Speech

for the general discussion of Hungary's 2015 central budget bill

19th November 2014

Dear National Assembly,

Mr. Speaker,

Pursuant to the authorisation of the Fundamental Law of Hungary the Fiscal Council, as a **supporting body** of the legislative work of the National Assembly, in the course of the **preparation of the bill** of the central budget shall examine the grounding of the bill. We are right in the middle of this process. Now, prior to the final voting on the bill, the Council shall watch the observance of the **government debt rule.** With respect I wish to notice that we are going to see this in the final phase, in December.

The Council delivered its opinion on the draft bill of the 2015 central budget of Hungary (henceforward: the Draft) that had been forwarded on 20th October 2014 by the minister for national economy to the Council. In preparing its Opinion, the Council was building on the findings of the State Audit Office of Hungary and the Central Bank of Hungary, while used the forecasts of various analysing institutes (these forecasts had been introduced also at a conference organised for this purpose) and resorted to the analyses and projections of independent experts and standard international organisations.

The Council formulated its Opinion concerning the Draft for the government at its meeting held on 27th October 2014, and forwarded it to the Ministry for National Economy that was the submitting organisation. At the same time the FC made the Opinion public.

At the beginning of the general debate, pursuant to the authorisation of the Council, hereby I wish to share with the House the brief content of the Opinion, focusing on the implementation of the targeted deficit and the government debt rule. Naturally, I also wish to deal with the issue as to what extent does the submitted bill take into consideration the Opinion of the Council.

Ladies and Gentlemen of the House,

First let me address the Draft budget bill submitted to the Council. I also wish to say some words concerning the response of the government to the Council's Opinion.

First of all, let's talk about **the expected implementation of the 2014 budget act,** as the basis of the plans for 2015.

According to the Council's judgement the gaining strength of the economic growth in 2014 – that even surpassed the planned measure – boosted the certainty of the budgetary revenues and expenditures.

At the same time, and maintaining its half-year evaluation on the state of the execution of the budget, the Council expects losses as regards specific payments of economic enterprises, VAT and excise tax.

The VAT shortfall is related to the low inflation. The shortfall however will be compensated by the expected surpluses of the personal income tax, the social contribution tax and the excise revenues. The not using of the Country Protection Fund and the mid-year introduction of blockings also serve the security of observing the targeted deficit goal.

In its Opinion the Council considered it important to emphasise that when determining the basis for the 2015 budget appropriations, the planning process validly assumed the expected realisation of the 2014 budget.

Coming to the **2015 budget bill,** as regards the authenticity and feasibility of the draft budget bill, the Council did not have such fundamental objections that would have justified the indication of non-concurrence.

Here, I should mention that between the **Draft** the Council formulated its opinion on, and the **Bill** in front of you, **there are barely any differences**, regarding the major amounts and indicators.

Accordingly, most of the findings of the Council as regards the Draft remain justified and correct also in respect of the bill.

As to the introduced **macroeconomic course,** taking into consideration the Convergence Programme of Hungary for the period of 2014-2017, the available professional papers and projections, respectively those commissioned by the Council, the FC reached the conclusion that the macroeconomic goals – and within them the 2, 5 percent growth – are feasible if the favourable external and internal conditions persist.

In 2015 domestic growth shall be led primarily by the strengthening of domestic demand as we can count on a more favourable boom in the business sector and investments are likely to be more intensive. The improving performance also shall support a higher wage growth and this shall have a positive effect on public finance revenues.

The high level of household indebtedness remains a slowing factor regarding the dynamics of household expenditures. At the same time, derecognition of foreign currency loans (the accounting between banks and debtors, exchanging foreign currency loans to loans in forints) could lead to a greater extent of household consumption. The Funding for Growth programme of the Central Bank of Hungary has been playing an important role in putting the economy on a sustainable growth track.

It’s rather likely that the economic development shall get somewhat slower next year. Compared to the strong 2014 basis it should be difficult to produce similar results – even if the favourable conditions persist.

This is especially true regarding the growth of investments where one of the energising factors was the huge expansion of the utilisation of EU funds.

Considering that the EU funds available until 2015 are given, a paradox situation might develop that the greater portion of utilisation in year 2014 might improve the growth potential of the economy in 2014 but might worsen that in year 2015.

Ladies and Gentlemen of the House,

The Bill determined the **targeted deficit of the governmental sector – calculated by EU methodology –** in 2, 4 percent of the GDP in 2015.

