# THREE-YEAR OUTLOOK OF THE FISCAL COUNCIL ON THE MACROECONOMY AND BUDGETARY DEVELOPMENTS

**24 FEBRUARY 2025**

# CONTENTS

## INTRODUCTION[1]

The Fiscal Council (hereinafter referred to as: the Council, FC) has the fundamental task of monitoring compliance with the debt rule. Until 2024, the Council's work was dominated by studies on the time horizon of the years under review, in preparation for decisions on the current annual budgets.[2] Starting from 2014, the medium-term outlooks appeared in various decision-making research materials as a response to the observations of the European Commission (hereinafter referred to as: Commission) on the functioning of the Fiscal Council. These have assisted the Council's work at expert level, but have not been the subject of a specific decision.[3]

On the other hand, while the economy was on a predictable path until 2020, the Council's work was dominated by an annual approach. With the emergence of new types of crises - such as COVID, the Russian-Ukrainian war, the energy crisis and turbulent global developments - and the subsequent period of fundamental economic changes, the Council's professional approach changed by 2022-2023. As part of this change, and to help implement and comply with the Stability Law, the Council produced a three-year outlook in January 2024, the first of its kind.[4] In April 2024, the European Parliament and the European Council adopted a regulation on the economic governance of the EU (see 'Framework paper: Reforming the EU's fiscal rules'), which created a new situation. This year, the Fiscal Council is already taking this into account when preparing its outlook for the next three years (2025-2027) on macroeconomic and budgetary developments and the positive or negative risks identified for compliance with the debt rule.

In this, the Council relies mainly on the analyses of the model calculations of the State Audit Office of Hungary and the National Bank of Hungary, which are already available to it, or have been prepared specifically for this purpose, and on the decision-preparatory analyses commissioned from independent research institutes to complement them. This broad professional base provides an adequate basis for the Council to make meaningful judgements from an independent fiscal perspective in this fundamentally uncertain, multi-factored and new

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[1] Staff of the SAO and the MNB - under the guidance of Chief Economist Gyula Pulay and Managing Director Gergely Baksay, respectively - as well as experts from the Secretariat of the Fiscal Council - Dániel Csomós, Dr. Tünde Gergics, András Botond Bősze and Dr. Ildikó Taksz - participated in the preparation of the document. The document took into account the information available until 21 February 2025.

2 See in part the European Commission's "Hungary's 2013 National Reform Programme" and the "Council opinion on Hungary's convergence programme for 2012-2016" (European Commission, 2013).

3 Transparency is also ensured by the fact that the short, medium and longer-term outlooks, sustainability studies and analyses related to the biannual monitoring of the implementation of the current budget law are available on the Fiscal Council's website under Documents/Research.

[4] See the analysis entitled "The Fiscal Council's three-year outlook on macroeconomic and budgetary developments", discussed and adopted by the Fiscal Council at its meeting of 5 January 2024.

environment, both to help medium-term budgetary planning and to understand and manage the uncertainties ahead.

The expected budgetary developments and their risks are assessed on the basis of the scenario for 2025-2027 adopted by the Government. This includes an assessment of the new challenges for fiscal policy posed by the fiscal consolidation outlined in this scenario, compared to the developments in 2019-2024. Second, we look at the internal consistency of the scenario and its macroeconomic implications, also in the light of other public documents reflecting the Government's medium-term objectives. The Outlook could not take into account the budgetary impact of the measures announced on 22 February 2025 without knowing the detailed regulatory plans.

Last year, the assessment was based on Hungary's Convergence Programme for the period 2023-2027, which was prepared by the Government on the basis of the EU legislation in force at the time and submitted to the competent EU institutions in April 2023. Since then, EU legislation has changed. In April 2024, the European Parliament and the Council decided in a regulation on the obligation to prepare a national medium-term budgetary structural plan. The Medium-Term Fiscal-Structural Plan (hereinafter referred to as: MTFSP or the Plan), prepared by the Government and subsequently amended, was approved by the Commission of the European Union in January 2025 and by the Council of the European Union in February 2025. Thus, the Fiscal Council takes as the starting point for the three-year outlook 2025 the document entitled "Hungary's Medium-Term Fiscal-Structural Plan 2024" prepared by the Government and the European Commission's "European Commission's assessment of Hungary's medium-term fiscal-structural plan" published on 16 January 2025, taking into account the recommendation of the Council of the European Union on the approval of Hungary's national medium-term fiscal-structural plan.

The focus of our analysis is on the commitments in this Plan, mainly on the deficit-to-GDP ratio and on government debt and net nationally financed primary expenditure (net expenditure). We examine the challenges and risks to the achievement of these commitments in the light of trends in recent years.

We consider the commitments in the Plan as given and do not qualify them. The Plan is interpreted as a scenario demonstrating that, under the committed restraint in net primary expenditure, Hungary would meet the conditions for exiting the excessive deficit procedure (i.e. the budget deficit would fall below 3.0% of GDP and the government debt would be on a declining path) by the end of 2026, even under the growth path considered most likely by the Commission. Consequently, a more favorable growth path than that foreseen in the previous

government projections provides room for a larger reduction in the debt ratio and/or a reduction in the centralization rate.

The commitments made in the Plan cover the period 2025-2028 (adjustment period), but our analysis looks three years out to 2027. Net nationally financed primary expenditure is assessed from 2021 onwards, as the Plan includes data back to that year. By contrast, the trends in the fiscal balance, interest expenditure and government debt are analyzed from 2019, the year before the COVID pandemic, in order to present as fully as possible, the impact of the shocks that have occurred since then on the fiscal balance.

In addition to the resources, it is important to define the principles that the Council follows when drafting the document. The outlook does not aim to analyze the social and political context, distribution policy and quality of service, but is primarily concerned with the need to achieve financial and budgetary balance. There are, of course, social risks that put pressure on the budget. However, in the independent fiscal institutions, including the Council, redistributive issues (distributive policy) in line with the government's internal budgetary priorities have so far only arisen when the Council has perceived a threat to financial stability and balance at the level of the national economy. The preparation of this document has also followed this principle.

As before, the first chapter of the Fiscal Council's Triennial Outlook examines the international environment, the growth prospects of the global economy, the situation and volatility of world trade and the shifts within it, the place and role of Europe and the European Union in the global economic and political transition, and the new challenges facing Hungary. The second chapter describes the evolution of macroeconomic developments in Hungary, their strengths and weaknesses, in particular since the COVID crisis, and presents the prospects for the three-year horizon. The third chapter analyses public finance and budgetary developments, including an overview of expected developments in revenues, expenditure and deficit. The fourth chapter draws attention to trends and developments over the next three years, with a particular focus on the risks to compliance with the debt rule. The final, fifth chapter of the analysis draws attention to three specific areas of these risks: developments in public and competitive sector wages, risks to pensions and wages, and the impact of the expected decline in public investment.

# SUMMARY

## Economic growth expected to accelerate

The years of the 2020 decade so far have been marked by a series of global crises. The pandemic, the Russian-Ukrainian war, the energy crisis and the global inflationary surge have created challenges not seen for decades or a century. Economic problems affecting the whole world have also led to multiple simultaneous crises in our country in the early 2020s. In 2022, after a rapid recovery from the pandemic, a duality in economic trends emerged with the rise in inflation and the rebalancing, leading to a stalling of growth. The main causes of the slowdown in economic growth were inflation, which eroded the purchasing power of incomes, a fall in external demand due to structural problems in the European economy, and a decline in economic confidence.

Looking ahead, the Hungarian economy could pick up again from 2025, but the growth projected in the 2025 Budget Law is subject to downside risks and the global economic environment is more uncertain than it was in the previous decade. Hungary is particularly exposed to global and European supply chains, so in addition to a possible return of past disruptions, the weakness of the German automotive industry also poses a risk to the industrial and export outlooks. External demand is expected by most analysts to begin to pick up in the second half of 2025, with a parallel pick-up in domestic exports, but this could become really dynamic in 2026-2027 as new capacity gradually comes on stream. Improving consumer and business confidence will be a critical factor for domestic demand growth this year. In the coming years, household consumption can only grow at a really dynamic pace if consumer confidence is boosted alongside rising real wages. An improvement in the outlook for the future for businesses and households, and the expected progress of large capacity creation and expansion projects, could lead to a renewed increase in investment activity. The upturn in domestic demand could continue in 2026-2027.

In the first years of the 2020s, global inflation will return to levels not seen since the 1970s, driven by supply-demand frictions following the COVID epidemic, the energy crisis and the Russian-Ukrainian war. The rapid rise in price levels spilled over to Hungary, followed by rapid disinflation. In the last third of last year, the pace of price increases accelerated again, with the result that inflation could average over 4 per cent per year in 2025, exceeding the forecast of the Budget Law. Rising inflation, based on the experience of recent years, has negative effects on economic growth, fiscal developments and economic confidence, making the return to price stability a precondition for sustainable growth and fiscal consolidation.

In the coming years, the main driver of the decline in the budget deficit could be a reduction in government interest expenditure, while the primary balance excluding interest expenditure is close to balance over the whole horizon. Hungary's revised medium-term fiscal structural plan expects higher interest expenditure than in the original plan, while there are positive risks to the evolution of government interest payments compared to the revised plan.

However, to achieve sustainable growth, a shift from the previous extensive growth model to an intensive model based on qualitative factors is essential. Productivity improvements must be put at the heart of growth. This step is essential because the employment expansion, which was a key underpinning of growth in the 2010s, is increasingly facing demographic constraints. The labour market is expected to remain tight in the 2020s, as the population decline will mainly affect the group with the highest employment rate (25-54 year olds). As a result, demand may outstrip supply in most areas, leading to only a slight increase in employment in the short to medium term between 2025 and 2027. A tight labour market could lead to faster wage growth, supported by the announced minimum wage agreement.

The EU's budgetary rules have undergone significant changes. The cornerstone of the changes, which took effect from 30 April 2024, is the national medium-term structural fiscal plan for a sustainable reduction in the debt ratio, which Hungary originally submitted in early November 2024. A new revised plan was subsequently submitted and received a positive opinion from the European Commission and the Council of the European Union in January 2025. The new plan caps net expenditure growth at 4.3 percent in 2025.

In this new fiscal rulebook, the potential growth rate of the economy is a priority. In the view of the Fiscal Council, the potential growth rate of around 1.5-1.7% assumed by the European Commission does not accurately reflect the Hungarian economy's capacity to grow. While quantitative growth factors may indeed be constrained, the relatively low domestic capital intensity and productivity still leave room for qualitative growth. Even without the increase in hours worked, the Hungarian economy would have achieved potential GDP growth of 2.5 percent in the second half of the last decade, which the FC believes is still sustainable thanks to identifiable margins in capital and productivity factors, and other international organizations (IMF, OECD) also forecast growth capacity above 2 percent.

According to preliminary estimates, gross public debt as a share of GDP could rise to 73.6% at the end of 2024. The increase in debt in 2024 was caused by a combination of a larger-than-planned cash deficit, interest expenditure and the revaluation of foreign currency debt, which, in the face of lower-than-expected GDP growth, were not able to reduce the overall debt ratio. The increase in the debt-to-GDP ratio in 2024 does not violate the debt rule of the Fundamental Law, as the state of emergency imposed in view of the armed conflict in the neighboring country

is a special legal order and therefore provides an exemption from the debt rule of the Fundamental Law.

**Tight fiscal policy needed to exit the excessive deficit procedure**

The assessment of budgetary developments was based on the medium-term budgetary structural plan prepared by the Government and revised in consultation with the Commission of the European Union. The analysis has been interpreted as a scenario demonstrating that, under the assumption of subdued growth in net nationally financed primary expenditure (net expenditure) committed by the Government, Hungary would fulfil the conditions for exiting the excessive deficit procedure by the end of 2026, even under the growth path considered most likely by the Commission. Consequently, this scenario requires a much tighter fiscal stance than would be necessary under the more dynamic growth path assumed in the government's forecast underlying the 2025 central budget. At the same time, the Government's commitment to a restrained increase in net expenditure means that the balance targets can be met even if economic growth does not reach the pace projected in the Government forecast. In this context, the analysis has identified the following challenges and risks:

1. The Plan assumes that government interest expenditure will no longer decline as a share of GDP in 2026 and 2027, after a significant decline in 2025, and therefore a significant improvement in the primary balance is needed to improve the government sector balance. The improvement is in line with the positive developments since 2021, but its size is challenging. The Plan targets a primary balance of 1.9 percent of GDP in 2027, significantly higher than the 0.2 percent achieved in 2019 under more favorable macroeconomic conditions.
2. A further challenge is that the Plan aims to increase the primary balance only through a modest increase in net expenditure, as opposed to the increase in the centralization rate, which has also contributed to the improvement in the primary balance since 2021.
3. The planned rebalancing also requires that the centralization rate does not fall. However, this does not imply an unchanged structure of government revenues. With earnings and household consumption expenditure growing faster than nominal GDP, earnings and taxes on consumption may also rise faster than GDP, creating some room for tax cuts, lower tax rates or the abolishment of select special taxes. This room, however, will be used by raising the family tax credit and reducing special taxes in 2026 under current rules. Further room for maneuver could be provided by higher-than-planned GDP growth increasing the tax base.

