PUBLIC FINANCE REVIEW
December 2011

MAGYAR NEMZETI BANK

Analysis of the 2012 Budget Bill – update

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In order to support its core purposes defined in Act LVIII of 2001 on the Magyar Nemzeti Bank ('MNB Act'), and particularly to support the formulation and implementation of monetary policy, the Magyar Nemzeti Bank regularly analyses developments in the budget deficit and debt, monitors the financing of general government, analyses the impact of financing on monetary developments, financial market movements and liquidity, and conducts research on fiscal policy issues. Under the provisions of the MNB Act, the MNB is entitled to express its opinion on the budget proposal to the Government and the competent committee of Parliament.

Pursuant to Act LXXV of 2008 on Fiscal Responsibility, the Governor of MNB is a member of the Fiscal Council (FC) and in this capacity participates in the formulation of the FC's assessment on the draft budget bill to be submitted to Parliament. The Act provides that the work of the FC may be indirectly supported by the professional knowledge and accumulated information available within the MNB, rather than by an independent FC team.

In order to support the fulfilment of these tasks at the highest professional level, the MNB's expert team regularly analyses budgetary processes. The general public can learn of the main findings of the expert analyses from the *'Public Finance Review'*. The findings and conclusions of the analyses reflect the opinions of the experts involved in the preparation of the analysis and should not be interpreted as the views of the MNB or the Monetary Council.

This analysis has been prepared by the Financial Analysis Department under the general direction of Director Áron Gereben. The publication has been approved by Governor András Simor.

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The analysis is based on information available up to 30 November 2011.

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Summary

The purpose of our analysis is to provide an overall picture on the Budget Bill for 2012 before the final vote on the Bill, taking into account new information available since the Bill was submitted, especially the effect of approved motions for amendment.

According to our updated forecast, in 2012 3.2 percent budget deficit is to be expected as a percentage of GDP, that is, our forecast has worsened by 0.1 percent of GDP compared to October. The updated forecast is based on our macroeconomic projection of October, however, since then our macroeconomic assumptions, the yields and the EUR/HUF exchange rate have changed in an adverse direction from a fiscal aspect. As a consequence, based on the preliminary calculations, our forecast of the 2012 budget balance may worsen by as much as 0.2-0.4 percent of GDP, therefore budget deficit may reach 3.4-3.6 percent of GDP in 2012.[1]

Based on the result of our analysis, by the cancellation of the entire amount of the new free reserves in the Budget Bill amounting to 0.7 percent of GDP, that is, assuming no unexpected expenditures or revenue shortfalls during the year, the GDP-proportionate budget deficit may remain below 3 percent in 2012. However, further measures, improving the balance by 1 percent of GDP, have to be implemented in order to achieve the 2.5 percent deficit target set by the Government with unchanged level of free reserves.

Our updated forecast of the cash flow deficit of the central government has increased from 2.8 percent published in October to 3.0 percent, which is 1 percent of GDP higher than the amended appropriation in the Budget Bill. Our forecast still differs from the legal appropriation mainly due to different estimate of the effects of measures.

Tax law amendments have opposite effects on the budget. Among these amendments, the newly imposed health care contribution on fringe benefits increases revenues, while the cost of wage compensation system introduced by the government can be significantly higher than we assumed previously. As a result of the changes in the simplified business tax, we reckon with a more modest tax revenue increase than the government's expectations.

On the expenditure side, measures regarding pharmaceutical subsidies and disability benefits yield savings. However, increase in the net expenditures of budgetary units and chapters, expenditures relating to state property, designated reserves and subsidy of Extrabudgetary Funds negatively affect the budget balance. The decreasing central subsidy of Road Budget will improve the deficit only in cash flow terms, because the use of free cash of the State Motorway Management Company Zrt. to compensate the missing subsidy deteriorates the accrual based balance to the same extent.

[1] The MNB will publish its new macroeconomic forecast in its '*Report on inflation*' to be released on 22 December 2011.

1 Introduction

In the *Public Finance Review* released on 20 October 2011, we published a detailed analysis of the Budget Bill for 2012. In the meantime, several developments have occurred which justify an update of our forecast and our assessment of the Budget Bill before the final vote on the Bill. On 29 November, Parliament decided on the motions for amendment and several new substantive laws were submitted or enacted.

In this analysis, we mainly focus on the way these changes affect our forecast for the various expenditure and revenue appropriations and the budget balance, the difference between our current forecast and the new appropriations in the Budget Bill resulting from the approval of the motions for amendment, and the causes of those differences. This analysis is based on the relevant information available up to 30 November 2011. The principles and methodological assumptions used in our forecast, as well as the background tables to the analyses, can be found in the Appendix.

2 Changes in the expected budget balance since the October forecast

2.1 CHANGES IN THE 2012 ESA BALANCE

As compared to the forecast published in October, our expectations for the ESA-based balance in 2012 have deteriorated slightly, by about 0.1 percent of GDP. This is attributable to the effects on the balance presented in Table 1, showing the major accounting components of the general government.

Even though the official appropriation for **the balance of the central government** remained unchanged, after calculating the changes up to the end of the first round of voting on motions for amendment, our estimated cash flow deficit-to-GDP ratio increased by 0.15 percentage points. Incorporation of new information from the tax legislation approved in the meantime, as well as the approved motions for amendment, resulted in a slightly higher deficit in our projection. This has been only partially offset by the balance improvement resulting from other measures, which came to light since the previous forecasting round, and from the incoming monthly actual data on expenditures and revenues.

The updated forecast shows an improvement in the balance in the **local government sector** which is practically equal in amount to the deterioration identified in the central government. This is mostly because, as indicated by the actual figures for Q1–Q3 2011, local governments implemented a stronger-than-expected fiscal adjustment. It is important to emphasize that our forecast for the balance of local government sector is surrounded by greater degree of uncertainty than the projection for the balance of the central government.

We recorded an almost 0.1 percentage point deterioration in the **GFS–ESA adjustment** taken into account for the calculation of the ESA balance. Except for interest adjustment, the MNB forecast tends to use the official GFS–ESA adjustment figure; however, three separate items arising from our forecast rendered modification of the official figure necessary this time in order to ensure the consistency between our cash flow based and accrual based projections. A positive adjustment was performed due to the expected postponement of some of the VAT reimbursement required by the decision of the European Court of Justice, while a negative correction of an almost identical amount was performed to take account of the accrual-based effects of the employers' compensation related to the phase-out of the tax credit. Furthermore, the ESA balance may be worsened by some HUF 30 billion as – pursuant to the Government's decision of 18 November – the free cash of the State Motorway Management Company Zrt. can be used as a substitute for the missing budget subsidy to the Road Budget.

Table 1
Changes in the MNB forecast for 2012 ESA balance compared to the MNB's October forecast
(% of GDP)

1. ESA balance of general government in our October forecast	**–3.1**
2. Change in the balance of central government	–0.15
of which:	
– Additional impact of tax laws	–0.08
– Impact of further measures	0.07
– Additional impact of motions for amendment	–0.27
– Other	0.12
3. Change in the balance of local governments	0.15
4. Change in GFS–ESA correction	–0.08
5. Total change in ESA balance (2+3+4)	–0.08
6. ESA balance of general government according to our updated forecast (1+5)	**–3.2**

Our current forecast is based on our **macroeconomic projection** of October, since then the used macroeconomic assumptions and the common effect of shift of yields and the EUR/HUF exchange rate have changed in an adverse direction from a fiscal aspect. Based on our preliminary calculations, the alteration of the macroeconomic projection may worsen our forecast of the budget balance of 2012 by 0.2-0.4 percent of GDP, therefore budget deficit may reach 3.4-3.6 percent of GDP in 2012. Based on the results of our analysis, by the cancellation of the entire amount of the **free reserves** in the Budget Bill amounting to 0.7 percent of GDP, that is, assuming no unexpected expenditures or revenue shortfalls during the year, the GDP-proportionate budget deficit may remain below 3 percent in 2012. However, **further measures, improving the balance** by 1 percent of GDP, have to be implemented in order to achieve the 2.5 percent deficit target set by the Government with unchanged level of free reserves.

