Resolution No. 3/2015.04.14.
of the Fiscal Council

OPINION OF THE FISCAL COUNCIL

on the draft Bill concerning the amendment of Act C of 2014 on the 2015 central budget of Hungary

I

Antecedents, legal basis and publicity of the preparation of the Opinion

On 9th of April 2015 the Fiscal Council (hereinafter: the Council or FC) received the electronic version of the draft Bill on the amendment of the 2015 central budget Act that had been discussed and approved at the 8th of April 2015 meeting of the Government. The same document was also sent as an attachment to the hard copy letter of the Ministry for National Economy under file number NMG/5227/9/2015, seeking the Opinion of the Council.

In harmony with Indent (2) Article 44 of the Fundamental Law of Hungary and § 24 of Act CXCIV of 2011 on the Economic Stability of Hungary (hereinafter: Stability Act), the Council shall deliver its Opinion on the draft Bill of the central budget Bill, the amendments changing the revenue or expenditure totals of the central budget, those increasing the extent of the budget deficit also included. In its Opinion the Council can make comments and, in case it has fundamental objections as regards the authenticity or the execution of the draft Bill, it shall express its non-concurrence.

In its Opinion no. 7/2014.12.10. on the uniform budget Bill T/1974/561. the Council found that „the GDP-proportioned extent of government debt expected by the end of year 2015 shall very likely be in harmony with the decreasing stipulation of Indent (5) Article 36 of the Fundamental Law” and, according to the stipulation of the ‚Stability Act the measure of government debt planned for 31st December 2015 is in harmony with the budgetary processes planned for 2015.

In the justification of the Council's Opinion the FC called the attention also to circumstances endangering the implementation – even by favourable macroeconomic and public finance processes – (like the effects of the moderate growth of the economic performance of the EU, the fact that the geo-political tensions might also spill over, the consequences of the EU sanctions against Russia, etc.). Thus the Council recommended tight budgetary management to promote the observance of the targeted deficit and the putting across of the government debt rule.

According to the motion the expenditure total of the central budget would increase by HUF 61 billion while the revenue total would increase by HUF 46 billion. In harmony with this the cash flow deficit of the central budget would increase by HUF 15 billion. The draft forwarded to the Council with the purpose of obtaining the FC's Opinion, proposes increases in the expenditure side of the central budget in the following major items:

- generates cover (HUF 15 billion) for the state, in cooperation with the European Bank of Reconstruction and Development, to obtain 15 % minority ownership interest in the Hungarian subsidiary of Erste Bank;
- creates an appropriation to support settlements in 2015 that had not participated in debt consolidations, in the frame of a four-year priority development programme, primarily by regrouping chapter resources available for this purpose; on the other hand by ensuring excess resources worth of HUF 3, 7 billion;
- the draft Bill proposes establishing the cover for the participation of Hungary in the Kurdistan project by increasing the budget of the Hungarian Army by HUF 10 billion;
- creates resources for the 2015 phase of the Liget Budapest project, the increasing of the appropriations dedicated to support the employment of disabled persons, the stepping-up of priority road constructions and the ensuring continuous provisions for the chimney-sweep industry, in the value of HUF 28 billion.

The draft Bill contains a proposal that shall not increase the cash-flow expenditures, to take over the accumulated debt of BKV Zrt (Budapest Community Transport Inc.) worth of HUF 52 billion and thus stabilizing the financial situation of the Budapest community transport in the long run. The final expiration of the credits of the corporation renewed in 2012 by the underlying guarantee of the state is due in 2015; thus it became necessary to take steps regarding the future management of the debt. As the takeover of the debts shall happen by burdening the debt of the central budget, it shall not concern the current budget.

Apart from increasing expenditures, the draft shall increase the cash-flow interest revenue appropriations amounting to HUF 41, 5 billion.[1]

Beyond the above the draft contains procedural and methodological actions supporting the law, together with some technological proposals regarding the calculation of extra wages due to the rating procedure of teachers, the calculation of the support for people assisting directly the teaching jobs, etc.

As regards the contents of the draft Bill the Council summarised and made public its Opinion as follows:

II

The Opinion of the Council

At its meeting held on 14th of April 2015, the Council formulated the following uniform Opinion on the draft amendment of Act C of 2014 about the 2015 central budget of Hungary:

1. As regards the authenticity and feasibility of the amendment of the revenue and expenditures sides of the budget, the Council has no such fundamental objections that would indicate the necessity of expressing its non-concurrence with the document

[1] Cash flow interest revenue stands for the interest revenues arising in the central budget in the course of debt management. Its major sources are interests realised from treasury deposits as well as the accumulated interest and premium gained from Treasury bond auctions (in case of issuing bonds at a rate higher than the nominal value).

presented with the purpose of formulating an Opinion on. The increase of expenditures described in the draft document is justified due to the decisions of the National Assembly and the Government.