4. The challenge for the reduction of the public debt ratio between 2025 and 2027 is that the implicit interest rate on public debt is projected to be higher than the GDP deflator and even higher than the nominal GDP growth rate in 2025 and 2027. This would imply that, all other factors affecting the value of the indicator remaining constant, the numerator of the public debt indicator would grow faster than its denominator. Consequently, the primary balance should be steadily positive not only to achieve the deficit target but also to reduce the debt indicator, as this will reduce government debt to the planned level. In addition, exchange rate developments have a significant impact on the value of government debt, as the share of foreign currency debt in central government debt is close to 30% by the end of 2024.
5. The challenge is that the planned rate of public sector wage growth (in line with dynamic wage growth in the competitive sector) is significantly higher than the committed rate of increase in net expenditure. As a consequence, wage increases will have to be offset by lower-than-average increases in other budgetary expenditure.
6. The expected dynamics of pension expenditure exceed the committed growth rate of net nationally financed primary expenditure. This is because, in addition to inflation-linked increases in pensions already accrued, dynamic wage growth will lead to a faster-than-inflation increase in the average amount of newly accrued pensions and an increase in the number of retired persons.
7. In order to achieve the balance targets, government investment expenditure as a share of GDP cannot be increased either, i.e. it cannot contribute to an increase in the investment rate.

# 1. THE EVOLUTION OF INTERNATIONAL CONDITIONS

Despite a series of crises in the current decade, global real GDP growth in 2024 is expected to be 3.2-3.4 percent, with a slight increase above this level in 2025-2027 (OECD, IMF, World Bank, European Commission, European Central Bank). From 2000 until the pandemic, this CAGR[5] growth was 3.1 percent, above the pre-COVID epidemic growth rate (World Bank).

Global inflation fell from 6.7% in 2023 to 5.7% in 2024. Expectations point to further disinflation, with the IMF forecasting inflation of 4.2 percent in 2025 and 3.5 percent in 2026. Although core inflation has declined to around the pre-pandemic trend, the services price index remains above its pre-COVID level, including in large economies such as the US and the euro area. It should be highlighted that protectionist tariffs and armed conflicts carry upside inflation risks.

Monetary conditions may differ depending on the stickiness of inflation, which also affects the inflation and growth outlook.

As the world's dominant economy, the United States of America produced 26 percent of global GDP in 2023. US GDP growth during 2024 was projected at 2.5-2.8 percent. It could slow down in 2025, with current forecasts from international institutions ranging from 2.1 to 2.7 percent.

China will account for more than 19 percent of global GDP output by 2024. China's GDP is expected to grow by 4.9-5.0 percent in 2024, and although this is forecast to moderate to 4.5-4.6 percent in 2025 and 4.0-4.5 percent in 2026, it should be noted that the World Bank raised its outlook for China's growth in December 2024 from its previous forecast.

The deepening differences between the US and China have made and are making the world bipolar. While the share of global GDP of the countries that founded BRICS in 2010 was less than 10 per cent in 2004 (Gómez-Mera et al., 2014), it exceeded 29 per cent in 2023 (IMF). Within the group India is the fastest growing country with a dominant economy, with GDP growth of 8.2 per cent in 2024 (IMF). Moreover, annual GDP growth could reach 7 per cent in the next three years (World Bank).

The administration that took office in January this year, following the 2024 elections, has significantly reoriented US foreign policy, and protectionist economic policies have been further intensified. In addition to the polarization between the US and China, the US has also engaged in protectionist measures against its traditional allies, including promises and imposition of tariffs, one of the main goals of which is to reduce America's net trade deficit.

[5] Compound annual growth rate - Compound annual growth rate is the average annual growth rate of compound values over a given period.

The European Union also imposed additional tariffs on electric vehicles against China in October 2024, citing unfair state subsidies. An indication of the competitiveness of Chinese batteries for electric cars is that while the market share of Chinese batteries for electric cars sold in the European Union was less than 3% in 2020, it was close to 22% in 2023 (European Automobile Manufacturers Association).

Although the value of world trade volumes could increase again in 2024, after a 1.2 percent decline in 2023, the rate of increase is low and below the rate of global GDP growth. For 2024, the World Trade Organization forecast growth of 2.6 percent, but this was before the outbreak of the conflict in the Middle East. The focus on supply chain security continues, including the impact of ongoing wars and minor armed conflicts, as well as the rise of protectionist economic policies that extend and increase tariffs and their negative impact on world trade.

Generally speaking, in a period of armed conflict and polarization, a measurable increase in government defense and military spending is expected. This is further reinforced by the expectation that the US will hold NATO members to account on their military spending commitments, given that many member states are not meeting even their defense spending commitments of 2 per cent of GDP.

The global decarbonization process is expected to slow down. In January 2025, the United States of America withdrew from the Paris Climate Agreement[6] (Whitehouse, 2025). Europe remains committed to the green transition, but there is growing support for a revision of the total ban on explosive vehicles from 2035, and a possible approval of hybrid vehicles is already on the horizon.

Average annual real GDP growth in the euro area was 0.7 percent in 2024, compared with 1.0-1.3 percent in 2025 and 1.4-1.6 percent in 2026 (European Central Bank, International Monetary Fund, European Commission, OECD). In addition, Germany, the largest economy in the European Union, shrank by 0.3 percent in 2023 (World Bank) and 0.2 percent in 2024, according to the German Federal Statistical Office.

This continues a decades-long trend in which the share of the European Union and the euro area in global GDP has been declining. According to World Bank data, this figure was around 20 per cent in 2010 and fell to 16.5 per cent in 2023 (Berg, 2025). It should be noted that in 2022, Chinese car exports exceeded those of German cars overall. The European Union is facing serious competitiveness challenges, which are also addressed in the Draghi report.

77 percent of Hungarian exports are destined for the European Union, while the EU accounts for 69 percent of imports. Germany is Hungary's most important trading partner,

[6] Paris Agreement (Climate Change Convention)

accounting for 26.3 percent of exports and 22.6 percent of imports in 2023. The growth difficulties of the European Union and the German economy therefore have a major impact on Hungary's growth prospects.

Sanctions imposed over the Russia-Ukraine conflict remain in place, with US LNG purchases exceeding 47 per cent during 2024, while the share of Russian natural gas in the energy mix has fallen to 16 per cent. The European Union is facing energy price challenges in the transition away from cheap Russian energy, among other things, and the green transition will entail significant investment costs. Meanwhile, Europe has suffered a serious setback in innovation and in the competition for AI, which is expected to be a key driver of efficiency and growth, and which will require significant investment.

In a changing global economic and geopolitical context, the EU needs to find answers to its competitiveness challenges as soon as possible, while Hungary, which has proclaimed a policy of economic neutrality abroad, faces challenges in achieving this in a polarizing world.

# 2. MACROECONOMIC FORECAST

## 2.1 Effective and lasting disinflation is a prerequisite for sustainable growth

Global inflation returned in the first years of the 2020 decade, with most countries in the world experiencing successive waves of price rises. Supply-demand frictions following the COVID epidemic, the energy crisis and the Russia-Ukraine war have all contributed to the rise in global inflation not seen since the 1970s. In Hungary, a period of rapid disinflation began after inflation peaked in January 2023, and within a year the rate of price increases had fallen below 4 percent, within the central bank's tolerance band. Bringing inflation down in such a short period of time is a clear economic success story, which, based on historical experience worldwide, has been achieved in only a quarter of cases. In 2024, inflation was between 3 and 4 percent for most of the year, but in the last third of the year the pace of inflation accelerated, with the result that inflation rose again to 5.5 percent in January 2025. The combined impact of the rise in global commodity prices and movements in the forint market quickly fed through to prices of imported goods, mainly food and fuel.

Inflation is expected to average above 4 percent per year in 2025, above the assumption of 3.2 percent in the Budget Law. Lower indexation of backward revaluations will help to moderate inflation over 2025, but the weakening of the forint exchange rate in the last quarter of 2024 will have an inflationary impact. World food and energy prices are volatile. Although they have moderated inflation overall in 2024, they are not expected to have such a clear positive impact in the coming years. The consumer price index is expected to return close to the central bank's target of 3% in 2026.

In Hungary, not only direct imports linked to exports but also imports linked to consumption are high. The global inflationary environment is causing upward inflationary pressures via imports compared to the pre-pandemic period, with global inflation ranging between 1.4 and 2.4 percent over the period 2015-2019, including low increases in energy and commodity prices.

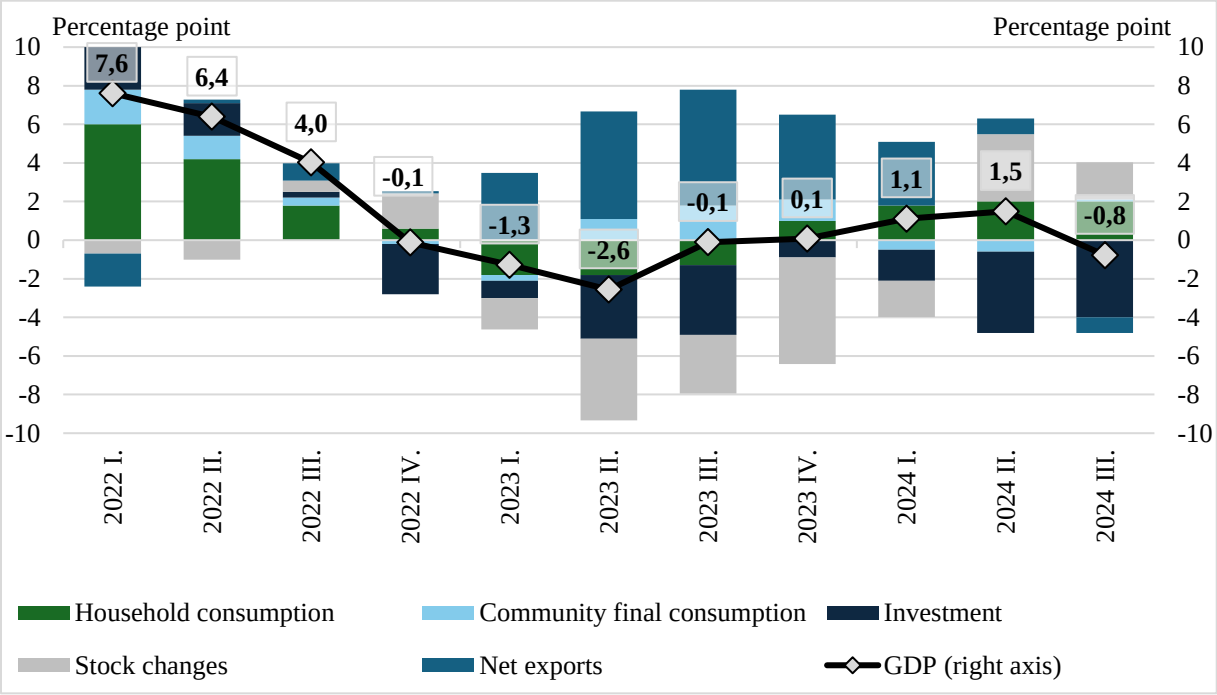
Achieving price stability on a sustainable basis is a key priority, laying the foundations for a lasting recovery in consumer confidence and growth. It is observed that rising inflation reduces not only real wealth and real incomes, but also consumer confidence. These combine to produce a significant fall in consumption. The prolonged low level of consumption is also holding back production and investments, causing a marked slowdown in overall economic growth. Boosting consumer confidence and reducing inflation expectations are therefore not only a key condition for strengthening balances but also for economic growth.

## 2.2 Economic recovery after years of difficult crisis

Economic problems affecting the whole world have led to a multicrisis in our country in the early 2020s. First the COVID epidemic, then the energy crisis, the inflation shock and the consequences of the Russian-Ukrainian war have set back economic growth. In 2022, the year following the post-COVID recovery, GDP growth was 4.6 percent overall, but the year was characterized by a duality: growth was strong in the first half of the year, but in the second half of the year the Hungarian economy slipped into a technical recession as a result of the war in our neighborhood and the inflationary shock. In 2023, these effects prevailed, with the economy contracting by 0.9 per cent during the year. Inflation fell significantly during 2023, but elevated price levels persisted, leaving both consumer and business confidence stuck at persistently low levels.

The impact of the lack of confidence on the real economy was also felt in 2024. Investment activity continued to decline, driven by high costs (i.e. indirectly inflation) and weak confidence, according to business surveys (see Figure 1). Over the first three quarters of 2024, gross fixed capital formation fell by more than 12 percent on average. The protracted crisis in the German economy also set back domestic industrial output and exports. This was offset by an even larger fall in imports, resulting in a trade surplus in 2024 despite weak export performance. Economic growth was also negatively affected by a decline in agricultural value added due to repeated drought. However, household consumption expanded, driven mainly by demand for services, thanks to a rebound in real wages. This, together with positive net exports due to the fall in imports, resulted in an overall expansion of 0.5% in 2024.

