



PUBLIC FINANCE REPORT



2018
JULY

“Intending to ensure the benefit of the general public ... and the good condition of the country by useful remedies...”

(from a charter of King Charles Robert - February 1318)



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Analysis of the 2019 budget bill

2018
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To support the fulfilment of its fundamental duties set forth in Act CXXXIX of 2013 on the Magyar Nemzeti Bank, in particular the tasks related to the definition and implementation of monetary policy, the Magyar Nemzeti Bank analyses developments in the budget deficit and debt, monitors the financing of the general government, analyses the impact of financing on monetary developments, capital markets and liquidity, and researches fiscal policy issues.

Pursuant to Act CXCV of 2011 on the Economic Stability of Hungary, the Governor of the MNB is a member of the Fiscal Council (FC), and thus the professional expertise and accumulated information available in the MNB can indirectly support the work of the FC. The MNB prepares background analyses for the duties of the FC stipulated in the Stability Act and makes them available for the FC. The general public can learn about the most important results of these expert analyses from the publication entitled 'Public Finance Report'.

The analyses in this Report were prepared under the general direction of Dániel Palotai, Executive Director for Economic Sciences and Priority Matters. This report was prepared by the staff of the Directorate for Fiscal and Competitiveness Analysis and the Directorate Economic Forecast and Analysis. It was approved for publication by Dr György Matolcsy, Governor.

The analysis is based on information available for the period ending on 25 June 2018.

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1 Summary

The subject of this analysis is the bill on Hungary's 2019 central budget, submitted to the Parliament on 13 June, which we assess in the light of the MNB's fiscal forecast. Based on the information available, as part of this analysis, the MNB prepared its own projection for the 2019 budget balance, and this projection is compared to the appropriations in the bill.

According to the budget bill, the ESA budget deficit in 2019 may be 1.8 percent of GDP. The set deficit target corresponds to the deficit path stated in the Convergence Programme and it is lower by 0.6 percentage point than the 2018 appropriation of 2.4 percentage points. After reviewing the details of the bill, we believe that certain revenue items may fall short of the appropriation; however, this is counterbalanced by the fact that we estimate the effective absorption of the EU transfers and the government's co-financing related to the payments to be lower than in the bill. Thus, according to our forecast, **the specified deficit target can be achieved.**

As a result of the declining deficit, the fiscal policy accumulates countercyclical reserves. In 2019, the fiscal policy may cause contraction in demand as a result of the decreasing deficit, which on the whole will result in a countercyclical fiscal policy.

The implementation of the bill – at constant exchange rate – would result in a meaningful, 2.6 percentage point, decline in the debt ratio as a percentage of the GDP in 2019, while according to our forecast a decrease of 2.2 percentage points may be expected under a more moderate economic growth. Calculating, as a rule, with unchanged end-2017 exchange rate of EUR/HUF 310.10, the gross general government debt-to-GDP ratio according to the EDP methodology is forecast to decline from 73.6 percent recorded at the end of 2017 to around 72.5 percent in 2018, and then to decrease further to 70.3 percent by the end of 2019. The debt rule of the Fundamental Law, which is in the focus of the Fiscal Council's decision, is expected to be satisfied safely.

In the macro path of the bill **the economic growth projection (4.1 percent) exceeds the projection prepared for the central bank's June Inflation Report (3.5 percent) and it is above the range of consensus forecast.** The higher GDP growth compared to the MNB's forecast is primarily explained by the faster upturn in households' consumption, which is in line with the assumed more favourable income trends resulting from the more dynamic real wages and employment. The macro path of the budget bill projects stronger growth in employment and wages for 2019 than the June Inflation Report. The estimated wage growth moderately exceeds the MNB's projection in 2018 and it is well above it in 2019, which is explained by the assumed more dynamic wage setting both by the private and the government sectors. The inflation projection in the bill is lower than the MNB's forecast for this year and next year as well. The underlying reason for the difference is presumably the diverging oil price assumptions. If the inflation exceeds the plan, in November an additional pension increase will become necessary (the assumed impact of this on the budget is already included in our forecast).

If economic growth and wage growth were lower than assumed in the bill, it would represent a risk for the feasibility of certain tax revenue estimates. The budget planned the labour and consumption tax revenues based on the fast-growing tax bases. The MNB's current macroeconomic forecast contains by roughly 3 percentage points smaller rise in the wage bill, and hence lower tax revenues.

According to our forecast, in 2019 the effective absorption of EU funds and the co-financing ratio may fall short of that anticipated in the bill. According to our forecast used for the June Inflation Report, the estimate of HUF 2,000 billion for the disbursement of funds may materialise; however, due to the different expectations related to the structure of disbursements and to the degree of the utilisation of the advance, the effective absorption of funds may fall short of the value indicated in the Budget Act. The different assumptions reduce the accrual-based deficit by roughly 0.4 percent of GDP compared to the bill.

The **key measures of the budget bill** include the reduction of the social contribution tax by 2 percentage points, the exemption of pensioner employees from the individual contributions and the social security contribution tax, the reform of the targeted allowances of the Job Protection Action Plan and the fringe benefit scheme, the targeted cut of the value added tax on milk, the increase of the family tax allowance of families with two children, the introduction of the exemption from financial transaction levy for household payments up to HUF 20,000, the increase in public investments (public road constructions, Modern Cities Programme), and the continuation and expansion of the career path models.

According to the bill, as a result of the growth in real wages, the social contribution tax will decrease by 2 percentage points already from 1 July 2019. Based on the wage agreement concluded at the end of 2016, the tax must be reduced two quarters after that the average growth in real wages exceeded 6 percent since the previous rate cut (i.e. from the start of 2018). According to the bill, this criterion will be met already in the first half-year of 2019, i.e. the tax cut will be implemented from 1 July 2019. In our analysis we took this as baseline scenario. Should the tax reduction not materialise yet in mid-2019, it could decrease the budget deficit by 0.2 percentage point compared to the baseline scenario.

The budget bill complies with the debt rule outlined in the Fundamental Law, as the expected decline in the debt ratio as a percentage of GDP is well above the prescribed rate of 0.1 percentage point. The bill also satisfies the European Union's requirement concerning the change in government debt, which at present prescribes the reduction of the debt ratio annually by 0.6-0.7 percentage point. The anticipated accrual-based balance is in line with the relevant rules of the EU and Hungary.

The 1.7 percent structural deficit indicated in the bill does not comply with the medium-term fiscal deficit target. The bill explains this by stating that in 2019 the ESA deficit of 1.8 percent corresponds to a structural deficit of 1.7 percent. On the other hand, the EU's structural deficit criterion and the requirements specified, based on the first, in Section 3/A (2) a) of the Stability Act, prescribe that the balance of the government sector must be determined in such a way that it should be in line with the attainment of the medium-term fiscal target, which at present in the case of Hungary is 1.5 percent of GDP. At the same time, the bill emphasises about the derogation that in 2019 the structural deficit approximates the target of 1.5 percent, with the difference falling to a minimum, i.e. 0.2 percentage point of GDP. In addition, the Government expects that after 2019 the structural deficit will be better than the targeted 1.5 percent.

2 General government balance

The bill sets the ESA deficit of the general government to 1.8 percent of GDP in 2019, representing a 0.6 percent decrease compared to the 2018 estimate of 2.4 percentage points. According to our forecast, the cash balance of the central budget may be slightly higher, while the balance of the local governments may be lower than the appropriations. The ESA bridge containing statistical corrections may be identical with those forecast in the bill (Table 1).

Table 1			
ESA balance of the government sector in 2019			
<i>(as a percentage of GDP)</i>			
	Deviation from appropriation		
	Statutory appropriation	MNB forecast	Difference
1 Balance of the central sub-sector	-2.3	-2.2	0.1
2 Balance of local governments	-0.5	-0.5	-0.1
3 Cash-based (GFS) balance of the general government (1+2)	-2.7	-2.7	0.0
4 GFS-ESA difference	0.9	0.9	0.0
5 ESA balance of the government sector (3+4)	-1.8	-1.8	0.0
6 ESA balance with cancellation of free central reserves	-1.7	-1.7	0.0
<i>Note: Amounts and differences may differ due to rounding</i>			

According to our forecast, the deficit target set in the bill may be achieved. According to our forecast, the tax and contribution revenues of the budget may fall short of the appropriations specified in the bill by 0.6 percent of GDP (Table 2). The difference is mostly attributable to the lower revenue expected from income and consumption taxes, which is primarily explained by the different macro paths. The budget bill forecasts a GDP growth of 4.1 percent for 2019, contrary to the MNB's expectation of 3.5 percent, included in the June Inflation Report. The tax bases are substantially influenced by the fact that the bill anticipates an increase in the wage bill, the rate of which exceeds the MNB's projection by roughly 2.7 percentage points. In addition, the most important factor that affects the value added tax is that according to our forecast, the households' consumption expenditure will rise by 3.2 percent in 2019 while the budget calculates with a growth of 4.8 percent.

However, the shortfall in the revenues compared to the appropriation is offset by the fact that according to our projection, the effective absorption of the EU transfers and the co-financing ratio may be lower than planned in the budget bill, and thus the net expenditure related to EU transfers may be lower by 0.4 percent of GDP.

According to the forecast included in the budget bill, the balance of the **local government sub-sector** will be a HUF -199 billion in 2019. The MNB's forecast expects a higher deficit than that for next year in the sub-sector; according to our expectations, the deficit of the sub-sector may reach HUF 236 billion. We expect higher fulfilment both on the revenue and the expenditure sides than indicated in the budget bill. The difference between the two projections is primarily on the expenditure side; we calculated with higher wage expenditure and higher purchased consumption expenditure than the general government's projection in the bill.

According to the deduction included in the bill, the **statistical corrections belonging to the ESA balance of the government sector** amount to 0.9 percent of GDP. The central bank's forecast related to the statistical corrections is essentially built on the adoption of the corrections compiled by the government, which are then modified in the case of those items for which the central bank prepares autonomous forecasts. Such items include the different accrual-based tax revenue statistical corrections resulting from the deviation of the macroeconomic parameters, the central bank's projection related

to interest expenses and the corrections resulting from the absorption of EU transfers to a different degree and in different structure. Despite the difference in the details, for 2019 the MNB calculates – in accord with the bill – with a balance improving statistical correction of 0.9 percentage point of GDP.

Table 2**Difference between the MNB forecast and the budget bill***(on ESA basis, as a percentage of GDP)*

	Deviation from appropriation
I. Central government revenues	-0.6
Consumption taxes	-0.3
Labour taxes	-0.3
II. Central government expenditures	0.5
Absorption of EU funds	0.4
Housing grants	0.05
III. Other effects	0.1 - 0.2
Blocking of the Country Protection Fund	0.0 - 0.1
Other	0.1
Total (II.+III.)	0.0 - 0.1

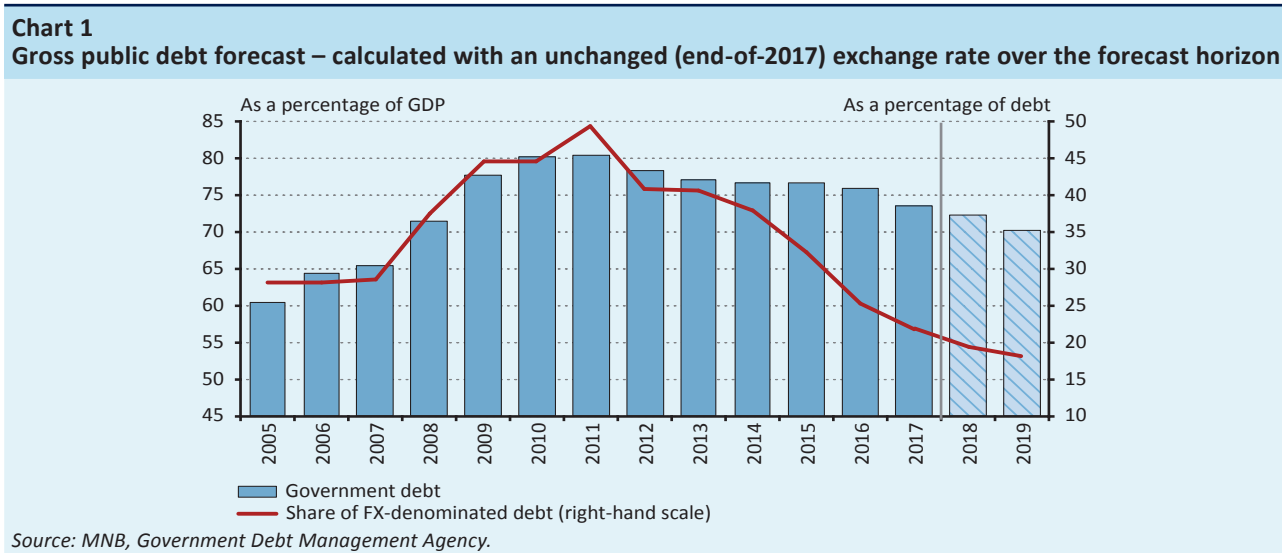
Note: The positive and negative signs indicate deficit-reducing and deficit-increasing effects, respectively, compared to the appropriations.

