PUBLIC FINANCE REPORT

2022

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)

PUBLIC FINANCE REPORT

Analysis of the 2023 Budget Bill

2022

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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 determination 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 CXCIV 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 provides them to the FC.

The analyses in this Report were prepared under the direction of Gergely Baksay, Executive Director for Economic Analysis and Competitiveness. This report was created by the staff of the Directorate for Fiscal and Competitiveness Analysis with the assistance of the staff of the Directorate Economic Forecast and Analysis. It was approved for publication by Governor György Matolcsy.

The analysis is based on information available for the period ending on 30 June 2022.

Contents

1 Summary

The subject of this analysis is the 2023 budget bill, submitted to the Parliament on 7 June 2022, which we assess in the light of the MNB's fiscal forecast. As part of this analysis, the MNB prepared its own projection for the 2023 budget balance and the government debt based on the available information, and this projection is compared with the appropriation in the bill.

According to the budget bill, in 2023 the ESA budget deficit target will be 3.5 per cent of GDP. Next year's deficit target is lower than the target of 3.9 per cent of GDP planned at the beginning of 2022 but corresponds to the figure indicated in the Convergence Programme published at end-April 2022. Reaching a balance that is in line with the deficit target is supported by the high tax revenues resulting from economic growth and by the fiscal measures announced in parallel with the 2023 budget bill, which offset the expenditure increasing effects of the war between Russia and Ukraine and the high energy prices through the increasing of tax revenues and the restraining of expenditures. Compared to the 2022 statutory appropriation and to this year's deficit target indicated in the Convergence Programme, the planned deficit-to-GDP ratio represents declines of 2.4 percentage points and 1.4 percentage points, respectively.

The measures announced in May contribute to achieving the planned deficit target. For the time being, the details of the measures taken in order to reduce the general government deficit this year and next year (mainly on the expenditure side) are not completely known. On the revenue side, the surtaxes imposed on corporate 'extra profit' in eight sectors have the greatest impact on the budget. In addition, the bill contains further tax measures amounting an annual HUF 100–200 billion. Most of the revenues from the surtaxes go to two new budgetary funds to be created, i.e. the Utilities Protection and Defence Funds, where they provide cover for the additional expenditures arising in the funds and related to the increase in energy prices and to national defence. Within the framework of consolidation measures concerning the expenditure side of the budget, certain public investment projects that have not started will be cancelled or postponed, and the other material and investment expenditures of budgetary institutions and chapters will be reduced.

In our opinion, the budget deficit target of 3.5 per cent of GDP can be achieved, provided that the planned macroeconomic path materialises and the announced tax changes as well as decline in expenditures are elaborated in detail and implemented. According to our projection, cash-based expenditures may exceed the appropriation, while revenues may slightly be lower than the statutory expectation, which is primarily related to the tax and contribution revenues on labour. According to both expectations, the balance of the local government sub-sector may be nearly neutral in 2023. At the same time, our forecast for the amount of accrual-based adjustments is much more favourable than the figure indicated in the bill. The difference between the forecasts for the accrual-based adjustments is mainly attributable to the difference between the items related to EU funds. In the case of EU funds, the difference between the expectations regarding the carry-over of the 2014–2020 funds between years may be significant. On the whole, the MNB's forecast suggests that the sum of next year's statistical adjustments points to a decline in deficit, which offsets our expectation related to a higher cash-based deficit. **Based on all the above, in line with the objective set forth in the bill, the year 2023 general government deficit is estimated to correspond to 3.5 per cent of GDP.**

The budget contains the cohesion and recovery funds of the 2021–2027 EU budget cycle. The bill envisages EU-related expenditures and revenues to amount to some HUF 3400 billion and a total HUF 2090 billion, respectively. More than two thirds of the expenditure target and around half of the planned revenue are related to the 2021–2027 funds, but their drawdown still requires the approval of the Partnership Agreement submitted in December 2021 and the individual operational programmes as well as of the Recovery and Resilience Plan submitted in May 2021.

According to the bill, the debt-to-GDP ratio is expected to decline by 2.3 percentage points in 2023. According to the bill, the gross debt-to-GDP ratio of the general government according to the EDP methodology will decline from 76.6 per cent at end-2021 to 76.1 per cent in 2022, followed by a decrease to 73.8 per cent by end-2023. According to our forecast, the decline in the government debt-to-GDP ratio in 2023 practically corresponds to the figure in the bill, although our projection suggests that the level of government debt may be somewhat lower at end-2023.

The 4.1 per cent forecast for economic growth next year in the macro path of the bill is higher than the range projection of the central bank. Growth prospects are significantly affected by the war and the ensuing sanction policies, which is also indicated by the wide dispersion of market analysts' growth expectations for both this year and next year. The projection of the Ministry of Finance expects the consumer price index to amount to 5.2 per cent in 2023, which falls short of the inflation band forecast by the MNB. Both the bill and the MNB project dynamic growth in the wage bill.

The budget bill complies with the debt rule outlined in the Fundamental Law, as the decline in the debt-to-GDP ratio is expected to exceed the required 0.1 percentage point. Nevertheless, the state of emergency introduced in view of the war situation in a neighbouring country allows exemption from the compliance with the provision. The degree of decrease in debt included in the bill complies with the provisions of the EU debt rule if the debt-to-GDP ratio declines in the coming years as described in the bill, at a satisfactory pace. The accrual-based balance of 3.5 per cent of GDP exceeds the Maastricht threshold, which is a part of both the Hungarian and EU legislation. However, in 2020, the institutions of the European Union temporarily suspended the application of sanctions related to the corrective fiscal rules, and the general escape clause remains in effect in 2023 as well. In line with that, pursuant to the amendment to the Stability Act, compliance with the provisions concerning the general government deficit and the medium-term budgetary objective is not required between 2021 and 2023.

The 4.5 per cent structural deficit indicated in the bill is higher than the requirement concerning the medium-term objective, but the degree of expected convergence to it has not been determined pursuant to the general escape clause, and thus compliance with the rules cannot be examined. The medium-term objective (MTO) framework stipulates that all Member States should reach the structural balance determined jointly with the European Commission or approximate it to a sufficient degree. The MTO for Hungary in 2023 is -1.0 per cent of GDP. According to the bill, in 2023 the structural balance will correspond to -4.5 per cent of GDP, which is higher than the requirement, but the expenditure benchmark that determines the adjustment path to achieving the medium-term objective was temporarily suspended in the past years. As the general escape clause will remain in effect in 2023 as well, and due to the exemption the two-year degree of the expected structural adjustment has not been defined either, compliance with the provisions concerning the medium-term objective cannot be examined.

2 General government balance

The bill defines the ESA deficit of the general government as 3.5 per cent of GDP in 2023, which represents declines of 2.4 percentage points compared to the 2022 statutory appropriation and 1.4 percentage points compared to this year's deficit target indicated in the Convergence Programme. The deficit stems almost completely from the cash-based deficit of the central sub-sector, the balance of local governments may be close to equilibrium in 2023, while the difference between the cash-based and accrual-based deficits contains a slight negative adjustment. Our forecast suggests that the cash-based deficit of the central sub-sector may be higher than the appropriation in the bill (Table 1). Our projection for the balance of local governments is also slightly less favourable than the expectation in the bill. At the same time, according to our forecast, in 2023 the ESA bridge containing statistical corrections may be much more favourable than the figure predicted in the bill, which offsets the difference stemming from the higher central cash-based deficit.

Table 1
ESA balance of the general government sector in 2023 (as a percentage of GDP)

	2023		
	Statutory appropriation	**MNB forecast**	**Difference**
1. Balance of the central sub-sector	-3.4	-3.9	-0.5
2. Balance of local governments	0.1	0.0	-0.1
3. Cash flow balance of central sub-sector and local governments (1+2)	**-3.3**	**-3.9**	**-0.6**
4. GFS-ESA difference	-0.2	0.4	0.6
5. ESA balance of the general government sector (3+4)	**-3.5**	**-3.5**	**0.0**

Source: 2023 budget bill, MNB projection

According to our forecast, the general government deficit may be 3.5 per cent of GDP in 2023, which equals the 3.5 per cent indicated in the bill. The cash-based deficit of the central sub-sector may exceed the appropriation in the bill by 0.5 per cent of GDP, which is mainly attributable to lower revenues from taxes on labour due to less favourable labour market assumptions. The tax and contribution revenues of the central sub-sector of the budget may fall short of the appropriation by more than HUF 80 billion, which is the result of somewhat higher corporate and consumption taxes as well as of tax and contribution revenues on labour that are expected to be significantly lower than the appropriation. According to our projection, revenues related to EU funds may be some HUF 100 billion lower than the figure in the bill. Budgetary expenditures are forecast to exceed the appropriation set forth in the bill by more than HUF 150 billion in total. Our forecast suggests that the expenditures related to EU programmes may be lower than the appropriation in the bill. At the same time, offsetting that, the value of pension expenditures, which exceeds the appropriation, points to a higher level of expenditure.