**Figure 1: Consumption-side breakdown of annual change in GDP, quarterly**




*Source: HCSO*

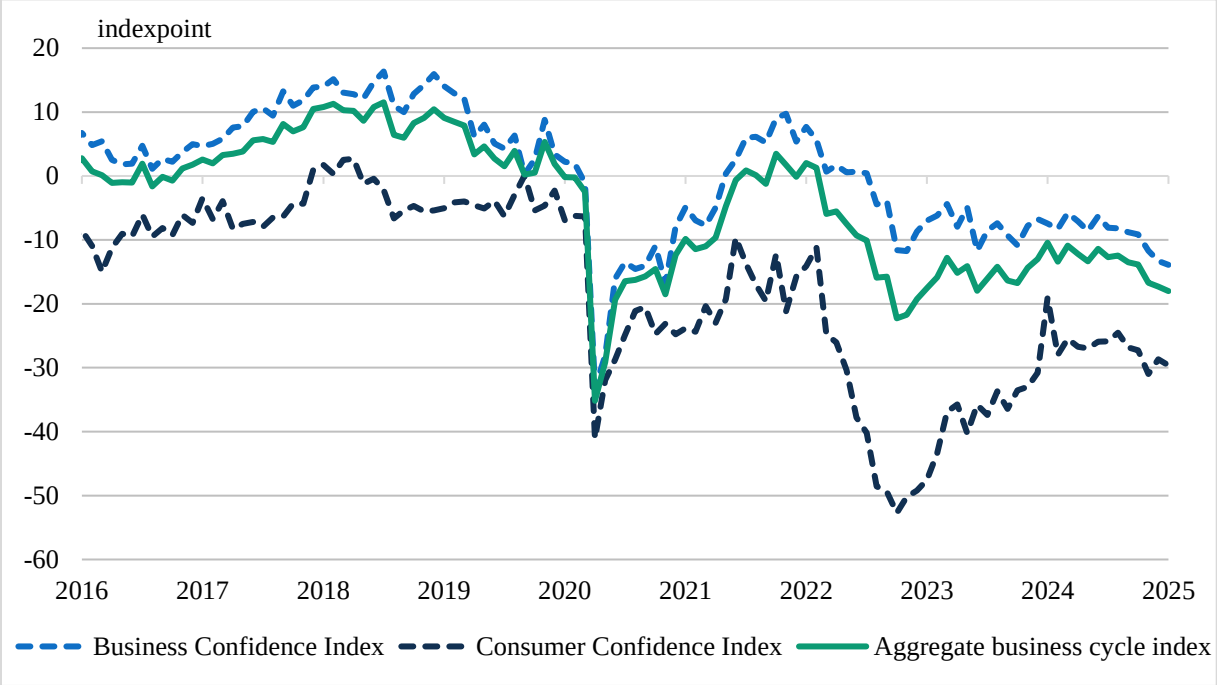
Looking ahead, the Hungarian economy may pick up again from 2025, but growth is subject to downside risks and the global economic environment is more uncertain than in the previous decade.

Geopolitical confrontations have intensified in recent years. Hungary, as a small open economy, is particularly exposed to challenges affecting global and European supply chains. The potential for greater fragmentation of world trade creates unfavorable conditions for the international business cycle, and in particular for the European economy. Hungarian industrial production and exports have been affected by the weakness of the European automotive industry. The situation of our most important external market also determines the production prospects of domestic industry. The turnaround in industrial trends in Europe, especially in Germany, is still in doubt, with analysts not expecting any significant improvement until the second half of 2025. After that, however, a gradual recovery of economic growth in Germany is expected by international benchmarks. On the other hand, rising real incomes and improving confidence could keep domestic demand dynamics stable in Hungary.

From 2025, the Hungarian economy is expected to expand again in a more balanced structure, according to most analysts' forecasts. The 3.4% growth assumed in the 2025 Budget Law is expected to be achieved this year, but the risks to its achievement have increased. Economic growth of 3 percent or above would require a positive turnaround in the external environment in at least the second half of the year, a sustained pick-up in domestic consumption and a change in the trend of investment dynamics. A good performance of consumption and

investment is conditional on a strengthening of consumer and business confidence in the economy. On this favorable basis, the growth rate could rise to close to 4 percent in 2026, before returning to a growth rate of 2.5-3.5 percent in 2027. In contrast, the medium-term structural plan adopted by the European Commission foresees substantially lower economic growth. However, this projection does not include macroeconomic data other than GDP, and thus does not include an overall macroeconomic path, and therefore the macroeconomic path in the Budget Law is taken as the benchmark in our analysis. The potential economic growth rate assumed by the European Commission is reflected in our analysis at the end of this chapter[7].

**Figure 2: Trends in the domestic business sentiment indices**




*Source: GKI*

Improving consumer and business confidence is therefore a critical factor for the expansion of consumption and especially investment this year. From 2022 onwards, as inflation rose sharply, falling real wages and rising living costs, coupled with the uncertain economic environment, increased households' financial caution, leading them to cut back on consumption, which started to decline in 2023 on an annual basis. Similarly, faced with subdued demand, companies have decided to postpone or cancel investments, as their return on investment in a rising cost environment has become questionable. Gross fixed capital formation has been falling steadily since the end of 2022. Restoring confidence is key to economic growth as it is a key factor influencing the future decisions of economic agents. On the one hand, a positive outlook and high confidence will lead to stronger demand in the present, which will underpin firms'

[7] See box - On the scale of potential growth

plans for the future and encourage them to expand production through investment and thus create new jobs. On the other hand, a slower recovery or persistent low confidence will make consumers more cautious and focus on increasing their savings. This reduces both consumption and investment, thereby slowing growth. This is why it is essential to rebuild fragile confidence as soon as possible after economic crises in order to create stability and a predictable future. Price stability and favorable labour market developments, as well as a predictable financial environment, are key determinants of households' perception of the economy.

Already in 2024, household consumption expenditure is set to expand thanks to rising real wages and a gradual recovery in savings. Consumption is expected to continue to rise in the coming years, remaining the main pillar of growth. In 2025, disposable income of the population will continue to rise, supported by the extension of the working-age credit, the baby loan borrowing age and the increase in the family tax credit. Part of the income from government bond interest could also lead to an increase in consumption. All of these factors could push up household consumption expenditure by 4.0-5.0 percent this year, in line with the budget law's baseline. In 2026 and 2027, the pace of consumption growth could slow slightly, in line with more subdued wage dynamics.

Investment could expand again in 2025. Gross fixed capital formation, which accounted for a large share of growth in the second half of the 2010s, has fallen at an unprecedented rate in the last two years, even by regional standards. This is primarily responsible for the recent underperformance of the economy relative to its immediate competitors. Provided the outlook for the future for businesses and households improves and large capacity creation and expansion projects proceed as expected, domestic investment should rise by between 3.5 and 6.5 percent this year. This is a similar pace to the forecast in the budget law. Investment growth is set to continue in 2026-2027, driven by a shift in the competitive sector, while fiscal investment could continue to moderate. The investment rate could remain stable at the current high level, but structural improvements are needed. The expected investment rate of around 24-25% from 2025 is still in the EU average after a decline in recent years, but with a low share of innovative investment, which is a priority for productivity-led, quality-based economic growth. In this respect, Hungary is ranked 18th in the EU, with investment in intellectual property products accounting for 2.7% of GDP in 2023.

A key factor for Hungarian exports is whether the European (German) economy can pick up in 2025. Analysts expect this to happen more gradually and in the second half of the year. In the long term, the expansion of exports could be supported by FDI investment in manufacturing. This will require the resolution of demand anomalies, mainly in the automotive and battery sectors. At the same time, global climate trends and the European drive towards a green

transition point to a temporary slowdown in demand. Hence, active involvement in manufacturing processes that facilitate the green technological transition could help to boost exports in the long term. Overall, domestic exports could grow by 3.5-5.5 percent in 2025, following a likely decline of around 2 percent in 2024, and then expand at an even faster pace in 2026-2027 as major manufacturing investments are completed and production picks up.

With the recovery in international economic activity and a normalizing growth path, the external balance is expected to remain positive for a sustained period. With improving external demand, higher utilization of existing capacity and the ramp-up of ongoing investments should increase export market shares. Looking ahead, we thus assume a sustained current account surplus, similar to the 2010s, even with a stable growth in domestic demand.

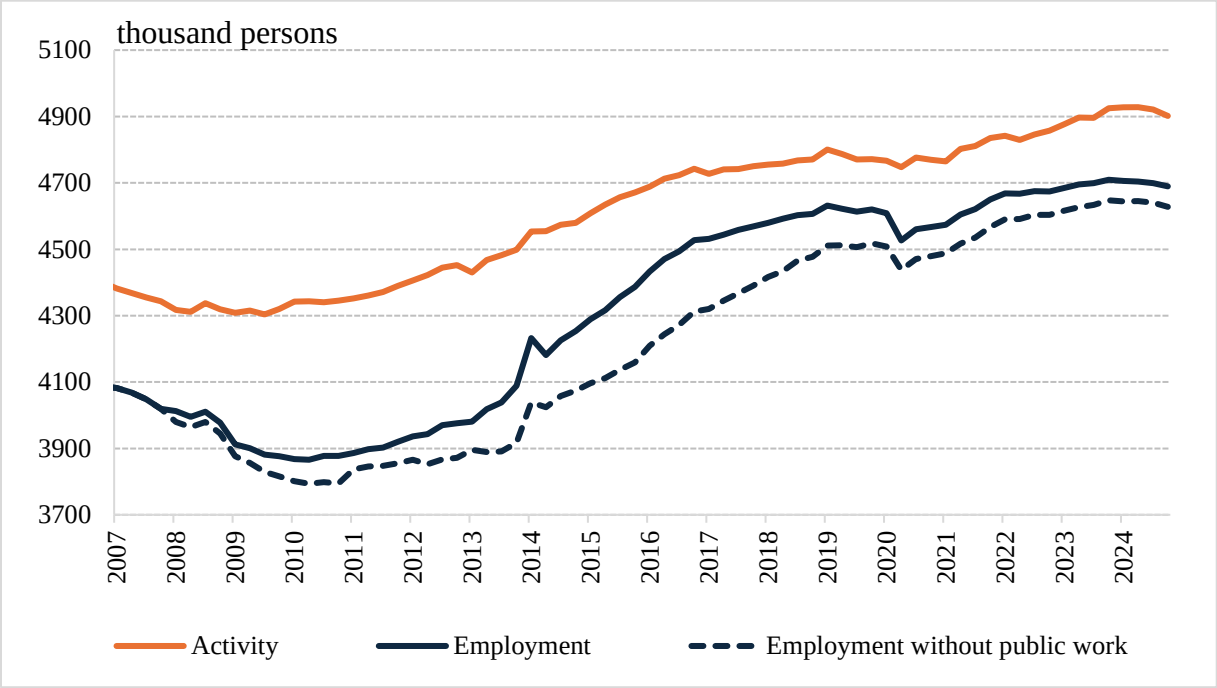
In order to maintain a high and sustainable rate of GDP growth, comprehensive competitiveness reforms are needed to facilitate the transition to a productivity-intensive economic model. In addition, restoring and maintaining equilibria remains key to our resilience. Economic performance in 2025 will depend on an improvement in the external environment, alongside a return of confidence and a resumption of investment. In the medium term, however, structural indicators of the economy, productivity and competitiveness will become more important alongside cyclical factors. These will determine whether the Hungarian economy can resume a rapid catching-up path with the EU average.

The reserves of the extensive growth model pursued in the previous decade are running out, so the quality of the factors of production needs to be improved to continue catching up. The transition to an intensive growth model requires the Hungarian economy to adapt to the needs of the 2020 decade and successfully catch up with the megatrends already underway. This would be helped by improvements in energy efficiency and a rapid expansion of digitalization. Key to this are a sufficient, healthy and skilled workforce, strengthening companies' capacity for innovation, digitization and export markets, easy and fast access to finance, and an energy-efficient and green economic transition.

### 2.3 Labour market remained stable during the crisis years

Since the beginning of the 2010s, Hungary has experienced a very successful employment expansion. While in 2010 the activity rate of 15-74 year olds in Hungary was one of the lowest in the European Union, it is now above the EU average and the number of unemployed has fallen by a third. The increase in employment was supported by the reduction of labour taxes, the low marginal tax rate of the single-rate tax and labour market reforms over the previous decade, raising the employment rate from 50.6% in 2010 to 65.1% in 2024 (Figure 3).

**Figure 3: Evolution of the number of active and employed persons in Hungary**

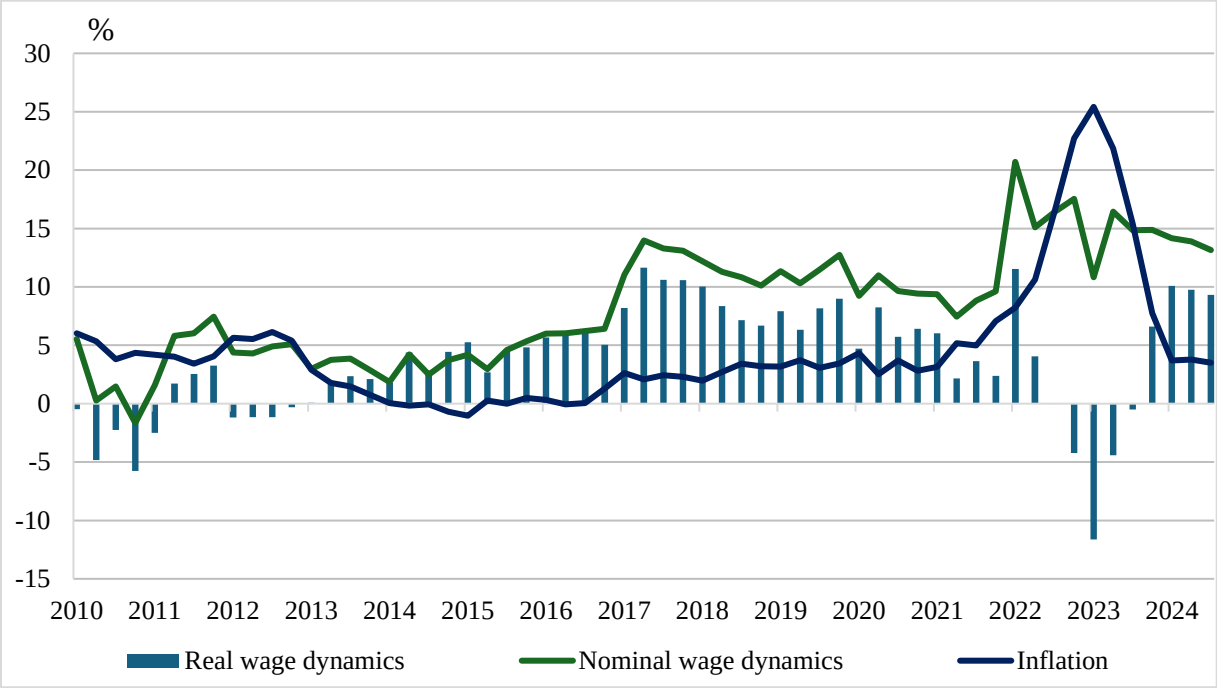



*Note: Seasonally adjusted data*
*Source: HSCO*

The labour market remained stable during the COVID crisis, thanks to government and central bank programmes, and did not show a significant decline during the inflationary surge. Employment remains well below its historic peak in 2023. Unemployment rose slightly during 2024, but remains low by international standards.