3 Expected developments in government debt

Calculating, as a rule, with unchanged end-2017 exchange rate of EUR/HUF 310.1, the **gross general government debt-to-GDP ratio according to the EDP methodology** is forecast to decline from 73.6 percent recorded at the end of 2017 to 72.5 percent in 2018, and then to decrease further to 70.3 percent by the end of 2019 (Chart 1). The substantial fall in the debt ratio may be supported, both in 2018 and 2019, by the low budget deficit and the dynamic economic growth, which may be partially offset by the currency effect.

	HUF billions	as a percentage of GDP
1 End-2018 EDP government debt	29,659	72.5
2 2019 cash-based deficit of the central budget	955	2.2
3 Other effect	-5	0.0
4 2019 expected EDP government debt (1+2+3)	30,610	70.3
5 Change in public debt-to-GDP ratio in 2019 (4-1)		-2.2

The prefinancing of the EU transfers influences the developments in the debt ratio. In 2018, the budget advances part of the EU transfers, which increases the cash-based deficit and through that also the value of the government debt. According to our forecast, the degree of this may be lower in 2019, and the previously prefinanced funds may be also paid to the budget. However, if the amount of the transfers received by the budget falls short of our expectation, the decrease in the debt ratio may be more moderate than our forecast.



As a result of negative net foreign currency issuance, the share of foreign currency within government debt is expected to continue to decline, contributing to a decrease in the external vulnerability of the economy. The foreign currency ratio of the central debt fell from 50 percent, recorded at the end of 2011, to 22 percent by the end of 2017, and according to our forecast it will decline to 18 percent by the end of 2019. In parallel with the major decline in foreign currency debt, the government debt’s exchange rate sensitivity also substantially lessened. At present, a shift of 1 forint in the forint-euro exchange rate – ceteris paribus – changes the value of the GDP-proportionate debt by 0.05 percentage point. In addition, the debt ratio is also influenced by the changes in the dollar-euro cross rate. This is because part of the public debt was issued in dollar bonds, and thus – although the Government Debt Management Agency swaps it to euro debt – it is also influenced indirectly by the dollar exchange rate movements, through the value of the market swaps.

4 Evaluation of the macroeconomic assumptions underlying the bill

For the coming years, the bill projects economic growth over 4 percent. The forecast related to this year is in line with the expectations in the MNB’s June Inflation Report, while the GDP growth in 2019 materially exceeds that (Chart 2). The higher GDP growth compared to the MNB’s forecast is primarily explained by the faster upturn in households’ consumption, which is in line with the income trends resulting from the more dynamic real wages and higher employment. As a result of this, the budget bill assumes a faster increase in the tax bases than the MNB’s current projection.

According to the macro path of the bill – in line with the Inflation Report – the **gross fixed capital formation will provide major support for the GDP growth this year and next year as well**, equally contributed to by the public projects, along with the rise in the investment activity of corporations and households. The budget’s macro path assumes slower growth rate both in exports and imports than the projection in the Inflation Report. According to the forecasts, net exports in 2018 may make negative contribution to GDP growth, while next year its growth contribution will be nearly neutral.

The macro path of the budget bill projects materially stronger growth in employment and wages for 2019 than the June Inflation Report. In the bill, the number of employees in the private sector dynamically rises, while according to the MNB’s assumptions, growth in employment will run into supply constraints in the coming years. The wage growth moderately exceeds the MNB’s projection in 2018 and it is well above it in 2019, contributed to by the more dynamic wage setting both by the private and the government sectors.

The inflation projection in the bill is lower than the MNB’s forecast for this year and next year as well. The dynamics of the GDP deflator included in the budget bill slightly exceeds the central bank’s expectations in 2019.

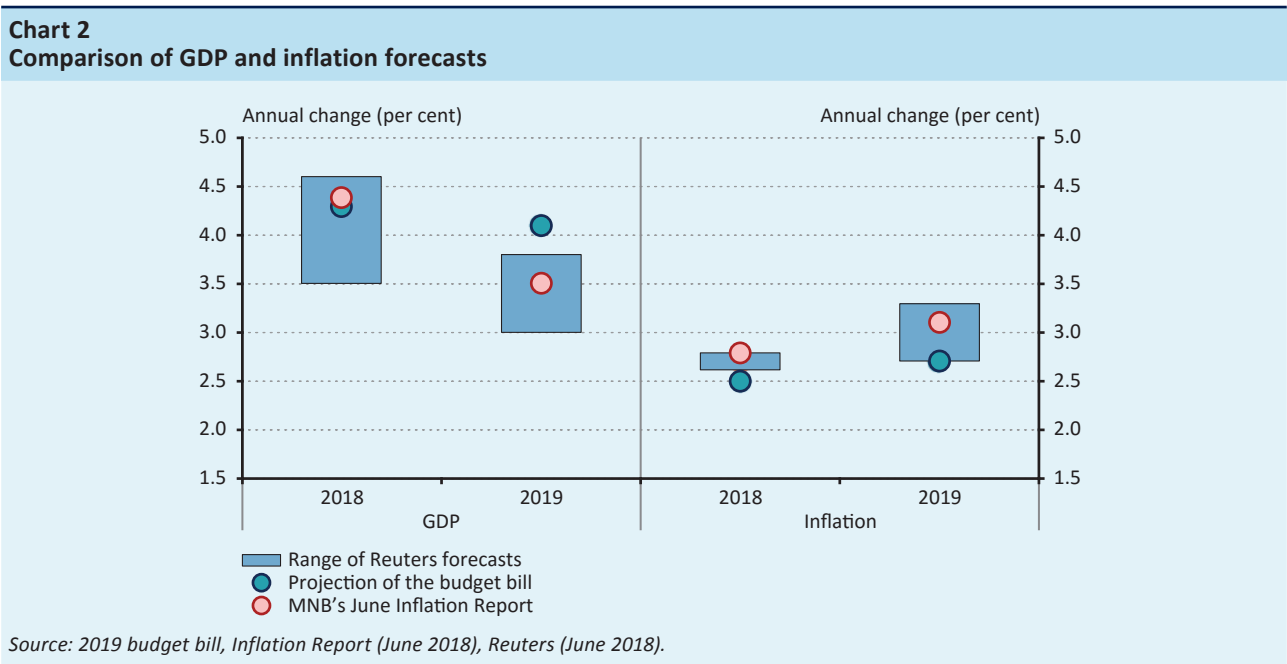


Table 4							
Comparison of macroeconomic forecasts							
<i>(percentage change compared to the previous year)</i>							
	2017	2018			2019		
	Actual	Budget	MNB	Difference	Budget	MNB	Difference
GDP	4.0	4.3	4.4	0.1	4.1	3.5	-0.6
Consumption expenditure of households	4.7	5.2	4.8	-0.4	4.8	3.2	-1.6
Public consumption	0.8	1.7	1.2	-0.5	1.0	0.5	-0.5
Gross fixed capital formation	16.8	12.8	14.9	2.1	7.5	8.8	1.3
Exports	7.1	7.2	7.5	0.3	6.9	7.5	0.6
Imports	9.7	9.2	9.7	0.5	7.4	8.2	0.8
Inflation	2.4	2.5	2.8	0.3	2.7	3.1	0.4
Gross wage bill	14.9	12.7	12.2	-0.5	10.3	7.6	-2.7
Gross average earning	12.9	10.7	10.3	-0.4	8.8	7.1	-1.7
of which: private sector	11.6	10.4	10.0	-0.4	9.3	7.2	-2.1
Number of employed	1.6	1.5	1.4	-0.1	1.5	0.4	-1.1
of which: private sector*	2.2 (2.9)	2.2	1.9 (2.2)	0.0	1.9	0.7 (0.6)	-1.3

*Note: * The budget bill defines the private sector differently; due to this, the headcount projection comparable with the budget's macro path is shown in brackets, and the difference is also calculated from that.*

Source: 2019 budget bill, Inflation Report (June 2018)

5 Detailed evaluation of the budget bill

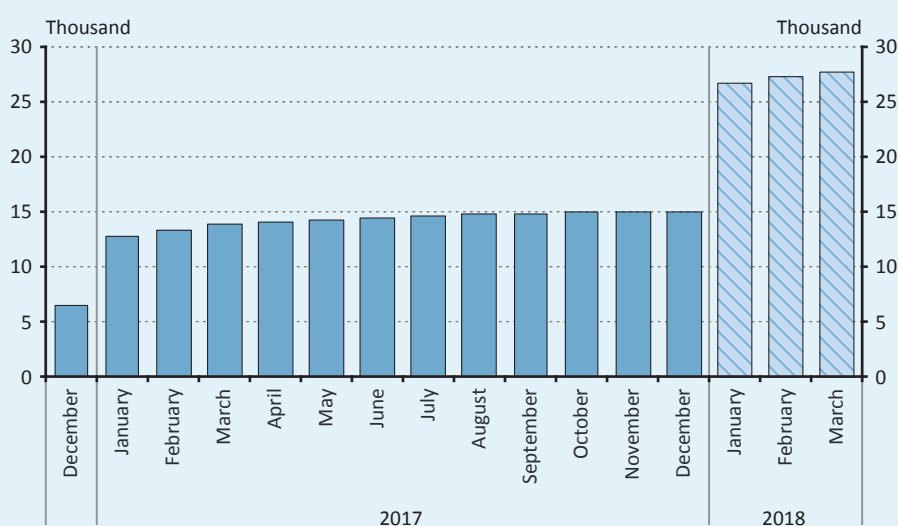
5.1 PRIMARY REVENUES

According to our forecast, the **primary revenues of the central sub-sector of the budget** may be lower than the appropriations in the bill by HUF 41 billion in total (Table 5). Within this, the cash-based tax and contribution revenues may fall short of the appropriations by 0.7 percent of GDP, the major part of which appears at the labour and consumption taxes, caused primarily by the bill's projection related to higher consumption and rise in the wage bill. On the other hand, this is offset by the fact that according to our forecast, the cash flow revenues related to EU transfers may exceed the appropriation in the bill.

Payments by economic organisations may essentially correspond to the appropriation, but there are differences in the composition of revenues in the appropriation and in our projection. In the case of revenues from corporation tax, the appropriation exceeds our forecast by HUF 9 billion, which may be attributable to the difference in the expectations about pre-tax profit of corporations. In the case of the special tax of financial institutions our forecast falls short of the appropriation by HUF 4 billion. The difference may be mostly attributable to the different assumptions regarding the tax allowances used. In the case of the small taxpayers' itemised lump sum tax (KATA) our projection falls short of the appropriation by HUF 4 billion. The Ministry of Finance estimates higher willingness to change over to this tax type in 2019 compared to the MNB's assumption.

The bill expects a revenue of HUF 50 billion from the **small business tax** in 2019, which essentially corresponds to our forecast and exceeds the 2018 appropriation by HUF 23 billion. The significant growth is attributable to the fact that the number of taxpayers opting for this tax type almost doubled in 2018 (Chart 3). In addition, the growth in cash revenues is also supported by the fact that the impact of the rise in the number of taxpayers affects the cash revenues of the base year only partially in 2018, while the effect thereof on the 2019 revenue is fully realised.

Chart 3
Number of companies opting for the small business tax (KIVA)



Source: Ministry of Finance.

On a cash basis, the budget expects revenues of HUF 4,286 billion from **value added tax**, which exceeds our projection by HUF 103 billion. The smaller part of the difference is attributable to the fact that the Ministry anticipates slightly higher revenue this year as well than the MNB, while the larger part thereof is due to the differences in the macroeconomic forecasts. Within this, the most important factor that affects the value added tax is that according to our latest forecast the households' consumption expenditure will rise by 3.2 percent in 2019, while the budget calculates with a growth of 4.8 percent. In addition, we also expect smaller growth in public consumption compared to the macroeconomic path indicated in the submitted budget bill. Our forecast includes the reduction of the VAT rate on long-life milk (ESL, UHT), which according to our calculations will decrease VAT revenues by HUF 22 billion next year.

The budget expects for 2019 a revenue of HUF 1,136 billion from **excise tax**, which exceeds our latest projection by HUF 30 billion. The difference is presumably attributable to the base effect. Compared to the practice of previous years, it is a change – with no effect on the balance – that in the 2019 budget the energy tax is stated in the excise tax row, which formerly used to be shown among the payments by economic organisations.