2.2 CHANGES IN THE CASH FLOW BALANCE OF THE CENTRAL GOVERNMENT IN 2012

In our October forecast, we estimated the additional revenues stemming from the budgetary tax package (excluding indirect macroeconomic effects) at HUF 382 billion, which corresponds to a balance effect of almost HUF 300 billion when the sum of the employer compensation (relating to tax changes and included in the designated reserve of the submitted budget) is also taken into account. Following the adoption of act on the **amendment of various tax laws and other related legislation,** we consider the budgetary effect to be HUF 22 billion lower than in the previous estimation, which is mostly the result of substantive changes and, to a lesser extent, the fine-tuning of our calculations. This barely 0.1 percentage point difference as a percentage of GDP is the net result of significant negative and positive movements. The most important changes relate to the following tax measures:

- The introduction of the **employer tax benefit** relating to compensation for the phase-out of the tax credit and to the minimum wage increase, available in the business sector, is estimated to worsen the balance by HUF 87 billion compared to the October forecast. Our calculations show that if the compensation covers practically all the eligible employees, a revenue shortfall of HUF 171 billion (or HUF 187 billion on an accrual basis) will result for the social contribution tax which replaces the employer's social contribution. However, almost HUF 85 billion of this is covered by the designated reserve that was taken into account in our October forecast.[2]

- Revenues from the **registration tax** are HUF 19 billion lower, due to the 50 percent cut in the standard tax rate, while on aggregate another HUF 10 billion revenue shortfall arises from parliamentary approval of the motions for amendment concerning the **accident tax** and the **public health product tax.**

- Among the new items increasing tax revenues, the health care contribution on **fringe benefits** yields the highest amount at almost HUF 47 billion. Furthermore, additional revenues of HUF 21 billion are expected from the **innovation contribution,** due to the abolition of its allowances, and HUF 7 billion from the expansion of the scope of **product taxes.**

- As a result of the changes in the **simplified business tax** next year, we reckon on a tax revenue increase of only HUF 10 billion (HUF 13 billion, if taking into account the possibility of issuing brought-forward invoices this year), a more modest number than the Government's expectations. This is because we expect taxpayers to adapt relatively actively.[3]

We estimate that additional measures relating to the expenditure side will yield savings of HUF 21 billion in total in the **field of pharmaceutical subsidies and disability benefits:**

- The net expenditures of the drugs budget will be HUF 11 billion lower than in our previous forecast, partly due to the reallocation of responsibilities to medical and preventive care (which we took into account previously in case of the appropriation for medical and preventive care), and partly because of the enactment of new subsidy mechanisms.[4] As a result of the latter, savings of HUF 2 billion may also arise in expenditures on **top-up drug price subsidy.**

[2] In October, we also took into account the effects of the wage compensation and the minimum wage increase on the wage bill already.

[3] We calculate that as a result of the 7 percentage point tax rate hike, 20 percent of the businesses may switch to the corporate income tax or personal income tax regime, which are more favourable to them, while their proportion of deductible expenditure is similar to enterprises engaging in similar activities outside the scope of the simplified business tax. Thus, our calculations indicate that in 2012, despite the tax rate hike, revenues from the simplified business tax will decline, but will be more than offset by increasing revenues from the corporate income tax, PIT, VAT and health care contribution.

[4] Note that the incorporation of the total of HUF 30 billion pharmaceutical subsidy quota into the specialised care appropriation causes a much more modest improvement in the balance of the pharmaceutical subsidy budget because, simultaneously, payments to be made by pharmaceutical companies in the baseline scenario and in case of the deficit turning out to be higher than projected will both decrease. Thus, the budget balance will be improved by the reallocation of responsibilities only as compared to our own October forecast but not in absolute terms.

- We estimate the savings from the bill on the reform of the **benefit system for persons with altered working ability** (No. T/5000) submitted in the meantime to amount to HUF 9 billion in 2012. This is because our calculations reveal that the average amount of the benefit decreases only marginally under the new rules, and by the end of next year we expect no more than 25,000 persons currently receiving disability pension or other benefits to be declared employable as a result of the proposed reviews and their benefits to be terminated because they enter employment (or because they have been working previously). The expenditure cut we estimate is only HUF 5 billion lower than the savings expected by the sponsor of the bill and, in light of the uncertainties around the implementation of the reform, it is more likely to fall short of our estimate than to exceed it.

In respect of the **motions for the amendment of the budget** approved in the first round of voting, only the discretionary items affect our forecast because we prepare our own estimates for appropriations determined by macroeconomic processes and parametric measures. Accordingly, the approved motions for amendment that we took into consideration caused an almost HUF 80 billion deterioration in the balance. Within this, the discretionary balance deteriorated by HUF 93 billion, which is reduced by the HUF 14 billion in tax revenue implied by the increase of wage expenditures and the purchase of goods and services:

- As a result of the motions for amendment, the **net expenditures of budgetary units and chapters** may increase by HUF 138 billion, but HUF 100 billion of this increase relates to the take-over of the institutions of county governments; thus, taking into account the reduction of the budget transfers to the local government sector, the negative impact on the balance is only HUF 40 billion.

- The appropriation for **expenditures relating to state property** has increased by HUF 17 billion, partly because of the stadium construction programme.

- A new expenditure item of HUF 21 billion has been added to **designated reserves** under the heading of employee compensation, with as yet unknown details of utilisation; furthermore, simultaneously with the increase of the innovation contribution, the amount allocated for the **central subsidy of extra-budgetary funds** has also been increased by HUF 15 billion.

Finally, our forecast has been changed as a result of **new information the underlying budgetary processes.** Consequently, we recorded a balance improvement of HUF 35 billion, which is attributable mostly to the better-than-expected cash flow figures for 2011. As a result of the positive base effect, we forecast that 2012 social contribution revenues will be higher by 0.1 percent as a percentage of GDP, compared to the previous estimation. Trends are similar in case of VAT revenues, but the cash flow effects are considerably reduced by the postponement of the reimbursements required by the decision of the ECJ regarding next year.

3 Comparison of our present forecast with the legal appropriation

Based on the considerations detailed above, our current forecast for the cash flow deficit of the central government is higher by HUF 302 billion, or by slightly more than 1 percent of GDP, than the appropriation included in the amended bill. Some HUF 279 billion of the difference is in the primary balance, while HUF 23 billion appears under net interest expenditures. Within the primary balance, three quarters of the difference between our projection and the appropriation, corresponding to 0.7 percent of GDP, relates to revenue items: compared to our October forecast, the difference has remained similar in terms of the ratio, while it has increased slightly in absolute terms.

As a result of the progress of the codification process of the Budget Bill, every measure relevant for the budget is sufficiently detailed to facilitate the assessment of its effects in our forecast. Table 2 reveals that our assessment is less favourable than the Budget Bill, mostly due to the more pessimistic evaluation of these measures. On the whole, our estimate for the budgetary effects of the government measures is 0.7 percent of GDP lower than the government's expectations. There has been no substantive change in that rate since our October forecast.

By contrast, the magnitude of differences resulting from macroeconomic assumptions and other methodological differences has increased from 0.1 percentage point in October to 0.3 percentage point, while the macroeconomic path underlying this forecast has remained unchanged. One reason for this change is our assumption that more than HUF 20 billion of the VAT reimbursements relating to the European Court of Justice decision will be postponed to 2012 in cash flow terms, while the appropriation in the budget bill is unlikely to contain that item. On the other hand, the change also reflects the impact of the motions for amendment that offset additional expenditures without any identifiable measures, by changing the appropriation of autonomous revenue appropriations (e.g. fictitious revenues).

