-China trade war, and a series of economic and political tensions in other regions around the world. The reduction of global FDI inflows, both in Mergers and Acquisitions (M & A) and greenfield investment, make the world economic outlook for 2020 somewhat less optimistic. In particular, the sudden outburst of COVID-19 pandemic and the risk of a second outburst makes the recovery of global FDI and international trade in 2020 unimaginable. Besides, tensions between the US and Western countries with China will be increasingly fierce, which will cause business confidence to decline, negatively affecting the global economy in 2020 and even the following years. However, it is undeniable that this is the decisive moment that the world economy is restructured in completely unexpected ways, with many risks but also many opportunities. The disruption of the global supply chain since the outbreak of COVID-19 has highlighted the urgent need for supply chain rearrangement in which investment flows, trade flows, and value chains are expected to experience big changes.

Being a deeply integrated economy with motivations for growth relying heavily on international trade, Vietnam is forced to adapt to changes in the world economy, and proactively transform the economy to keep up with these changes, to timely take advantage of opportunities. Currently, Vietnam is in a better position than many countries in the world, due to the total control of the COVID-19 pandemic. Even when the world economy faces many instabilities, Vietnam's economy still witnessed impressive economic growth in 2019, 7.02%, exceeding the targets set by the National Assembly; Economic growth in Q1 / 2020 is still at 3.82% and growth for the whole 2020 is expected to remain positive despite the influence of COVID-19 being more and more widespread globally.

Inflation in 2019 remained at a low level as in previous years but increased in the last months of the year. However, consumer prices have started to decline since the beginning of 2020 due to the COVID-19 pandemic. With declining income and social distancing, the demand for shopping and consumer goods tends to decrease. At the same time, the decline in energy demand

and disagreements in production cuts among oil-exporting countries have made the price of fuels and input materials at a record low. Therefore, in general, in 2020, the risk of demand-pulled inflation and inflation due to currency depreciation is low, while the risk of inflation due to supply disruption (of grain food and foodstuffs) is significantly higher. The goal of controlling inflation below 4.0% can be achieved if food prices for the rest of the year are well controlled.

In 2019, deposit rates of commercial banks remained relatively stable at 5-7% p.a for the first nine months of the year and only slightly decreased at the end of the year due to the SBV's lowering of policy rates. Meanwhile, lending rates were in the range of 7-11%. This makes the cost of capital for businesses remain high. Meanwhile, the size of the corporate bond market has increased sharply in 2019 to 11.5% of GDP, compared to only about 7% in 2018. In early 2020, COVID-19 broke out, hindering business operations. To support business activities, SBV lowered a series of policy rates to create better access to capital, however, the current level of interest rate in Vietnam is still high. Meanwhile, the corporate bond market is risky. Vietnam has not had an independent organization for corporate credit rating, thus, the warming up of the bond market can lead to interest rate competition, uneven corporate bond quality, pushing the risks of assessing and evaluating the asset to investors. The total cost of issuing bonds is even higher than the borrowing rate. Currently, due to the negative impact of COVID-19 on production and business activities, the pressure on payment of bond issuers will also be higher, increasing the risk of default.

The budget deficit of 2019 is estimated to be VND 209.5 trillion, equal to 3.4% of GDP, slightly lower than the estimate approved by the National Assembly at the beginning of the year (3.6%). The budget deficit in 2019 increased compared to 2018 due to increasing recurrent expenditure. The expenditure structure has experienced no improvement when spending on development & investment only accounts for a small proportion (less than 30%) and the demand for expenditure was far beyond the ability to collect budget revenue. The ratio of budget revenue to GDP has fallen sharply in 2019 due to the reduction of revenue from import-export activities (resulting from the reduction of tariffs in free trade agreements) and the reduction of ODA. Entering 2020, Vietnam's budget deficit is expected to increase by 1.5-1.6 percentage points, to 5% -5.1% of GDP, as the COVID-19 pandemic causes budget spending to increase while tax revenues are reduced. The Ministry of Finance announced that Vietnam is now planning to borrow 1 billion USD from abroad in 2020 to make up for the budget. Persistent budget deficits coupled with rapidly increasing payment obligations are notable fiscal risks. If this does not improve, the introduction of new tax or increase of old tax will likely be inevitable in the near future.