According to our forecast, revenues from **personal income tax** may fall short of the estimate included in the budget bill by HUF 53 billion. The difference arises primarily from the difference in the macroeconomic assumptions underlying the growth in tax revenues; the MNB's latest forecast regarding the gross salary and wage bill falls short of the that in the bill by almost 3 percentage points. The difference in the tax revenue forecasts may be also attributable to the budget bill's higher headcount growth assumption related to the pensioner's allowances (the pensioner employees using the allowance continue to pay personal income tax) and to the different expectations related to the reform of fringe benefit scheme. The assumptions related to reduction of the shadow economy arising from the reform of the health contribution may also diverge: from 2019, the lower-than-before upper limit of tax payment on mixed income encourages taxpayers to report higher incomes, which may increase the personal income tax payments.

The bill includes the rise in the family tax allowance for families with two children, based on which the monthly amount of the allowances increases from HUF 17,500 to HUF 20,000 in 2019. Our forecast related to the family tax base and the first marriage tax allowance – being the most important items among the personal income tax allowances – falls short of the bill's estimate of more than HUF 300 billion. The submitted new tax bill affects the personal income tax in three major areas. If the Act is approved, from 2019 the National Tax and Customs Administration will prepare the draft tax return also for sole traders. From next year, upon the letting of real property, the public utility costs are no longer included in the rental income, which simplifies the administration and may contribute to the reduction of the informal economy in the sector. The comprehensive reform of the fringe benefit scheme may entail a material fall in personal income tax revenues, and the fact that in the case of the fringe benefits the multiplier applied to the tax base is also cancelled further reduces the revenues (it remains in place in the case of certain defined benefits). In addition, the tax bill also includes several smaller measures, aimed at the easing of administration (for more details on the tax package see Section 7.1).

According to our forecast, the **social insurance and extra-budgetary fund revenues** may be lower by HUF 117 billion in total than the appropriations in the budget bill. Among the tax and contribution revenues of the extra-budgetary funds, the revenues from vocational training contribution and innovation contribution may exceed the estimate, while the social contribution tax payments may slightly fall short of it. Within the revenues of the social security funds, primarily the payments from the social contribution tax and the individual insured's contribution may be materially lower than the values estimated in the budget bill. The bill's gross wage and wage bill growth forecast exceeds our expectations by almost 3 percentage points, which explains a large part of the difference. Our projection related to the loss of tax and contribution revenues resulting from the various measures is in line with the budget estimates.

From next year, the health contribution will be integrated in the social contribution tax, and thus the incomes subject to health contribution will be taxed at a single rate in the future. The lower of the two rates (14 percent and the upper rate of the prevailing social contribution tax) will be cancelled and the higher one will continue to exist, which may decrease in the future in line with the continued decrease in the social contribution tax rate based on the wage agreement of 2016. The HUF 450,000 upper limit of the health contribution changes to twice the minimum wage, which on the whole means a tax cut and encourages taxpayers to report higher incomes. In 2019, a comprehensive reform will be implemented in the fringe benefit scheme, which will reduce the revenues formerly realised in the form of health contribution and from next year in the form of social contribution tax; at the same time, the payment of the fringe benefits as wage may

counterbalance this through the rise in the other labour taxes. On the whole, the reform of the benefits of the Job Protection Action Plan reduces the amount of the tax allowances, in view of the fact that the number of beneficiaries may decrease in the short run, while the allowance per person is expected to rise as a result of the changed rules and the raising of the tax base limit from HUF 100,000 to the prevailing minimum wage.

According to our forecast, the other contribution and tax revenues of the social security funds may almost correspond to the estimate in the budget bill. The revenues from the accident tax are transferred to the insurance tax estimate, and thus our relevant projection corresponds to the value included in the bill. According to our projection, the payments from the public health product tax may fall short of the estimate by roughly HUF 3 billion. In the case of this tax type, the tax rate will be increased by about 20 percent, and the range of alcoholic beverages subjected to this tax will be also expanded.

The budget anticipates a revenue of HUF 192 billion from **duties and levies** in 2019, which, according to our forecast, exceeds the 2018 expenditures – expected to fall short of the appropriation – by 5.3 percent. The revenues from duties and levies is substantially influenced by the degree of real estate duties, which recorded a dynamic, 13 percent year-on-year growth in 2017. According to our projection, the growth is expected to decelerate, and thus we find the statutory estimate realistic.

The **cash revenues related to the EU transfers** is budgeted in the total amount of HUF 1,483 billion, of which the *revenues from the EU programmes* amount to HUF 1,348 billion and the *subsequent reimbursement of the EU funds* amounts to HUF 135 billion. Thus the 2019 revenue estimate's part related to the programmes of 2014-2020 is lower by roughly HUF 560 billion than the estimate for 2018. The revenue estimate, which is materially lower than the expenditure, still implies major advance payments; however, the bill does not mention the degree thereof.

Considering the acceleration in the absorption of the advances paid in previous years and the rise in the invoice-based disbursements, the *revenues from EU programmes* may exceed the estimate, which may reduce the cash-based deficit and the government debt. According to the MNB's projection, the amount of the invoice-based disbursements and the absorption of advances may exceed HUF 2,300 billion in 2019, and thus if the related incoming invoices are sent in the reporting year and no factor that hinders absorption arises, according to our calculations the *revenues from EU programmes* may exceed HUF 1,600 billion. With this, the revenues related to EU transfers may exceed the estimate by HUF 280 billion and reach HUF 1,762 billion.

Table 5
Revenues of the central sub-sector – comparison of the forecasts
(HUF billion)

	2018			2019		
	Statutory appropriation	MNB forecast	Difference	Statutory appropriation	MNB forecast	Difference
TAX AND CONTRIBUTION REVENUES OF THE CENTRAL SUB-SECTOR	14,287	14,400	114	15,642	15,340	-302
Payments by economic organisations	1,354	1,403	49	1,444	1,448	4
Corporate income tax	370	370	0	400	390	-9
Special tax of financial institutions	50	50	0	53	49	-4
Sector-specific surtax	0	0	0	0	0	0
Simplified entrepreneurial tax	70	54	-16	45	45	0
Mining royalty	37	37	1	36	38	2
Gambling tax	26	31	5	31	34	3
Income tax on energy providers	52	57	5	59	61	2
Lump sum tax of small entrepreneurs	113	123	10	136	132	-4
Small business tax	27	42	15	50	49	-1
E-road toll	178	187	9	198	193	-5
Utility tax	55	55	0	55	55	0
Other taxes and payments	377	397	20	381	402	20
Consumption taxes	5,266	5,222	-44	5,827	5,688	-139
Value added tax	3,839	3,811	-27	4,286	4,183	-103
Excise duties	1,099	1,061	-39	1,136	1,107	-30
Registration tax	24	25	1	28	28	0
Telecommunication tax	52	54	1	52	54	1
Financial transaction levy	205	222	18	228	225	-3
Insurance tax	35	38	2	82	82	0
Tourism development contribution	11	11	0	16	11	-4
Payments by households	2,338	2,389	51	2,608	2,558	-50
Personal income tax	2,096	2,148	52	2,361	2,308	-53
Duties, other taxes	198	193	-5	199	200	1
Motor vehicle tax	44	48	4	48	49	1
Tax and contribution revenues of extra-budgetary funds	356	374	19	468	474	6
Tax and contribution revenues of social security funds	4,973	5,012	39	5,295	5,173	-123
Social contribution tax and contributions	4,645	4,676	31	5,124	5,006	-118
Other contributions and taxes	329	337	8	172	167	-5
REVENUES RELATED TO EU TRANSFERS	1,987	1,508	-479	1,483	1,762	280
OTHER REVENUES	280	295	14	344	326	-18
Other revenues of the central budget	142	152	10	191	191	0
Other revenues of social security funds	38	38	0	34	34	0
Other revenues of extra-budgetary funds	100	104	4	119	101	-18
TOTAL REVENUES	16,554	16,203	-351	17,469	17,428	-41

Note: partly consolidated data.

5.2 PRIMARY EXPENDITURES

The budget bill contains an expenditure of HUF 90.5 billion for the **social policy fare subsidy**, which falls short of the 2018 appropriation by HUF 7 billion. Since the bill contains no measures that affect the titles related to subsidies, our forecast for 2019 calculates with an expenditure of HUF 94 billion, corresponding to the expected expenditure of 2018.

In 2019, we expect savings on the **housing subsidy** expenditures of similar magnitude as in 2018. We expect a growth in 2019 corresponding to the expected soar in 2018 (compared to 2017 roughly HUF 20 billion); our forecast of HUF 222 billion, consistent with this, falls short of the 2019 appropriation by HUF 20 billion.

Of the key items of the **National Family and Social Policy Fund, at the family benefits**, the 2019 appropriation for family allowance is consistent with our projection and it is expected to be around HUF 310 billion. At other items of the family allowances, similarly to the income substitute and supplementary social benefits, and reimbursements given under various titles, we take over the appropriations.

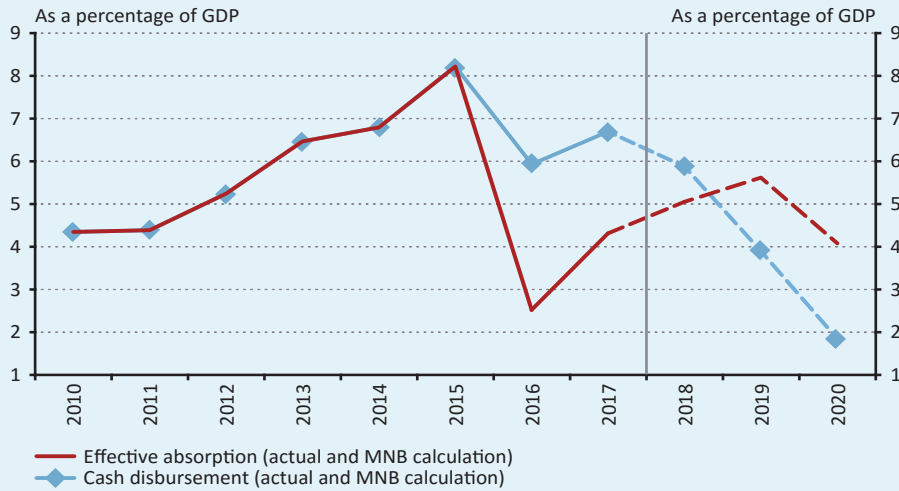
At the **budgetary institutions and chapters** we calculate with a net cash expenditure that is lower by HUF 100 billion, in total, than the appropriations in the budget bill. The difference is attributable to our assumption, according to which the absorption of the previously disbursed advances for the programmes financed by the European Union will be slower than the statutory appropriations. The appropriations contain major wage increase and growth in wage costs in several areas; of these, it is worth mentioning the measures affecting the State Audit Office, the National Tax and Customs Administration, the courts and the national defence areas.

The 2019 budget bill plans the **expenditures related to the EU programmes** in the amount of HUF 1,955 billion, which falls short of the 2018 appropriation by HUF 460 billion. Of the total expenditure amount, the expenditure related to the cohesion policy, rural development and the fisheries operational programmes between 2014 and 2020 amount to HUF 1,734 billion. According to our projection prepared for the June Inflation Report, disbursements may exceed the appropriation by roughly HUF 44 billion. According to our expectations, of the disbursements in 2019, advance payments may amount to about HUF 700 billion, without direct cash revenue in the reporting year.

The cash-based deficit reflects the amount of domestic co-financing, as well as 10 percent of the funding that is not reimbursed by the European Commission in 2019, and thus it has to be advanced from the budget. As 10 percent may be accounted for as accrual-based revenue, it does not affect the ESA balance, but substantially adds to the financing requirement and the public debt.

According to our expectations, owing to the rise in the invoiced-based disbursements and absorption of advances, the effective absorption, reflecting the real economy implementation of the projects related to the EU transfers, may exceed this year's level in 2019, followed by a decline in 2020 (Chart 4).

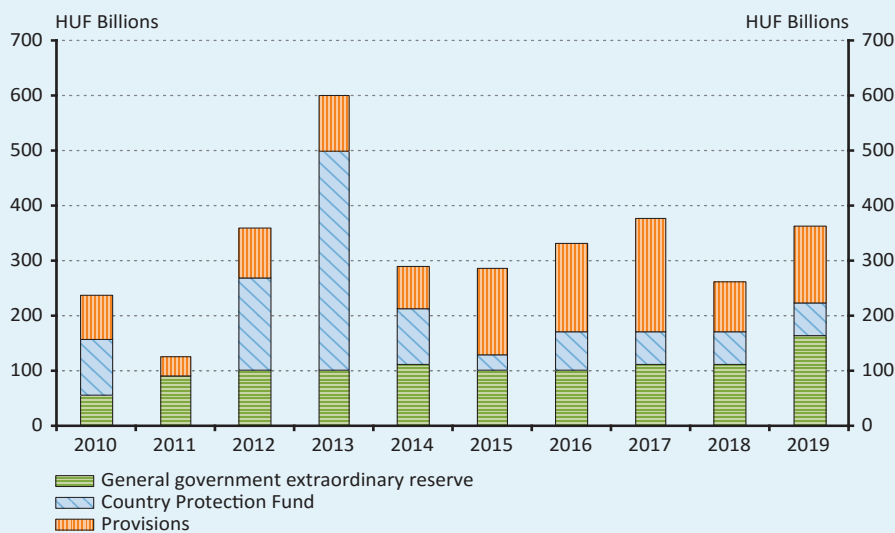
Chart 4
Developments in the effective absorption related to EU transfers and in cash payments



Source: Hungarian State Treasury, Ministry of Finance, MNB.