In the second half of the 2010s, domestic economic agents experienced buoyant wage dynamics, which have been sustained in recent years. This has led to a significant increase in real wages in most years, with the exception of 2023, when inflation started to surge. From autumn 2023, real wages will start to rise again, as inflation moderates significantly (Figure 4).

**Figure 4: Wage dynamics in the Hungary**




*Note: Seasonally adjusted data*
*Source: based on HSCO MNB*

An important factor in the medium-term economic projections is that employment growth, which was a key driver of growth in the 2010s, is increasingly facing demographic constraints. Even in the event of a renewed economic recovery, employment growth is unlikely to continue at the pace seen in previous decades. The demographic constraints on employment growth are becoming increasingly effective as the inactive labour reserve declines. As in the previous decade, the ageing of society will continue in the years ahead, with the number of people leaving the labour force outstripping the number entering it. The rate of depopulation could average around 50,000 people per year by the end of the decade, above the average of the previous decade and a half. As a result, the domestic working-age population (15-74 years) could fall by nearly 300 thousand by 2030. The problem will be exacerbated by the fact that the decline will occur mostly in the group with the highest employment rate (25-54 year olds). The labour market is therefore expected to remain tight in the 2020s, with demand likely to outstrip supply in most areas, so that only a slight increase in employment is expected in the short to medium term, between 2025 and 2027. The unemployment rate is likely to remain low by European standards, at around 3-4% in the coming years.

The impact of the sharpening demographic constraints may be partly offset by a further rise in employment rates. Although employment has increased significantly since 2010 and the employment rate is now above the EU average, there is still room for catching up compared to developed northern and western European Member States. The challenges of structural

unemployment make it difficult to attract the unemployed as a potential reserve. The geographic distribution of the labour force and labour reserve is uneven: the more developed, typically north-western regions of the country and the capital area have employment rates almost ten percentage points higher than the eastern and north-eastern counties, and the unemployment rate differential is close to seven percentage points between counties. The potential for attracting additional groups of the inactive population is limited, and therefore targeted measures and the spread of more flexible forms of work (part-time work, working from home, flexible working hours, etc.) are needed, as these are among the lowest in Hungary compared to the EU. Employment rates tend to be higher among the more educated groups, so there are also gaps in the educational structure of the Hungarian labour force, as the share of tertiary education is below the EU average.

The announced minimum wage agreement will have an impact on wage dynamics in the coming years. In January 2025, the minimum wage was increased by 9 percent and the guaranteed minimum wage by 7 percent, while minimum wage increases of 13 percent are expected in 2026 and 14 percent in 2027, provided that the macroeconomic expectations that are a condition for the implementation of the planned minimum wage increase path are met. The parties have agreed to renegotiate the agreement in case of a significant deviation from expectations. In addition, the fact that inflation expectations of the general public remain above the actual data, while the easing of labour market tensions since mid-2022 will also weigh on wage growth. Against this background, wage dynamics should remain strong in the medium term. There is scope for catching up, as the domestic wage share is the second lowest in the EU: an increase of more than 10 percentage points would be needed to reach the EU average. However, it is important that wages rise in line with the productivity that underpins them, in a sustainable manner, while ensuring adequate living standards and increasing prosperity. Getting the ratios right is of paramount importance. Hungary has achieved significant wage catching-up over the past decade, but this can only continue in a sustainable manner in parallel with productivity growth.

**On the scale of potential growth**

An important element of medium- and long-term projections and plans is how the economy could perform, i.e. how potential GDP would evolve, after cyclical cycles and other transitory factors have been eliminated, making optimal use of available resources. Estimating potential economic growth has become particularly important as it is an important parameter of the new fiscal framework of the European Union. Indeed, the newly introduced fiscal expenditure rule requires, as a matter of priority, that the annual growth rate of fiscal expenditure (adjusted for a number of factors) should not exceed the dynamics of the agreed path, in the construction of

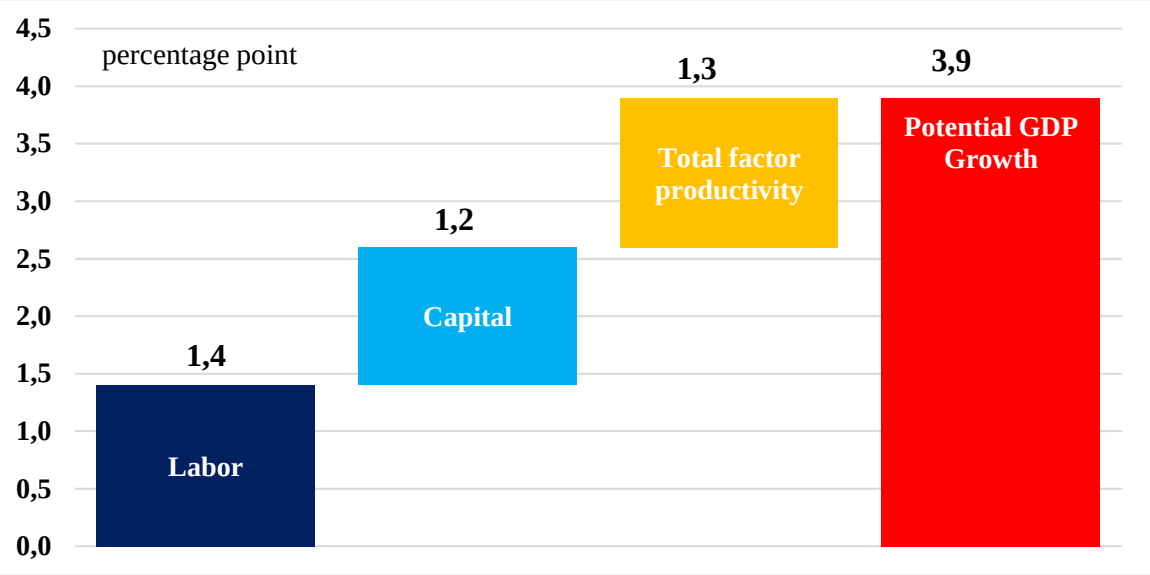
which the growth rate of potential GDP plays a prominent role. Consequently, an important element of the expected fiscal path is the estimate of potential GDP growth itself.

The European Commission's assessment of Hungary's medium-term fiscal structural plan (MTFSP) projected a potential growth rate of around 1.5-1.7% for the years 2025-2027, and this was taken into account in the Council of the European Union's recommendation. The Fiscal Council considers that this estimate does not accurately reflect the growth potential of the domestic economy, which could be higher.

The underlying components of potential GDP, itself a theoretical variable, cannot be measured directly, which complicates the estimation process. Potential GDP can also be generated using a number of different approaches, which may also give different results. Because of these circumstances, any estimate of potential GDP is subject to considerable uncertainty.

There are three main factors that influence potential economic growth: the labour force available, the capital that can be attracted and productivity. These factors can also be estimated in terms of the evolution of actual GDP. Hungarian GDP has grown significantly over the past decade, particularly in the years 2013-2019. The average growth rate over this period was 3.9 percent, which can be decomposed into the contributions of the three factors above. The three sources of growth are calculated to have supported actual growth to essentially similar extents. On the one hand, the significant increase in the number of employed persons alone contributed around 1.4 percentage points to average annual GDP growth. Favorable conditions and targeted central bank and government programmes have stimulated corporate borrowing and investment, so that capital accumulation has also boosted GDP by an average of 1.2 percentage points per year. In addition to the quantitative factors, productivity in the economy also increased (in the second half of the decade), so that the improvement in total factor productivity contributed an additional 1.3 percentage points per year on average to growth (Figure 5).

**Figure 5: Components of Hungarian GDP growth between 2013 and 2019**




*Source: based on HSCO MNB estimate*

In estimating the current potential level of domestic GDP growth, it is worth starting from the previous data, as the crises of the 2020 decade have created exceptional economic conditions in virtually every year, which are unlikely to be repeated in the long run.

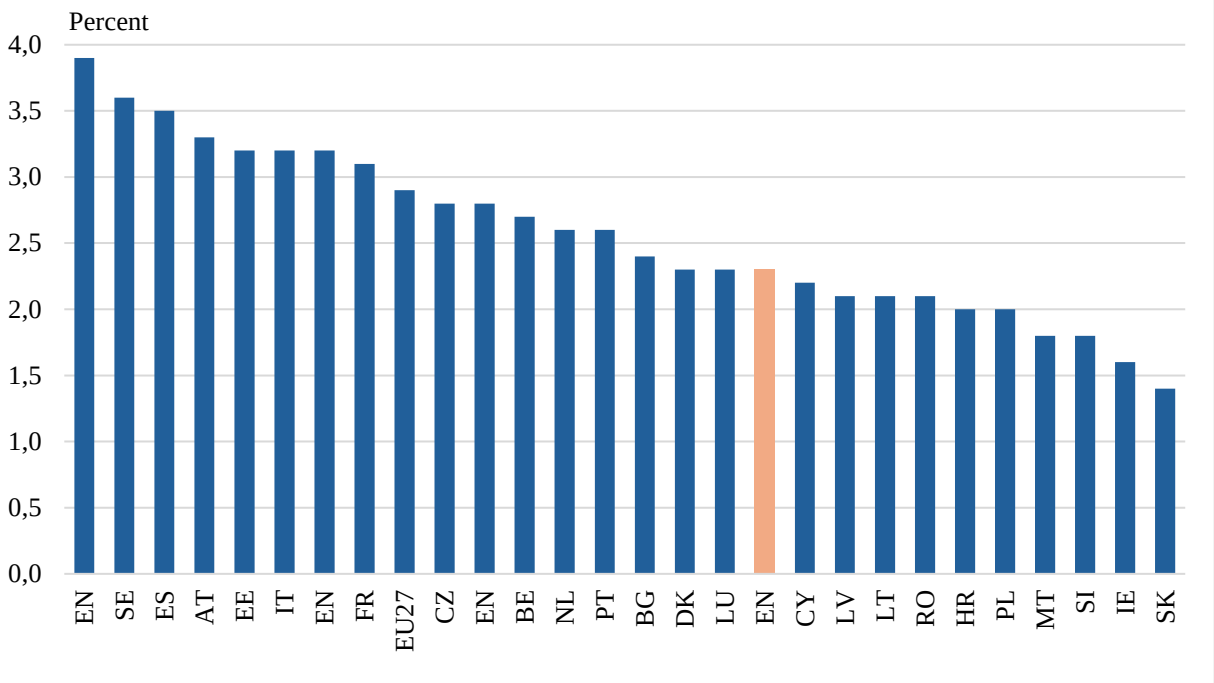
Estimates of potential GDP in the present should take into account that the conditions for growth in the 2020s, based on the significant inflow of new labour in the previous decade, are no longer in place. Natural attrition and ageing will reduce the working-age population, so that even in the medium term a moderate number of new groups could be brought into the labour market. As a result, the contribution of the labour force to growth in the coming years is likely to remain neutral.

However, the second half of the last decade is encouraging, as the Hungarian economy would have achieved potential GDP growth of 2.5% even without the contribution of labour, which the Fiscal Council believes remains sustainable thanks to the identifiable reserves in capital and productivity factors.

The capital intensity of the Hungarian economy is relatively low, with the stock of capital per euro of output lagging behind the European leaders and the EU average, leaving considerable scope for further capital inflows (Figure 6). In Hungary, the capital stock per euro of GDP generated in 2023 is 2.3 euros, compared to an EU average of 2.9 euros and above 3.5 euros in the leading countries. The capital intensity of the highest capital-intensive economies, Greece and Sweden, is thus more than one and a half times that of Hungary. Capital intensity can be increased through innovation, investment and the introduction of new technologies, among other things. Growth in gross fixed capital formation could return this year as the external environment strengthens and business confidence improves, supported by significant

FDI-led foreign projects. Besides the quantity of investment, the quality of investment is also key. Supporting investment in ICT[8] and intangible assets is essential for future productivity and growth.