International trade in 2019 also has noticeable changes. By the end of the year, the trade balance had a surplus of about US $ 9.9 billion, nearly double the US $ 5.6 billion surplus of 2018. However, similar to previous years, exports came from the FDI sector accounted for the major proportion (68.8%). This shows that Vietnam's economy has not yet promoted potential internal resources, but still depends mainly on the FDI sector. While the economic benefits from the FDI sector are still small, environmental risks, inequality in the business environment, foreign labor management issues, etc. is making Vietnam's foundation for growth precarious. The import structure has remained stable compared to previous years, which focuses mainly on machinery, equipment and components for export. That continues to pose unsolved problems for Vietnam on the development of supporting industries or the transformation of the economy from outsourcing.

Vietnam's economic outlook in 2020 and beyond depends on the ability to control the disease, both domestically and globally. Vietnam's economy is facing many opportunities and well as challenges. Factors that can support growth for the rest of the year include: (i) Free Trade Agreement and Investment Protection between Vietnam and the European Union (EVFTA and IPA)) has been completed and approved, and will take effect from August 1, 2020; (ii) Progress of disbursement and construction of key public investment projects is accelerating; (iii) Costs of raw materials and fuels remain low due to the declining global demand and production; (iv) Opportunity to receive the flows of investment, as foreign investors attempt to disperse risks from the US-China trade war, while taking advantage of FTAs, cheap labor, tax incentives, and lax environmental management in Vietnam; (v) Inflation rate is moderate, creating favorable conditions for the implementation of macroeconomic policies to support growth.

Nevertheless, Vietnam is also facing many risks and challenges in an unstable global economic landscape. The risk of a second wave of COVID-19 infection with the possibility of further blockade measures and supply chain disruption is still present in many major economies around the world. In addition, geopolitical conflicts between large countries can cause a largely open economy like Vietnam to suffer regardless of the victory in favor of either side. In addition, the domestic macroeconomic condition is still weak, not much improved compared to previous years with chronic problems such as: high fiscal deficit, low budget for development investment; insufficiently improved health of the banking - financial system; the heavy dependence of growth on the FDI sector; labor force is high in quantity but low in quality; low efficiency of public investment and widespread corruption; the delayed equitization process of SOEs; inadequacies regarding institutional and business environment. These shortcomings, if not improved soon, will not only hinder short-term recovery, but also adversely affect the stability of Vietnam's economy in the long term

Taking into consideration the positive as well as the negative factors affecting the Vietnamese economy today, we make forecasts of growth and inflation under different scenarios regarding different possibilities of disease control. With the removal of the social distancing earlier than expected (from the end of April compared to the expected end of May before), we update the

Vietnam's economic growth to be higher than the previous forecast. The most optimistic scenario is based on the assumption that the disease was completely controlled domestically by the end of April and the economic activity gradually returned to normal. Meanwhile, the world has begun to relax blockade measures since the beginning of June, helping Vietnam's goods export industry grow well in the second half of the year. However, economic activities in the field of tourism, accommodation and passenger transport are still reserved and only gradually recover. The worst impact of COVID – 19 will be in the second quarter. With this optimistic scenario, Vietnam's economic growth is forecast to reach about 5.3% in 2020. With neutral and pessimistic scenarios, epidemics (in many important economic and financial centers around the world) is presumed to recur and countries must extend the blockade period to the second half of the third quarter, even the fourth quarter of 2020. The impact of COVID – 19 on agriculture, forestry & fishery, manufacturing sector and service sector will be more serious. Economic growth in 2020 might be only 3.9% in the neutral scenario, or just 1.7% in the pessimistic scenario.