In 2023, reserves in the central sub-sector amount to HUF 1230 billion, i.e. 1.8 per cent of the nominal GDP indicated in the bill, with the reserves of the Utilities Protection Fund as one of the contributors. The central expenditure reserves of the newly set up Utilities Protection Fund amount to HUF 600 billion. In addition to that, further reserves comprise the HUF 70 billion reserve envelope created for the Energy Price Increase Compensation, which is part of the Utilities Protection Fund, the HUF 170 billion appropriation of the Extraordinary Government Measures, the Provisions of HUF 179 billion, the HUF 200 billion Investment Fund as well as other lower-value reserves.

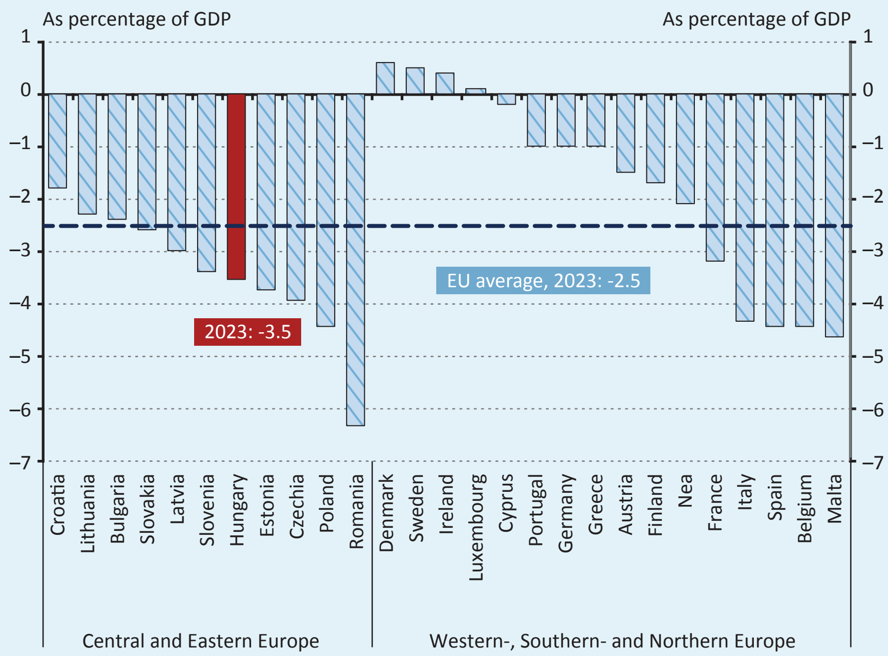
The cash-based balance of the local government sub-sector shows a surplus of HUF 67 billion in the budget bill. Our projection presumes a less favourable cash-based balance than the budget bill; the balance of the sub-sector is expected to be close to equilibrium in 2023.

According to the budget bill, the ESA bridge, which comprises **the accrual-based and other ESA adjustments**, contains a deficit increasing adjustment of HUF 137 billion for 2023. The ESA bridge estimated and applied by the MNB contains balance improving adjustment amounting to some HUF 260 billion. The difference of nearly HUF 400 billion between the forecasts is primarily attributable to the difference in the accrual-based adjustments of EU settlements, which may be caused by the difference between the expectations related to the carry-over of the 2014–2020 funds. The act is based on a negative ESA bridge item that exceeds even the positive adjustments related to the advance disbursements, thus assuming that a major portion of the cash-based revenues expected for 2023 are related to the subsequent settlement of the accounts already recognised as accrual-based revenue in the previous years. The different expectation related to the 2023 accrual-based adjustments offsets the difference existing in the cash-based deficit of the central sub-sector, and thus our projection for the ESA balance of the year under review is in line with the deficit target set forth in the act.

Pursuant to the budget bill, in 2023 the additional revenues related to additional growth are required to be spent on the reduction of the deficit and thus of public debt. Pursuant to the rule, if real growth exceeds 4.1 per cent, the deficit target must be reduced by an amount equalling the accrual-based annual tax and tax type revenue surplus originating from the higher than planned real growth, deducting from it the amount of pension premium that is in excess of the plan.

Hungary's deficit target of 3.5 per cent of GDP is nearly the same as the average of the CEE region, although it falls short of the 2.5 per cent EU average (Chart 1).

Chart 1
Government deficit forecast for 2023 in the EU



Note: Hungarian data is in line with the government target announced in the 2023 budget bill
Source: European Commission

3 Expected developments of government debt

According to our forecast, **the gross debt-to-GDP ratio of the general government** will decline from 76.6 per cent at end-2021 to 74.7 per cent in 2022, as a result of a decrease in deficit and a dynamic upswing in the economy. According to our forecast, in 2023 the government debt ratio will decline by 2.4 percentage points to 72.3 per cent.

Table 2
Developments in government debt (in HUF billions and as percentage of GDP)

	Statutory appropriation	MNB	Statutory appropriation	MNB
	HUF billions		as a percentage of GDP*	
1. 2022 initial government debt	46,551	46,490	76.1	74.7
2. 2023 cash-based deficit of the central budget	2,352	2,685	3.4	3.9
3. Other effects	1,607	885	2.3	1.3
4. 2023 expected government debt (sum of 1+2+3 in nominal terms)	50,510	50,060	73.8	72.3
5. Change in government debt-to-GDP ratio in 2023 (4-1)			**-2.3**	**-2.4**

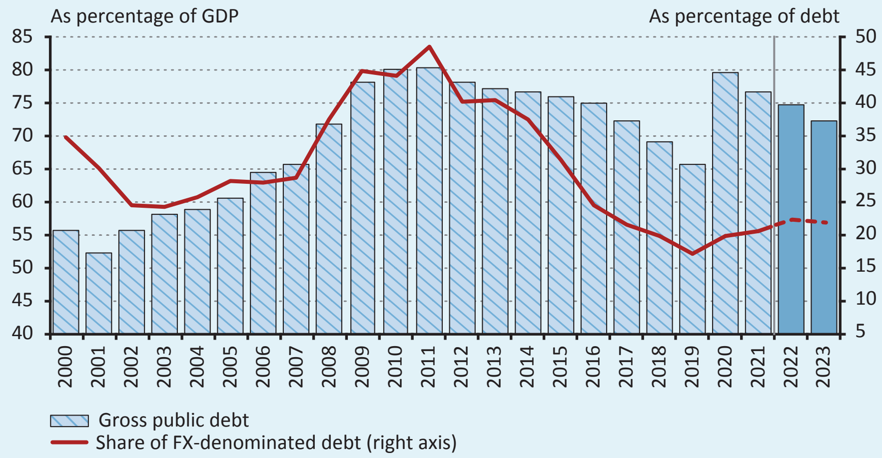
*Note: * The MNB and the Budget Act calculate with different nominal GDP. The sum of partial data may differ from the aggregated values due to rounding.*
Source: 2023 budget bill, MNB projection

The MNB's projection for nominal debt at end-2022 practically corresponds to the expectation of the bill, while it is somewhat lower for end-2023 than the projection in the bill. The higher end-2023 value presumed in the bill is mainly attributable to the higher debt issuance, which exceeds the budget deficit, whereas the ensuing difference is offset to some extent by the MNB's forecast for a higher cash-based balance of the central budget. The difference between the forecasts concerning the change in the gross government debt-to-GDP ratio is partly explained by the difference in the assumptions for nominal GDP.

The budget bill expects the nominal government debt to increase to a much greater degree than the deficit, i.e. by some HUF 1600 billion. The underlying reason is that for 2023 the budget bill assumes very significant financial reserves in excess of HUF 2000 billion at the end of the year, in view of the uncertainty perceived in the borrowing requirements outside the budget and in financing possibilities. The securities issued in order to increase these reserves increase gross nominal debt in addition to the deficit.

As a result of last year's FX bond issuances, the share of foreign currency within the debt of the central government debt rose to 20.6 per cent by end-2021. According to our forecast this ratio will be within the tolerance band of 10–25 per cent, which corresponds to the target of the Debt Management Agency. In view of this year's FX bond issuances, the share of foreign exchange within the central debt may increase further, before declining slightly, to 22 per cent in 2023. **Households' government securities holdings continued to increase during 2021,** and the demand for retail government securities may remain buoyant in the future as well. As a result, the ratio of domestic financing may continue to rise. **In 2021, the average term to maturity of the government debt rose to 6.8 years with the preference towards longer-term bonds,** and the average maturity is expected to increase in the coming years.