**Figure 6: Ratio of capital stock to GDP in the EU countries (2023)**

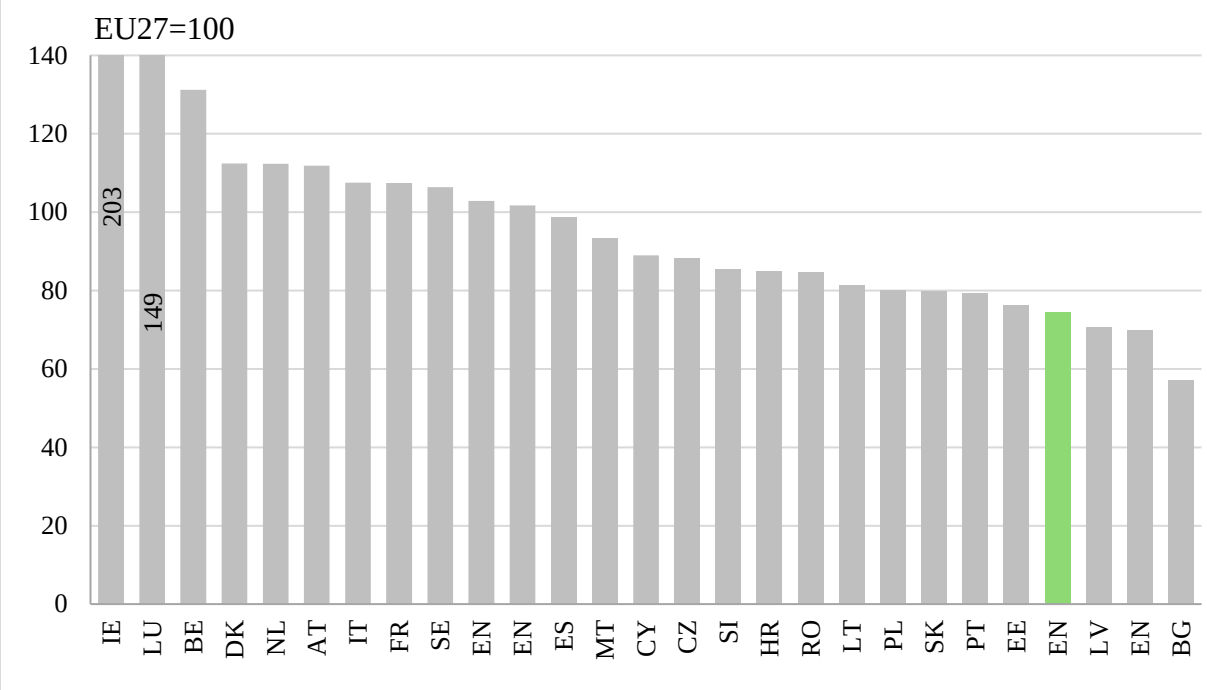



*Note: At constant, 2020 prices*
*Source: AMECO*

Hungary currently lags significantly behind the European leaders in productivity (Figure 7). Convergence with the technological leaders in terms of adoption and application of proven technologies and structures, digital transformation can raise the domestic productivity growth rate for a long time to come, and thus make a long-term successful catching-up path achievable. While in the Czech Republic the indicator stands at 88.1% of the EU average, in Hungary it is 74.5%. It is important to underline that labour productivity does not depend on the individual worker, but on the business and economic environment, including the technology used, management, energy efficiency and tax and business conditions, among others. Productivity can of course also be boosted by effective research and development through innovations, new products and technologies. Our country is also in the middle of the pack in terms of R&D spending. In Hungary, R&D spending accounted for 1.4% of GDP, below the EU average (2.2%) but above the average for the region.

[8] Information and communication techniques and technologies

**Figure 7: Labour productivity levels in the EU countries (2023)**




*Note: GDP per person employed, at purchasing power parity*
*Source: Eurostat data, MNB calculation*

Overall, the potential growth rate of the Hungarian economy may fall short of the high growth achieved in the previous decade, but despite the difficulties of the new decade, it is still above the European Commission's current estimate. This is supported by the fact that previous calculations by major international organizations and even the European Commission[9] have resulted in higher assumed potential growth. The European Commission had previously estimated growth of 2.2 and 2.4 percent, while the OECD had reported a similar potential GDP trajectory for Hungary of 2.2 and 2.1 percent. The IMF's forecast is even more favorable, with the Fund’s analysts projecting that the Hungarian economy, emerging from the multicrisis, could gradually rise from 2.6 percent from 2025 onwards, and could even expand by close to 3 percent by the end of the decade. Sustainable economic growth should be driven primarily by productivity growth, which should offset the adverse impact of demographic trends.

[9] European Commission (2024): In-Depth Review, 2024 Hungary

**Table 1: Expected development of domestic macroeconomic indicators (annual change)**

| | 2025 | | 2026 | | 2027 | |
|---|---|---|---|---|---|---|
| | **Fiscal Council** | **budget law** | **Fiscal Council** | **budget law** | **Fiscal Council** | **budget law** |
| Inflation (annual average) | | | | | | |
| Inflation | 4,0 - 5,0 | 3,2 | 2,5 - 3,5 | 3,0 | 2,5 - 3,5 | 3,0 |
| Economic growth | | | | | | |
| Household final consumption expenditure | 4,0 - 5,0 | 4,4 | 3,5 - 4,5 | 4,5 | 2,5 - 3,5 | 4,5 |
| Gross fixed capital formation | 3,5 - 6,5 | 5,1 | 2,5 - 5,5 | 4,6 | 1,5 - 4,5 | 4,2 |
| Exports | 3,5 - 5,5 | 3,6 | 6,0 - 8,0 | 6,7 | 5,0 - 7,0 | 6,1 |
| Imports | 4,5 - 6,5 | 4,1 | 5,0 - 7,0 | 6,1 | 4,5 - 6,5 | 5,1 |
| GDP | 2,5 - 3,5 | 3,4 | 3,5 - 4,5 | 4,1 | 2,5 - 3,5 | 4,3 |
| External balance (as a percentage of GDP) | | | | | | |
| Current account balance | 1,0 - 2,5 | 1,6 | 1,5 - 3,0 | 1,7 | 2,0 - 3,5 | 1,9 |
| Labour market | | | | | | |
| Average gross earnings by industry | 8,5 - 9,5 | 8,7 | 10,0 - 11,0* | 7,6 | 7,0 - 8,0 | 7,4 |
| Employment by economic activity | (-0,5) - 0,5 | 0,1 | (-0,5) - 0,5 | 0,3 | (-0,5) - 0,5 | 0,3 |

*Note: *The average gross earnings in 2026 will be increased by about 1 percentage point by the already declared arms allowance for law enforcement and defense personnel.*
*Source: Fiscal Council, Act XC of 2024 on the 2025 Central Budget of Hungary*

# 3. GOVERNMENT SECTOR BALANCE TARGETS 2025-2027 AND RISKS TO EXPENDITURE

In April 2024, the European Parliament and the Council adopted a new regulation on the effective coordination of economic policies and multilateral surveillance of budgetary positions, repealing the previous regulation. The main feature of the new regulation is that it focuses on the medium term (4-7 years) in fiscal policy. The basic instrument for this is a national **medium-term structural fiscal plan**, the mandatory content of which is set out in the regulation. All Member States are required to prepare such a plan, but Member States with a budget deficit below 3 percent of GDP and a debt ratio below 60 percent have a large degree of autonomy to prepare their own plans. In contrast, Member States that do not meet these conditions have a pro-active role in preparing their plans and later in adjusting the existing plan.

The medium-term budgetary-structural plan was prepared by Hungary in early November 2024, but the Commission's objections led to an amendment of the medium-term budgetary-structural plan, which was adopted by the Commission on 16 January 2025 and by the Council of the European Union on 18 February.

**The reform of EU fiscal rules**

**In April 2024, both the European Parliament and the Council adopted a new regulation on EU economic governance and amendments to previous regulations, so the revised set of budgetary rules entered into force on 30 April 2024.** In total, three pieces of legislation have been affected: the Regulation on **the preventive arm of the SGP** (MTO, expenditure rule, SDP) has **been replaced**, the Regulation on **the corrective arm** (Maastricht indicators, EDP) has been **amended** and the Directive on **the budgetary framework of the Member States** (statistical accounts, medium-term planning requirements, budgetary advice) has **been amended.**

**The reform was primarily designed to focus on debt sustainability in the medium term.** The amendments have removed a number of indicators and requirements, but have also introduced new rules and procedures. As a result of the reform, the so-called "one-over-twenty" debt reduction rule, the medium-term budgetary objective (MTO) for the structural deficit and the conditionality that requires a structural adjustment towards it, as well as the significant deviation procedure (SDP) for the preventive arm have been abolished.

**The cornerstone of the changes is the newly submitted national medium-term fiscal-structural plan**, **which aims to bring Member States' debt ratios to sustainable levels.** The

FSP and the accompanying annual progress report will replace the Stability, Convergence and National Reform Programmes. The time horizon of the fiscal-structural plan is four or five years by default (depending on the electoral cycle of the Member State), but this period can be extended by up to three years by the Member State if it proposes structural and investment reforms to improve the sustainability and resilience of public finances.

**For those Member States with high deficits or high debt, the Commission will prepare a preliminary reference path, while for the others it will only provide technical information.** If a country has a budget deficit above 3 percent of GDP or a debt ratio above 60 percent of GDP, the budgetary structural plan to be submitted by the Member State will be preceded by a reference path prepared by the Commission based on the institution's own debt sustainability analysis[10]. For the other Member States, i.e. those with deficits below 3 percent and debt below 60 percent, only technical information is provided. The Commission will engage in a prior dialogue with the Member States concerned, the outcome of which should be included in the budgetary structural plan to be submitted.

**The key indicator for assessing the performance of the assigned budget path is the net expenditure path.** The net expenditure path comprises government budget expenditure less subsidies related to EU funds, interest expenditure, the cyclical part of unemployment benefits and discretionary revenues, and excluding the impact of one-off and temporary measures. The actual deviations from the net expenditure path will be monitored in a control account and if the deviations recorded in the account exceed the specified thresholds, this will lead to an Excessive Deficit Procedure[11] . The threshold for the deviations recorded in the control account is 0.3 percent of GDP per year or 0.6 percent of GDP cumulatively. If a Member State's net expenditure figures deviate by more than these thresholds from the path set in the agreed structural budgetary plan, it will be subject to an excessive deficit procedure. Of the rules considered for the launch of the EDP, the **deficit-based procedure** linked to the Maastricht 3 percent threshold will remain as it is, while the **debt-based EDP** will now be launched in response to deviations in the control account.

**Two new numerical requirements, known as safeguards, are introduced into the rules.** The **safeguard on public debt** sets a minimum debt reduction requirement of at least 1 percentage point per year for countries with a public debt-to-GDP ratio above 90%, and at least 0.5 percentage point per year for Member States with a debt ratio between 60% and 90%. In addition to the previous Maastricht threshold of 3 percent, a **guarantee on the government**

[10] Debt sustainability analysis - DSA
[11] Excessive deficit procedure - EDP

**deficit will** be introduced, under which the Commission's reference path will require an adjustment until the Member State's government deficit in structural terms is 1.5 percent of GDP away from the Maastricht 3 percent level. The minimum annual adjustment is 0.4 percentage point, which is reduced to 0.25 percentage point per year if the fiscal-structural plan is extended (reforms, investments). The minimum annual deficit reduction requirement for Member States in excessive deficit procedure remains 0.5 percentage points, which is not affected by this safeguard.

**Last year, the excessive deficit procedures (EDPs), in which Hungary is also involved, were launched again.** In June 2024, the Commission published the Spring Package for the European Semester, in parallel with EDP reports and a proposal to the Council to open procedures. An EDP can be initiated if the actual or planned government deficit exceeds 3% of GDP. The procedure can only be waived if the Member State's debt ratio does not exceed 60 percent of GDP or, if it does, the excess over the 3 percent of GDP deficit threshold is not significant and temporary and the relevant factors that can be taken into account in such a case exempt the country concerned.

**The first Hungarian national medium-term structural fiscal plan was presented in early November.** Submitted at the same time as the planning of the Hungarian budget for 2025, the fiscal-structural plan included a 6.1% increase in net expenditure, above the European Commission's preliminary guidance (Table 2). As a consequence, the European Commission has requested the Hungarian authorities to revise the plan. The revised plan submitted in December maximises net expenditure growth to 4.3 percent in 2025 and projects growth of up to 4 percent and 3.9 percent respectively for the following years. This draft received a positive opinion from the European Commission in January and was adopted by the Council of the European Union in February.