Table 2
Difference between the MNB forecast for the balance of the central government and the appropriation in the amended Budget Bill for 2012
(% of GDP)

	Deviation from statutory target	Different estimate of the effects of measures	Net impact of other differences (macroeconomic forecast, base effect, methodological differences)
1. Primary revenues	−0.73	−0.60	−0.13
2. Primary expenditures	0.23	0.14	0.09
3. Net interest expenditures	0.08	0.00	0.08
4. Balance (1–2–3)	**−1.03**	**−0.73**	**−0.30**

Appendix 1
Background tables

Table A1
Comparison of the macroeconomic forecast of the Budget Bill and the MNB forecast
*(% change from the previous year)**

	Budget		MNB		Difference	
	2011	2012	2011	2012	2011	2012
	Forecast		Forecast		(MNB – budget)	
1. GDP growth (%)	1.9	1.5	1.6	0.6	−0.3	−0.9
2. GDP at current prices (HUF billion)	27,947	29,111	27,720	29,282	−0.8	0.6
3. GDP deflator (%)	2.6	2.6	2.0	5.0	−0.6	2.4
4. Changes in the consumer price index (annual average)	3.8	4.2	3.9	4.9	0.1	0.7
5. Growth rate of labour productivity	1.2	0.0	0.5	−1.0	−0.7	−1.0
6. Investment ratio (as a percentage of GDP)	18.6	19.0	17.0	16.6	−1.6	−2.4
7. Household consumption	0.5	0.0	−0.2	−1.0	−0.7	−1.0
7/A of which: consumption expenditure of households	0.7	0.2	0.4	−0.4	−0.3	−0.6
8. Collective consumption	−2.5	−0.2	0.2	−4.5	2.7	−4.3
9. Gross fixed capital formation	−2.0	3.2	−4.1	−0.1	−2.1	−3.3
10. Domestic absorption	0.4	0.6	−0.5	−1.2	−0.9	−1.8
11. Exports of goods and services	8.8	8.4	9.3	7.4	0.5	−1.0
12. Imports of goods and services	7.7	8.1	7.8	6.5	0.1	−1.6

** Our forecast is based on our macroeconomic projection of October. The MNB will publish its new macroeconomic forecast in its 'Report on inflation' to be released on 22 December 2011.*

Table A2
Summary data of MNB forecast for the 2011 general government budget

	MNB forecast	
	HUF billion	as a percentage of GDP
1. Balance of central government	−1,415	−5.1
2. Balance of local governments	−22	−0.1
3. GFS balance of general government (1+2)	−1,437	−5.2
4. ESA balance of the government sector	1,244	4.5

Table A3
Cash flow balance of the central government
(HUF billion)

	2011		2012		
	Statutory target	MNB forecast	Statutory target	MNB forecast	Difference
1. Balance of central budget	−1,138	−1,509	−601	−891	−290
2. Balance of Extrabudgetary Funds	41	62	60	58	−2
3. Balance of social security funds	−88	33	−35	−45	−10
4. Balance of central government, total (1+2+3)	**−1,184**	**−1,415**	**−576**	**−879**	**−302**
of which:					
Net interest expenditure	−1,008	−967	−1,006	−1,029	−23
Primary balance	−176	−448	430	150	−279
Balance of central government without extraordinary one-off specific items for 2011	**−1,214**	**−1,069**	**−576**	**−857**	**−280**

Note: The cash flow balance adjusted with certain one-off items was deducted deduced from the uncorrected balance; in the adjusted balance, we disregarded funds taken over from private pension funds (HUF 529 billion), the acquisition of MOL shares (HUF 499 billion), partial debt consolidation of MÁV (Hungarian State Railways) (HUF 64 billion), the planned capital injection for MFB (HUF 62 billion) and the amount of negative VAT due to the ruling of the Court (HUF 250 billion). We suppose that a smaller part of the VAT refund (HUF 22 billion) will take place in 2012.

Table A4
Presentation of the ESA balance of the general government
(% of GDP)

	2010	2011	2012		
	Fact	MNB forecast	Statutory targets	MNB forecast	Difference
1. Balance of central government	−3.3	−5.1	−2.0	−3.0	−1.0
2. Balance of local governments	−0.8	−0.1	−0.5	−0.1	0.4
3. GFS balance of general government (1+2)	−4.2	−5.2	−2.5	−3.1	−0.7
4. GFS–ESA difference	−0.1	9.7	0.0	0.0	0.0
5. ESA balance of general government (3+4)	**−4.3**	**4.5**	**−2.5**	**−3.2**	**−0.6**

Table A5
Augmented cash flow balance
(% of GDP)

	2010	2011	2012
1. GFS balance of general government	−4.2	−5.2	−3.1
2. Corrections	0.7	−1.0	−0.5
3. Augmented balance of general government (1+2)	**−3.5**	**−6.1**	**−3.7**

Table A6
Budget balance by classes of items
(HUF billion)

	2011		2012		
	Statutory target	MNB forecast	Statutory target	MNB forecast	Difference
1. Balance of exogenous items	5,380	5,218	6,265	5,966	−299
2. Balance of discretionary items	−5,556	−5,665	−5,836	−5,815	20
3. Net interest expenditures	−1,008	−967	−1,006	−1,029	−23
4. Balance of central government (1+2+3)	**−1,184**	**−1,415**	**−576**	**−879**	**−302**

Table A7
Change of the cash flow balance of the central government compared to the adjusted 2011 base, by main categories
(% of GDP)

	2011 MNB forecast	2012 MNB forecast	Difference
1. Exogenous revenues, total	34.5	34.9	0.5
2. Exogenous expenditures, total	14.7	14.5	−0.2
3. Balance of exogenous items (1−2)	19.7	20.4	0.7
4. Balance of discretionary items	*−20.1*	*−19.9*	*0.2*
5. Net interest expenditures	−3.5	−3.5	0.0
6. Balance of central government (3+4+5)	**−3.9**	**−2.9**	**0.9**

Note: In the exogenous revenues adjusted with certain one-off items, we disregarded the negative VAT due to the ruling of the Court (HUF 250 billion in 2011, HUF 22 billion in 2012). The balance of discretionary items was adjusted by funds taken over from private pension funds (HUF 529 billion), the acquisition of MOL shares (HUF 499 billion), the partial debt consolidation of MÁV (Hungarian State Railways) (HUF 64 billion), and the planned capital injection for MFB (HUF 62 billion) in 2011.

Table A8
Changes in exogenous items
(HUF billion)