Chart 2
Expected developments of government debt



Source: MNB, ÁKK (Government Debt Management Agency)

4 Evaluation of the macroeconomic assumptions underlying the bill

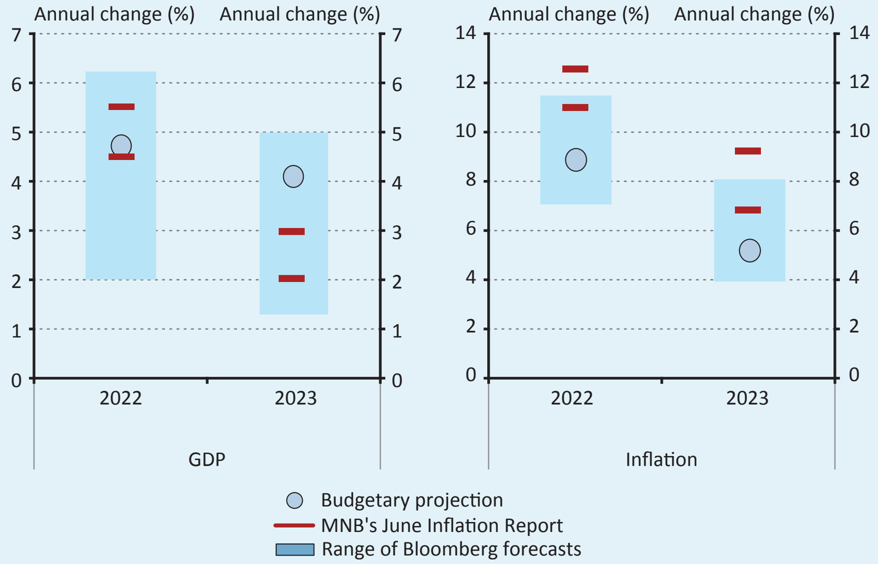
This year the growth expectation of the budget bill is within the band forecast by the MNB, while it is higher than that for next year. According to the macro path of the bill, the GDP may grow by 4.7 per cent in 2022 and by 4.1 per cent in 2023. The June Inflation Report of the MNB contains a forecast range; economic performance may expand by 4.5–5.5 per cent this year and by 2–3 per cent next year. Major uncertainty around the future developments in GDP is indicated by the wide range of market analysts' growth expectations (Chart 3).

This year, economic expansion is supported by the pick-up in domestic demand, but GDP growth in 2023 is surrounded by downside risks compared to the expectation of the budget bill. According to our forecast, domestic demand will be strong in the short run, and household consumption will be increased by the rise in wages and by government measures that expand households' income. Both projections expect dynamic growth in household consumption this year. Starting from next year, the growth rate of consumption will decline with the ceasing of the one-off income increasing measures. Compared to the budget bill, the forecast in the June Inflation Report expects a greater loss in momentum for both consumption and investment. According to the bill, the contribution of net exports to growth will be positive this year and next year as well, whereas the June Inflation Report expects a slower recovery of external markets and supply chains, and thus net exports restrain GDP expansion in 2022 (Table 3).

Both the bill and the MNB project dynamic growth in the wage bill. Wage growth in the fiscal macro path will remain double-digit in 2023 as well and will be above the band forecast by the MNB in both years. The growth in the number of employees in the whole economy will decelerate next year.

The bill expects inflation to be 8.9 per cent this year and 5.2 per cent in 2023, which represent lower annual price rises than the bands forecast by the MNB.

Chart 3
Comparison of GDP and inflation forecasts



Source: 2023 budget bill, MNB's Inflation Report (June 2022), Bloomberg (June 2022)

Table 3
Comparison of the macroeconomic forecasts (percentage change compared to the previous year)

	2021	2022			2023		
	Actual*	Budget	MNB	Difference	Budget	MNB	Difference
GDP	**7.1**	**4.7**	**4.5 – 5.5**	**(-0.2) – 0.8**	**4.1**	**2.0 – 3.0**	**(-2.1) – (-1.1)**
Consumption expenditure of households	4.6	6.9	8.4 – 8.7	1.5 – 1.8	5.0	0.6 – 1.4	(-4.4) – (-3.6)
Public consumption*	3.6	1.1	2.4 – 3.1	1.3 – 2.0	1.2	0.4 – 1.6	(-0.8) – 0.4
Gross fixed capital formation	5.9	2.7	3.7 – 4.8	1.0 – 2.1	4.2	(-0.9) – 1.8	(-5.1) – (-2.4)
Exports	10.3	3.8	4.8 – 5.7	1.0 – 1.9	5.9	5.0 – 6.9	(-0.9) – 1.0
Imports	8.7	3.4	6.0 – 6.9	2.6 – 3.5	5.5	2.7 – 4.6	(-2.8) – (-0.9)
GDP deflator	6.9	5.8	7.2	1.4	7.4	8.9	1.5
Inflation	**5.1**	**8.9**	**11.0 – 12.6**	**2.1 – 3.7**	**5.2**	**6.8 – 9.2**	**1.6 – 4.0**
Gross wage bill*	**10.3**	**18.5**	**17.4**	**-1.1**	**10.5**	**8.0**	**-2.5**
Gross average earnings	8.7	16.7	15.8 – 16.4	(-0.9) – (-0.3)	10.2	7.1 – 8.3	(-3.1) – (-1.9)
Number of employees	0.8	0.7	1.0 – 1.2	0.3 – 0.5	0.3	(-0.2) – 0.5	(-0.5) – 0.2

*Note: *Definition of public consumption and gross wage bill are different at the two institutions.*
Source: 2023 budget bill, MNB's Inflation Report (June 2022)

5 Detailed evaluation of the budget bill

5.1 PRIMARY REVENUES

According to our forecast, in 2023 **the primary revenues of the central sub-sector of the budget** may be HUF 180 billion lower in total than the appropriations in the bill (Table 4). Within that, tax and contribution revenues may fall HUF 84 billion short of the appropriations, most of which is related to the revenues from taxes and contributions on labour. The difference in the case of revenues from taxes on labour is primarily caused by the different assessments concerning labour market developments in 2023. This effect is offset by the fact that due to our higher forecast for nominal consumption expansion our expectations regarding consumption tax revenues are higher than the Budget Act, and we also expect more tax revenues from payments by economic organisations. Moreover, according to our forecast, the cash-based revenues related to EU funds may come in lower than the appropriation in the bill.

Payments by economic organisations may exceed the appropriation for 2023 by HUF 116 billion. Changes in revenues in 2023 will be greatly affected by fiscal consolidation steps in 2022 and 2023. Most of the measures are introduced during 2022 and will remain in place in 2023 as well.

Revenues from the **corporate income tax** may be HUF 31 billion higher than the relevant appropriation. The difference may originate from the macroeconomic developments: in 2023, nominal GDP, which is higher than the government estimate, may raise the tax base to a higher level than the one assumed by the Budget Act. This type of tax is affected by a measure as well that was announced in parallel with the submitting of the budget: according to the Budget Act, the transposition of the OECD's transfer pricing directives into Hungarian practice may result in an additional revenue of HUF 40 billion in 2023.

In the case of the **special tax of financial institutions** the revenue may be HUF 10 billion lower than the appropriation[1] in 2023. A new element introduced here is the surtax on interest income as well as on fee and commission income. Pursuant to the Budget Act, the additional revenue from this may amount to HUF 250 billion in 2023. The difference in the case of this type of tax is attributable to the slight difference between the estimates for the payments originating from the previous tax introduced in 2010 and paid on the basis of the adjusted balance sheet total.

The **revenues from the advertising tax** may exceed the appropriation by HUF 3 billion in 2023. In the case of this type of tax the 0 per cent tax rates introduced for the period between July 2019 and end-2022 will cease to have effect as of the end of the year. The upper rate will be reset to the previous 7.5 per cent starting from 1 January 2023 in line with the original, 2019 amendment to the law.

Revenues from the **itemised lump sum tax of small entrepreneurs** may be HUF 10 billion higher than the appropriation, due to the difference in forecasts regarding the 2022 revenues. In the case of this type of tax it is to be emphasised that the Budget Act does not assume any major changes in the rules in relation to this type of tax, only the projection for payments by payers was amended in line with the experiences of its introduction in 2021.

Payments from the **mining royalty** may exceed the appropriation also by HUF 10 billion in view of the higher energy prices compared to the assumptions of the Budget Act. One of the consolidation measures affecting energy producing taxpayers was the tripling of the mining royalty related to hydrocarbons, which was partly offset by the suspension of the correction mechanism related to the high energy prices (according to the original law, the relevant rates increase automatically by 3 percentage points each following the reaching of certain price levels). This may result in additional revenues of HUF 130 billion for the State Treasury.

[1] This appropriation is to be found under the title Payments by Financial Institutions within the Defence Fund.

The revenue from the **income tax on energy providers** may exceed the appropriation[2] by HUF 26 billion in 2023. Three measures increase the revenues in this row in 2022 and 2023. Firstly, the scope of taxpayers is expanded to include bioethanol and biofuel producers as well as sunflower seed oil and starch producers. The ministry expects additional revenues of HUF 30 billion from this. The second measure concerned is the tax on the oil price difference, where the 25 per cent tax on the profit from the difference between the prices of the Brent and Ural type crude oils may contribute some HUF 140 billion to the revenue side of the budget. It is uncertain, however, how long the significant difference between the prices of the two types of crude oil may exist. The surtax to be paid by those who leave the feed-in tariff/ renewable subsidy system (KÁT/METÁR) also needs to be mentioned here.

The **company car tax** will be 1.8–1.9 times higher on average, with the logic of the type of tax and the collection of the tax adapting to the motor vehicle tax, with more emphasis on the protection of the environment (the annual effect of the measure may amount to some HUF 40 billion). Revenues from the company car tax will be mostly recognised in the motor vehicle tax row as of 2023 and completely as of 2024.

Revenues from the **retail tax** may exceed the relevant appropriation by HUF 10 billion. In the case of this type of tax the difference may be attributable to the higher nominal consumption compared to the government's expectation. The progressive nature of the extent of the retail tax will strengthen in 2023: the tax rate will remain 0 per cent up to a net sales revenue of less than HUF 500 million, whereas the previous 0.1 per cent rate between HUF 500 million and HUF 30 billion increases to 0.15 per cent. Between HUF 30 billion and 100 billion the current 0.4 per cent rate changes to 1 per cent, while the tax rate above HUF 100 billion will rise from the present 2.7 per cent to 4.1 per cent. The ensuing revenue increasing effect may amount to HUF 70 billion in 2023.