According to the bill, the amount of the **central reserves** is HUF 361.5 billion, which exceeds the 2018 appropriation by HUF 95 billion (Chart 5). The reserve limit appropriated for the extraordinary expenditures of the government rose by 50 percent compared to the base; this reserve limit of HUF 165 billion, utilisable freely without any restriction, is close to 0.4 percent of GDP. The amount of the central provisions exceeds HUF 136 billion, of which the budget utilises more than HUF 96 billion for public wage expenses. Contrary to the practice of previous years, the budget also appropriated HUF 40 billion for the enhancement of public services. Thus, also taking into consideration the Country Protection Fund’s unchanged amount of HUF 60 billion, the general government disposes above free reserves of HUF 225 billion. This amount exceeds 0.5 percentage point of GDP, and thus it can be stated that the 2019 budget bill contains higher reserve compared to the base year.

Chart 5
Central reserves included in the budget



Source: 2010-2018 Budget Acts and 2019 budget bill.

At the expenditures of the **extra-budgetary funds**, our forecast related to the passive expenditures of the **Labour Market Fund** is almost the same as the appropriation, based on the labour market processes. Compared to 2018, the most significant shift can be expected in the Start labour scheme. In 2019, the anticipated saving on expenditures at the Start labour scheme is HUF 45 billion compared to the 2018 statutory appropriation and it is HUF 8 billion compared to the central bank’s projection for 2018. The saving on expenditures is the consequence of the labour market’s tightness and of the fact that the government encourages jobseekers to find employment primarily in the open labour market.

The statutory appropriation related to **pensions** essentially corresponds to our projection, which is the combined result of impacts of opposite direction (Table 6). On the one hand, in the case of the dependents' pensions and women's early retirement pension we calculate with lower expenditure by HUF 23 billion due to the different assessment of the baseline scenarios, and on the other hand, the difference between the macroeconomic paths results in the projection of higher expenditures by roughly HUF 20 billion. We anticipate higher inflation than indicated in the budget bill, and thus we calculate with higher nominal indexation of the benefits at the beginning of the year, the impact of which is partially offset by the fact that, contrary to the bill, we do not calculate with pension premium payment in 2019.

- 1) Our projection related to the **old-age pensions over the retirement age** exceeds the budget bill's appropriation by HUF 44 billion, which is primarily attributable to the different estimate of the inflation underlying the regular pension increase at the beginning of the year. The macroeconomic projection of the budget bill calculates with a 2.7 percent change in the consumer price index for 2019, while the MNB's latest projection, published in the June Inflation Report, is 3.1 percent. Based on the projection of higher inflation, we assume that there will be a one-off supplementary pension increase in November. In the case of the old-age pensions, in 2019 new pension will be assessed in each month of the year (in 2017 and 2018 this took place only once every six months), since the retirement age for those born in 1955 is 64 years, which results in higher inflow in 2019 compared to the base year. Due to the replacement effect, our projection for 2019 assumes a 4.3 percent growth in expenditures, exceeding the assumed inflation of 3.1 percent.
- 2) In the case of the **pensions payable to women after a 40-year eligibility period**, our projection is lower by HUF 16 billion than the statutory appropriation, which may be due to the different forecast for the number of beneficiaries. As regards the early retirement benefit of women, we continue to calculate with increasing utilisation (Chart 7), considering the fact that with the rise in the retirement age for old-age pension an increasing number of women earns the 40-year eligibility period necessary for retirement. At the same time, in 2019 the flow of the beneficiaries to the group of pensioners over the retirement age will also accelerate, since in 2019 the retirement age will be 64 years throughout the year (in the case of those born in 1955).
- 3) The statutory appropriation for **dependents' pension** exceeds our projection by HUF 7 billion. In the case of the dependents' pensions, assuming a moderate decrease in the number of beneficiaries and an inflation of 3.1 percent, we project only a moderate growth in expenditures. The moderate growth in expenditures may be attributable to the fact that an increasing number of beneficiaries earn entitlement to benefits in their own right.
- 4) The budget bill calculates with the disbursement of **pension premium** in the amount of HUF 25 billion based on the GDP growth of 4.1 percent included in the macroeconomic path. The MNB's macroeconomic forecast projects a GDP growth of 3.5 percent for 2019, and thus we do not calculate with pension premium payment in our forecast (the pension premium is paid if the real growth exceeds 3.5 percent).

Table 6
Comparison of the statutory appropriation related to old-age pensions disbursed from the Pension Insurance Fund and our projection

(HUF billions)

	Statutory appropriation	MNB forecast	Difference
1 Old-age pensions over the retirement age	2,773	2,817	-44
2 Early retirement benefit for women	259	242	16
3 Retirement provision to dependents	388	381	7
4 Provision for pension premium	25	0	25
5 Total pension expenditures (1.+2.+3.+4.)	3,444	3,440	4

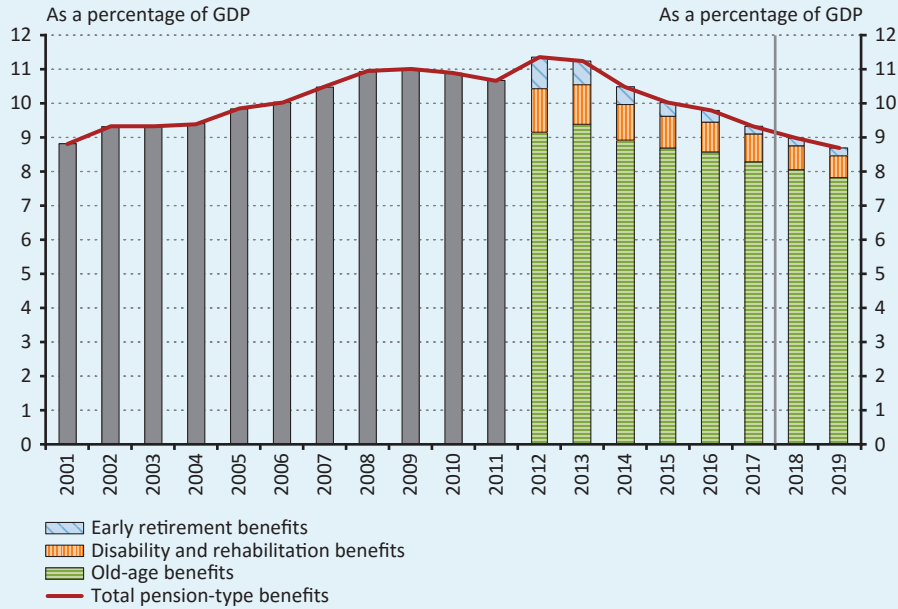
The pension expenditures as a percentage of GDP¹ may fall from 9.3 percent of 2017 to 9 percent in 2018 and to 8.7 percent of GDP in 2019. The fall is caused by the fact that the growth rate of the nominal GDP substantially exceeds the dynamics of pension expenditures. The moderate rise in pension expenditures is attributable to the inflation indexation

¹ Expenditures of pensions and pension-type benefits, including the disability, rehabilitation and early retirement benefits as well

and to the measures taken in recent years, affecting the number of the beneficiaries (raising of the retirement age, tightening the disability benefit eligibility criteria, tightening the early retirement criteria).

Chart 6
Expenditures of pensions and pension-type benefits, 2001-2019

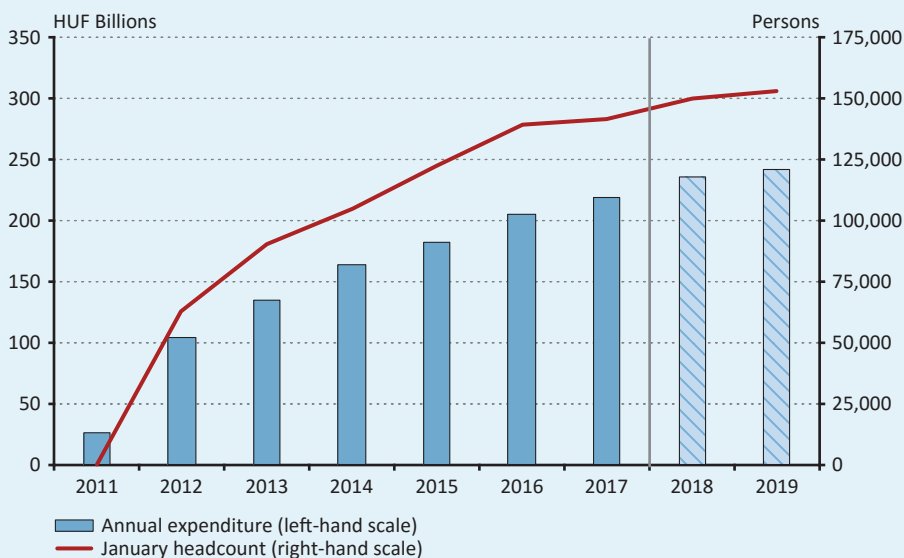
(as a percentage of GDP)



Note: Data between 2001 and 2011 indicate spending on pension and pension-type benefits based on the budget closing accounts; this item cannot be mapped with categories of the accounting regime introduced in January 2012. From 2012, the category of 'old-age benefits' includes over retirement age benefits, over retirement age disability benefits, service dependent pension available for women with 40 years of service, and provisions to dependents. Values for 2017 indicate preliminary cash data, while the 2018 and 2019 values show our forecast.

Source: Hungarian Central Statistical Office, Hungarian State Treasury, Magyar Nemzeti Bank, Act on the Closing Accounts.

Chart 7
Annual budget expenditure related to the pensions payable to women based on 40 years of service and changes in the number of beneficiaries between 2011 and 2019



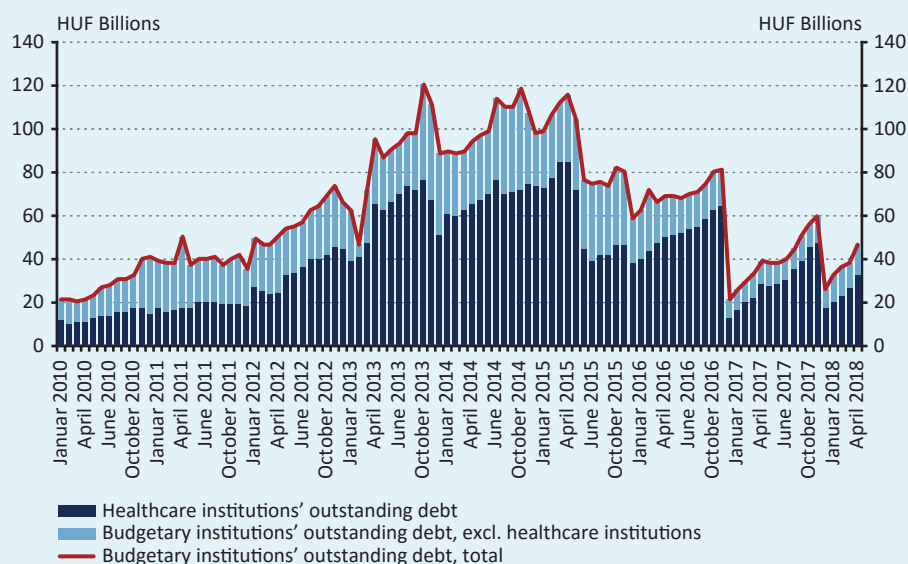
Note: The pensions payable to women based on 40 years of service may be applied for from 1 January 2011, and thus the number of persons starts from zero at the beginning of January 2011. The 2017 expenditure amount indicates preliminary actual data, while the 2018 and 2019 data show our projection.

Source: Hungarian State Treasury, Magyar Nemzeti Bank, Act on the Closing Accounts

The 2019 appropriation for **medical and preventive care** is HUF 1,273 billion, which exceeds the 2018 appropriation by HUF 40 billion. In nominal terms the expenditures for this purpose increase, but as a percentage of GDP a moderate decrease can be expected. According to our forecast, the appropriation includes a moderate upside risk due to the mid-year amendments of the appropriations, which characterised the previous years, and the increasing outstanding debt of the hospitals.