**Table 2: Expected evolution of the net expenditure path, in chronological order**

| | 2025 | 2026 | 2027 |
|---|---|---|---|
| European Commission (june) | 4,8 | 4,5 | 4,3 |
| National MTSFP (start of november) | 6,1 | 3,8 | 4,0 |
| European Commission (end of november) | 3,9 | 3,3 | 3,2 |
| **National MTSFP (january)** | **4,3** | **4,0** | **3,9** |

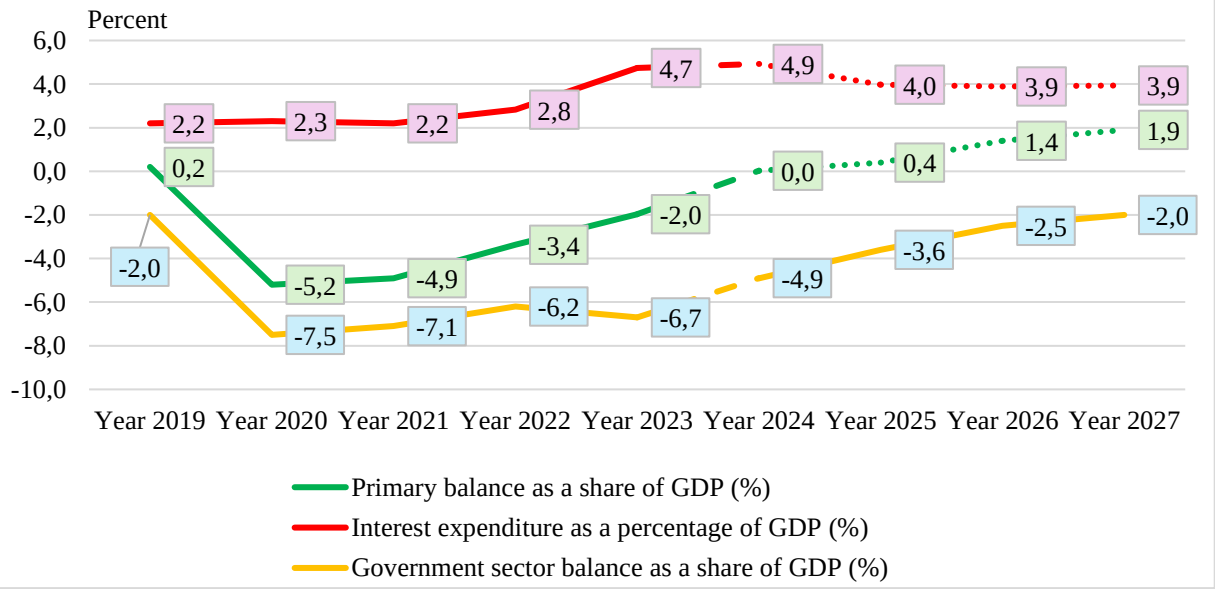
*Source: European Commission*

## Evolution of the primary balance of the general government sector (2019-2027)

The primary balance can be directly influenced by fiscal policy through the planning of tax and expenditure rates and their planned implementation, while interest expenditure is mainly determined by the value of government debt and the benchmark yields on the government debt. Consequently, the primary balance is the one through which the government can intervene to maintain the deficit target, since the room for maneuver for reducing interest expenditure related to the financing of public debt is severely limited. Optimally, fiscal policy will slow down the growth of public debt by improving the primary balance (reducing the deficit), thereby reducing the rate of interest expenditure in the future.

The evolution of the general government sector balance, the primary balance and interest expenditure as a share of GDP between 2019 and 2027 is shown in Figure 8.

**Figure 8: Government sector balance, primary balance and interest expenditure as a share of GDP, 2019-2027, percentage**




*Note: calculation based on MTSFP data for 2024-2027.*

*Source: Eurostat (2025), based on MTSFP (2025) SAO calculation and editing*

Figure 8 shows that the primary balance and the government sector balance improved from the trough in 2020 to 2024, and the trend is projected to continue until the end of 2027, according to the Plan.

In relation to interest expenditure, the Plan includes the value of long-term and short-term interest rates on government debt, summarized in Table 3.

**Table 3: Evolution of the long-term and short-term interest rate on government debt between 2019 and 2027, in percent[12]**

| Year | Long-term interest rate (percent) (annual average) | Short-term interest rate (percent) (annual average) |
|---|---|---|
| 2019 | 2,4 | 0,1 |
| 2020 | 2,2 | 0,4 |
| 2021 | 3,2 | 1,3 |
| 2022 | 7,7 | 9,1 |
| 2023 | 7,5 | 16,0 |
| *2024* | *6,5* | *7,3* |
| *2025* | *6,7* | *5,9* |
| *2026* | *6,8* | *5,7* |
| *2027* | *6,8* | *5,8* |

*Note: 2024-2027 figures are MTSFP values*

*Source: based on Convergence Programmes 2020-2023, MTSFP (2025) SAO editing*

In 2025, interest expenditure as a share of GDP is projected to decline by 0.9 percentage point of GDP, so that a 0.4 percentage point improvement in the primary balance (as a share of GDP) is sufficient to achieve the required improvement in the general government balance. However, in 2026 and 2027, interest expenditure as a share of GDP is projected to decline by a total of 0.1 percentage point of GDP, so that a significant increase in the primary balance of 1.5 percentage point over two years is required to achieve the required improvement in the general government balance.

Conclusion: the gradual improvement in the primary balance under the Plan is in line with the favorable developments since 2021. However, the challenge is that reducing the government sector deficit to below 3 percent of GDP will require achieving a positive primary balance of around 1 percent of GDP by 2026, after which the Plan projects the primary balance to rise to 1.9 percent of GDP, significantly higher than the 0.2 percent primary balance achieved in 2019 under favorable macroeconomic conditions.

[12] Planned, based on adjustment scenario (Short-term interest rates / Long-term interest rates of the debts)

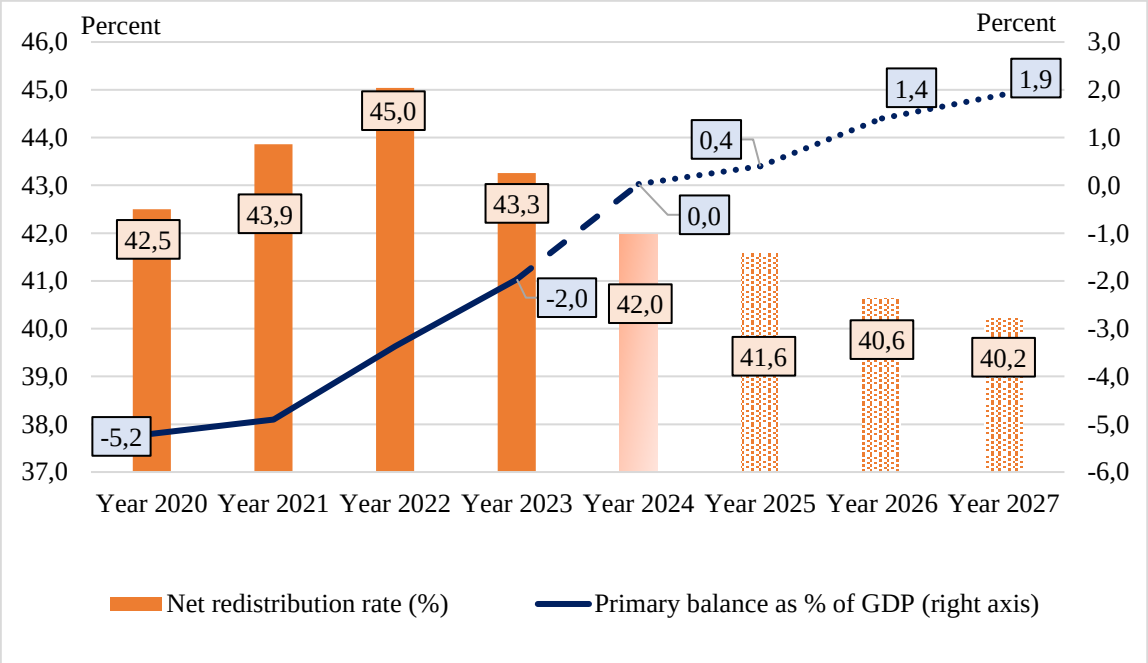
### 3.2 Projected increase in net nationally financed primary expenditures and its contribution to the improvement in the primary balance

In the following, we examine the contribution to the improvement in the primary balance of the reduction in the growth of net nationally financed primary expenditure under the Plan.

The Plan includes commitments to maximum increases in net nationally financed primary expenditure (net expenditure). The annual growth ceilings for net expenditure for the period 2025-2027 are 4.3 percent, 4.0 percent and 3.9 percent.

The analysis introduces the concept of the *net redistribution rate*, defined as the ratio of net nationally financed primary expenditure to GDP. The evolution of the net redistribution rate and the primary balance as a share of GDP between 2020 and 2027 is shown in Figure 9.

**Figure 9: Net redistribution rate and primary balance to GDP ratio from 2020 to 2027, in percent**




*Note: 2024-2027 data are calculated from Plan data*

*Source: Eurostat (2025), based on Plan (2025) SAO calculation and editing*

It can be seen that the net redistribution rate increased dynamically from 2020 to 2022, but decreased in 2023 and 2024. The decrease is projected to continue between 2025 and 2027.

The graph also shows that there is a close relationship between the decline in the net redistribution rate and the improvement in the primary balance as a share of GDP[13] , but to quantify the exact relationship it is necessary to take into account the other two determinants of

[13] The closeness of the relationship is not clearly visible because the value of the net redistribution rate fluctuates between 2025 and 2027. However, this is due to the denominator of the indicator, as the Plan forecasts much more dynamic GDP growth for 2026 than for the other two years.

the primary balance, the difference between total government expenditures and net expenditures, and revenues.

For total government expenditures and total government revenues, the Plan does not include data for the period 2024-2027, so the path of the centralization rate (government revenue as a share of GDP) for the net redistribution rate was estimated from the available data.[14]

The evolution of the net redistribution rate, interest expenditure as a share of GDP, estimated EU expenditure as a share of GDP, the primary balance as a share of GDP and the centralization rate for the period 2021-2027 are summarized in Table 4.

**Table 4: Evolution of the net redistribution rate, interest expenditure per GDP, estimated EU expenditure per GDP, and primary balance per GDP and centralization rate between 2021 and 2027, in percent**

| Title | 2021 | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 |
|---|---|---|---|---|---|---|---|
| 1) Net redistribution rate (% of GDP) under the Plan | 43,9 | 45,0 | 43,3 | *42,0* | *41,6* | *40,6* | *40,2* |
| 2.) Interest expenditure as a share of GDP, actual data 2021-2023 Eurostat, planned data according to the Plan (%) | 2,2 | 2,8 | 4,7 | *4,9* | *4,0* | *3,9* | *3,9* |
| 3) EU spending 2021-2021-2023 Plan back-calculated, 2024-2027 data estimated | 2,0 | 0,8 | 1,5 | *1,2* | *1,1* | *1,0* | *1,0* |
| 4) General government sector balance as a share of GDP actual data 2021-2023 Eurostat, planned data according to the Plan (%) | -7,1 | -6,2 | -6,7 | *-4,9* | *-3,6* | *-2,5* | *-2,0* |
| **Centralisation rate (% of GDP) (rows 1+2.+3.+4)** | **41,0** | **42,5** | **42,8** | ***43,2*** | ***43,0*** | ***43,1*** | ***43,1*** |

*Note: 2024-2027 figures calculated from Plan values*

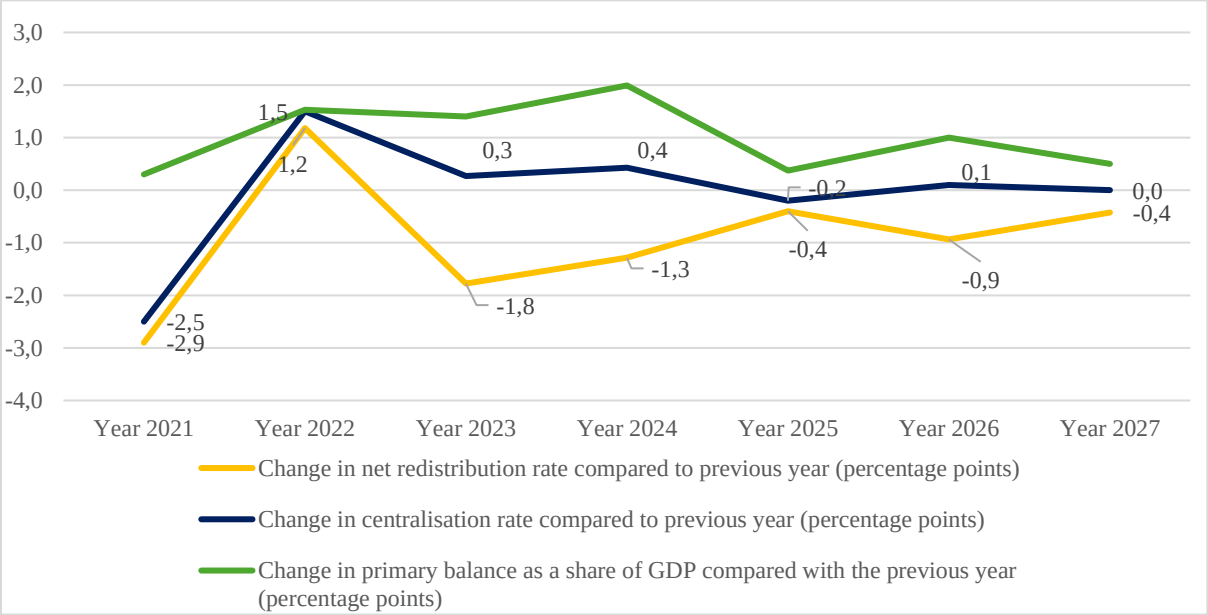
*Source: Eurostat (2025), based on Plan (2025) SAO calculation and editing*

[14] The centralization rate is defined as government revenue as a share of GDP calculated from net nationally financed primary expenditure before revenue measures. The centralization rate for the period 2024-2027 is estimated as follows. From the total government expenditure available for the years 2021-2023, we subtracted interest expenditure and net nationally financed primary expenditure to obtain the total expenditure financed by EU transfers and national co-financing (hereafter EU expenditure) for each of the three years, from which we averaged (HUF 931.4 billion). For the period 2024-2027, we assumed that EU expenditure would amount to HUF 931.4 billion in each year. For the period 2021-2023, the cyclical component of unemployment benefits and the one-off expenditure (levels) in the projections were zero, so these two adjustment factors were not taken into account for this period and were assumed to be zero for the period 2024-2027. On this basis, we have calculated total government expenditure by cumulating the sum of net nationally financed primary expenditure, interest expenditure and EU expenditure for each year of the period 2024-2027. By adding the total government expenditure thus estimated and the government balance under the Plan scenario, total government revenue was calculated for each year of the 2024-2027 period. The centralization rate was calculated as the ratio of total government revenue to the nominal GDP expected for each year in the Plan scenario.