Within **other centralised revenues** the 2023 appropriation for environmental product fees declines considerably, by HUF 25 billion compared to the 2022 appropriation. Although the budget bill indicates an expected measure, without knowing the details we have been unable to take into account its expected impact. Mostly this provides an explanation for our expectation of the centralised revenues to be HUF 26 billion higher than the relevant appropriation. The differences related to other tax types of economic organisations are justified by the different assessments of the economic developments.

The budget expects to collect HUF 7100 billion from **value added tax** on a cash basis in 2023-ban, while our forecast foresees a somewhat higher revenue of HUF 7159 billion as a result of higher nominal consumption assumptions. The appropriation for 2023 exceeds the one for 2022 by around HUF 1600 billion, but this year as well we expect the actual revenues to be significantly, i.e. some HUF 1200 billion higher.

[2] This appropriation is to be found under the title Payments by the Energy Sector within the Utilities Protection Fund.

Table 4
Revenues of the central sub-sector – comparison of the forecasts (HUF billions)

	2023		
	Statutory appropriation	**MNB forecast**	**Difference**
TAX AND CONTRIBUTION REVENUES OF THE CENTRAL SUB-SECTOR	**23,411**	**23,327**	**-84**
Payments by economic organisations	**3,016**	**3,132**	**116**
Corporate income tax	792	823	31
Special tax of financial institutions	338	327	-11
Advertising tax	15	18	3
Lump sum tax of small entrepreneurs	227	236	10
Small business tax	166	163	-3
Utility tax	53	54	1
Eco-tax	5	6	0
Mining royalty	240	250	10
Gambling tax	39	44	5
Other payments	12	12	0
Other centralized revenues	557	593	36
Income tax on energy providers	242	268	26
Company car tax	6	7	0
Retail tax	173	183	10
Rehabilitation contribution	150	149	-1
Consumption taxes	**9,248**	**9,309**	**60**
Value added tax	7,100	7,159	59
Excise duties	1,459	1,421	-38
Registration tax	19	22	3
Telecommunication tax	96	116	19
Financial transaction levy	324	356	32
Insurance tax	**180**	**173**	**-6**
Airline tax	30	30	0
Tourism development contribution	42	33	-9
Payments by households	**4,168**	**4,027**	**-141**
Personal income tax	3,734	3,562	-171
Duties, other taxes	261	292	30
Motor vehicle tax	173	173	0
Tax and contribution revenues of extra-budgetary funds	**462**	**457**	**-5**
Tax and contribution revenues of social security funds	**6,516**	**6,402**	**-114**
Social contribution tax and contributions	6,309	6,193	-116
Other contributions and taxes	208	210	2
REVENUES RELATED TO EU FUNDS	**2,090**	**1,988**	**-102**
OTHER REVENUES	**879**	**884**	**5**
Revenues on public property	**517**	**517**	**0**
Other revenues of the central budget	**239**	**239**	**0**
Other revenues of social security funds	**27**	**33**	**5**
Other revenues of extra-budgetary funds	**96**	**96**	**0**
TOTAL REVENUES	**26,379**	**26,199**	**-180**

Note: Partly consolidated data.
Source: 2023 budget bill, MNB

The budget foresees revenues from **excise duties** amounting to HUF 1459 billion in 2023, exceeding our forecast by HUF 38 billion. Revenues from excise duties are increasing by around HUF 90 billion in 2023 due to the changes already in force as of 1 July 2022: excise duties on energy, alcohol and tobacco products are rising, on the latter in order to comply with the minimum EU level. Within that, the tax on new tobacco product categories (heated tobacco products) accounting for one quarter of the market is also increased from HUF 15 to HUF 35 a piece, approaching the piece-price of cigarette.

The Budget Act foresees revenues from the **telecommunication tax** to amount to HUF 96 billion next year, whereas we expect HUF 19 billion higher revenues. The surtax concerning the telecommunication sector will bring additional revenues of some HUF 40 billion in 2023, in addition to this year's expected tax revenue in excess of HUF 75 billion. While until now the telecommunication tax was paid by phone service providers on the calls and the number of subscribers, the scope of enterprises paying the new type of surtax is wider, as it covers internet service providers as well. The rate of the telecommunication surtax is 0 per cent on the part of the net sales revenue not exceeding HUF 1 billion, 1 per cent on the part exceeding HUF 1 billion but not reaching HUF 50 billion, 3 per cent on the part above HUF 50 billion but not exceeding HUF 100 billion and 7 per cent on the part above HUF 100 billion.

The budget expects to collect HUF 180 billion from the **insurance tax** in 2023, which is HUF 6 billion more than our projection. With the insurance surtax the budget imposes an extra tax burden of around HUF 50 billion on insurers in addition to the current tax originally amounting to some HUF 120 billion. The revenues will go into the newly established Defence Fund. Next year, the surtax, which is to exist until end-2023, will be 2 per cent on the part of the **non-life premium income** not exceeding HUF 2 billion, 4 per cent on the part exceeding HUF 2 billion but not exceeding HUF 36 billion and 7 per cent on the part above HUF 36 billion, while in the case of the **premium income from life insurance** it is 1 per cent on the part not exceeding HUF 2 billion, 1.5 per cent on the part exceeding HUF 2 billion but not exceeding HUF 36 billion and 3 per cent on the part above HUF 36 billion.

According to the Budget Act, HUF 30 billion is expected on the revenue row **airline tax** in 2023. The departure tax, which is a new type of tax to be paid for each person leaving Hungary is HUF 3900 for those who fly to European countries and HUF 9750 for those going to other countries, and the taxpayer is the ground service provider, which may pass the tax burden on to the airlines.

Revenues from **tourism development contribution** may amount to HUF 42 billion pursuant to the 2023 budget, which exceeds our projection by HUF 9 billion due to the effect of the different revenue expectations for 2022. As of 2020, in addition to restaurants, the 4 per cent tax was extended to accommodation services as well, but there were no significant revenues on this tax revenue row in the past 2 years, as accommodation establishments and eateries were exempted from paying it until 31 December 2021.

According to the bill, next year's estimate for the **financial transaction levy** is HUF 324 billion, which is HUF 32 billion lower than our forecast. The difference is attributable to the lower 2022 base, which may be explained by the difference between macroeconomic assumptions. **Amendments to the financial transaction levy:** the HUF 6 thousand upper limit of tax payment on bank transfers rises to HUF 10 thousand, and – with an unchanged rate of 0.3 per cent – the government is extending it to securities transactions as well, except for the transactions performed by the Treasury and the Post Office.

According to the bill, next year's appropriation of **revenues from duties** amounts to HUF 261 billion, which is HUF 31 billion lower than our forecast. Firstly, the difference may be explained by the different macroeconomic assumptions, and secondly, our forecast expects a lower decline in revenues as a result of a measure introduced as of last year, i.e. the exemption from duty of the homes purchased using the Home Purchase Subsidy Scheme for Families (HPS).

According to our forecast, the revenue from **personal income tax** may be lower than the appropriation of HUF 3734 billion set forth in the bill. The difference may primarily stem from the difference between macroeconomic assumptions. At the same time, according to our estimate the revenue projection in the budget indicates higher dynamics than what would be justified by the macroeconomic forecast presented in the annex to the bill. The budget does not contain any new measure in connection with the personal income tax. Against this background, our projection for tax benefits practically corresponds to the expectation included in the bill.

Similarly to the personal income tax, the **tax and contribution revenues of social security and extra-budgetary funds** may fall short of the appropriation. According to our forecast, the revenues from the social security contribution and the tax revenues from social contribution may fall HUF 82 billion and some HUF 40 billion short of the appropriation, respectively. The difference is attributable to the different macroeconomic assumptions. Namely, compared to the bill, the MNB projects a roughly 2 percentage point lower wage and salary bill increase for 2023. The utilisation of job protection benefits in the budget bill exceeds our forecast by HUF 15–25 billion.

The fiscal consolidation steps directly affect the revenues of the social security and extra-budgetary funds in the case of two items. The public burden on **simplified employment** (odd jobs, seasonal work in agriculture, walk-on in the film industry) is increasing, and may result in additional revenues of some HUF 25 billion next year. Most of the alcoholic products ceased to be subject to the **public health product tax**, which will be offset in the case of these product groups by an increase in the excise duty in the future. The tax burden on several product groups affected by this type of tax is being transformed into a bracket system, and the lump-sum tax rate that was the general one until now and applies to the upper band as of July is increasing by some 30 per cent on average, and two new product groups (delicacy, pre-packaged sweet, salty pastry) will also be subject to the tax. These measures may result in additional revenues of around HUF 30–40 billion in total in 2023.