Table 21. Growth and Inflation forecast, 2020 (%, yoy)

GDP Growth (%)			**Average Inflation Rate (%)**
Optimistic	Neutral	Pessimistic	
5.3	**3.9**	**1.7**	**3.5 – 4.0**

Source: VEPR Macroeconomic Team’s forecast, June 2020

SHORT-TERM POLICY RECOMMENDATIONS

In short-run, promoting public investment in the second half of the year can offset the temporary difficulties of many manufacturing industries. However, we cannot promote public spending in the long run due to limited resources, the consequence of chronic fiscal deficit. Besides, monetary policy is also constrained by inflation and exchange rate targets. If applying monetary easing as many economies today, it can lead to currency devaluation, riskier investment environment, or the delay of flow of capital investment. With such limited resources, policies need to be well-targeted, avoiding waste of resources. Different policies in response to different scenarios for the pandemic should be developed. In all circumstances, we must develop plans to achieve a duel target: combating the epidemic and maintain business activities, creating the best conditions for enterprises that are still able to operate. The importance of economic development should be placed on par with disease prevention.

Social security policies such as payment of unemployment insurance, support for people temporarily suspended from work, allowances for the poor and those who lose their livelihood due to social distancing should be a top priority, which needs to be implemented quickly. In particular, workers in the informal sector need to be paid more attention because this group is likely to be outside the scope of beneficiaries of current policies.

Meanwhile, policies to support businesses also need to be more classified and focused. The freezing / stopping or reduction of financial expenses such as loan interest and land rent should be applied to groups of enterprises that have to stop operating; for businesses that are negatively affected but still operate, policies to postpone social insurance contributions, reduce land rents, reduce interest rates and debt freezing, and collect VAT arrears should be implemented but there should be clear criteria for the level of support to avoid NPLs. On the other hand, for groups of businesses that are less affected or not affected, or those who are able to effectively transform business operations, credit should be encouraged and favorable conditions on both institutional and industrial level should be ensured.

Even if the epidemic is fully under control domestically, many export-oriented manufacturing and services sectors may face long-term difficulties once the epidemic has not completely disappeared in our trading partner economies. Therefore, promoting public investment in the second half of the year is recommended, to support economic growth. Vietnam should only accelerate projects that have been approved and available for implementation, especially national key projects. Dividing large projects into multiple bidding packages and implementing them in a scattered manner should be considered, as more businesses and localities can access them, creating a better spillover effect. At the same time, a regular budget reduction (consumption) of at least 10% should be done to devote resources to addressing the consequences of the disease.

Finally, in line with the current short-term policies to mitigate the negative impacts of COVID – 19, Vietnam should continue working on longer-term policies to improve macroeconomic foundation and reduce future risks. In all situations, inflation, interest rates, and exchange rates need to be maintained stably. Diversification of export/import markets needs to be paid more attention, to avoid heavy dependence on some major economic partners. In this time of difficulties, many inadequacies in managing economic policies were revealed, so efforts to improve the institutional environment need to be sustained. Especially, Vietnam should gradually build a fiscal buffer to prevent external shock.

CONSOLIDATING THE BASE FOR FISCAL POLICY

Vietnam is a transitional economy and there are strong changes in thoughts and practices regarding operating the economy. The government has made increasingly tight commitments in opening markets and developing the private sector. In particular, tax is one of the areas with great reforms since the implementation of Doi Moi and the open of the economy. Overall, the current tax system in Vietnam is quite similar to countries with the oldest market economy in the world. However, international integration is creating challenges for the fiscal system.

Despite the strong application of information technology in tax administration, the issue of Vietnam's budget transparency is still a big question mark in both spending and revenue. Specifically, the data on the national and international disclose of the national budget is not consistent in terms of structure; there are too many non-state revenue funds but these funds are not disclosed; Vietnam's management of tax incentives and tax expenditure is less transparent and not in line with international practice; t tax structure is unsustainable, inefficient and inequitable; budget settlement process is still very slow. In addition, the process of international integration is also causing many sources of budget revenues to fall sharply. Vietnam's tax incentives/expenditure measures are relatively large, spread out, and causes inequality across business sectors. In particular, like many other ASEAN countries, Vietnam tends to use tax incentives as a tool to encourage investment, especially foreign investment, to compete, rather than cooperate with other countries to promote regional economic growth. This creates concern about the increase in financial costs as a side effect of tax incentives.