This means that – in case of the realisation of the planned economic growth - there is a significant gap for the deficit compared to the 3 percent upper limit stipulated by the public finance act.

At the same time, in its Opinion, the Council pointed out that the setting up of the **Country Protection Fund** worth of more than the HUF 40 billion mentioned in the Draft would deserve consideration. The Council reached this conclusion by analysing the macroeconomic processes, respectively comparing the forecasts (evaluations) of the commissioned analysing institutions, to thus ensure the secure realisation of the 2, 4 percent targeted deficit.

As regards the analysis of the targeted deficit, the Council did not find any explanations for the Draft mentioning that **the debt of the local governmental subsystem** shall grow from HUF 40 billion of the previous year to HUF 200 billion while the respective deficit would be merely HUF 15 billion.

According to the Council's judgement the growth of the current deficit by HUF 160 billion shall implicate a growth higher than HUF 15 billion, even considering that part of the borrowed loans shall not be used by the local governments immediately, respectively that there will be local governments that shall have a positive balance of their 2015 budget.

Apart from initiating the repeated review of this relation, in order to avoid a new wave of local governmental indebtedness, the Council emphasised the necessity that the Government should contribute only to such borrowings the repayment of which is ensured from local governmental resources.

This was the first time that the bill contained a reference to **structural deficit.** This indicator stands for the balance cleaned off from the cyclical effects of the economy and of individual items that are related to the mid-range orientation of fiscal policy. The Council did not get enough information from the Draft thus was unable to evaluate the formulated 2015 target. The Council deemed it justified that the Government should present the respective calculations.

Due to lack of specific decisions presented in the Draft and being rather laconic, when analysing the **revenues,** the Council found that the major tax and excise revenues of the budget – considering the expected realisation in 2014, the GDP growth in 2015, the expansion of the inflation, employment and consuming, as well as the additional results of measures intended to assist the whitening of the economy – were mostly realistic.

In case of consumption taxes – mostly in case of VAT – however the Council expects some risks, due to the unreasonable expectations as regards the results of the battle against black economy and respective tax evasions.

Namely, the effects of the measures laying the foundation for growing VAT revenues in 2015, like the introduction of Trade Control beginning with 1st January 2015, connecting online cash machines, the tightening of the frequency of tax declarations and the expansion of the number of small taxpayers, can be measured only later.

The downward indicating risks surrounding the inflation might also mitigate specific revenues of the budget but this can be counterbalanced by the bigger than planned growth of consumption.

The fact that the tax system shall change only to a little extent in 2015 should mitigate the risks of the realisation of tax revenues and via this, strengthen the stability of the budget.

In order to preserve the accountability of the tax system the Council emphasised the importance of further improvement of tax collection and preventing the emergence of receivables – instead of the expansion of taxes.

In its Opinion the Council also underlined that within **revenues related to public assets,** the Draft set very high „other selling and utilisation revenues" (HUF 169 billion) however, the exact contents of this was not clear and thus can be regarded as a significant uncertainty from the aspect of statistical accounting.

In the Council's opinion it might create a problem if – in case of revenue loss – the expenditures of the Investment Fund related to revenues cannot be stopped mid-year. In case of investments this has a high probability.

Here I should mention a problem that I consider worth of attention and that is related to encouraging private investments. I think that, beside the favourable effects, we should not disregard the fact that supports attracting investments tie down budgetary resources to a growing extent. Namely, comparing these to the respective proceeds we shall not get a positive balance all the time.

Here we should also note that from the justification of the Draft the Council could not get familiar with the contents of the measures behind significant expenditure changes and this made the evaluation of the **expenditure** appropriations very difficult.

Additionally, I should note that the response of the government that these can be learned in detail from the chapter tomes did not help the FC’s work in delivering its opinion.

Namely, the House also received these tomes only very recently. Hence the Council formulated its opinion based on the projection of the tendencies of the past years and the already well known measures.

In light of this, the cutbacks of the National Fund for Family and Social Policy and the recently launched processes (the downturn in the number of those receiving entitlements prior to reaching retirement age, the mitigation of the number of children entitled to family allowance due to the higher number of exiting age groups) were in harmony.

On the basis of the realisation of year 2014 it is also realistic that the 2015 budget envisaged a lower amount for housing support than in 2014.