The appropriation concerning the **revenues from EU programmes** amounts to a total HUF 2,090 billion, of which more than HUF 860 billion is related to the 2014-2020 programmes. According to the bill, more than HUF 930 billion may be received from the 2021-2027 envelope, of which RRF funds may amount to nearly HUF 400 billion. The plan falls HUF 360 billion short of the expected value for 2022. According to our forecast, if agreement is reached in connection with the Recovery Plan, the operational programmes and the rule of law mechanism, the revenues may be close to the appropriation. The budget bill does not provide any details of its expectations regarding invoiced payments and the expected payment of advances, which fundamentally determine the level of cash-based revenues.

Within the **revenues related to the National Land Fund** the government expects revenues of HUF 300 billion from the selling of real estate. The planned amount of revenues from the selling of real properties is based on the transfer of ownership of 187 500 hectares of land in total – calculating with an average price of HUF 1.6 million per hectare.

Box 1
Fiscal measures to be introduced in 2022–2023

In the 2022–2023 fiscal years the government is implementing high-amount adjustments. The objective of the measures is to allow the achievement of the deficit targets of 4.9 per cent in 2022 and 3.5 per cent in 2023. In several cases the exact content of the measures is still being worked out, and not all the details of the technical conditions on their implementation are known yet. Based on preliminary indications, the announced measures and the information included in the 2023 budget bill, the share of revenue items may be 45 per cent this year and may be close to 40 per cent in 2023. Most of the revenue measures (some HUF 800 billion a year) are related to the surtaxes imposed on so-called 'extra profit', in addition to which the announcement contains further tax revenue measures as well amounting to around HUF 100–200 billion a year (Table 5). Most of the newly raised revenues will be placed in two new funds, the Utilities Protection and Defence Funds.

Table 5
The effect of revenue and expenditure measures on the budget in 2022 (as a percentage of GDP)

Measures	Budgetary effect in 2022
Revenue-side measures	**1.34%**
Special taxes on windfall profits	1.14%
Duties, taxes on company cars and public health taxes	0.15%
Formal sector widening and employability simplifying measures	0.05%
Expenditure-side measures	**1.7%**
Economising and efficiency increase at ministries, budgetary authorities, and government programs	1.0%
Rescheduling and preplanning of public investment projects	0.5%
Utilisation of revenues from feed-in tariffs (KÁT) in universal services	0.2%

Source: Ministry of Finance, 2023 budget bill

The measures affecting the revenue side in detail:

'Extra profit' surtaxes:

1. Payments by the banking sector:

a. **Surtax on interest gain**: credit institutions pay the new tax on their previous year's net interest income as well as fee and commission income. The tax rate in 2022 is 10 per cent and will be 8 per cent in 2023, to be paid by financial enterprises in two equal instalments this year and three equal instalments next year.

b. **Amendments to the financial transaction levy**: the HUF 6 thousand upper limit of tax payment on bank transfers rises to HUF 10 thousand, and – with a rate of 0.3 per cent – the government is extending it to securities transactions as well, except for the transactions performed by the Treasury and the Post Office. The budget strives to extend the effect of the tax onto foreign FinTech service providers as well.

2. Raising the insurance tax: Next year, the surtax, which is to exist until end-2023, will be 2 per cent on the part of the non-life premium income not exceeding HUF 2 billion, 4 per cent on the part exceeding HUF 2 billion but not exceeding HUF 36 billion and 7 per cent on the part above HUF 36 billion, while in the case of the premium income from life insurance it is 1 per cent on the part not exceeding HUF 2 billion, 1.5 per cent on the part exceeding HUF 2 billion but not exceeding HUF 36 billion and 3 per cent on the part above HUF 36 billion. The revenues will go into the newly established Defence Fund.

3. **Payments by energy companies**:

   a. **Raising the mining royalty**: compared to the current rate, the mining royalty will triple for the companies involved in hydrocarbon production (crude oil and natural gas), and the revenues will go to the Utilities Protection Fund.

   b. **Tax on the oil price difference**: the base of the tax is the difference between the Ural type crude originating from Russia and the world market price of oil, which difference provides profit for MOL, which refines the crude, and the tax rate is 25 per cent.

   c. **Extension of the income tax on energy providers**: the income tax on energy providers is extended to further actors and sectors: bioethanol and biofuel producers as well as starch producers.

4. **Raising the retail tax**: The structure of this type of tax remains unchanged in 2022, but the taxpayers are obliged to pay an additional amount corresponding to 80 per cent of the previous year's tax liability. In 2023, the base of this type of tax remains, but the progressive nature of the tax will strengthen: the tax rate will remain 0 per cent up to a net sales revenue of less than HUF 500 million, whereas between HUF 500 million and HUF 30 billion it increases to 0.15 per cent from the current 0.1 per cent. Between HUF 30 billion and HUF 100 billion the current 0.4 per cent rate changes to 1 per cent, while the tax rate above HUF 100 billion will rise from the present 2.7 per cent to 4.1 per cent.

5. **Raising the telecommunication tax** (previously called surtax on telecommunication companies): the existing tax is complemented; its base is the net sales revenue and not the previously reported data usage. While until now the telecommunication tax was paid by phone service providers on the calls and the number of subscribers, the scope of enterprises paying the new type of surtax is wider, as it covers internet service providers as well.

6. **Airline tax**: a new type of tax is the *departure tax*, i.e. the tax to be paid for each person leaving Hungary is HUF 3900 for those who fly to European countries and HUF 9750 for those going to other countries, and the taxpayer is the ground service provider, which may pass the tax burden on to the airlines.

7. **Pharmaceutical industry payments**: the base of the tax is the part of the social security subsidy resulting on the basis of the prescription turnover data of the given month and proportional to the producer price, on which the distributor has a 20 per cent payment obligation in the case of medicaments whose producer price does not exceed HUF 10 thousand and 28 per cent in the case of medicines with a producer price of more than HUF 10 thousand.

8. **Reintroduction of the advertising tax**: the previous suspension of this type of tax, i.e. the 0 per cent rate will cease to exist at end-2022 by law, and thus the tax will be imposed again as of next year, with a 7.5 per cent rate projected to the net sales revenue.

Other revenue measures:

- **Excise duty and PHPT (public health product tax) increases**: the tax burden on the product groups affected by the public health product tax increased significantly, partly because the tax was transformed into a bracket system and partly due to the raising of the lump-sum tax rate. In addition, the majority of the alcoholic products were taken out from the scope of the PHPT and became subject to excise duty instead, whose rate on alcohol, tobacco products and energy (natural gas, electricity) is increasing as of 1 July.

- **Raising the company car tax**: on average, the company car tax will be 1.8–1.9 times higher than the current level. The logic of this type of tax and its collection is adjusted to the motor vehicle tax, with more emphasis on the protection of the environment.

- **Valorisation of simplified employment**: the lump-sum tax burden on this type of employment (odd jobs, seasonal work in agriculture, walk-on in the film industry etc.) approximately doubles.

Table 6
Fiscal effect of the sectoral surtaxes in 2022 and 2023 (HUF billion)

Measures	Budgetary effect (bn HUF)	
	2022	2023
Special taxes for extra profit	**792**	**815**
1. Payments by the banking sector	**345**	**300**
1a. Special tax on interest gain	250	250
1b. Changes in the financial transaction levy	21	50
2. Insurance tax increase	**50**	**50**
3. Payments by energy companies	**300**	**300**
3a. Mining royalty increase	130	130
3b. Tax on oil price difference	140	140
3c. Extension of income tax on energy providers	30	30
4. Special retail tax increase	**60**	**60**
5. Telecommunication tax increase	**17**	**40**
6. Airline tax	**13**	**30**
7. Pharmaceutical contribution increase	**8**	**20**
8. Reintroduction of the advertising tax	**0**	**15**

Source: MNB estimate

Measures affecting the expenditure side:

In order to achieve the deficit targets of 4.9 per cent and 3.5 per cent of GDP in 2022 and 2023, respectively, the government also took measures that affect the expenditure side of the central budget[3]:

- **Saving and increase of efficiency in ministries, at budgetary institutions and government programmes:** through the reduction of chapter expenditures of the central budget the government intends to save 10 per cent, i.e. HUF 581 billion in 2022 and HUF 500 billion in 2023.

- **Postponing and cancelling public investment:** in order to revise them, the government suspends public investment projects (other than the ones that are already being implemented), and it intends to save HUF 1150 billion in total in 2022 and 2023 as the related budgetary effect.

- **Streamlining the utility price reduction:** in order to avoid infringements, the utility price reduction rules are amended, and accordingly only retail consumers are entitled to universal electric energy and natural gas services.

Nevertheless, the details of expenditure side measures were not yet completely known when the report was prepared. Pursuant to the Government Resolution, the ministries concerned must elaborate the detailed proposals for 2022 by 1 July 2022.

[3] Government Resolution 1281/2022 (VI. 4.) on fiscal measures necessary in order to protect the utility price reduction and achieve national defence objectives at the time of the war going on in Hungary's neighbourhood

5.2 PRIMARY EXPENDITURES

According to our forecast, the primary expenditures of the central sub-system of the budget may exceed the appropriation set forth in the bill by HUF 77 billion, and net cash-based interest expenditures may also be HUF 76 billion higher than that (Table 8). The majority of expenditure appropriations are in line with our forecast. Differences pointing to higher total expenditures are identified in the case of provisions paid from social security funds and in the case of net interest expenditures, which is partly offset by the lower net own expenditures of central budgetary organisations and chapters as well as the disbursements related to EU funding projected by the MNB compared to the appropriations set forth in the bill.