Based on the data of the first four months of the year, the outstanding debt of the healthcare institutions rose to HUF 33 billion (Chart 8). The re-accumulation of debt has necessitated debt consolidation several times in recent years, typically in the form of a one-off consolidation support at the end of the year, or through the reallocation of the residual amount of the appropriation for medical and preventive care, providing the main source of funding for public healthcare institutions. Although due to the consolidation implemented at the end of 2016, the level of the outstanding debt has set on a lower path, from January 2017 it once again shows a rising trend. As regards the composition of the debt, the debt past due for less than 60 days was similar in the first four months of 2018 to the 2017 year-on-year figure, while the balance past due over 60 days doubled. Based on these data, the gradual reproduction of the debt balance may represent a negative risk, as a result of which the need for budgetary intervention may once again arise.

8. Chart
Outstanding debt of budgetary organisations



Note: The time series of healthcare institutions includes institutions for both outpatient and hospital services, the background institutions of the healthcare sector, as well as universities with clinical centres. The time series contains an increasing number of institutions, hence its comparability is limited.

Source: Hungarian State Treasury.

The appropriation for the **health insurance cash benefits** amounts to HUF 394 billion, which exceeds our expenditure forecast for 2019 by HUF 6 billion. This is since our forecast, prepared in line with the June Inflation Report, calculates with lower salary and wage bill compared to the 2019 budget bill.

Within expenditures related to health insurance benefits in kind, the appropriation related to **net expenditures of the drug budget** is HUF 281 billion, which exceeds our forecast by HUF 6 billion. The difference is related almost in full to the expenditure side. Until 2018, this item was regularly underestimated in the budget, but in 2019 we do not anticipate any mid-year increase in the appropriation.

Table 7
Expenditures of the central sub-sector – comparison of the forecasts
(HUF billion)

	2018			2019		
	Statutory appropriation	MNB forecast	Difference	Statutory appropriation	MNB forecast	Difference
PRIMARY EXPENDITURE ITEMS	17,010	16,779	-230	17,507	17,417	-90
Special and normative subsidies and support to the public media	444	444	0	448	448	0
Social policy fare subsidy	98	94	-4	91	94	3
Housing grants	236	203	-33	242	222	-20
Family allowances, social benefits	555	553	-2	551	553	2
Early retirement benefits	90	90	0	89	88	-1
Expenditures of central budgetary organisations and chapters	7,710	7,692	-18	7,801	7,746	-56
Net own expenditures	5,292	5,282	-10	5,846	5,746	-100
Expenditures related to EU transfers	2,418	2,410	-8	1,956	2,000	44
Support to local governments	705	710	5	737	737	0
Contribution to the EU budget	310	310	0	352	352	0
Expenditures related to MNB settlements	0	0	0	0	0	0
Central reserves	261	108	-153	362	362	0
Debt assumption	0	0	0	0	0	0
Other expenditures	440	448	8	492	492	0
Expenditures of extra-budgetary funds	553	530	-24	530	519	-11
NEF – Passive allowances	55	56	1	75	70	-5
NEF – Active allowances	225	188	-38	180	179	-1
Other expenditures	273	286	12	275	270	-5
Expenditures of social security funds	5,608	5,598	-10	5,811	5,804	-7
PIF - Pensions	3,343	3,318	-26	3,420	3,441	21
HIF - Disability and rehabilitation benefits	309	289	-20	287	284	-3
HIF - Cash benefits	352	357	5	394	387	-6
HIF - Medical and preventive care	1,204	1,234	30	1,274	1,274	0
HIF - Net expenditures of the drug budget	265	260	-5	281	275	-6
Other expenditures	134	139	5	156	144	-12
NET INTEREST EXPENDITURES	905	919	14	952	967	15
TOTAL EXPENDITURES	17,914	17,699	-216	18,458	18,383	-75

Note: partly consolidated data.

5.3 INTEREST BALANCE

According to our projection, the net accrual-based interest expenditure may slightly exceed the statutory appropriation, being around 2.2 percent of GDP. The difference compared to the appropriation, approximating 0.1 percent of GDP, may be caused by the yield increase realised since the preparation of the bill, which results in higher government interest expenditure.

The appropriation for the net cash-based interest expenditures falls short of our projection by roughly HUF 15 billion. Our forecast is higher than the appropriation both for the gross interest expenditures and interest revenues. The higher expenditures and revenues may be attributable to the slightly different yield assumption, which in the case of expenditures causes a larger difference between the appropriation and our projection.

6 Legal compliance of the bill

6.1. The debt rule of the Fundamental Law

According to the budget bill and based on the MNB's projection, the gross public debt-to-GDP ratio defined in line with the Stability Act will decrease; accordingly, the bill satisfies the debt rule requirement specified in the Fundamental Law. Based on the Fundamental Law, in 2019 the rate should decrease by 0.1 percentage point, which is safely met according to both forecasts (bill: -2.6 percentage points; MNB -2.2 percentage points). The substantial decrease expected by the projections also means that the decrease in the debt prescribed by the Fundamental Law is guaranteed even if the external or internal economic processes develop slightly less favourably than expected at present.

The MNB's nominal debt projection for the end of 2019 is slightly lower than that stated in the bill. According to the MNB's projection, at the end of 2018 the value of the nominal debt may still be slightly higher than indicated in the bill. The higher initial level is offset by the fact that according to the MNB, in 2019 the cash balance of the central budget may be HUF 955 billion, which is lower than HUF 998 billion, i.e. the value indicated in the bill. The bill anticipates a growth in the debt of the local government sub-sector and a moderate decline in the debt of the companies allocated to the general government sector, which we enforced in our forecast. However, there is a difference between the two projections, according to which, the bill plans to raise funds more than the cash-based deficit, which results in a slightly higher debt.

Due to the different nominal GDP projections, the forecasts related to debt-to-GDP ratio also differ. The 2019 bill indicates a nominal GDP growth of 7.4 percent, while the MNB anticipates a rise of 6.4 percent. As a result of the higher growth, the debt ratio falls short of our forecast by 0.5 percentage point.

Table 8

Development of public debt

(in HUF billion and as percentage of GDP)

	Bill	MNB	Bill	MNB
	HUF billions		As a percentage of GDP*	
1 Year 2018 initial government debt according to the Stability Act	29,809	29,851	72.9	73.0
2 2019 cash-based deficit of the central budget**	998	955	2.3	2.2
3 Other effect	84	6	0.2	0.0
4 Expected gross public debt according to the Stability Act in 2019 (1+2+3)	30,891	30,813	70.3	70.8
5 Change in public debt-to-GDP ratio in 2019 (4-1)			-2.6	-2.2

Note: * The MNB and the bill calculate with different nominal GDP.

The gross debt-to-GDP ratio of the general government according to the EDP method differs from the above due to methodological differences. Calculating, as a rule, with unchanged end-2017 exchange rate of EUR/HUF 310.1, the debt ratio is forecast to decline from 73.6 percent recorded at the end of 2017 to 72.5 percent in 2018, and then to decrease further to 70.3 percent by the end of 2019.

6.2 THE 3 PERCENT DEFICIT RULE OF THE STABILITY ACT

The budget balance expected in 2019 satisfies the deficit rule of the Stability Act. Article 3/A (2) b) of Act CXCV of 2011 on the Economic Stability of Hungary provides that the general government deficit must not exceed 3 percent of GDP. According to the bill, in 2019 the deficit as a percentage of GDP will be around 1.8 percent, while in the MNB's forecast, it will be around 1.7 - 1.8 percent of GDP, i.e. the balance meets the deficit target set forth in the Stability Act.

6.3 DEBT INCREMENT PERMITTED BASED ON THE DEBT FORMULA SPECIFIED IN THE STABILITY ACT

The bill complies with the debt formula specified in the Stability Act. The maximum degree of the nominal increase in the government debt is prescribed by Article 4 (2) and (2a) of the Act on the Economic Stability of Hungary. The rule stipulates that if the rates of inflation and real economic growth forecast for the fiscal year both exceed 3 percent, the balance of the budget should be planned in such a manner that the annual growth rate of the nominal government debt must not exceed the rate of the difference between the inflation and half of the real GDP growth planned in the bill. If at least one of the two ratios is lower than 3 percent, the debt rule prescribes a decrease in the debt ratio of 0.1 percentage point. According to the MNB's forecast both inflation and growth may exceed 3 percent in 2019; however, **in respect of the source of the conditions, the Stability Act names only the macroeconomic path specified in the Budget Act, and thus the decrease in the debt expected by debt formula must be determined based on the forecast included in the budget bill.** According to the bill, although the real growth in 2018 will be higher than 3 percent, the inflation will be lower than that, **thus the debt formula prescribes a decrease of 0.1 percentage point, which is satisfied based on the bill and of the MNB's projection as well.**

6.4 REQUIREMENT PERTAINING TO THE STRUCTURAL BALANCE OF THE GENERAL GOVERNMENT

According to the bill, the structural deficit will exceed the relevant requirement in 2019 and according to the Convergence Programme it will reach the threshold value in 2020. Article 3/A (2) a) of Act CXCV of 2011 on the Economic Stability of Hungary provides that the balance of the government sector has to be determined in a way that it should be in line with the achievement of the medium-term fiscal target. The domestic medium-term fiscal target in 2019 represents a structural balance equalling -1.5 percent of GDP. The structural balance is the cyclically adjusted government balance net of the of the special and temporary budget items. The 2019 bill allocates a structural balance of -1.7 percent to the accrual-based deficit of 1.8 percent as a percentage of GDP, and thus it does not reach the medium-term fiscal target, but at the same time the fiscal position may come close to it in 2019. Regarding the derogation, the bill emphasises that in 2019 the structural deficit approximates the target of 1.5 percent, with the difference falling to a minimum, i.e. 0.2 percentage point of GDP. In addition, the budget expects that after 2019 the structural deficit will be already better than the targeted 1.5 percent.

6.5 RULES OF THE CORRECTIVE ARM OF THE STABILITY AND GROWTH PACT

The budget bill is expected to satisfy the requirements of the corrective arm of the EU fiscal framework. The correction arm includes the 3 percent deficit target, which is also specified in the Hungarian legislation, and requirements of the European Union's debt rule.

- The criterion related to **the 3 percent deficit** prescribes that the accrual-based deficit of the Member States must not exceed 3 percent of GDP. The deficit target of 1.8 percent, included in the bill, complies with the rule.
- The **EU debt rule** states that the Member States' gross, consolidated government debt ratio calculated in nominal value must not exceed 60 percent of GDP, or if it does, the debt ratio must be reduced to a satisfactory degree. The appropriate decrease in the debt is quantified by the "one twentieth" rule, according to which the debt ratio should be reduced by one twentieth of the part that exceeds 60 percent on the average of three years. Based on the bill, the GDP-proportionate government debt will decrease by 2.6 percentage points in 2019, while according to the forecast² of the European Commission, it will decline by 2.3 percentage points, which satisfies the European Union's debt rules.

² Assessment of the 2018 Convergence Programme for Hungary, 3.4. Debt developments, 23 May 2018

6.6 RULES OF THE PREVENTIVE ARM OF THE STABILITY AND GROWTH PACT

The bill is unlikely to satisfy the preventive arm of the Stability and Growth Pact. The rules of the preventive arm serve the achievement of budget deficit target in the medium run, by designating the structural balance and determining the corrective path leading to the medium-term objective.

- The framework related to the **medium-term objective** (MTO) prescribes that the Member State should reach the structural balance designated jointly with the European Commission or approximate it to sufficient degree. The MTO set for Hungary in 2016 is -1.5 percent of GDP. Based on the bill, the 2019 structural balance will be -1.7 percent of GDP, which is a substantial move from the value of -2.1 percent, expected for 2018 in this year's Convergence Programme; at the same time, the degree of the decline does not comply with the expected decline of 1 percentage point, prescribed by the correction path outlined in the Significant Deviation Procedure (SDP)³ launched by the European Commission and the Council. According to the Commission's forecast, this year's structural balance may be -3.6 percent of GDP, while next year's may be around -3.3 percent, i.e. the decline does not comply with the criterion applicable to the medium-term fiscal objective.
- Upon non-compliance with the MTO rules, the **expenditure rules** of the European Union will enter into force, the purpose of which is to ensure the approximation of the medium-term fiscal objective. According to the rule, compared to the previous year, the general government's net primary expenditures may increase by not more than the potential GDP growth rate, unless the increasing expenditures are offset by certain discretionary revenue measures. Based on the rule, the domestic fiscal expenditures may rise by 3.8 percent in real terms; at the same time, based on the Convergence Programme and the assessment by the European Commission⁴, next year's fiscal expenditure processes deviate by 1.1–1.2 percentage points, i.e. the rule is unlikely to be met, but based on this – similarly to the MTO – no excessive deficit procedure may be launched.

³ Recommendation of the Council on the correction of the significant deviation from Hungary's adjustment path toward the medium-term budgetary objective, 23 May 2018.