Tax evasion & avoidance is another problem that Vietnam's tax system is facing in the integration process. Tax violations occur not only with CIT but also in a range of other taxes. Tax evasion and avoidance can occur in all types of businesses, from SOEs to multinational or private companies, and tend to increase. In particular, there is evidence that evasion and tax avoidance in multinational companies can be widespread and more serious than domestic companies.

In order to work towards a transparent, fair and effective tax system, which underpins Vietnam's sustainable development in the long term, in this report, we offer several policy recommendations as follows:

Firstly, Vietnam needs to build a transparent budget system, complying with international standards in accounting, publishing, and budget monitoring. Budget revenues and expenditures should be consolidated, avoid being off-balance sheet. The revenue losses due to tax exemptions should also be disclosed. At the same time, Vietnam needs to increase the application of information technology to limit violations and ensure transparency in tax and budget management.

Secondly, Vietnam needs to undertake a comprehensive tax system reform instead of fragmented changes. These reforms must address the inequality, complexity, and inefficiency of the entire tax system. Tax policies need to be reviewed, assessed for impacts on socio-economic development, and revised in a consistent manner towards a sustainable tax system.

Thirdly, Vietnam needs to review and restructure the tax incentive system. Generous and redundant incentives need to be eliminated to lead the economy toward a fair business environment, enabling many individuals and organizations to participate in economic activities, contributing to the process of innovation, accumulate knowledge in the economy. At the same time, Vietnam needs to cooperate with countries in the region to form a common regional mechanism on tax incentives, avoiding the race to the bottom regarding tax incentives to attract investment, which leads to distortion of the tax structure in every country.

Fourthly, over the past years, Vietnam has strived to establish and strengthen the legal framework for tax administration, moving closer to international standards for increasing transparency and combating tax evasion. However, the current legal framework is still inadequate, inconsistent, and has not kept pace with the fast and complicated developments of the reality. Decree 20/2017 / ND-CP should be replaced by another decree with more relevant content in the spirit of the Law on Tax Administration 2019, effective July 1, 2020. In the next phase, Vietnam needs to make more efforts to perfect the legal system of tax administration, and especially to make the law come to life.

Fifthly, Vietnam should quickly study and apply anti-tax avoidance measures currently applied in advanced countries around the world, especially the provisions of the Anti-tax Avoidance Directive - ATAD, which is being applied in EU member countries, or measures recommended by international organizations such as the Base Erosion and Profit Shifting Program (BEPS) or Tax Justice Network Global, etc. In addition, it is also necessary to strengthen the inspection, increase the level of penalties, and improve the qualifications of tax officials to ensure tax compliance of enterprises.

Sixthly, Vietnam should carry out research on the implementation of regulations to combat tax base erosion and against thin capital. In order to ensure the sound financial structure of businesses and the banking system in the long term, the borrowing behavior of businesses, regardless of whether they are associated or independent, should be controlled. The limit on debt must cover all types of businesses, whether they are state-owned or private, multinational corporations or domestic corporations, independent companies or joint ventures, etc... to ensure an equal business environment.

Seventhly, In addition to increasing information exchange with other countries, Vietnam needs to improve the database for tax administration purposes by requiring all major multinational companies to make annual reports with aggregated data on the distribution of income, profits, taxes, and economic activities among tax jurisdictions in which it operates. In addition, Vietnam needs to implement tax administration regulations for e-commerce, digital-based business, and other services provided by foreign suppliers who have no permanent establishment in Vietnam. This contributes to creating a fair business environment and preventing revenue loss for the state budget.

Finally, Being ASEAN chairman in 2020, Vietnam should add issues of tax competition, tax incentives, and tax avoidance to ASEAN's agenda to raise awareness and initiate multilateral discussions on these topics. OECD emphasizes that unilateral actions of individual countries are ineffective in preventing and limiting businesses' tax evasion and avoidance. Therefore, comprehensive measures to strengthen tax regulations for regional countries need to be taken.