The data in the table show that, assuming that the net redistribution rate and interest expenditure evolve as planned and that other expenditure remains unchanged according to our estimates (HUF 931.4 billion), the planned deficit of the general government sector can be achieved with an almost unchanged centralization rate, i.e. there is no need to increase the centralization rate in the period 2025-2027, but there is no significant room for its reduction either.

The year-on-year changes in the net redistribution rate, the estimated centralization rate and the primary balance to GDP ratio are shown in Figure 10.

**Figure 10: Net redistribution rate, estimated centralization rate and year-on-year change in the primary balance to GDP ratio between 2021 and 2027 in percentage points**




*Note: figures for 2024-2027 are calculated from Plan values, centralization rate for 2024-2027 calculated from own estimates*

*Source: based on EDP report (2024), Plan (2025) data SAO calculation and editing*

In 2022, the increase in fiscal revenues as a share of GDP (centralization rate) played a significant role in the improvement in the primary balance. In 2024, the improvement in the primary balance was more strongly driven by the decline in the net redistribution rate (1.3 percentage points) than by the increase in the estimated centralization rate (0.4 percentage point). In 2025, the committed deficit can be met even with a small decline in the centralization rate, while from 2026 onwards it will no longer play a role in the improvement of the primary balance, as we calculate that it will remain unchanged over the period 2026-2027, while the net redistribution rate will decline each year.

Conclusion: the planned reduction in the net redistribution rate, assuming nominal GDP and interest expenditure developments according to the plan and no change in other

expenditure, will ensure the necessary improvement in the general government sector balance and the primary balance without increasing the centralization rate. At the same time, there is no room for maneuver to reduce the centralization rate, assuming GDP growth as planned. An unchanged centralization rate is a challenge, as the steady increase in the centralization rate between 2021 and 2024 has also contributed to the improvement in the government sector balance. Fiscal consolidation over the next three years under the Plan is entirely based on government expenditure rising more slowly than nominal GDP, but this also implies that in the period 2025-2027, less and less government expenditure as a share of GDP will be financed each year.

### 3.3 Evolution of tax and contribution revenues between 2025 and 2027

The fact that the centralization rate is unchanged does not mean that the government revenue structure is unchanged. **Government tax and contribution revenues** account for about 80.0 percent of government revenues, so their evolution will be of crucial importance for budgetary processes in the 2025-2027 period. Therefore, we have focused our analysis on this. In addition to changes in the relevant legislation, the possibility that some tax revenues may increase faster than GDP growth will allow the tax revenue structure to be rearranged with unchanged tax revenues. A comparison of the three-year wage agreement for the years 2025-2027 and the macroeconomic forecast (macro forecast) for the 2025 budget bill suggests that the growth rate of wages will exceed the growth rate of nominal GDP, except in 2027, and may imply that consumption will also grow faster than nominal GDP. This would imply that taxes and contributions on earnings and taxes on consumption grow faster than nominal GDP, with the exception of 2027. This in turn implies that, with unchanged centralization rates, no other revenues need to be realized, for example tax cuts can be introduced or special taxes can be abolished/decreased. Therefore, calculations have been carried out to give an idea of the scope for reducing other taxes if earnings and consumption grow faster than nominal GDP.

In 2024, the gross wage and salary bill increased by 13.5 per cent until the end of November compared to the previous year, so this was taken as the estimated growth rate of the tax and contribution receipts in relation to earnings for the full year 2024, while the change in the gross wage and salary bill for the remaining years was taken as the basis for the macro forecast. The growth rate of tax revenues as a share of consumption is estimated by multiplying the change in consumer expenditure by the change in consumer price levels in the macro forecast. The estimated growth rate of tax revenues related to contributions from business organizations is estimated by the change in nominal GDP in the macro forecast. Based on our calculations, the

share of consumption-related taxes and contributions in the tax and contribution revenue of the central subsystem was 37.8 percent, the share of earnings-related taxes and contributions was 47.0 percent and the share of tax revenue from payments by business entities was 15.2 percent in 2023. Based on the actual tax and contribution revenue available for 2023 as a share of GDP and the above ratios, the nominal value of tax and contribution revenue in 2023 was determined by consumption, earnings and business organization contributions tax revenue categories. Starting from the nominal data for 2023, we estimated the tax and contribution revenues for the period 2024-2027. In the trajectory used as a benchmark, based on the 2018-2023 actual data, we stipulate that the value of tax and contribution revenues as a share of GDP in each year of the 2024-2027 period will be equal to the average value of the 2018-2023 actual data, i.e. 35.4 percent.

The results are presented in Table 5. (Actual data for 2024 are not yet available, so the estimated value of tax and contribution revenues is only used to draw conclusions for the period 2025-2027.)

**Table 5: Key tax and contribution revenue data 2023-2027 in HUF bn and in %**

| Title | Year 2023 (fact) | Year 2024 (prel. fact) | Year 2025 (plan) | Year 2026 (plan) | Year 2027 (plan) |
|---|---|---|---|---|---|
| 1.Nominal GDP, HUF billion (macro forecast value) | 75 086,6 | 81 791,4 | 87 954,5 | 94 497,8 | 101 685,7 |
| 2. Nominal GDP growth, percentage (macro forecast) | 13,5 | 8,9 | 7,5 | 7,4 | 7,6 |
| 3. Tax and contribution revenue as a percentage of GDP | 35,0 | *no data* | *no data* | *no data* | *no data* |
| 4. Tax and contribution receipts, HUF billion | 26 280,3 | *no data* | *no data* | *no data* | *no data* |
| 5. Consumption-related tax revenues, HUF bn (estimate) | 9 936,5 | *no data* | *no data* | *no data* | *no data* |
| 6. Earnings-related tax and contribution receipts, HUF billion (estimate) | 12 355,8 | *no data* | *no data* | *no data* | *no data* |
| 7. Tax receipts related to payments by business organizations, HUF bn (estimate) | 3 988,0 | *no data* | *no data* | *no data* | *no data* |
| 8. Estimated increase in consumption-related tax revenues, percentage | - | 7,8 | 7,7 | 7,6 | 7,6 |
| 9. Estimated increase in earnings-related tax and contribution receipts, percentage | - | 13,5 | 8,8 | 7,6 | 7,4 |
| 10. Estimated increase in tax receipts related to contributions from business organizations (line 2) | - | 8,9 | 7,5 | 7,4 | 7,6 |
| 11. Estimated tax and contribution receipts, HUF bn<br>(row 5 x row 8 + row 6 x row 9 + row 7 x row 10, based on 2023 data) | - | 29 078,3 | 31 462,9 | 33 844,8 | 36 384,1 |
| 12. Estimated change in tax and contribution receipts compared to the previous year, % | | 10,6 | 8,2 | 7,6 | 7,5 |
| 13. Estimated tax and contribution revenue as a percentage of GDP, % | - | 35,55 | 35,77 | 35,82 | 35,78 |
| 14. Assuming no change: Tax and contribution revenue as a percentage of GDP, % | - | 35,40 | 35,40 | 35,40 | 35,40 |
| **15. Potential tax and contribution revenue surplus as a percentage of GDP (line 13 - line 14)** | **-** | | **0,37** | **0,42** | **0,38** |
| **16. Potential tax and contribution revenue surplus, HUF bn (as a percentage of line 1 x line 15)** | **-** | | **327,0** | **392,5** | **387,4** |

*Source: Plan (2024) and calculated and edited on the basis of macro forecast data*

The data in the table show that if the ratio of tax and contribution revenues to GDP remained unchanged compared to 2024, it would amount to 35.4% of GDP over the period analyzed. However, under our estimated assumptions, they would increase to 35.8 percent of GDP in the period 2025-2027. The amount of this increase can be found in the last row of the table. This is therefore the amount that could be used for tax cuts, tax rate reductions or the abolition of

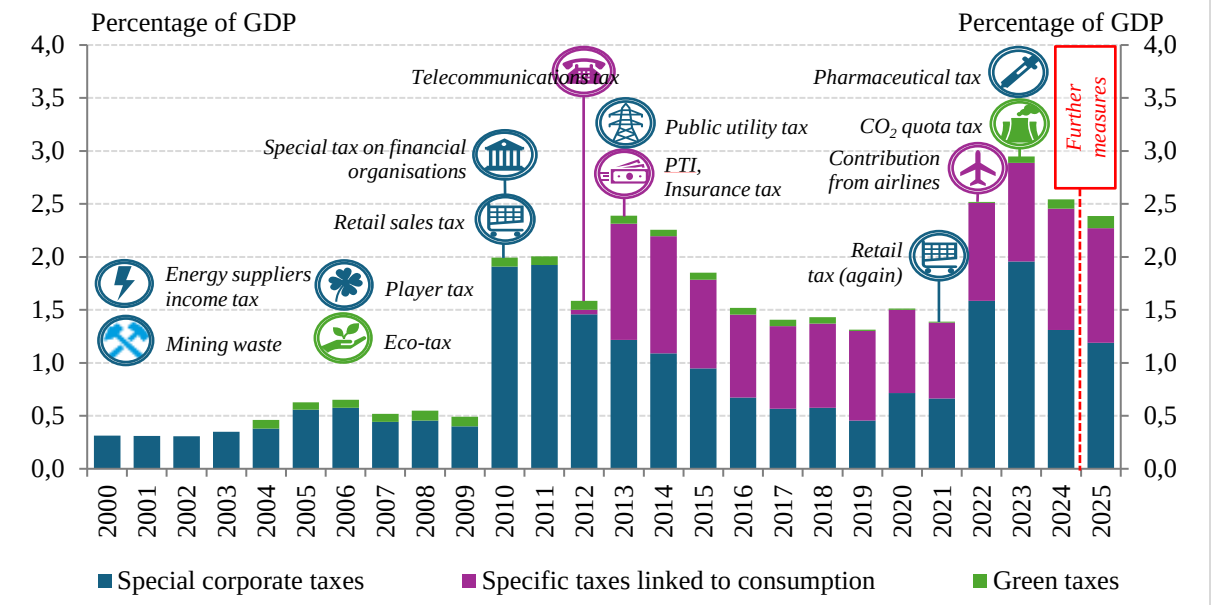
special taxes. Under this assumption, the tax surplus on consumption or earnings (assuming that tax revenues linked to farmers' contributions grow at the same rate as nominal GDP) cannot be used to increase net nationally financed primary expenditure, as this would exceed the maximum growth rate committed in the Plan. This amount will already be burdened in 2025 by the loss of revenue due to the increase in the family tax credit, which, under the law already adopted, will increase almost fourfold in 2026. In addition, under current legislation, the carbon quota tax and other extra-profit taxes could be phased out in 2026 (the oil price differential tax, the income tax on energy suppliers and, in the case of retail taxes, the rate increases linked to the extra-profit tax regime, the extra-profit tax on financial institutions and the insurance extra-profit tax).

Conclusion: If nominal GDP, the aggregate wage bill and household consumption expenditure in current prices evolve as projected by the government, there is room for a reduction in tax revenues of 0.4% of nominal GDP, which could take the form of the abolition of some special taxes, the extension of tax concessions or a reduction in the tax rate.

**The role of special taxes in the Hungarian budget**

**Special taxes are a major source of revenue for the Hungarian budget.** Revenues from special taxes could be around 2.5 percent of GDP in 2024. These taxes are typically levied on a single sector (e.g. financial institutions or retail trade), on a single product (e.g. oil) or single service (e.g. financial transactions). The impact of specific taxes directly affects only a subset of corporate actors. Three types can be distinguished: capital taxes (also known as corporate taxes), consumption taxes and green taxes.

**Figure 11: Evolution of specific tax revenues as a share of GDP between 2000 and 2025**




*Note: 2025 data is based on the 2025 budget appropriations.*

*Source: HCSO, MÁK, Budget Act 2025*

**The importance of special taxes increased significantly after 2010.** The first special taxes were introduced in the 1990s and 2000s (income tax on energy suppliers, mining tax), but the revenue from these taxes as a share of GDP rarely exceeded 0.5%. The special taxes introduced in the 2010 tax reform under the new public tax system, together with an increase in the weight of consumption tax revenues, offset the effect of the reduction in labour taxes and contributed significantly to fiscal consolidation. During this period, special taxes on capital (special tax on financial institutions, retail sales tax) have been the main source of special tax revenues, which have reached 2 percent of GDP.

**In the second half of the 2010 decade, the focus shifted from capital taxes to sales taxes within special taxes.** Increased budgetary room for maneuver has allowed for a reduction in the special taxes on capital, in particular on financial institutions. As a result, between 2015 and 2020, the share of turnover taxes (e.g. telecommunication tax, financial transaction tax or insurance tax) in total special tax revenue exceeded that of capital taxes.

**The crisis tax measures of the 2020 decade have led to a renewed rise in the role of special taxes.** In 2020, the special tax on financial institutions was temporarily increased for one year in response to the crisis related to the coronavirus epidemic, while in 2021, following the resolution of international litigation on the tax, the retail sales tax became part of the Hungarian tax system for the second time.