⁴ Assessment of the 2018 Convergence Programme for Hungary, 3.4. Debt developments, 23 May 2018

7 Special topics

7.1 THE SUBMITTED TAX PACKAGE AND THE ESTIMATED IMPACTS THEREOF

After the submission of the 2019 budget bill, next year's tax bill and the bill on the new social contribution tax were also submitted. The tax package amends several acts affecting tax and contribution types, as well as other acts on tax procedure, accounting and tax enforcement; thus, in addition to a number of tax policy measures, it contains practical measures easing the administration and thereby improving competitiveness. According to our forecast, the tax policy measures result in a total reduction of taxes of roughly HUF 40 billion (Table 9). The largest change affects the labour and income taxes and contributions, but at the same time the burdens of enterprises, the consumption and sales taxes also decline. Upon the approval of the tax package, three tax types – generating negligible revenue – (cultural tax, credit institutions' special tax, private individuals' special tax) will be cancelled, while two other tax types (health contribution and accident tax) will be merged with other tax types, and thus the number of tax and contribution types will decrease by five.

The corporate income tax is affected by two larger measures in the taxation act, which on the whole may reduce fiscal revenues by HUF 9 billion. The first one is a tax base reducing item, which modifies the rules applicable to development reserves. The development reserve is an amount within retained earnings, transferred to the reserve appropriated for investment purposes in the tax year and stated as appropriated reserve on the last day of the tax year, which is at present limited by the Corporate Income Tax Act in 50 percent of the pre-tax profit of the tax year, but maximum HUF 500 million per tax year. The submitted tax package raises this latter limit to HUF 10 billion. Due to this measure, in 2019 corporate income tax revenues are expected to decline by HUF 7 billion. The second amendment expands the tax allowance of investments serving energy efficiency purposes: upon the approval of the tax package, the tax allowance may be requested not only for investments, but also for renovations, which is expected to result in a revenue shortfall of HUF 2 billion.

In the case of the local business tax, the taxation act cancels the tax base exemption related to the increase in employment. Pursuant to the current rule, if a company was able to increase its average statistical headcount by creating new, non-state subsidised jobs, between two tax years, it could reduce its tax base by HUF 1 million per person in respect of the increment. As a result of the measure, revenues may increase by HUF 2.5 billion.

In the case of the small business tax, the amendment doubles the limit regulating the eligibility criteria for selecting this tax type. According to the prevailing regulation, when selecting taxation under the small business tax, the sales revenue and balance sheet total of the taxpayer enterprise in the previous tax year must not exceed HUF 500 million (or the pro rata part thereof when the tax year is shorter than 12 months). The taxation act raises this condition to HUF 1 billion. Although the amendment of the rules may generate an increase in the revenues from small business tax (KIVA), due to the lost social contribution tax and corporate income tax payments of the newly joining KIVA taxpayers, the overall impact of the measure may be a decline of HUF 1.5 billion in fiscal revenues.

Table 9			
Brief description of the 2019 tax measures and their static fiscal effect			
	Tax type	Measure	Impact (HUF billions)
Payments by economic organisations	Corporate income tax	Raising the development reserve to HUF 10 billion from the present HUF 500 million	-7
		Extension of the energy efficiency tax allowance to renovations	-2
	Local business tax	Cancellation of the exemption of tax base for increase in employment	3
	Small business tax	Raising the sales revenue and balance sheet total limits from HUF 0.5 billion to HUF 1 billion.	-2
Consumption, sales taxes	Value added tax	Cutting the VAT rate on milk (ESL, UHT)	-22
	Financial transaction levy	Exemption from the levy for all household credit transfers up to HUF 20,000 per transaction	-2
	Insurance tax	Merging the accident tax and the insurance tax	0
Labour taxes and contributions	Labour taxes and contributions	Exemption of the pensioner employees from certain contributions and the social contribution tax	-61
		Alteration of the fringe benefit scheme	8
		Integration of the healthcare contribution in the social contribution tax	8
	Social contribution tax	Transformation of the targeted allowances of the Job Protection Action Plan	19
Other	Public health product tax	Raising the tax rates by 20 percent, cancellation of the allowances	10
		Expanding the alcoholic beverages product range	4
	75 percent special tax of private individuals	Full cancellation of the special tax	-1
	Innovation contribution	Change in the definition of SME in the case of the innovation contribution	5
Total			-41

Source: Bill T/625, Bill T/627, MNB calculation.

The already preferential tax rate of 18 percent on long-life (UHT and ESL) milk will decrease next year to 5 percent. Similar measure in respect of the other milk types was introduced in 2017, which, according to our estimate, caused a revenue shortfall of roughly HUF 5 billion in the budget. Long-life milk dominates domestic milk consumption, this is why according to our calculations the new measure will decrease the 2019 fiscal revenues by HUF 22 billion.

The tax package exempts the households' credit transfers from the payment of the transaction levy up to HUF 20,000. The measure may cause a revenue shortfall of merely HUF 2-3 billion, while the amendment may contribute to the more dynamic spread of the instant payment system implemented in 2019, as well as to the gradual suppression of the large-scale use of cash in Hungary. In addition, the taxation act introduces the upper limit of HUF 6,000 – applied elsewhere as well – for the credit transfers executed by the Hungarian State Treasury, not belonging to the scope of treasury.

The insurance tax revenues are expected to increase substantially in 2019, as the revenues from the accident tax will be transferred to this estimate, while the latter will be cancelled. By integrating the accident tax in the insurance tax, the taxpayer will be the insurer instead of the insured. Accordingly, the tax rate will change from 30 percent to 15 percent (truck, trailer) and to 20 percent (car, motorcycle), while according to our forecast the expected revenue will not change substantially.

Labour taxes and contributions are affected by several major measures of the tax package. The largest changes include the partial tax and contribution exemption of pensioner employees in their own right, the tightening of the fringe benefit scheme, the transformation of the healthcare contribution into social contribution tax, and the transformation of the

allowances provided under the Job Protection Action Plan. From 2019, **pensioner employees** will benefit from allowances also in the area of employer's contributions, since the employers employing them will not be required to pay the social contribution tax and the vocational training contribution, in addition to the exemption from the in-kind health insurance contribution and the pension contribution. The static fiscal impact of the measures compared to our baseline scenario is roughly HUF 60 billion. The revenue shortfall is mitigated by the fact that the rise in the number of pensioners in their own right taking a job, raises the personal income tax and pecuniary healthcare contribution payments, as the respective employees continue to pay these burdens. For the purpose of the forecast we calculated with more than 60,000 employees, earning almost 80 percent of the anticipated average wage (their wage remains below the average wage, because the large number of part-time pensioner employees reduce the level thereof).

According to our forecast, on the whole, the comprehensive reform of the fringe benefit scheme may have a nearly neutral effect on the budget balance. Of the three components of the fringe benefit scheme, the tax-exempt benefits are terminated almost in full, after the cancellation of the cash benefits only the "SZÉP" card remains in the category of preferential fringe benefits up to an annual limit of HUF 450,000, while most of the certain defined benefits will be also cancelled or taxed as wage. For the purpose of the forecast we assumed that the utilisation of the tax exempt and certain defined benefits will substantially decline, while the degree of the fringe benefits will decrease by one quarter. Thus, due to the low utilisation of the fringe benefits, the companies will transfer to the employees 90 percent of the wage costs not spent on the fringe benefits in the form of a major wage increase. As a result of this the net income of employees may somewhat decrease, while the budget revenues will rise in parallel with this, in view of the fact that the tax burdens of employment are higher than those of the fringe benefits. The fringe benefits and the certain defined benefits are burdened by healthcare contribution and personal income tax, and thus according to our forecasts these revenues will materially decline, which on the other hand are offset by the labour tax revenues, rising on the whole.

The healthcare contribution is cancelled from 2019 and in the future it will be payable as social contribution tax. The previous five rates of this tax type decreased to two in 2017 and it is expected to decrease to one next year. The lower, 14 percent, tax rate will be terminated and the prevailing social contribution tax rate shall govern. This affects primarily two key income categories, i.e. the preferential fringe benefits and the mixed incomes, but in both cases these increases have been compensated. In the case of the fringe benefits, the presently applied tax base multiplier of 1.18 is cancelled, as a result of which the tax burden of the preferential benefit practically remains unchanged (the tax base multiplier applicable to certain defined benefits remains in place). The taxable upper bound of the mixed incomes, such as the incomes withdrawn from enterprises, income from securities lending, dividends, exchange rate profit and agricultural small and primary producers will decrease to twice the minimum wage from HUF 450,000, i.e. the amount effective in 2018. This would reduce the fiscal revenues from social contribution tax but encourages taxpayers to report higher incomes (rather than registering for minimum wage), and thus we expect a moderate income increasing effect at the other labour tax revenues.

The beneficiary target groups of the Job Protection Action Plan will be substantially transformed upon the approval of the act on the new social contribution tax. Two large categories have been removed from the target groups: employees over the age of 55 and below the age of 25 representing about 510-530,000 employees of the average monthly headcount of 900,000 of the Job Protection Action Plan. A new preferential group is created for women with not more than two children, returning from maternity leave, for permanent jobseekers and career starters, uniformly referred to by the act as "labour market entrants". The condition of the utilisation is that within the period of 275 days preceding the beneficiary's employment he had employment relationship for not more than 92 days, i.e. practically, from the past 9 months he was employed for not more than 3 months. The new category also extends the potential range of beneficiaries, since contrary to the former target group of permanent jobseekers, registered job search is no longer a precondition for the utilisation of the allowance, i.e. this opens the way toward the employment of persons formerly being fully inactive in terms of the labour market. It is a further change that while the allowances at present are available up to the gross wage, but not more than HUF 100,000, next year this maximum amount will be revaluated and the upper bound of the allowance base will be the prevailing minimum wage. As a result of the package of policies, on the whole we expect lower utilisation of the allowance; according to our forecast, the growth in revenues compared to the baseline scenario may be as high as HUF 20 billion in 2019 (Table 10).

The public health product tax is amended in three points, which, according to our expectations, together will raise revenues by HUF 14 billion. In the product categories affected by the tax, the tax rate increases on average by about 20 percent, and – with a view to preventing future frauds – the taxation act cancels the allowance available through the

organisation of health maintenance programmes; these measures will result in a growth of HUF 10 billion in fiscal revenues. The range of taxable alcoholic beverages is extended by the formerly tax-exempt fruit spirits and herbal beverages, which may improve the general government balance by HUF 4 billion.

The taxation act contains several other smaller tax policy measures and administrative changes. The package cancels the cultural tax, which generated negligible income, and the 75 percent special tax imposed on certain incomes of private individuals. The Act on Innovation Contribution amends the range of enterprises qualifying as SMEs. In the case of the personal income tax, the submitted bill calculates with the possibility that in 2019 the National Tax and Customs Administration would prepare the draft tax return also for the sole traders. From next year, real estate lessors will be no longer obliged to account for the public utility costs paid by the lessee as income, which will substantially simplify the lease of property, as the lessor will not be required to report all incomes earned on independent activity by itemised cost accounting. In addition, the tax package reduces the registration tax on electric and hybrid engines to 0 forint.

Table 10
Allowances used under the Job Protection Action Plan according to our baseline scenario, after the measures, and the difference between the two
(HUF billions)

Baseline scenario			
	2018	2019	2020
Not requiring qualification	31.5	31.9	32.4
Below 25 years (not more than 180 working days)	5.2	4.8	4.5
Below 25 years (at least 180 working days)	15.1	15.0	14.9
Over 55 years	36.5	36.1	35.7
Permanent jobseekers	3.7	3.2	2.8
Women returning from maternity leave	5.9	5.2	4.7
Agricultural jobs	2.2	2.1	1.9
Total	100.1	98.4	96.8
After the measure			
	2018	2019	2020
Not requiring qualification	31.5	47.2	51.1
Labour market entrants	5.2	27.3	25.6
	15.1		
	36.5		
	3.7		
Women returning from maternity leave (3+ children)	5.9	1.6	1.5
Agricultural jobs	2.2	3.1	3.0
Total	100.1	79.2	81.4
Difference			
	2018	2019	2020
Not requiring qualification	0.0	15.3	18.8
Labour market entrants	0.0	-31.9	-32.2
	0.0		
	0.0		
	0.0		
Women returning from maternity leave (3+ children)	0.0	-3.6	-3.1
Agricultural jobs	0.0	1.0	1.1
Total	0.0	-19.2	-15.5

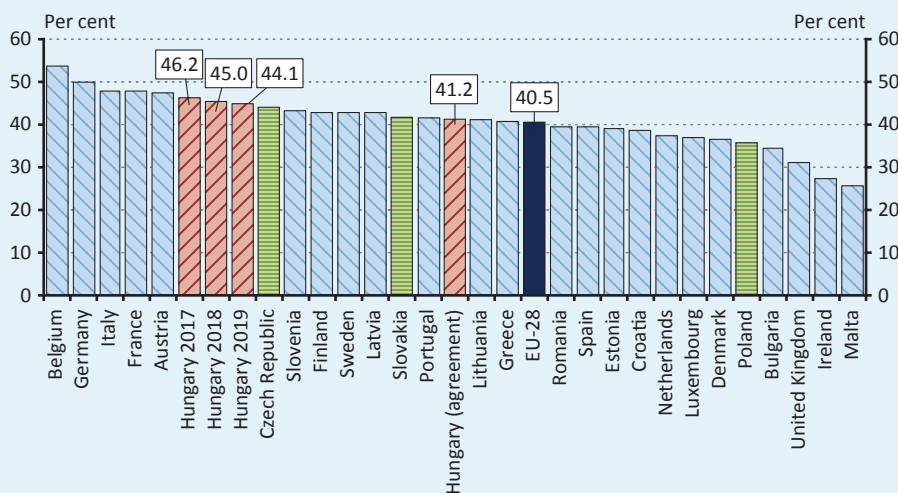
Source: MNB calculations.