	2011		2012		
	Statutory target	MNB forecast	Statutory target	MNB forecast	Difference
Revenues	**9,539**	**9,300**	**10,419**	**10,205**	**–214**
Payments by businesses, total	**1,159**	**1,155**	**1,348**	**1,178**	**–171**
Corporate income tax	288	289	356	304	–52
Surtax of corporations	0	–16	0	0	0
Fees of financial institutions	11	9	8	8	0
Special tax of financial institutions	187	186	187	186	–1
Sector-specific taxes	161	164	155	160	5
Simplified entrepreneurial tax	180	171	225	147	–78
Green taxes	27	23.5	26	23.6	–3
Mining royalty	88	109	94	99	5
Gambling tax	51	51	78	55	–24
Income tax of energy companies	20	17	14	14	0
Company car tax	28	25	46	36	–10
Enviromental protection product fee	21	26	60	45	–15
Rehabilitation contribution	65	66	65	67	2
Other payments	32	36	33	33	0
Consumption taxes	**3,402**	**3,085**	**3,630**	**3,594**	**–36**
Value-added tax	2,489	2,177	2,718	2,670	–47
Excise duties	881	874	898	905	7
Registration tax	32	34	14	18	4
Payments by households	**1,446**	**1,456**	**1,677**	**1,647**	**–31**
Personal income tax	1,363	1,378	1,574	1,552	–22
Fees and duties	82	74	103	94	–9
Other taxes	1	4	0	0	0
Revenues from the EU	**9**	**9**	**9**	**9**	**0**
Refunds on custom duties and contribution to sugar industry	9	9	9	9	0
Exogenous revenues of extrabudgetary and social security funds	**3,522**	**3,594**	**3,755**	**3,778**	**23**
LMF – Health insurance and labour market contribution	188	187	194	195	1
LMF – Vocational contribution	49	50	53	53	0
LMF – Repayment of wage guarantee	1	1	1	1	0
RDF – Innovation contribution	23	24	45	46	1
NCF – Revenues from lottery	9	10	10	10	0
PIF – Employer's and insured persons' contribution	2,553	2,613	2,537	2,552	15
PIF – Other contributions (exogenous items)	28	22	20	20	0
HIF – Employers' and insured persons' contribution	597	593	709	698	–11
HIF – Other contributions (exogenous items)	39	40	43	47	4
HIF – Per capita health contribution	36	54	99	109	9
HIF – Accident surcharge	0	0	24	25	1
HIF – Public health product tax	0	0	20	22	2
Expenditures	**4,159**	**4,082**	**4,154**	**4,239**	**85**
National Social Policy Fund	**474**	**474**	**776**	**793**	**17**
Family allowances, social benefits (exogenous)	474	474	472	471	–1
Benefits under retirement age	n. a.	n. a.	304	321	18
Expenditures related to settlements with the MNB	**0**	**0**	**0**	**34**	**34**
Payments to the EU	**258**	**258**	**264**	**286**	**22**
Exogenous expeditures of extrabudgetary and social security funds	**3,427**	**3,349**	**3,114**	**3,126**	**13**
LMF – Jobseekers' assistance and wage guarantee	142	128	63	68	5
PIF – Pensions	3,054	3,028	2,555	2,561	6
HIF – Cash benefits	231	193	211	217	5
HIF – Disability benefits (exogenous items)	n. a.	n. a.	284	281	–3
Balance of the items	**5,380**	**5,218**	**6,265**	**5,966**	**–299**

Table A9
MNB forecast and budgetary target relating to discretionary items

	2011		2012		
	Statutory appropriations	MNB forecast	Statutory appropriations	MNB forecast	Difference
Discretionary revenues	**227**	**257**	**449**	**450**	**2**
Other discretionary revenues of central budget	112	129	164	165	2
Revenues of Extrabudgetary Funds	60	69	63	63	0
Own revenues of social security funds	55	58	222	222	0
Discretionary expenditures	**5,813**	**5,826**	**6,285**	**6,266**	**−19**
Consumer price subsidy	109	109	93	93	0
Family allowances, social subsidies (discretionary items)	154	150	77	77	0
Housing grants	126	126	120	120	0
Net expenditures of budgetary institutions and chapters	2,255	2,330	2,354	2,312	−42
Transfers to business organisations	274	274	302	302	0
Transfers to local governments	1,173	1,197	1,043	1,043	0
Expenditures related to state property	96	177	128	128	0
Other discretionary expenditures	107	44	268	268	0
Expenditures of Extrabudgetary Funds	232	238	322	322	0
Net expenditures of the drugs budget	300	315	226	240	14
HIF – health impairment benefits	0	0	58	67	9
Other discretionary expenditures of HIF (in-kind benefits)	862	867	904	904	0
Designated and general reserves	124	0	190	190	0
National Protection Fund and Interest Risk Reserves	0	0	200	200	0
Discretionary balance without one-off items	**−5,586**	**−5,569**	**−5,836**	**−5,815**	**20**
Corrections for one-off items	30	−96	0	0	0
Discretionary balance in accordance with Act on public finances	**−5,556**	**−5,665**	**−5,836**	**−5,815**	**20**

Table A10
MNB forecast and budgetary target – revenues
(HUF billion)

REVENUES	2011		2012		
	Statutory target	MNB	Statutory target	MNB	Difference
CENTRAL BUDGET					
PAYMENTS BY BUSINESSES					
Corporate income tax	288	289	356	304	–52
Surtax of corporations	0	–16	0	0	0
Fees of financial institutions	11	9	8	8	0
Special tax of financial institutions	187	186	187	186	–1
Sector-specific taxes	161	164	155	160	5
Simplified entrepreneurial tax	180	171	225	147	–78
Green taxes	27	24	26	24	–3
Mining royalty	88	109	94	99	5
Gambling tax	51	51	78	55	–24
Other payments	32	32	33	33	0
Other centralized payments	110	119	179	163	–16
Income tax of energy companies	20	17	14	14	0
Company car tax	28	25	46	36	–10
TOTAL	**1,183**	**1,179**	**1,402**	**1,229**	**–173**
CONSUMPTION TAXES					
Value-added tax	2,489	2,177	2,718	2,670	–47
Excise duties	881	874	898	905	7
Registration tax	32	34	14	18	4
TOTAL	**3,402**	**3,085**	**3,630**	**3,594**	**–36**
PAYMENTS BY HOUSEHOLDS					
Personal income tax	1,363	1,378	1,574	1,552	–22
Fees and duties	82	74	103	94	–9
Other taxes	1	4	0	0	0
TOTAL	**1,446**	**1,456**	**1,677**	**1,647**	**–31**
CENTRAL BUDGETARY INSTITUTIONS AND CHAPTER ADMINISTERED APPROPRIATIONS					
Revenues of central budgetary institutions	567	817	949	949	0
Chapter administered professional appropriations	81	311	16	16	0
EU support of chapter administered professional appropriations and central investments	1,147	873	1,528	1,108	–420
TOTAL	**1,795**	**2,002**	**2,493**	**2,073**	**–420**
PAYMENTS FROM FUNDS OF THE GENERAL GOVERNMENT	33	43	49	49	0
PAYMENTS RELATED TO STATE PROPERTY	44	49	50	50	0
OTHER REVENUES	24	29	20	20	0
REVENUES FROM EU	29	29	49	53	4
REVENUES OF PENSION REFORM AND DEBT REDUCTION FUND	96	96	0	0	0
REVENUES RELATED TO DEBT SERVICE	60	100	59	77	17
TOTAL REVENUES OF CENTRAL BUDGET	**8,111**	**8,067**	**9,429**	**8,790**	**–639**
EXTRABUDGETARY FUNDS					
LMF – Health insurance and labour market contributions	188	187	194	195	1
LMF – Vocational contributions	49	50	53	53	0
RDF – Innovation contributions	23	24	45	46	1
NCF – Revenues from lottery	9	10	10	10	0
Revenues of other funds	148	157	144	144	0
TOTAL REVENUES OF EXTRABUDGETARY FUNDS	**416**	**428**	**445**	**448**	**3**

Table A10
MNB forecast and budgetary target – revenues (cont'd)
(HUF billion)

REVENUES	2011		2012		
	Statutory target	MNB	Statutory target	MNB	Difference
SOCIAL SECURITY FUNDS					
PENSION INSURANCE FUND	**3,074**	**3,131**	**2,750**	**2,765**	**16**
Contributions	2,593	2,650	2,575	2,590	16
Benefits and subsidies from central budget	0	0	150	150	0
Revenues from Pension Reform and Debt Reduction Fund	433	433	0	0	0
Other revenues	47	47	25	25	0
HEALTH INSURANCE FUND	**1,371**	**1,407**	**1,700**	**1,742**	**42**
Contributions (Per capita health contribution incl.)	673	688	853	855	2
Benefits and subsidies from central budget, transfers from Pension Insurace Fund	642	642	738	738	0
Public health product tax	0	0	20	22	2
Accident surcharge	0	0	24	25	1
Other revenues	55	76	65	102	37
TOTAL REVENUES OF SOCIAL SECURITY FUNDS	**4,444**	**4,538**	**4,450**	**4,507**	**57**
TOTAL REVENUES OF CENTRAL GOVERNMENT	**12,971**	**13,033**	**14,324**	**13,745**	**–579**