Compared to the 2022 statutory appropriation, **the expenditures of special and normative subsidies** for next year are HUF 635 billion higher. This high-amount growth is attributable to the expenditures of the 35-year concession created to maintain and expand the highways and the regrouping of the availability fee of the M5 and M6 motorways from chapters. In addition, the budgetary support of companies that provide public transport services will increase dynamically in 2023, because the raised amount of subsidy also contains the compensation of the rise in energy prices.

According to our forecast, net expenditures of budgetary institutions may fall short of the amount in the budget bill by HUF 36 billion, which is primarily explained by the usual carry-over between years of the capital expenditures. The appropriations of personal expenditures in the bill contain the wage measures concerning 2022 as a base, and the budget provides significant pay rises to the employees of various institutions in 2023 as well. In the spirit of commitment to fiscal consolidation, the government decided to reduce investment expenditures significantly. Accordingly, the government sector's investment expenditures may decline to some 4.5 per cent of GDP in 2023. According to the bill, consumption expenditures of the general government contain adjustment amounting to hundreds of billions of forints, and most of this saving is in the institutional and professional chapter-managed expenditures.

In the case of the Start public work scheme, for 2023 we expect expenditures to be HUF 16 billion higher than the appropriation of HUF 110 billion set forth in the bill. The reason for the difference is that we do not expect the number of participants in the scheme to decline compared to the base period.

The 2023 appropriation of housing subsidies is nearly HUF 110 billion higher than the 2022 appropriation. The significant increase may be attributable to the extension of and upswing of the programmes that were to end originally in 2022 (rural HPS, home renovation subsidy). The budget bill foresees expenditures to amount to a total HUF 175 billion in the case of the **prenatal baby support**. The 2022 budget appropriation expects expenditures to amount to a mere HUF 92 billion in relation to the prenatal baby support, while the target for next year is nearly twice as much. The major increase is partly attributable to the extension of the programme for next year that had been announced to last until end-2022, and in view of the rising yield environment – as a result of maintaining the consistently low interest rates for households – the state provides higher interest rate subsidy for the newly disbursed loans. The expenditures set forth in the bill fall significantly, i.e. some HUF 35 billion short of our forecast, which may primarily be explained by the higher yield environment.

According to our forecast, in 2023 the expenditures of the social security funds may exceed their amount allocated in the bill by HUF 323 billion. The difference mainly stems from the difference between the macroeconomic assumptions that serve as a basis of our forecast and the government's expectations.

The expenditure appropriated to the debit of the Health Insurance Fund is nearly HUF 84 billion lower than our projection. The primary reason for the difference is that in our forecast the rise in price level, which exceeds the expectations of the bill, appears in the expenditures of medical and preventive care and pharmaceutical subsidies, which is partly offset by the presumed lower recourse to cash benefits.

The expenditure appropriation for medical and preventive care amounts to HUF 2254 billion, which is HUF 71 billion less than our forecast. At the same time, the bill expects additional expenditures amounting to HUF 87 billion compared to the 2022 government expectation, which is mainly attributable to the pay rises of doctors working at health institutions maintained by the state and local governments as well as to the further raising of wage subsidies for family doctors and dentists that work as entrepreneurs. A further explanation is that in the case of the financing of high-value medicaments and the material expenditures related to in kind provisions we expect an increase in expenditures that follows the rise in inflation. At the same time, it is a positive risk that, depending on adequate leeway, the budget may also cover these expenditures from regrouping across appropriations.

Gross expenditures on **drug subsidies** amount to HUF 472 billion in the 2023 budget bill, which is HUF 22 billion higher than this year's appropriation. Nevertheless, our projection suggests that the expenditure on drug subsidies may be higher by a further HUF 16 billion.

The amount of the appropriations for cash benefits is HUF 705 billion, which slightly exceeds our forecast, by nearly HUF 28 billion. The appropriation for expenditures on **sick pay** is HUF 182 billion for 2023, which is HUF 39 billion higher than the 2022 level. In view of the fading of the pandemic, in the case of the sick pay expenditure we expect the number of people applying for this benefit to decline, and thus our projection is some HUF 12 billion lower compared to the bill. The appropriation for **childcare fee and adoption allowance** is HUF 318 billion for 2023, which is nearly HUF 52 billion higher than the expenditure level planned for 2022, which is mostly explained by the strong growth in gross average earnings. The bill foresees HUF 154 billion to be spent on **infant care allowance**, which exceeds the appropriation for 2022 by nearly HUF 27 billion. Our projection expects the childcare fee and the infant care allowance to be HUF 9 billion and nearly HUF 8 billion lower, respectively, which is primarily attributable to our assumption of a lower number of beneficiaries.

According to the bill, the appropriation for **disability and rehabilitation benefits** amounts to HUF 339 billion, which is HUF 37 billion higher than the 2022 budget. Our forecast is based on HUF 19 billion higher expenditures in 2023, which is primarily explained by the indexation necessary as a result of the higher inflation expectations, which is only partly offset by the decline in the number of those entitled to these benefits.

The expenditure planned in the bill for the Pension Fund is HUF 4903 billion for 2023. The **retirement provisions** paid from the Fund account for most of the expenditures, for which the appropriation in the 2023 bill is HUF 4895 billion in total, exceeding the level planned on the rows of the 2022 budget by HUF 732 billion. Our forecast presumes that the expenditures will be HUF 238 billion higher compared to the bill. The main underlying reason for the difference is that the macroeconomic assumptions used in our projection expect higher inflation for both 2022 and 2023: in addition to the total 8.9 per cent pension increase planned by the budget, according to our forecast a further 2.9 per cent adjustment may be needed in 2022, the carry-over effects of which will prevail in the following years as well. The middle of the band of the macroeconomic path that serves as a basis for our forecast assumes an annual average 8 per cent price level increase in 2023, which justifies a 2.8 percentage point higher pension increase compared to the budget. The bill anticipates HUF 8 billion for the **other expenditures** of the Pension Fund, which corresponds to our forecast.

The 2023 appropriation for the largest pension expenditure item, **old-age pensions over the retirement age**, amounts to HUF 3,664 billion, whereas our forecast includes HUF 204 billion higher expenditure. The difference is mainly explained by the higher inflation path of the macroeconomic outlook that is the basis of our forecast, while our expectations for the other developments that affect the expenditures, such as the increase in the number of beneficiaries, and for the effect of the increase in gross average earnings in the case of newly determined pensions correspond to the bill in terms of their magnitude.

Women are entitled to receive pension below the age limit after a 40-year eligibility period. The 2023 bill expects expenditures to amount to HUF 372 billion, which is HUF 20 billion less than our projection. We continue to expect an increase in the number of women entitled to receive pension below the age limit, taking into account that in parallel with raising the retirement age of old-age pension to 65 years more and more women may reach 40 years of service before reaching the retirement age for old-age pension.

In the case of **retirement provisions to relatives** the 2023 bill appropriates for expenditures of HUF 462 billion, which is HUF 21 billion lower than the MNB's forecast. Nearly the whole amount of the difference is on the rows of widows' pensions, and is related to our forecast for a higher price level increase compared to the macroeconomic expectations that serve as a basis for the budget.

The 2023 budget bill presumes the disbursement of **pension premiums** amounting to HUF 25 billion on the basis of the 4.1 per cent real growth indicated in the macroeconomic outlook that serves as a basis for planning the budget. By contrast, the middle of the band of the macroeconomic forecast that is consistent with the MNB's June 2022 Inflation Report expects the real GDP to expand by 2.5 per cent in 2023, which falls short of the higher than 3.5 per cent level necessary for the disbursement of the pension premium.

Table 7
Comparison of the 2023 appropriation and our projection for expenditures on pension and pension-type benefits (HUF billions)

	2023		
	Appropriation	**MNB forecast**	**Difference**
I. Pensions	**4,895**	**5,133**	**238**
1. Old-age pensions	4,036	4,260	224
1.1 Old-age pensions over the retirement age	3,664	3,868	204
1.2 Early retirement benefit for women	372	392	20
2. Retirement provision to relatives	462	483	21
3. One-time subsidy	1	1	0
4. Provision for pension premium	25	0	-25
5. 13th-month pension	372	390	18
II. Early retirement benefits	**109**	**122**	**13**
III. Disability and rehabilitation benefits	**339**	**358**	**19**
Total pensions and pension-like benefits	**5,343**	**5,613**	**270**

Source: 2023 budget bill, MNB

The 2023 bill contains an appropriation of HUF 372 billion for the disbursement of **13th month pensions**, which is HUF 18 billion less than the amount in our forecast due to the higher inflation expectations that serve as a basis for our estimate. The effect of pension increases appears in the 13th month pension as well, which is disbursed in a full one-month amount as of 2022, as the rises during the year following the February disbursement prevail with retroactive effect for the amount of that as well.

Accordingly, pursuant to the 2023 budget bill, the appropriations belonging to the expenditures of the **pensions and pension-like benefits** (retirement provisions, early retirement benefits, disability and rehabilitation benefits) amount to a total HUF 5343 billion. According to our forecast, the budget may spend HUF 5613 billion on the above provisions in 2023 (Table 7), which exceeds the government target by HUF 270 billion.