At the same time uncertainties of expenditures appear as regards public education where – being aware of the measures introduced so far – it would be expected that expenditures related to staff grew to a greater extent.

Honourable National Assembly,

The government debt indicator planned according to the stipulations of the Stability Act is foreseen to decrease from the 76, 3 percent at the end of 2014 to 75, 4 percent, thus the **government debt rule** shall be observed in 2015.

The improvement of the indicator by 0, 9 percent means that the debt rule shall be met even if the GDP or the budget deficit turns out to be slightly less favourable than stipulated by the bill – due to the risks pointed out by the Council.

At the same time, in order to meet the requirements stipulated by the new EU law (i.e. the obligation to reduce annually by at least one twentieth portion of the part of the government debt over 60 percent as of 2016 and until then, improving the structural balance) and for the sake of the development of the country, the measured downsizing of government debt is equally important.

This is why the Council recommended the Government to elaborate a **debt reduction programme** until at least 2022 – i.e. the termination of the ongoing EU budgetary cycle – by also taking into consideration the results of economic development built on EU funds.

On the whole, apart from the favourable processes the Council identified several risks concerning the implementation of the targeted deficit and the government debt rule. The Council deems the macroeconomic course and – within that – the 2, 5 percent economic growth attainable if the external conditions, the international boom and investors' trust shall not worsen significantly. Additionally, if the influx of EU funds related to the 2007 – 2013 period shall be in harmony with the Bill.

As to the revenue side, the Council identified risk concerning the trend of tax bases related to consumption and the selling of public assets.

Ladies and Gentlemen of the House,

The **response of the government** to the Council's Opinion this time was more detailed than before. This document is public and available for everybody and can be found at the end of the main tome of the Bill. Because of this, I'm reflecting to it this time only briefly.

First of all, I wish to note that we consider the changes of the appropriations in the Government's response as a gesture.

Without describing the risks that they'd also expected, the Government raised the **Country Protection Fund**

appropriation by HUF 20 billion to HUF 60 billion. At the same time they indicated that by making this step the targeted deficit – calculated by EU methodology – can be maintained even in case the economic growth shall be lower by 0, 4 percent than planned.

At the same time they raised the VAT appropriation compared to the Draft. As the FC had labelled the original appropriation overstretched, this step shall increase the chance of loss of revenue.

The Government also **increased the deficit of the local government subsystem** – from HUF 15 billion to HUF 25 billion. By this step, to some extent, they granted the argument of the Council that it is questionable whether the HUF 15 billion deficit planned in this sector can be maintained in case of the increase of the debt by HUF 160 billion.

At the same time they noticed that the debt amounting to HUF 200 billion calculated this way was rather a theoretical maximum instead of a concrete forecast.

Perhaps the opinion of the Council according to what, **instead of the expansion of taxes,** it would be justified to focus on preventing the development of receivables and the improving of the efficiency of tax collection, contributed to the withdrawal of the original intention to expand the telecom tax to the internet service.

Additionally, for future consideration, I should mention that the widening of tax bases might increase the costs of taxing and, occasionally, it could be problematic from social and social political aspects by making tax collection more and more expensive and increasing the risk of tax losses.

Despite their explicit commitment to maintain the targeted deficit and to reduce government debt, the Government did not accept the Council's recommendation to elaborate a mid-range **government debt decreasing programme.** The explanation was that the existing EU and domestic regulations offer adequate security to continuously mitigate the debt.

Due to the laconic nature of the Draft, the Council was not in the position to pass judgement on the feasibility of the **structural debt.** In the general justification of the Bill the Government presented in details that the debt for 2015 would be 1, 6 percent and - according to the mid-range budgetary target of the Convergence Programme - this is already in harmony with the 1, 7 percent GDP proportionate value.

Honourable Members of the House,

Finally, I would like to take the opportunity and express my thanks to the minister for national economy and his staff for having extensively assisted our job and for making it possible – amid the not too easy planning conditions – that the Council prepared its Opinion by doing substantive work.

I wish to thank also the staffs of the State Audit Office of Hungary, the Central Bank of Hungary, the Secretariat of the FC, the commissioned analysing institutions and individual economic actors for having supported the many-sided and thorough foundation of the Council’s Opinion by their alternative macroeconomic model-calculations, sensitivity examinations, independently from the governmental forecasts.

Thank you for your attention. I wish you a good job for the debate of the central budget bill and the discussion of the amendments that shall serve the purpose of the development of the country.