Table A11
MNB forecast and budgetary target – expenditures
(HUF billion)

EXPENDITURES	2011		2012		
	appropriation	MNB	appropriation	MNB	difference
CENTRAL BUDGET					
SUBSIDIES TO ECONOMIC UNITS	215	215	238	238	0
SUPPORT TO THE MEDIA	59	59	65	65	0
CONSUMER PRICE SUBSIDY	109	109	93	93	0
HOUSING GRANTS	126	126	120	120	0
NATIONAL SOCIAL POLICY FUND					
Family benefits, social subsidies	628	624	549	548	–1
Benefits under retirement age	n. a.	n. a.	304	321	18
GOVERMENT AGENCIES AND CHAPTERED-ADMINISTERED APPROPRIATIONS					
Expenditures of central budgetary institutions	1,849	2,133	2,420	2,420	0
Chapter-administered professional appropriations	2,233	2,234	2,458	1,996	–462
EXPENDITURES RELATED TO MNB	0	0	0	34	34
RESERVES	124	0	390	390	0
TRANSFERS TO FUNDS OF GENERAL GOVERNMENT	1,898	1,925	1,846	1,846	0
SUPPORT TO CIVIL ORGANISATIONS	4	4	4	4	0
EXPENDITURES RELATED TO STATE PROPERTY	594	675	128	128	0
EXTRAORDINARY AND OTHER GOVERNMENTAL EXPENDITURES	36	36	33	33	0
EXPENDITURES RELATED TO STATE GUARANTEES	35	35	40	40	0
DEBT ASSUMPTION AND RELEASE	0	64	0	0	0
CONTRIBUTION TO EU BUDGET	258	258	264	286	22
DEBT SERVICE, INTEREST PAYMENT	1,079	1,079	1,079	1,119	41
TOTAL EXPENDITURES OF CENTRAL BUDGET	**9,249**	**9,577**	**10,029**	**9,681**	**–348**
EXTRABUDGETARY FUNDS					
LMF – Passive allowances	135	124	59	64	5
LMF – Active and other expenditures	176	171	249	249	0
Expenditures of other funds	62	72	78	78	0
TOTAL EXPENDITURES OF EXTRABUDGETARY FUNDS	**374**	**367**	**385**	**390**	**5**
SOCIAL SECURITY FUNDS					
PENSION INSURANCE FUND	**3,074**	**3,047**	**2,750**	**2,756**	**6**
Pensions	3,054	3,028	2,555	2,561	6
Other expenditures	19	19	195	195	0
HEALTH INSURANCE FUND	**1,459**	**1,458**	**1,735**	**1,797**	**62**
Sick allowance	86	68	73	73	0
Child care allowances	146	136	140	145	5
Drugs	344	376	278	328	51
Medical and preventive care	770	774	825	825	0
Disability and rehabilitation benefits	0	0	342	348	6
Other provisions and expenditures	112	105	77	77	0
TOTAL EXPENDITURES OF SOCIAL SECURITY FUNDS	**4,532**	**4,505**	**4,485**	**4,553**	**68**
TOTAL EXPENDITURES OF CENTRAL GOVERNMENT	**14,155**	**14,449**	**14,900**	**14,624**	**–276**

Appendix 2
Forecasting principles and methodology

Fiscal forecasting is undertaken on a rule basis. In that context, the best international practice has been followed in the Reports on Inflation since August 2003.[5] According to international recommendations, the fiscal measures adopted (or announced) should only be taken into account if they are **sufficiently detailed.**[6] The criterion of sufficient detail may have different interpretations for the various budget items, depending on the level of government control over the particular items. The following section will focus on the cash flow items of the central government and the local government and the accrual-based figures of the government sector in that respect.

The level of control is quite varied between the various cash flow items of the **central government.** One potential approach is to break down the items into interest balance and exogenous and discretionary items.

Exogenous items include the primary revenues and expenditures, the realisation of which is clearly determined by the private economy and demographic trends, and the laws creating individual entitlements or obligations. Such items include, among others, tax revenues and pension expenditures. On the basis of our rule-based forecast, a measure is not considered to be sufficiently detailed in that context unless the envisaged parameters of the entitlement and obligation are available. In the absence of the above, the implications of these measures cannot be calculated. Similarly, the impact of measures envisaged in connection with the efficiency of tax collection cannot be taken into account. In other words, no forecast is prepared on the changes in the rate of tax evasion.

Discretionary items including all other items constitute a more mixed group in terms of the extent of government control. As far as capped expenditure appropriations are concerned, their numerical amount is a sufficient condition of detail, as they cannot be exceeded. This cannot be automatically assumed for allowances which are also partly determined by certain demographic trends. On the revenue side, EU funds, institutional revenues and the disposal of real assets may differ from the target. The net expenditure of budgetary institutions and chapters is, however, only affected by this factor to the extent that co-financing is required for the part of EU financing used in the budget.

In addition to the exogenous and discretionary items, a rule-based forecast is also prepared for the **interest balance.** While in principle the government has little control over the interest balance, the forint-currency composition and breakdown by maturity in the financing plan do affect the net interest expenditure. The official financing plan is therefore taken into account or, if it is not available, the assumption concerning the financing structure is based on the basic principles of the established interest management strategy.

While our forecast concerning the central government is purely rule-based, an expert forecast is prepared for the cash flow items determined by **local governments.** This is because the government does not exercise full control over local governments and, therefore, our forecast is based on the sources received from the central government, historical tendencies (the local election cycle) and financing opportunities.

Similarly, there is no government control over **accrual-based** developments or institutions (e.g. not-for-profit institutions) considered to be part of the government sector for statistical purposes. The sum of these items (i.e. the difference of the cash-flow and the accrual-based balance) is the so-called ESA bridge adjusting the government deficit. With the exception of the interest adjustment recorded on an accrual basis, no specific projection is made for the ESA bridge. Instead, we use the most recent official forecast (published in the Budget Bill or Eurostat notification).

[5] For a more detailed description of our method, see pp. 76-77 of the 2003 August *Report on Inflation*.

[6] Of the fiscal measures announced, the OECD's rule of forecasting only takes into account the ones manifested in sufficiently defined programs (http://www.oecd.org/document/40/0,3746,en_2649_34573_1850792_1_1_1_1,00.html). On the basis of international experience, the ECB has stressed that fiscal forecasts should only take into consideration sufficiently detailed measures passed or likely to be passed by Parliament without changes (see Leal, Teresa, Javier J. Pérez, Mika Tujula and Jean-Pierre Vidal (2007), 'Fiscal Forecasting – Lessons from the Literature and Challenges', *ECB working paper,* no. 843, December.)