Table 8
Expenditures of the central sub-sector – comparison of the forecasts (HUF billions)

	2023		
	Statutory appropriation	MNB forecast	Difference
PRIMARY EXPENDITURE ITEMS	**26,968**	**27,045**	**77**
Special and normative subsidies	**1,114**	**1,114**	**0**
Support to the public media	**110**	**110**	**0**
Social policy fare subsidy	**105**	**105**	**0**
Housing grants	**491**	**491**	**0**
National Family and Social Policy Fund	**724**	**737**	**13**
Net expenditures of central budgetary organisations and chapters	**7,904**	**7,868**	**-36**
Expenditures related to EU transfers	**3,408**	**3,180**	**-228**
Support to local governments	**969**	**969**	**0**
Contribution to the EU budget	**604**	**604**	**0**
Central reserves	**1,230**	**1,230**	**0**
Support to social self-organisations	**6**	**6**	**0**
Expenditures on public property	**700**	**700**	**0**
Other expenditures	**363**	**363**	**0**
Expenditures of extra-budgetary funds	**548**	**554**	**6**
NEF – Passive allowances	116	116	0
NEF – Active allowances	110	126	16
Other expenditures	323	313	-10
Expenditures of social security funds	**8,691**	**9,013**	**323**
PIF - Pensions	4,895	5,133	238
HIF - Disability and rehabilitation benefits	339	358	19
HIF - Cash benefits	705	677	-28
HIF - Medical and preventive care	2,254	2,325	71
HIF - Net expenditures of the drug budget	354	369	16
Other expenditures	144	151	7
NET INTEREST EXPENDITURES	**1,763**	**1,839**	**76**
TOTAL EXPENDITURES	**28,731**	**28,884**	**153**
BALANCE	**-2,352**	**-2,685**	**-333**

Note: Partly consolidated data.
Source: 2023 budget bill, MNB

Our forecast suggests that the expenditures of EU programmes may be lower in 2023 than the appropriation. In terms of expenditures, mainly the HUF 2100 billion target for the 2021–2027 cycle is surrounded by risks, as for the significant disbursements related to the new cycle to materialise in 2023 the approval of the Partnership Agreement, the Recovery Plan and the individual operational programmes by the European Commission and the European Council is required. The expenditures of EU programmes are planned by the government to amount to HUF 3408 billion in 2023, which exceeds the amount expected for 2022 by more than HUF 800 billion. The expenditures in connection with the cohesion, rural development and other programmes related to the 2014–2020 cycle may amount to some HUF 680 billion according to the plan, whereas the expenditures related to the 2021–2027 programmes may exceed HUF 2100 billion, of which the payment to be disbursed within the framework of the Recovery and Resilience Facility (RRF) amounts to HUF 590 billion. Taking into account the difference between expenditure and revenue appropriations, significant advance payments are presumed for 2023 as well, but their planned amount is not indicated in the bill.

5.3 INTEREST BALANCE

According to our projection, the gross accrual-based interest expenditure as a proportion of GDP may be in line with the statutory appropriation and may amount to 3.2 per cent in 2023. The rise in interest expenditures is mainly caused by the increase in the yield environment. At the same time, as a result of the more favourable maturity structure of the debt and the high share of fixed-rate debt elements, the effect of the increase in yields appears more slowly than experienced before.

The budgetary appropriation for **net cash-based interest expenditures** is HUF 76 billion lower than our projection. Our forecast expects higher gross interest expenditures, while it is lower than the appropriation in the case of interest revenues. In addition to the yield increase that has taken place since the preparation of the bill, the differences may be attributable to the differences in the projections for the underlying issuance structure.

Chart 4
Development of gross interest expenditures in accrual term (as a percentage of GDP)

Source: Eurostat, MNB forecast

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 will decrease in 2023; accordingly the bill satisfies the debt rule requirement specified in the Fundamental Law. Pursuant to the Fundamental Law, as long as the debt ratio exceeds 50 per cent of GDP, the government debt ratio has to decline by 0.1 percentage points, which is projected to occur in 2023 according to both forecasts. According to the bill, following the 76.1 per cent expected for the end of this year, the government debt rate will decrease by 2.3 percentage points to 73.8 per cent in the next year. Based on the MNB forecast, the debt-to-GDP ratio may decline by 2.4 percentage points in 2023. Exemption from compliance with the debt rule of the Fundamental Law is provided by the state of emergency introduced in view of the armed conflict and war situation in the neighbouring country, as pursuant to the Fundamental Law, in times of special legal order it is possible to deviate from the rule to the extent necessary for easing the consequences caused by the circumstances that triggered the special legal order.

6.2 THE 3-PER CENT DEFICIT RULE OF THE STABILITY ACT

The budget balance expected for 2023 would not comply with the deficit rule of the Stability Act, but at the same time exemption from the requirement is allowed by the transitional provision of the law related to the state of emergency, based on which it is not necessary to comply with the requirement between 2021 and 2023. Article 3/A (2) b) of Act CXCIV of 2011 on the Economic Stability of Hungary provides that the general government deficit shall not exceed 3 per cent of GDP. According to the budget bill, in 2023 the deficit will correspond to 3.5 per cent of GDP, which would not comply with the deficit target set forth in the Stability Act. Exemption from compliance with the rule is allowed by the transitional provision of the Stability Act, pursuant to which the rule does not have to be applied in the fiscal years between 2021 and 2023.

6.3 THE DEBT RULE OF THE STABILITY ACT

The debt ratio foreseen in the 2023 budget bill is in line with the debt formula specified in the Stability Act. According to the provision, the year-end value of the government debt indicator has to be determined in a way that the annual decline in the debt-to-GDP ratio must reach at least 0.1 percentage point, while the EU rules regarding the reduction of public debt are complied with. The European debt rule states that the Member States' government debt ratio must not exceed 60 per cent of GDP, or if it does, the debt ratio must be reduced by a satisfactory pace. The appropriate decrease in the debt is defined by the one-twentieth rule, according to which the debt ratio should be reduced by one twentieth of the part that exceeds 60 per cent on average over three years.

Based on its own forecast, the European Union uses three types of methodologies (forward-looking, backward-looking and cyclically adjusted) to calculate the degree of the change in the government debt ratio, and it is sufficient to comply only with one of them. The EU debt rule calculated using the forward-looking and backward-looking methods are expected to be complied with, provided that the decline in debt that is forecast in the bill takes place. At the same time, it is important to emphasise that the date of phasing out the general escape clause that partly and temporarily suspends the **application of EU rules was postponed by the European Commission to after 2023**.

6.4 REQUIREMENT PERTAINING TO THE STRUCTURAL BALANCE OF THE GENERAL GOVERNMENT

The 4.5-per cent structural deficit in the budget bill does not fulfil the medium-term budgetary objective. At the same time, the Hungarian and EU rules that require it have also been suspended until end-2023. Article 3/A (2) a) of Act CXCIV of 2011 on the Economic Stability of Hungary provides that the balance of the government sector must be determined in a way that is in line with the achievement of the medium-term budgetary objective (MTO). The Hungarian MTO in 2023 represents a structural balance equalling -1 per cent of GDP. The structural balance is the cyclically adjusted government balance net of one-off and other temporary items. The 2023 budget bill assigns a -4.5 per cent structural balance to the accrual-based balance of -3.5 per cent of GDP. In addition to the negative output gap, which improves the structural balance, the bill contains a high-amount, one-off temporary revenue item, which is mostly related to the surtaxes, which amount to 1 per cent of GDP, and to a lesser extent to the selling of state-owned land. The 4.5 per cent structural deficit would not achieve the medium-term budgetary objective, but **the transitional provision of the Stability Act provides exemption from the rule regarding the medium-term objective as well between 2021 and 2023.**

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

In 2020, by activating the general escape clause, EU institutions partly and temporarily suspended the application of the EU fiscal rules, and it will remain in place in 2023 as well. Under the clause, Member States are exempt from the sanctions applied in the case of breaching the rules of the corrective arm, but at the same time the European Commission continues to examine the compliance with the rules in the EDP reports, which are still prepared. If the fiscal rules entered into force again, of the requirements belonging to the corrective arm of the EU fiscal framework the budget bill would probably comply with the Maastricht criterion (following a comprehensive assessment, which takes into account all the relevant circumstances), and the degree of debt reduction would meet the requirement.

The **Maastricht 3-per cent deficit** criterion defines that the accrual-based deficit of the Member States must not exceed 3 per cent of GDP. In itself, the deficit target of 3.5 per cent of GDP indicated in the budget bill would not meet the requirement but taking all the relevant circumstances into account (the general government deficit would decline to an adequate degree approaching the 3 per cent criterion or would exceed that only to a small degree) in all likelihood the rule may still be complied with.

The **EU debt rule** states that the Member States' gross, consolidated government debt ratio calculated at face value must not exceed 60 per cent of GDP, and in case it does, the debt ratio must be diminishing at a satisfactory pace. 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 average over three years. Pursuant to the bill, in 2023 the government debt-to-GDP ratio will decline by 2.3 percentage points compared to this year, while the MNB expects a decrease of 2.4 percentage points, which would be in line with the requirements of the rule if they were effective.