7.2 IMPACT OF THE PERMANENT REDUCTION OF THE SOCIAL CONTRIBUTION TAX ON THE TAX WEDGE

The submitted 2019 budget bill conditionally includes the 2 percentage points decrease in the social contribution tax expected next year. The bill tied the tax cut to the 6 percent growth in the private sector's gross real wages adjusted for the consumer price index, as specified in the wage agreement. Based on the wording of the general justification of the budget, a repeated cut in the tax rate may take place from the second half of 2019, i.e. the growth in real wages will reach the underlying threshold in the first quarter of next year. According to the MNB's forecast, the cutting of the rate of this tax type by 2 percentage points from 1 July 2019 represents a saving of roughly HUF 100 billion on a cash basis for the Hungarian employers in 2019.

Accordingly, looking ahead, the tax wedge is gradually decreasing over the next years. The tax wedge indicator shows how much the state draws off from the gross wage cost (net wage plus employee's and employer's burdens) paid by the employer. Last year this ratio was 46.2 percent, which is a material decline compared to the previous years; however, in an EU comparison it can still be deemed high (Chart 9). Based on the rules stipulated in the wage agreement, the 5 percentage points and 2.5 percentage points cuts in the social contribution tax last year and this year will be followed by further four cuts of 2 percentage points, and thus it will decline from the previous 27 percent gradually to less than half of it, to 11.5 percent. The rate cuts will be also reflected in the tax wedge, which may fall to 41.2 percent by the end of the rate cut cycle, which already will be almost identical with the 2017 EU average.

Chart 9
Average tax wedge of the childless employee earning average wage in 2017 in the EU Member States and in Hungary, upon a further 8 percentage point decrease in the social contribution tax, specified in the wage agreement

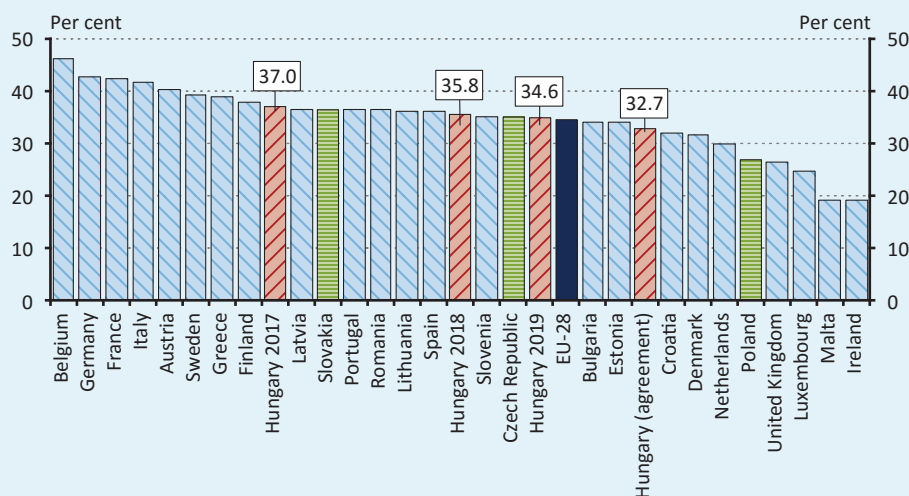


Source: European Commission, MNB calculation.

The reduction of the tax burdens of employees with lower income and of those being in less favourable labour market situation is facilitated by a variety of targeted allowances. The target groups of the Job Protection Action Plan will be transformed in 2019, and from the HUF 100,000 monthly gross threshold the base of the allowance available to the employers increases to the prevailing minimum wage. The largest allowance available to employees is the family tax and contribution allowance, where the allowance available to families with two children next year will increase from this year's HUF 17,500 to HUF 20,000 per dependent, which contributes to the decrease in the tax wedge in 2019 through the rise in net wages (Chart 10). Thus, the average tax wedge of families with two children will decrease from last year's 37 percent to 34.6 percent next year, and later – after the completion of the four times 2 percentage points cuts in social contribution tax – it is expected to fall below 33 percent. This level is lower than the EU member states' average in 2017 and based on the current processes, it is expected to belong to the lower third of the EU countries.

Chart 10

Average tax wedge of families with two children, earning 100 and 67 percent of the average wage in 2017 in the EU Member States and in Hungary, upon a further 8 percentage point decrease in the social contribution tax, specified in the wage agreement



Source: European Commission, MNB calculation.

7.3 DEVELOPMENTS IN INTEREST EXPENSES PAID IN HUNGARY

In the past five years the major decline in the yields of the government securities market, the fall in the government debt and the growth in the share of residents within the debt had a substantial effect on the interest expenses. The changes had an interest expense reducing effect and resulted in a shift in the distribution of the expenditures between the sectors, as a result of which the ratio of interest expenses paid to residents rose. Over the forecast horizon we expect the favourable trends to continue.

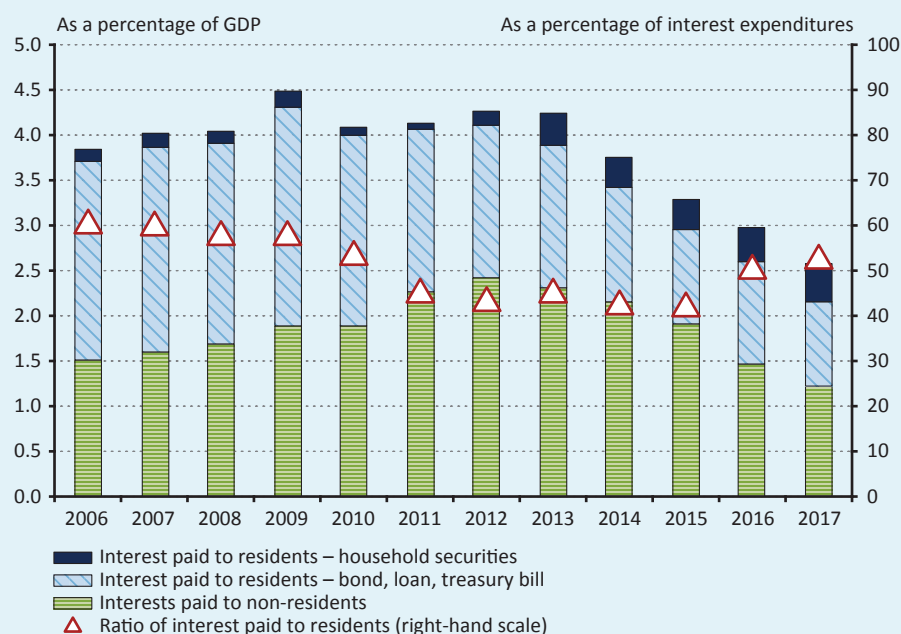
Compared to the interest expenditure level of 4.3 percent of GDP in 2013, they fell substantially, i.e. to 2.6 percent in 2017. As a result of the major decline in the government securities market yields, the budget realises increasing interest saving year by year since 2013. The saving supported the maintenance of the persistently low budget deficit and materially contributed to the decline in government debt. As a result of the gradual repricing of the government debt, the annual saving may rise in the next two years as well, since the share of the low-yield components within the debt is rising.

Interest expenses as percentage of GDP paid to residents and non-residents substantially declined. After the crisis, the ratio of the interests paid abroad substantially rose, caused primarily by the drawdown of the IMF-EU loan and the issuance of the refinancing foreign currency bonds. Thereafter, the decrease in the ownership share of non-residents, and in parallel with that the decline in the ratio of foreign currency within the government debt, substantially reduced Hungary's external vulnerability and the ratio of interest paid abroad also materially declined. The interest paid abroad and on the domestic non-retail government securities, as a percentage of GDP, were roughly halved, while interest payment on household securities rose.

The ratio of interests paid to residents within the total interest expenditures has substantially increased since 2011, and in 2017 it once again exceeded 50 percent. In line with strategic objective of debt management, the ownership share of the domestic sectors with the government debt rose, as a result of which the ratio of interests paid in Hungary already exceeds 50 percent in 2016 after the earlier fall to 40 percent. The domestic ownership share within the debt and the interest paid to residents are continuously increasing in line with the strengthening of self-financing (Chart 11).

Chart 11
Distribution of the interest expenditures paid to residents and non-residents

(as percentage of GDP)



Note: Net of the imputed interests arising due to the transformation of the pension scheme.

Source: Eurostat, MNB.

The interests paid on household securities materially increase the households' disposable income. There was a realignment within the interests paid to residents, and in parallel with the decrease in the total interest expenses paid to residents as a percentage of GDP, the interest paid on household securities rose. However, the growth rate in the paid interest expenses lags behind the growth rate in the household securities portfolio, i.e. the interest on household securities also fell in the declining yield environment. Moreover, the interest paid to the households generates fiscal revenue through several channels, contrary to the interest expense paid to non-residents.

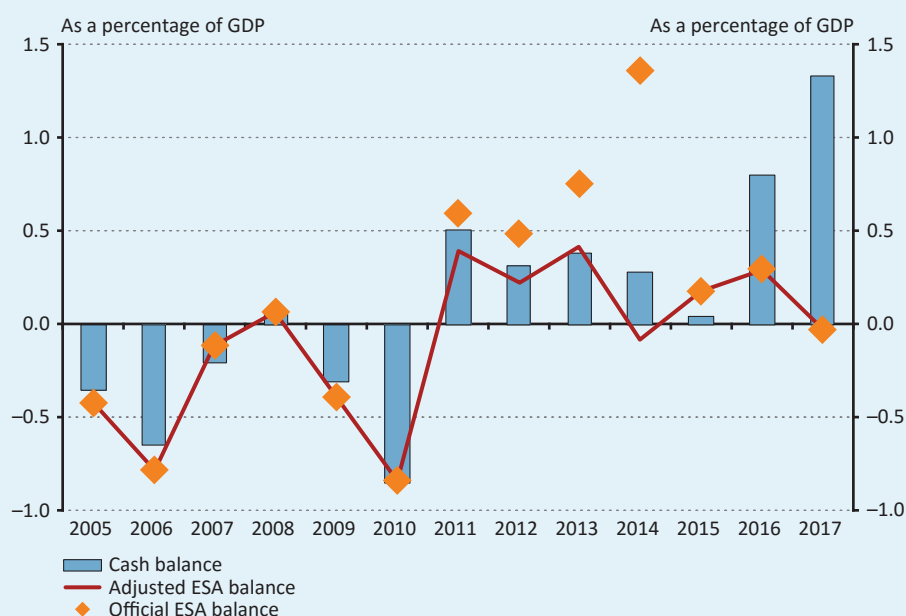
7.4 DEVELOPMENTS IN THE BUDGET MANAGEMENT OF THE LOCAL GOVERNMENT SECTOR BETWEEN 2010 AND 2017

The budgetary consolidation in 2012 also covered the local government sub-sector, similarly to the entire general government. In the years preceding the turn, the aggregate balance of local governments was typically a deficit (between 2005 and 2010 -0.4 percent of GDP on average); however, after the budgetary consolidation their balance shows a trend surplus (+0.2 percent of GDP on average). The reversal of the loss-making management was mostly attributable to the measures taken by the central government in 2010-2014, which may be linked to four basic factors:

- The takeover of part of the local governments' duties resulted in a higher decrease in expenses than the decrease in the subsidies received from the central sub-sector due to the takeover of the duties,
- the debt assumption performed by the central budget in 2013-2014 exempted the indebted local governments from the debt servicing burdens,
- the provisions of the Stability Act increased central control over the borrowings of local governments, and thus the legislative environment prevented and substantially restricted the repeated indebtedness of local governments,
- The EU transfers covered the financing requirement of more than half of the investments in 2012-2015.