Table A12
Measures considered in our forecast

	Own estimation based on regulation enacted or proposal submitted to Parliament	Applying statutory target/appropriation (strong governmental control on items)
Széll Kálmán Plan		
Employment and labour market		
Shortening disbursement period of unemployment benefit and removal of unemployment assistance	x	
Overhaul of the wage supplement system		x
Partial substitution of the financing of active labour market policies with EU funds		x
Modification of sick pay eligibility rules	x	
Capping social benefits		x
Nominal freezing of family benefits	x	
Reform of pension system		
Pension benefit increase based on CPI	x	
Review of early retirement pension benefits	x	
Review of disability pension eligibility rules	x	
Public transport		
MÁV–Volán integration and cost-efficiency improvement of MÁV		x
Review of the preferential tariff system	x	
Higher education		
Reducing the enrollment in tertiary education and capacity downsizing		x
Drugs budget		
Revenue increasing measures	x	
Expenditure decreasing measures	x	x
State and municipal financing		
Reorganisation of local government duties by economies of scale, restriction and control of borrowing	x	
Rationalisation of central and background institutions		x
Government Debt Reduction Fund		
Unchanged regulation on special tax of financial institutions	x	
Convergence programme measures		
Cancellation of stability reserve		x
Nominal freezing of wages in public sector		x
Maintaining the nominal level of material expenditures in chapters in central budget		x
Announcements related to Budget Bill		
Change in PIT	x	
Classification of entertainment under PIT	x	
Corporate income tax: limitation on loss write-offs	x	
VAT increase	x	
Increase of excise duties	x	
Increase of company car tax	x	
Increase of taxes on slot machines	x	
Taxing online gambling	x	
1 percentage point increase of employee contribution	x	
Expansion of the contribution base	x	
Accident surcharge	x	
Increase of environmental protection product tax, expanding its tax base	x	
Expansion of the base of public health product tax	x	

Table A12
Measures considered in our forecast (cont'd)

	Own estimation based on regulation enacted or proposal submitted to Parliament	Applying statutory target/appropriation (strong governmental control on items)
Increase of fees and duties	x	
Increase of simplified entrepreneurial tax	x	
Limitation of allowances of innovation contribution	x	
Change in registration tax	x	
Change in health contribution	x	
Increase in flat rate health insurance contribution	x	
Reduction of social benefits and assistances		x
Abolishment of subsidies on road toll		x
Other expenditure decreasing measures relating to budgetary chapters and entities		x

Table A13
Applied estimation methods – revenues

REVENUES	Applied methodologies
CENTRAL BUDGET	
PAYMENTS BY BUSINESSES	
Corporate income tax	estimation based on effective tax rate and tax base (without corporations in the finance sector), corrected for the estimated effects of government measures (e.g. stricter rules for writing-off losses) and economic cycle; expert judgement on tax payment of financial sector (consistent with assumption concerning effect of early repayment scheme on profits of financial institutions)
Surtax of corporations	estimation based on actual development of tax refund
Fees of financial institutions	2011: estimation based on actual development of quarterly revenues; 2012: assuming a 10% decrease compared to 2011
Special tax of financial institutions	2011: statutory target and taking into account actual revenue development, 2012: kept fixed at 2011 base
Sector-specific taxes	product of estimated weighted total net revenues of sectors involved and expected base 2010
Simplified entrepreneurial tax	base 2011 increased with the growth rate of real GDP
Green taxes (energy tax, etc.)	base 2011 multiplied by the average growth rate of real GDP and nominal GDP
Mining royalty	corrected base 2010, oil price futures assumption for the exchange rate, trend of oil and gas exploitation
Gambling tax	projected change in real disposable income for lottery games taking into account recent price-policy, tax revenues from slot machines is projected using historical trend of the number of such machines online gambling: low level of revenues
Other payments	statutory target
Other centralized revenues	
Rehabilitation contribution	for 2011 estimation based on ARIMA-modell; for 2012 estimation historical trend
Enviromental protection product fee	2011 statutory target of sub-items augmented by tax increase, modified with the estimated effect of possibly stricter tax-exemption rules
Other revenues	statutory target for discretionary items; correction for items involved due to changes in number of slot-machines operated (consistent with the estimation of gambling tax)
Income tax of energy companies	expert estimation for 2011; statutory target for 2012
Company car tax	base 2011 multiplied by the growth rate of real GDP 2011: estimation based on actual data development
CONSUMPTION TAXES	
Value-added tax	base 2010 multiplied by household consumption expenditure corrected by government consumption and investment expenditure; correction using expert judgement for the effects of certain measures (eg. simplified clearance procedure)
Excise duties	expert judgement on volume of fuel consumption and tax reinbursement; in case of tobacco: estimated behavioral effect due to tax increase, assuming no change in volume consumed; alcoholic beverages: expected base 2011 indexed by forecasted volume of consumption
Registration tax	base 2011 mulplied by the growth rate of nominal GDP with some minor corrections based on expert judgement
PAYMENTS BY HOUSHOLDS	
Personal income tax	calculated tax liability indexed by the growth of wage bill corrected by the effect of changes in tax rate; expert judgement on tax allowance in line with tax code; for income items taxed separately tax base indexed by nominal GDP growth rate; estimation for all separable items' tax base in the case of witholding tax; sum of claimed tax credit given in the tax proposal corrected by expert judgment

Table A13
Applied estimation methods – revenues (cont'd)

REVENUES	Applied methodologies
Fees and duties	statutory target with corrections (taking into account actual revenue development)
Other taxes	statutory target
CENTRAL BUDGETARY INSTITUTIONS AND CHAPTER ADMINISTERED APPROPRIATIONS	
Revenues of central budgetary institutions	statutory target and correction based on expert judgement
Chapter administered professional appropriations	statutory target and correction based on expert judgement
EU support of chapter administered professional appropriations and central investments	statutory target and correction based on expert judgement
PAYMENTS FROM FUNDS OF THE GENERAL GOVERNMENT	statutory target with corrections (taking into account actual revenue development)
PAYMENTS RELATED TO STATE PROPERTY	statutory target
OTHER REVENUES	statutory target
REVENUES FROM THE EU	statutory target
REVENUES OF PENSION REFORM AND DEBT REDUCTION FUND	statutory target
REVENUES RELATED TO DEBT SERVICE	estimation (based on yields curves, exhange rates and expected issuance schedule)
EXTRABUDGETARY FUNDS	
LMF – Health insurance and labor market contributions	base 2011 muliplied by forecasted groth of wage bill, modified with the effect of measures and changes in effective level of tax compliance
LMF – Vocational contributions	base 2011 muliplied by forecasted growth of wage bill
RDF – Innovation contributions	base indexed by nominal GDP growth rate
NCF – revenues from lottery	consistent with the estimated gambling tax revenue for regarding lottery game
Revenues from other funds: wage-guarantee repayment	historical seasonal pattern of wage-guarantee payment
Revenues of other funds: other revenues	statutory target
PENSION INSURANCE FUND	
Contributions	base 2011 muliplied by forecasted growth rate of wage bill, modified with the effect of measures and changes in effective level of tax compliance
Revenues of Pension Reform and Debt Reduction Fund	statutory target (discretionary item)
Other revenues	statutory target (discretionary item)
HEALTH INSURANCE FUND	
Contributions	base 2011 muliplied by forecasted growth rate of wage bill, modified with the effect of measures and changes in effective level of tax compliance
Per capita health contribution	base 2011 indexed by forecasted growth rate of nominal GDP
Benefits and subsidies from central budget	statutory target (discretionary item)
Public health product tax	forecasting volumes and turnovers (relevant CPI and consumption) of taxed products based on HKF-database, estimated price-elasticities
Accident surcharge	based on estimated gross insurance premium from third-party liability for motor vehicles
Other revenues	payments of the pharmaceutical companies is assumed to be consistent with projected pharmaceutical expenditures and expected relevant, other revenues are assumed to meet the statutory targets