2. According to the Council’s opinion, by the end of 2015 the GDP-proportionate gross government debt – calculated at constant exchange rate – is expected to decrease, compared to the previous year thus, the government debt rule shall be observed.

3. Despite the higher expenditures the Council is on the opinion that the targeted 2, 4 percent, GDP-proportionate deficit is feasible, although the risks might grow somewhat, primarily because the feasibility of the planned revenues from selling state assets might be affected by the possible unfavourable downturn of external conditions. The new measures shall increase the deficit however, this might be balanced by the more favourable balance of interests and – to a certain degree – the Country Protection Fund.

4. The Council deems it justified to point out that – especially due to the possibility of the unfavourable downturn of external conditions – even by the favourable macroeconomic and public finance processes of this year so far, further disciplined economic management is necessary to ensure the targeted public finance deficit and the safe implementation of the government debt rule.

III

Justification

The Council did not meet such objectionable regulations in the draft Bill that would have justified the indication of non-concurrence regarding the submitted document.

When formulating its Opinion the Council considered the favourable macroeconomic and public finance processes of the first quarter of 2015 (production, consumption, increasing exports, employment and lower public finance deficit compared to the previous years, etc.) as well as the effect of the above factors on the feasibility of the targeted deficit and the government debt rule.

The Ministry for National Economy prepared some calculations for the Council related to the document submitted for seeking the Opinion of the FC. These calculations illustrated the government debt and cash flow public finance deficit expected for year 2015.
The recommended changes of the draft Bill shall affect the cash flow balance, the deficit and government debt calculated by EU methodology to different extent.

- Taking into consideration that the taking over of the BKV debt shall not involve budgetary expenditure, the cash flow deficit would increase by HUF 15 billion.
- However, the ESA deficit calculated by EU methodology would increase by a greater extent, i.e. by HUF 52 billion. Two items are behind the change of the ESA balance compared to the cash-flow. On one hand, the taking over of the BKV debts shall increase the deficit calculated by EU methodology because BKV is a company that does not belong to the government sector. On the other hand, according to the EU methodology, acquiring minority ownership in Erste Bank does not qualify as expenditure, thus it shall not affect the deficit. All in all, the ESA deficit might grow by 0, 15 percent of the GDP as a consequence of the planned changes.
- The change in the cash flow deficit and the taking over of the debt would increase government debt by approximately HUF 67 billion, i.e. by 0, 2 percent of the GDP.

At the time of the acceptance of the 2015 central budget Act it contained a 0, 9 percent decrease of the debt indicator, according to the Stability Act. Based on the processes of the first quarter of 2015 this seems to be feasible. According to the Council’s judgement, even by the effect of the recently submitted measures amounting to 0, 2 percent increase of the debt; the government debt decreasing stipulation concerning the GDP-proportionate government debt, prescribed by the Fundamental Law, is feasible. As regards the trend of the debt the dynamic increase of revenues in the first three months of the year, especially the VAT trend and the expected dynamics of the GDP[2] are favourable.

According to the Opinion of the Fiscal Council the increasing of the interest revenues' appropriation is justified. The interest rate appropriations have been topped considerably in the past two years, primarily thanks to the securities' rate premiums put down as interest revenues of emission auctions in a low yield environment. The Council deems it justified to note that contrary to the cash flow appropriation, in the ESA-statistics calculated by EU methodology, the effect of low yields shall appear in the decreasing interest expenditures and not in the increase of interest revenues, when compared to the plans of the budget act. The expected decrease of expenditures roughly equals with the increase of the cash flow revenues, thus the balance shall improve to a similar degree in both approaches.

Consequently, as a whole, the changes in amount included in the draft Bill shall increase the cash flow deficit of the central budget by HUF 15 billion and by approximately HUF 50 billion (0, 15 percent of the GDP) the deficit calculated by EU methodology. This would make the realisation of the targeted ESA balance (2, 4 percent) difficult. According to the Council's judgement, on the basis of the data of the first quarter of year 2015 this target could be met only if the trend of the revenues shall turn out as expected and the Government shall follow the practice of keeping strict control over the expenditures, especially with regards to the possible unfavourable downturn of external conditions. The fact that the Country Protection Fund (0, 1 percent of the GDP, i.e. HUF 30 billion) remains available for the correction of the budgetary processes also in the future, shall assist the implementation of the targeted deficit.

The other remaining recommendations of the draft Bill concerned the interpretation of the specific stipulations of the act and the changes and clarifications assisting the execution of the bill. As these have no substantive influence on the feasibility of the targeted deficit and the

[2] Nominal GDP: GDP calculated at current price, the trend of what is determined by the growth of economic performance calculated at constant price on the one hand and the change of the price level of the added value, on the other hand.

enforcement of the government debt rule, the Council did not find it necessary to examine these recommendations.

Budapest, 14th of April 2015

Kovács Árpád Matolcsy György