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

The structural deficit target foreseen in the bill would not comply with the requirements concerning the medium-term objective. At the same time, the activation of the general escape clause suspended not only the application of the preventive rules but also their examination.

The framework related to the **medium-term budgetary objective** (MTO) provides that Member States should achieve the structural balance designated jointly with the European Commission or converge towards it on the designated adjustment path to a sufficient degree. Hungary's MTO for the coming year is -1.0 per cent of GDP. According to the bill, in 2023 the structural balance will correspond to -4.5 per cent of GDP, and thus - as in the previous years - the deficit on the structural balance will be higher than the medium-term objective. Nevertheless, compliance with the rule is temporarily not examined by the European Commission while the general escape clause is in effect.

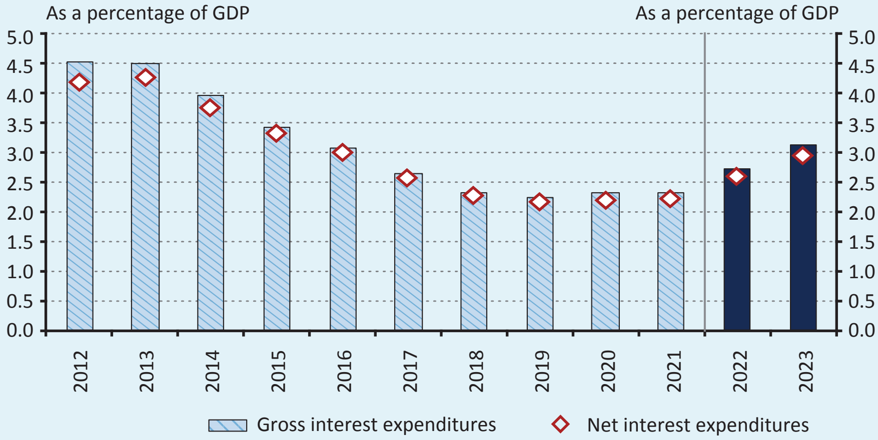
The EU **expenditure benchmark** enters into force if the requirement related to the MTO is not complied with, and it is intended to ensure convergence to the medium-term objective. According to the benchmark, compared to the previous year, the general government's net primary expenditures may increase by no more than the potential long term GDP growth rate, unless the increasing expenditures are offset by other, discretionary revenue measures. Considering that the rule has been suspended due to the effect of the general escape clause, and the European Commission did not determine the two-year degree of structural adjustment expected by the adjustment path, the expenditure rule for Hungary has not been defined, and thus compliance with the latter also cannot be assessed.

7 Special topic

7.1 DEVELOPMENTS IN GOVERNMENT INTEREST EXPENDITURES

In the seven-year period between 2013 and 2019, gross interest expenditure of the budget declined from 4.5 per cent of GDP to 2.2 per cent (Chart 5). In that period, Hungary's annual interest expenditure as a percentage of GDP declined to nearly one half, which was a major contributor to the decrease in the government debt ratio and the improvement in the budget balance. Hungary's interest savings exceeded 9 per cent of GDP in this period.

Chart 5
Development of government interest expenditures in accrual term

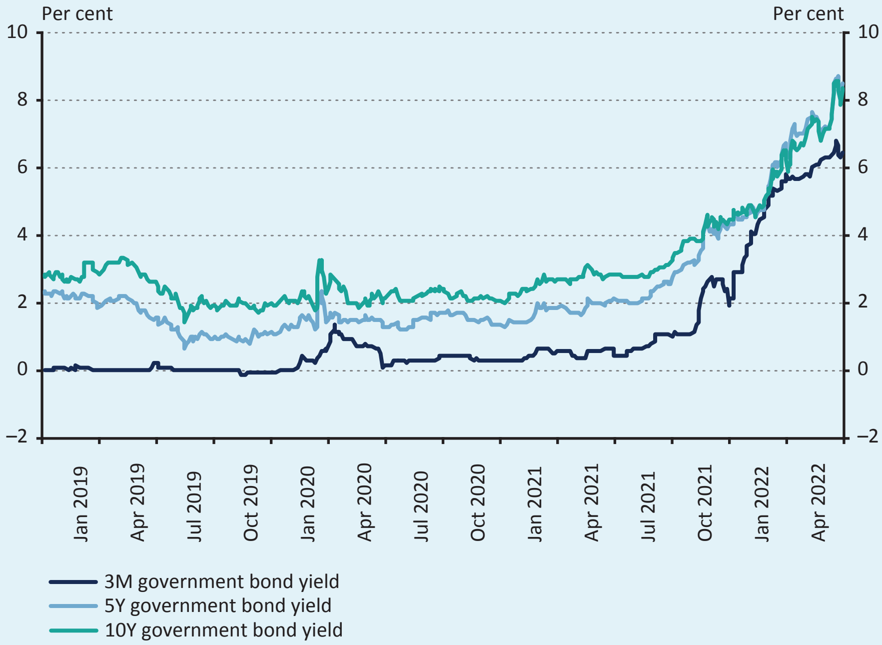


Source: Eurostat, MNB forecast

Following a steady decline since 2011, the gross government debt-to-GDP ratio was around 14 percentage points up in 2020 as a result of the coronavirus crisis. After the temporary increase, in view of the major GDP growth, the declining budget deficit and the decrease in the high-level liquid reserves, in 2021 the government debt ratio took a declining path again, which is expected to continue in the coming years as well.

The increase in government debt in 2020 broke the downward trend of government interest expenditures, whereas looking ahead the rise in yields is resulting in an increase in interest expenditures. Government securities yields have been increasing since end-June 2021. Prior to the closing of our analysis, since the beginning of the year short-term yields and long-term benchmark government securities yields had increased by some 350–450 basis points and 360–430 basis points, respectively (Chart 6). An upward shift and flattening of the yield curve have been observed since the middle of last year.

Chart 6
Development of government bond yields

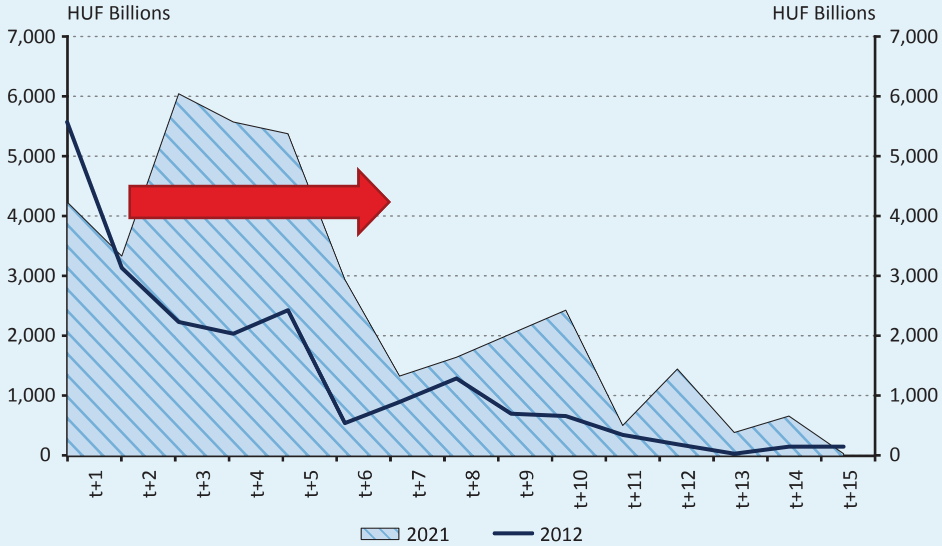


Source: ÁKK (Government Debt Management Agency)

Pursuant to the budget bill, government interest expenditure may rise to 3.2 per cent by 2023, and our forecast also contains a similar increase. The outlook of the Convergence Programme expects increases in interest expenditures in 2022 and 2023, followed by a decline in interest expenditures as of 2025. According to the forecast of the Convergence Programme, yields may be between 6–7 per cent between 2022 and 2026, reaching their peak in 2023: short-term yields may reach 6.6 per cent, while long-term yields may rise to 7.0 per cent. Following that, the Convergence Programme foresees a gradual decline and a level of 6.0–6.3 per cent in 2026.

The expected increase in the yield environment appears more slowly in the interest expenditures because the lengthening of government debt restrains the repricing to some extent, and interest expenditures as a percentage of GDP may rise moderately in the future as a result of dynamic economic growth. The rise in yields contributes to the growth in interest payment, but as a result of the lengthening of the maturity of government debt in recent years (Chart 7), only around one fifth of the government debt originates from new issuance in 2022, while the lower interests typical of the past years have to be paid for the debt elements that have not been renewed. The average term to maturity of government debt increased by more than 1 year in 2021, which is the highest rise across EU member countries. The higher ratio of fixed-rate debt elements in the debt portfolio also points to a decline in the pace of repricing. Economic growth partly offsets the increase in interest expenditures in the case of expenditures as a proportion of GDP. At the same time, in view of the rising government interest expenditures, looking ahead **a more favourable primary balance is needed in order to achieve the Maastricht deficit criterion.**

Chart 7
Maturity profile of the central government debt in 2012 and 2021



Source: ÁKK (Government Debt Management Agency)

Charles Robert

(1308 – 1342)

King Charles I. was one 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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