Table A14
Applied estimation methods – expenditures

EXPENDITURES	Applied methodologies
CENTRAL BUDGET	
SUBSIDIES TO ECONOMIC UNITS	statutory target
SUPPORT TO THE MEDIA	statutory target
CONSUMER PRICE SUBSIDY	statutory target and taking into account actual revenue developments
HOUSING GRANTS	statutory target
NATIONAL SOCIAL POLICY FUND	
Family benefits, social subsidies	estimation using trends of reference population and number of recipients and expected developments of specific benefits (typically kept fixed at 2011 level)
Benefits under retirement age	estimated using age-distribution and average benefits of recipients, average benefit increased by pensioner's CPI without concerning measures
GOVERMENT AGENCIES AND CHAPTERED-ADMINISTERED APPROPRIATIONS	
Expenditures of central budgetary institutions	statutory target with corrections based on expert judgement
Chapter-administered professional appropriations	statutory target with corrections based on expert judgement
RESERVES	statutory target with corrections based on expert judgement
TRANSFERS TO FUNDS OF GENERAL GOVERNMENT	statutory target with corrections based on expert judgement
SUPPORT TO CIVIL ORGANISATIONS	statutory target
EXPENDITURES RELATED TO MNB	MNB forecast
EXPENDITURES RELATED TO STATE PROPERTY	statutory target
EXTRAORDINARY AND OTHER GOVERNMENTAL EXPENDITURES	statutory target
EXPENDITURES RELATED TO STATE GUARANTEES	statutory target
DEBT ASSUMPTION AND RELEASE	statutory target
CONTRIBUTION TO EU BUDGET	statutory target and taking into account actual revenue developments
DEBT SERVICE, INTEREST PAYMENT	estimation (based on yields curves, exhange rates and expected issuance schedule)
EXTRABUDGETARY FUNDS	
LMF – Passive allowances	expected base 2011 muliplied by forecasted growth rate of wage bill and change in the number of unemployed, corrected with effect of recent measures and that of the increased minimum wage; transfer items from central budget: appropriation
LMF – Active and other expenditures: wage-gaurantee payments	base 2011 increased by the forecasted growth rate of wage bill
LMF – Active and other expenditures: other payments	statutory target
Expenditures of other funds	statutory target
SOCIAL SECURITY FUNDS	
PENSION INSURANCE FUND	
Pensions	base 2011 muliplied by pensioners' CPI corrected with actual data and seasonal developments based on past recent years
Other expenditures	statutory target (discretionary item)
HEALTH INSURANCE FUND	
Sick allowance	base 2011 muliplied by forecasted growth of wage bill, modified with the effect of measures come into force recently
Child care allowances	base 2011 muliplied by forecasted growth of wage bill augmented by the effect of measures and demographical development
Drugs	projected using the corrected subsidy-outflow on monthly basis, taking into account the effects of expected measures
Disability and rehabilitation benefits	base 2011 muliplied by pensioners' CPI corrected with actual data and seasonal developments
Medical and preventive care	statutory target (discretionary item)
Other provisions and expenditures	statutory target (discretionary item)

Appendix 3
Terms and definitions of general government

Act on public finances Act XXXVIII of 1992 on public finances, adopted by simple majority, sets out rules relating to the operation and monitoring of general government. Accordingly, the Budget Act of the given year may overwrite its provisions.

Augmented (SNA) balance The analytical indicator of the MNB has been used for fifteen years to carry out adjustments that support the adaptation of Hungarian budgetary settlement to the standard payment framework. This includes the adjustment of the late performance of payments, tax refunds, the non-funded financing requirement of certain state-owned companies, PPP investments and capital revenues in excess of real asset sales. It serves the settlement of similar economic events each year, with a similar method and at the same time, that is, the filtering of the effects of creative accounting.

Budgetary authorities and chapters In the balance sheet of the central government, this item includes the revenues/expenditures of central budgetary authorities (budgetary institutions, ministries, authorities) and the revenues/expenditures of budgetary targets managed under chapters (programme financing under direct ministerial supervision).

Capped discretionary item Discretional item among expenditure budgetary targets, where the budgetary target may only be exceeded with separate regulation. Over-spending requires transfers, the use of reserves or carryover funds or the amendment of the Budget Act.

Carry-forward, write-off of loss Under certain conditions, business organisations subject to corporate taxation may offset their cumulated loss arising in the reference year (negative tax base) with profit arising in a subsequent profitable year, that is, reduce future profit up to the amount of cumulated loss carried forward, but for up to the amount of profit.

Carryover funds (budget carryover funds) In relation to authorities and chapters, if budgeted amounts are unspent at the end of the year, these are settled as carryover funds and, under certain conditions, these can be carried over to the next year. The budgetary targets specified in the Budget Act can be implemented by maintaining the level of carryover funds.

Carryover obligation An instrument of budgetary payments control. Ordering of a budgetary institution or chapter to save a portion of its budgetary amount at the end of the year, increased with the carryover funds of the previous year. In practice, this typically means that the budgetary carryover funds should not decrease from one year to another (the use of carryover funds should not increase).

Central government Pursuant to the provisions of the Act on public finances in force, the central government in the general government includes the Hungarian State, as the subject of obligations and rights under public law, central budgetary authorities, and unless provided otherwise by law, budgetary authorities that are founded by the Government or legal entity belonging to the central government. Within the central government, three main subsectors are distinguished in payment settlements: the central budget, extrabudgetary funds and the social security fund.

Contribution effectiveness

It shows how actually collected contribution revenue relates to theoretical revenue calculated on the basis of the wage bill of the national economy and the percentage rates set out in legislation.

Cyclical component

Effect of the economic cycle on the general government balance, manifested predominantly through the fluctuation of tax revenues and to a lesser extent through changes in unemployment benefits and expenditures (e.g. pension) indexed to real variables.

Cyclically adjusted augmented (SNA) balance

Analytical indicator calculated by the MNB, indicating the balance expected after the end of the economic cycle's effect without further measures, provided that the effect of "creative accounting" – reversed by itself in the long term – does not distort the balance.

Debt rule set out in the Constitution

Pursuant to the Constitution effective as of 1 January 2012, Parliament may not adopt a law on the central budget, where government debt would exceed half of the gross domestic product. As long as government debt exceeds half of the gross domestic product, Parliament may only adopt a law on the central budget that sets out the reduction of government debt-to-GDP ratio.

Designated reserves

Statutory target specified in the budget, serving as cover for central (government) measures in the given subsector, the aim and purpose of which is concurrently defined, where the distribution of the budgeted amount's spending according to chapter, title and sub-title is not yet specified in the Budget Bill. It is principally used in 2011 and 2012 to provide compensation for the phasing out of tax credits.

Discretionary items

Discretionary items are budgetary expenditure and revenue items that are approved by Parliament in the form of the Budget Act (these are also defined as "discretional" items). Public sector wages, for example, are discretional expenditures, while fine revenues of budgetary authorities are discretionary revenues.

EDP balance

Indicator of general government balance used in the framework of the excessive deficit procedure (EDP). Methodologically the EDP balance almost fully corresponds to the ESA balance, only the settlement of interest expenditures varies (see EDP based interest expenditures), but the resulting difference between the two indices is less than 0.1 per cent of GDP.

EDP based interest expenditure

The EDP and ESA based interest expenditure differ methodologically in that the EDP methodology accounts for interest payments modified by swap and FRA transactions, while the ESA methodology accounts for interest payments related to original issues. The sign of the difference may vary year to year; its value did not reach 0.1 per cent of GDP in recent years. Our forecast assumes that the expected value of the difference is zero.

Efficiency of tax collection

Ratio of actual tax revenue and revenue collectible pursuant to tax legislation.

ESA balance

Index defined by the European System of National Accounts (ESA). It differs in several points from the indicator defined in the Act on public finances. See ESA-GFS methodological bridge. Key differences: 1) use of accrual-based instead of cash-flow accounting, 2) expansion of institutional scope defined by the Act on public finances with non-profit organisations and state-owned companies.

ESA-GFS methodological bridge

Difference between the ESA deficit and the indicator defined in the Act on public finances. The difference is attributable, among others, to the difference between cash flow and accrual accounting and variation between institutions covered by the two indices. In the forecast, the MNB applies the official ESA–GFS difference published by the Ministry for National Economy, based on the Eurostat notification or exposition of the Budget Bill. Since our interest rate forecast differs from that of the government, our accrual adjustment with accrued interest accordingly also differs, and we thereby modify the methodological bridge published by the Ministry for National Economy.

Eurostat notification

Pursuant to legislation relating to the excessive deficit procedure (EDP), balance and debt data reported by the national statistical offices to Eurostat, verified and published by Eurostat.

Exogenous items

Primary revenues and expenditures that are clearly determined by macroeconomic and demographic trends and laws establishing individual rights or obligations. These include, for example, tax revenues and retirement benefits.