Following the major deficit recorded in the previous years, from 2011 the ESA balance of the local governments showed a surplus continuously until 2016, and then in 2017 – according to the available preliminary data – it closed with a minor deficit (Chart 12). The latter is the result of the sub-sector's recovering investment activity.

Chart 12
Changes in the local government balance



Note: The time series of the ESA balance included in the official statistics is distorted by the debt assumption implemented during the period under review, as the statistics accounts for the transactions belonging to the debt assumption as capital revenue. Accordingly, the "adjusted ESA balance", eliminating the impact of the debt assumption, is more appropriate for the purpose of the analysis; this shows a minor deviation from the official balance between 2011-2013 and a larger one in 2014.

Source: HCSO, MNB calculation.

Material difference in the cash balance compared to the accrual-based ESA balance was observed only in 2016-2017.

The difference was caused by the pre-financing by the central budget of the future expenditures related to the absorption of EU funds. These types of revenues increase the cash revenues of the sub-sector, but in an ESA approach they will be recognised only upon their actual absorption (simultaneously with the related local government expenditure, e.g. investment, procurement). According to the first data dissemination by the HCSO, in 2017 the cash balance of the local governments was HUF 508 billion, contributed to by the EU advance revenues by almost HUF 475 billion.

The local governments' revenues as a percentage of GDP declined, in line with the assumption of tasks by the central sub-sector.

The sub-sector's revenues – net of the EU advances – fell from 11.7 percent of 2010 to 6.3 percent by 2017 as percentage of GDP. This was mostly caused by the roughly 4 percent decline in the funds received from the central budget, which essentially took place in 2012-2013 in line with the assumption of tasks. In the same years, the institutional and certain general government revenues declined in connection with the transfer of duties. The local governments' own tax and tax-type revenues as a percentage of GDP were stable throughout the entire period under review. Substantial EU funds were recorded in 2012-2015. In 2016-2017 the local governments received EU funds mostly only as an advance.

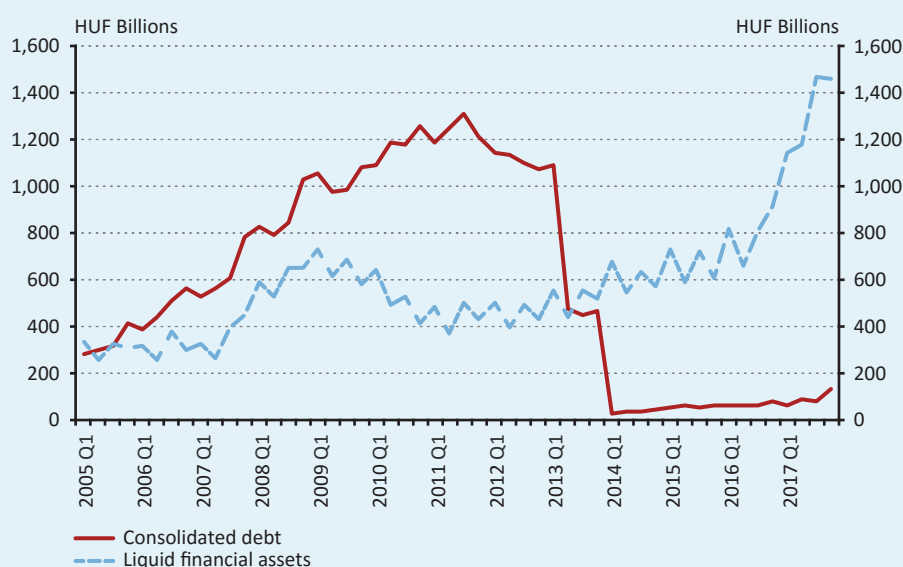
The expenditures of the sub-sector fell from over 10 percent of GDP, recorded in 2010, to around 6 percent of GDP by 2017.

The local governments' GDP-proportionate expenditures fell to a larger degree compared to the level of 2010 than their GDP-proportionate revenues. The different dynamics is primarily related to the deprivation and centralisation of part of the local governments' duties. As regards the entirety of the sub-sector, the degree of the curtailment of funds due the centralisation of tasks was smaller than the decrease in expenditures. As a result of this process, the loss-making management that used to characterise the budget balance of the local government sub-sector has changed for a business management that was close to the equilibrium or even realised budget surplus, already in the short run.

As a result of the debt assumption, the debt of the local government sub-sector fell from HUF 1,260 billion recorded at the end of 2010 to HUF 46 billion by the end of 2014 (Chart 14). The debt assumption of more than HUF 1,200 billion in 2011-2014 took place as part of the government's package of policies transforming the functional duties of the local governments. The statutory regulation limiting the future indebtedness of local governments was also elaborated within the framework of this. Formerly not only the high level of debts and the related debt servicing represented a severe burden for the local governments, but the foreign currency exposure of the outstanding debt also substantially increased the vulnerability of the sector. The debt consolidation intended to remove these risks, at the same time laying the foundation of sustainable business management. After the debt assumption, the local governments may take development loans only subject to the government's permission. Accordingly, the new regime substantially restricts the local governments' possibility of getting indebted.

In recent years there was a substantial increase in the financial assets of local governments (Chart 13). In line with the positive cash balance of local governments, their stocks of assets showed a moderate rise in 2010-2015. The growth accelerated in the past two years due to the advances linked to the EU transfers. The high asset portfolio signals that in the coming years the local governments may implement major investments, absorbing the EU advances or even relying on their own funds. The three-year budgeting outlook of the 2019 budget bill also implies this, as it calculates with a cash-based deficit of around HUF 400 billion in 2020 in the local government sub-sector, and this high cash-based deficit may remain in 2021 as well. Further decrease in assets may be generated by the self-financing connected to the absorption of the EU advances and by the sourcing of the surplus expenditures related to the full implementation of the projects. In addition, uncertainties may be caused by the difficult-to-estimate impacts of the implementation of the Modern Cities Programme on the balance of the sub-sector and through that on the changes in the net financial assets of the sub-sector.

Chart 13
Changes in the consolidated debt and liquid financial assets of the local government sub-sector
(2005Q1 – 2017Q4)



Note: Liquid financial assets include the local government's cash, deposit, short- and long-term securities portfolio.

Source: MNB.

8 Appendix

Table 11
Developments in the cash revenues of the central government between 2017 and 2019
(as percentage of the GDP)

	2017	2018	2019
	Preliminary actual	MNB forecast	MNB forecast
TAX AND CONTRIBUTION REVENUES OF THE CENTRAL SUB-SECTOR	35.9	35.1	35.0
Payments by economic organisations	4.1	3.4	3.3
Corporate income tax	1.6	0.9	0.9
Special tax of financial institutions	0.2	0.1	0.1
Sector-specific surtax	0.0	0.0	0.0
Simplified entrepreneurial tax	0.2	0.1	0.1
Mining royalty	0.1	0.1	0.1
Gambling tax	0.1	0.1	0.1
Income tax on energy providers	0.1	0.1	0.1
Small taxpayers' itemised lump sum tax (KATA)	0.3	0.3	0.3
Small enterprise tax (KIVA)	0.1	0.1	0.1
E-road toll	0.5	0.5	0.4
Utility tax	0.1	0.1	0.1
Other taxes and payments	0.9	1.0	0.9
Consumption taxes	12.8	12.7	13.0
Value added tax	9.2	9.3	9.5
Excise duties	2.7	2.6	2.5
Registration tax	0.1	0.1	0.1
Telecommunication tax	0.1	0.1	0.1
Financial transaction levy	0.6	0.5	0.5
Insurance tax	0.1	0.1	0.2
Tourism development contribution	0.0	0.0	0.0
Payments by households	5.6	5.8	5.8
Personal income tax	5.0	5.2	5.3
Duties, other taxes	0.5	0.5	0.5
Motor vehicle tax	0.1	0.1	0.1
Tax and contribution revenues of extra-budgetary funds	1.4	0.9	1.1
Tax and contribution revenues of social security funds	12.0	12.2	11.8
Social contribution tax and contributions	11.2	11.4	11.4
Other contributions and taxes	0.8	0.8	0.4
REVENUES RELATED TO EU TRANSFERS	3.0	3.7	4.0
OTHER REVENUES	1.3	0.7	0.7
Revenues related to state property	0.7	0.2	0.3
Other revenues of the central budget	0.2	0.1	0.1
Other revenues of social security funds	0.1	0.1	0.1
Other revenues of extra-budgetary funds	0.3	0.3	0.2
TOTAL REVENUES	40.1	39.5	39.8

Note: partly consolidated data.

Table 12**Changes in the cash expenditures of the central sub-sector between 2017 and 2019***(as a percentage of the GDP)*

	2017	2018	2019
	Preliminary actual	MNB forecast	MNB forecast
PRIMARY EXPENDITURE ITEMS	42.7	40.9	39.7
Special and normative subsidies and support to the public media	1.0	1.1	1.0
Social policy fare subsidy	0.2	0.2	0.2
Housing grants	0.5	0.5	0.5
Family allowances, social benefits	1.5	1.3	1.3
Early retirement benefits	0.2	0.2	0.2
Expenditures of central budgetary organisations and chapters	19.5	18.7	17.7
Net own expenditures	12.8	12.9	13.1
Expenditures related to EU transfers	6.5	5.9	4.6
Support to local governments	1.8	1.7	1.7
Contribution to the EU budget	0.7	0.8	0.8
Expenditures related to MNB settlements	0.0	0.0	0.0
Central reserves	0.0	0.3	0.8
Debt assumption	0.0	0.0	0.0
Expenditures related to state property	1.2	0.8	0.8
Other expenditures	0.3	0.3	0.4
Expenditures of extra-budgetary funds	1.7	1.3	1.2
NEF – Passive allowances	0.2	0.1	0.2
NEF – Active allowances	0.7	0.5	0.4
Other expenditures	0.8	0.7	0.6
Expenditures of social security funds	14.1	13.6	13.2
PIF - Pensions	8.3	8.1	7.9
HIF - Disability and rehabilitation benefits	0.8	0.7	0.6
HIF - Cash benefits	0.8	0.9	0.9
HIF - Medical and preventive care	3.1	3.0	2.9
HIF - Net expenditures of the drug budget	0.7	0.6	0.6
Other expenditures	0.3	0.3	0.3
NET INTEREST EXPENDITURES	2.6	2.2	2.2
TOTAL EXPENDITURES	45.3	43.1	41.9

Note: partly consolidated data.

Charles Robert

(1308 – 1342)

King Charles I. was one of the most significant rulers of Hungary. He eliminated the anarchy that came about at the end of the Arpadian age, restored the prestige of royal power and its real influence as well as managed to put the economy back on its feet again. King Charles could well be called the new founding father of Hungary, since he could make Hungary a unified and great economic power even in the state of feudal division. A Hungarian king of French ancestry, the descendant of the Capeting dynasty and member of the Anjou family with great influence in Europe, Charles could only take the throne after considerable struggle.

Charles laid royal power onto new foundations and introduced profound reforms. The old and rebellious nobility was replaced by noblemen loyal to him and seized lands were divided up among them, but only as an office fief for the time they held a royal office. The king became even stronger after establishing a new military organisation with the royal banderium, shire banderium and cuman light cavalry.

He pursued a peaceful foreign policy establishing dynastic ties with neighbouring states, which enabled his son to become heir to the Polish crown. At the congress of Visegrád in 1335 (which is also the basis of our current neighbourhood policy) with the Polish and Czech king present, among others decision was made to create a new trade route,

Charles strengthened royal power in terms of finances as well by filling up the treasury. Since Hungary was the primary source of gold and silver in Europe, Charles put mining and trading under close royal control. Charles shared a significant part of royal revenues from mining lease paid for mining precious metals with the owner of the land to facilitate the discovery of new mines. He forbade the export of precious metals; gold and silver had to be given to newly established minting chambers at a price set by the king.

Instead of numerous various currencies, he started minting the silver denarius with a permanent value, then coining golden florins modelled on the golden coins of Florence with the silver farthing becoming its change. Charles abolished the practice of former rulers to inflate money by occasionally reducing the precious metal content of minted coins.

He increased royal revenues by imposing a new tax. Gate tax was levied for each land that had a gate wide enough to let through a cart laden with hay. Customs duty was introduced set at 1/30 of the value of goods exported to or imported from the west or north and 1/20 of southbound goods. Relying on sound economic foundations, in the second part of Charles' reign numerous gothic buildings were constructed, e.g. the royal palace in Visegrád and the Diósgyőr Castle. However, only traces of many of these buildings were left to posterity due to the Turkish devastation.

A Hungarian king with a truly outstanding life, Charles passed away after his 40-year-long reign, and left a strong and rich kingdom to his son. The political ambitions of the Hungarian Anjou dynasty were embodied in Louis the Great, Sigismund and Matthias Corvinus who restored the bygone glory of royal power, but the first stones in this path were laid by Charles I.

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