Extrabudgetary funds

Pursuant to the provision of the Act on public finances in force, Extrabudgetary Funds are funds that finance certain duties of the state partly from non-general government funds, necessitating appropriated financing within general government due to the nature of its operation. The Budget Bill for the year 2012 lists the Central Nuclear Financial Fund, Labour Market Fund, National Cultural Fund, Wesselényi Miklós Flood and Inland Waterway Protection Compensation Fund, Bethlen Gábor Fund and the Research and Technological Innovation Fund as extrabudgetary funds.

General government

According to the provision of the Act on public finances in force, general government consists of the central government and local government subsector. General government covers a narrower scope of fiscal processes than the government sector defined according to the methodology of the European Union (see government sector). Thus, the Pension Reform and Debt Reduction Fund, for example, managing the asset portfolio transferred from private pension funds, is not part of general government, but belongs to the government sector.

General government debt

According to the Act on Public Finances, general government debt is the sum of government debt and local government debt, where debts between the subsectors must be consolidated.

General reserve (Reserve serving exceptional government measures)

Pursuant to provisions of the Act on public finances in force, general reserve is a reserve set aside by the central budget, covering contingent, unforeseeable expenditures, structural transformation and the supplementing of budgeted, but unexpected revenue shortfalls. According to the provision in force, the budgeted reserve may not exceed 2 per cent of aggregate expenditures of the central budget or be less than 0.5 per cent thereof. Obligations undertaken in H1 may not exceed 40 per cent of the reserve.

GFS balance

Payment balance prepared according to the methodology of the International Monetary Fund issued in 1986. With some differences (e.g. in relation to the management of privatisation revenues), it approximates the balance defined by the effective provisions of the Act on Public Finances. For the sake of simplicity, we define the balance under the Act on Public Finances as the GFS balance.

Government debt

According to the Act on public finances, government debt is the consolidated debt of the central government in the general government.

Government sector	Scope of institutions defined in accordance with the rules of the ESA methodology. Reclassification from the corporate sector is conditional on 1) state control, and 2) less than half of the production costs of the company are covered with sales revenue (including state support provided to all similar producers). On the basis of this criterion, the units of BKV and MÁV producing the largest losses remain in the corporate sector.
Interest risk reserve	Appropriated reserve among budget expenditures to cover the risk of higher-than-budgeted interest expenditures. The actual value of interest expenditures significantly depends on unforeseeable economic trends, particularly changes in the forint exchange rate and yields on the government securities market. The reserve ensures that higher-than-planned interest expenditures do not cause an increase in the budget deficit up to the amount of the reserve.
Local government debt	Debt jointly encumbering local governments and local minority governments; when calculating such debt, debt between the individual local governments has to be consolidated.
Local government subsector	Pursuant to the provision of the Act on public finances in force, the local government subsector of general government covers the following legal entities: local governments, local minority governments, local government budgetary authorities, legal entities classified by law in the local government subsector and budgetary authorities, where the founder is classified in the local government subsector.
Medium-term objective (MTO)	Budgetary deficit objective defined in the Stability and Growth Pact of the European Union, varying for each country. The MTO defines the medium-term, cyclically adjusted deficit objective, filtered from one-off items. It is in all cases more stringent than the Maastricht criteria to ensure that the deficit does not exceed 3 per cent of GDP in an adverse economic environment either, and ensure the long-term sustainability of the budget. In relation to Hungary, the MTO is 1.5 per cent of GDP.
National Protection Fund	Reserve appropriated in the 2012 budget for the management and offsetting of macroeconomic and other external risks.
Net expenditures of budgetary authorities and chapters	In the balance sheet of the central government under the Act on public finances, the arithmetical difference between the expenditure and revenue rows related to budgetary authorities and budgetary targets managed under chapters (accordingly, for example, payments from central budgetary authorities to the central budget are accounted for among revenues). Expenditures calculated in this manner are basically deemed to be consolidated expenditures. The analysis of net expenditures is justified instead of the separate analysis of revenues and expenditures, as the funding requirement in the scope of institutions and chapters, not covered with own revenues in the reference year, as well as the amount of budgetary support necessary for the performance of duties can be directly determined. Net expenditures also effectively reflect fiscal trends if substantial funds are transferred between authorities. The reorganisation of public administration, the delivery-acceptance of duties between institutions and chapters, namely, increases both revenues and expenditures (accumulation), but the budget balance remains unchanged.
Open-ended discretionary item	Discretionary expenditure item, in relation to which the Budget Bill contains a budgetary target which, however, may be exceeded without separate regulation or with government approval (e.g. pharmaceutical subsidies).
Pension indexing	Statutory annual increase of retirement benefits and pension-type benefits. According to regulations in force, if GDP growth remains below 3 per cent, pensions increase by the rate of the pensioner consumer price index. If GDP growth is between 3 and 4 per cent, the ratio of inflation and net average wage increase equals 80-20 per cent in the pension increase; this

ratio is 60-40 per cent if growth is between 4 and 5 per cent. If GDP growth reaches 5 per cent, the net average wage-inflation ratio equals 50-50 per cent.

Pensioners' consumer price index
Annual change in the price of products and services in the pensioner consumer basket.

PPP investment
Investment implemented through cooperation between the government and private sectors. Its most common form, the PPP contract, applies to the formation, as well as the operation of fixed assets. Uniquely in Hungary, in some cases in the past, the private partner was also a state-owned company, thus Eurostat classified these investments as government investments.

Primary balance
In this publication, we interpret the primary balance as the balance calculated without interest expenditures and interest revenues. According to the definition of the MNB, the MNB payments and loss reimbursements are excluded from the primary balance as well, but in this case, we included these as part of the primary balance to ensure comparability with the Bill.

Real debt rule
The fiscal regulatory framework set out in Act LXXV of 2008 on prudent state finances and fiscal responsibility fundamentally aims at maintaining the real value of government debt (debt of central government pursuant to the Act on public finances). For the purpose of achieving the target, the law sets out a regulatory framework based on a three-year planning cycle that aims at maintaining the real value of debt in the medium term, but allows deviation from this path in the short term, on the basis of the unforeseeable volatility of the economy.

Reserve serving exceptional government measures
See General reserve.

Semi-super grossing, super grossing
In Hungary, semi-super grossing defines a form of the personal income tax system, where personal income tax is paid on the "super-gross" wage increased with employer contributions, but the simple gross income is the contribution base. In a consistent super-gross system, all contributions would also be taxed on the basis of total labour cost (i.e. super-gross income). From 2010 to 2011, and partially in 2012, however, only the tax base of personal income tax, and not of contributions is raised in Hungary; the system was termed as "semi-super grossing" as a result of the "semi-sided" tax base.

Social security funds
These include the Pension Insurance and Health Insurance Funds. The social security funds function as an insurance system based on risk pooling; most of their revenues are covered by contributions and to a lesser extent by budgetary funds and other revenues.

Super grossing
See Semi-super grossing, super grossing.

Supplier debt
Financial obligation of government institutions (generally vis-à-vis enterprises).

Tax avoidance, tax evasion
Avoidance of tax obligation. For example declaring labour incomes as capital incomes; its illegal form is a simulated contract, its legal form is present when private entrepreneurs voluntarily determine lower labour income. The illegal form is called tax evasion, while the form exploiting loopholes in the tax system is termed as tax avoidance.

Tax credit
Item decreasing personal income tax, provided on a monthly basis in Hungary, up to a certain level of eligibility based on wage income.

Tax evasion See Tax avoidance, tax evasion.

Wage bill index The gross wage bill of the national economy, i.e. annual change in the amount of the basic wage including personal income tax, health insurance and pension contributions and employee contributions, and wage elements paid under other titles (wage supplement, supplementary salary, premium, bonus, 13th month and additional monthly wages).

Write-off of loss See Carry-forward, write-off of loss.

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