**The share of special taxes as a share of GDP increased significantly in 2022 with the introduction of extra profit taxes.** The budget expects to raise more than HUF 2,000 billion in 2025, equivalent to 2.4% of GDP. In response to the increased spending during the energy crisis, the government has introduced additional tax payments for certain sectors affected by the special taxes, called extra profit taxes, mainly on capital. In addition to increases in certain tax rates and extra profit tax obligations linked to previous year's payments, three new taxes have been introduced: the airline levy, the pharmaceutical tax and the carbon tax.

**The gradual reduction of special taxes started in 2024 and will continue in 2025, with an extra profit tax of 0.6% of GDP running out at the end of 2025 under current legislation.** The process of reducing special taxes has started with the introduction of various tax incentives (e.g. the tax credit for the extra profit tax on financial institutions linked to the purchase of government securities or the R&D tax base credit for the pharmaceutical tax). This was followed by the simplification of extra profit tax obligations and the complete abolition of several special taxes from 1 January 2025: utilities tax, pharmaceuticals tax and airline contributions. Under the current regime, the carbon quota tax and other extra-profit taxes could be phased out in 2026 (the oil price differential tax, the income tax on energy suppliers and, in the case of retail taxes, the rate increases linked to the extra-profit tax regime, the extra-profit tax on financial institutions and the insurance extra-profit tax).

**Table 6: Amount of certain specific taxes in 2025 and the amount of the special taxes to be phased out at the end of 2025**

| | 2025 appropriation | of which special taxes expiring at the end of 2025* |
|---|---|---|
| Income tax on energy suppliers | 297 | 90 |
| Insurance tax | 213 | 60 |
| Retail tax | 295 | 150 |
| Extra-profit tax on financial institutions | 253 | 150 |
| Carbon quota tax | 75 | 75 |
| **Total (bn HUF)** | **1133** | **525** |
| **Total (as percentage of GDP)** | **1,3** | **0,6** |

*Note: The Budget Act of 2025 does not include a separate appropriation for extra-profit taxes, which are included in the appropriations on the former special tax revenue lines.*

**Fiscal Council estimate included.*

*Source: Budget Law 2025, Fiscal Council*

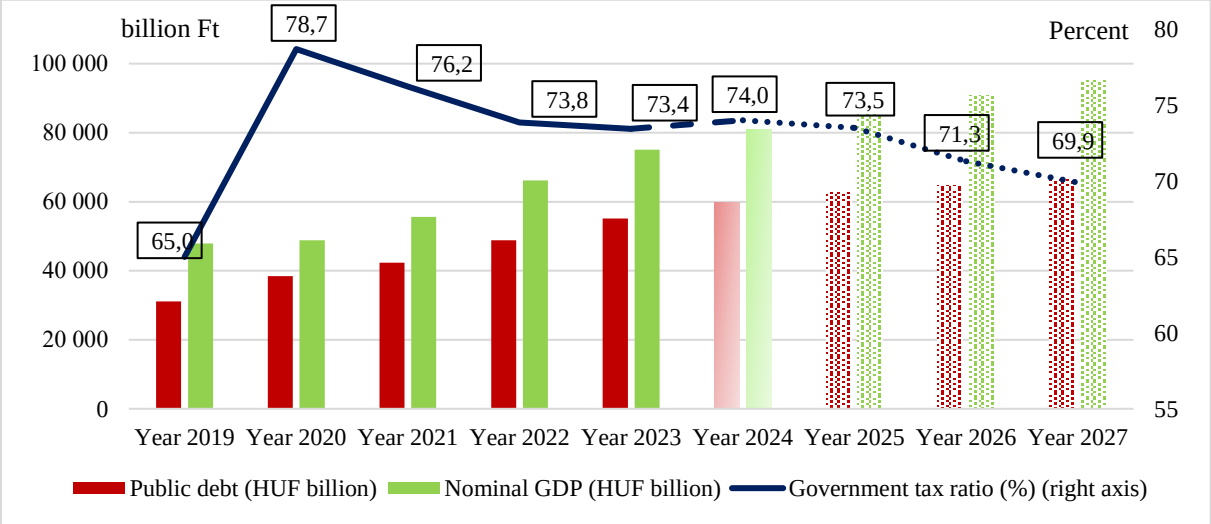
# 4. THE PUBLIC DEBT TARGETS FOR 2025-2027 AND THE RISKS ASSOCIATED WITH THEM

According to EU rules, the Plan must ensure that the government debt ratio is on a plausible downward path by the end of the adjustment period (2028) or remains on such a path.

## 4.1 Actual and projected evolution of the public debt indicator (2019-2027)

The evolution of the government debt indicator is determined by the change in the amount of government debt and nominal GDP. The denominator of the debt indicator, i.e. the amount of gross government debt, is basically determined by the primary balance and interest expenditure, which were discussed in the previous chapter, in addition to the previous year's base, while the denominator of the indicator is the evolution of nominal GDP. The actual and planned evolution of the debt indicator and its factors between 2019 and 2027 is shown in Figure 12.

**Figure 12: Evolution of public debt, nominal GDP and the public debt ratio between 2019 and 2027 in HUF bn and in percent**




*Note: 2024-2027 figures are Plan values*

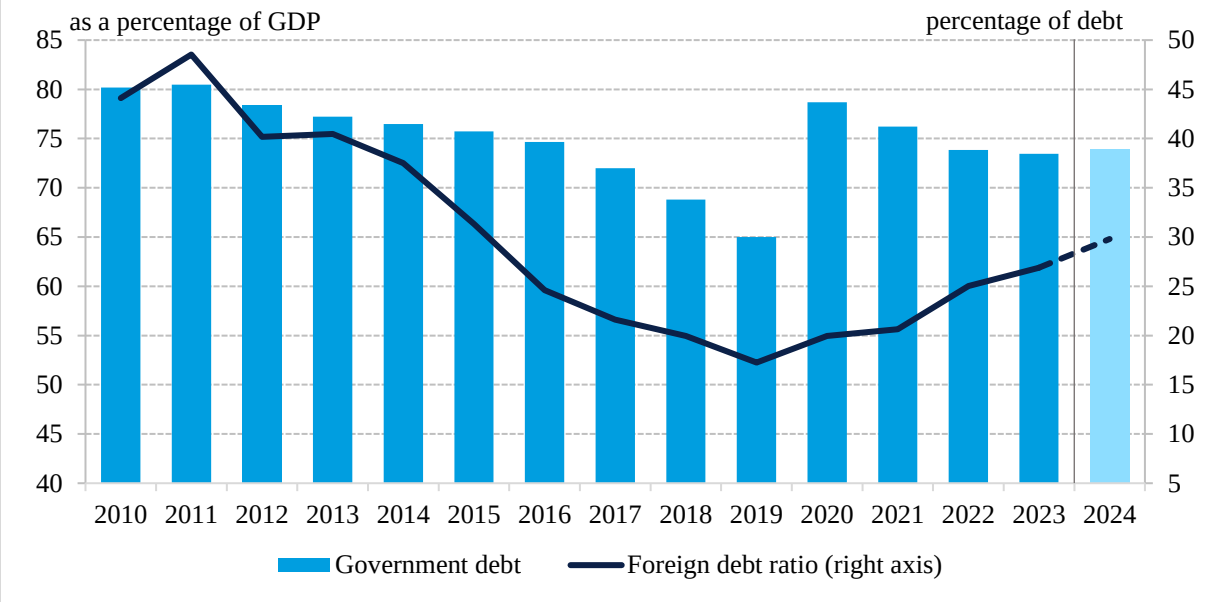
*Source: based on EDP report (2023, 2024), Plan (2025) SAO calculation and editing*

Figure 12 shows that, after a significant increase in 2020, the public debt ratio declined from 78.7% to 73.4% between 2021 and 2023, and then rose from 2023 to 74.0% (73.6% according to the MNB's preliminary financial account data) by the end of 2024. According to the Plan, the public debt ratio is projected to improve to 69.9 percent by the end of the period, declining steadily between 2025 and 2027, but still not expected to reach the end-2019 level of 65.0 percent.

**Public debt at the end of 2024**

**According to the preliminary fiscal accounts data released by the MNB, the gross public debt-to-GDP ratio at the end of 2024 rose to 73.6 percent (Figure 13),** 0.2 percentage point higher than the debt ratio at the end of 2023. The actual nominal GDP data will be published by the HCSO on 4 March, which may still change the evolution of the debt ratio compared to the preliminary data.

**Figure 13: Evolution of public debt**




*Source: ÁKK, MNB*

**The value of the debt ratio at the end of 2024 was strongly influenced by the repurchase of HUF 1,077 billion of government securities in two stages by the State Debt Management Centre Zrt. (ÁKK) from the Magyar Nemzeti Bank in December.** The repurchase helped to reduce government debt, thereby strengthening Hungary's risk perception and reducing financial vulnerabilities.

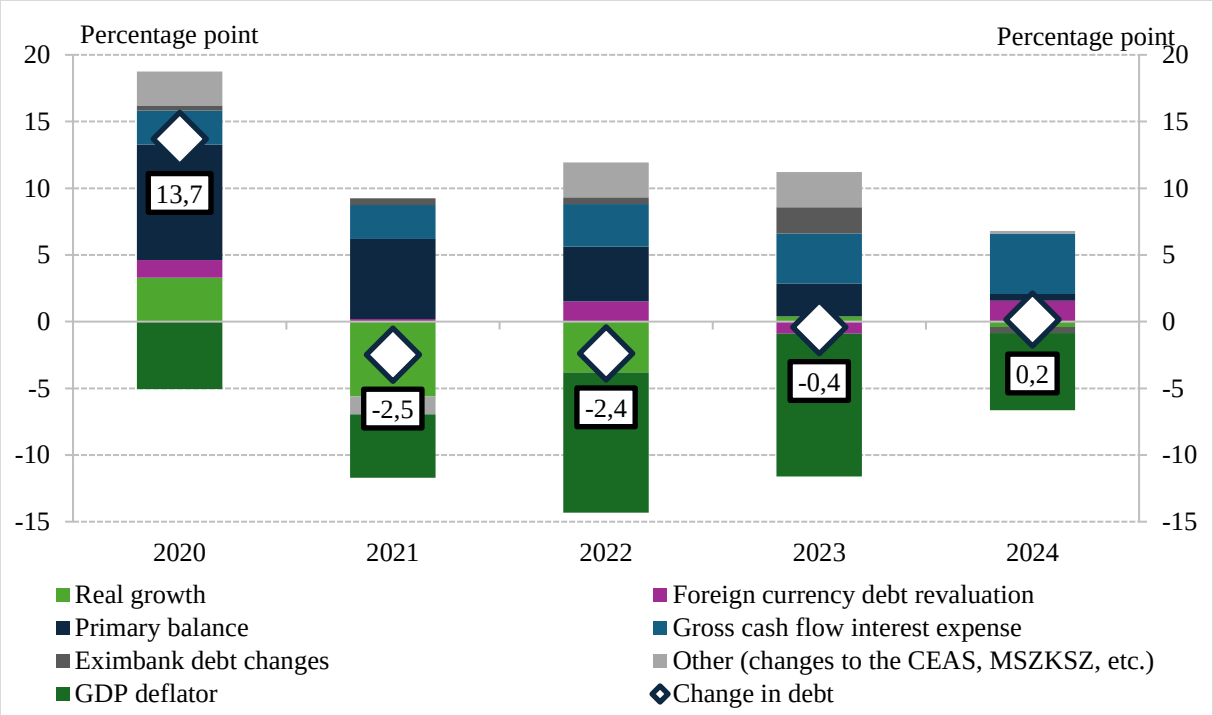
**The 2024 budget law included a 3 percentage point reduction in debt for 2024 compared to the 2023 debt indicator**. The EDP report submitted to Eurostat in the spring lowered the expectation for the debt reduction in 2024 to 0.3 percentage points. The autumn EDP report expected a debt reduction of 0.2 percentage points compared to the revised figure of 73.4% at the end of 2023.

**The 3 percentage point reduction in the debt-to-GDP ratio in 2024, as planned in the Budget Law, was not achieved due to a higher cash budget deficit, lower-than-expected GDP growth and a revaluation of foreign currency debt.** The 2024 budget law, adopted in 2023, projected a cash deficit of HUF 2,515 billion, GDP growth of 4 percent and an exchange

rate of 385.5 forint/euro. A higher-than-planned cash deficit of almost HUF 1,600 billion and lower-than-planned annual GDP growth of 0.5 percent significantly increased the year-end debt ratio. In addition, the end-2024 HUF/euro exchange rate of 410.1 per euro also contributed to the higher debt ratio through the revaluation of foreign currency debt compared to the original legal expectation. The share of foreign currency debt in central government debt was 29.8 percent, so a change of 10 forints in the forint/euro exchange rate changes the debt-to-GDP ratio by almost 0.6 percentage points.

**The 0.2 percentage point of GDP increase in debt in 2024 was mainly due to high current interest expenditure and the revaluation of foreign currency debt, partly offset by nominal GDP growth**. In 2024, gross current interest expenditure increased government debt by 4.6 percentage points, while the revaluation of foreign currency debt caused a 1.6 percentage point increase in debt, which was further increased by 0.5 percentage point by the primary cash deficit. These were partly offset by a combined debt-reducing effect of 6.2 percentage points from the GDP deflator and real economic growth, and 0.5 percentage point from the debt reduction of Eximbank's liabilities, which are classified as government debt (Figure 14).

**Figure 14: Factors driving the change in the public debt ratio in 2020-2024**




*Source: ÁKK, KSH, MNB, own calculation*

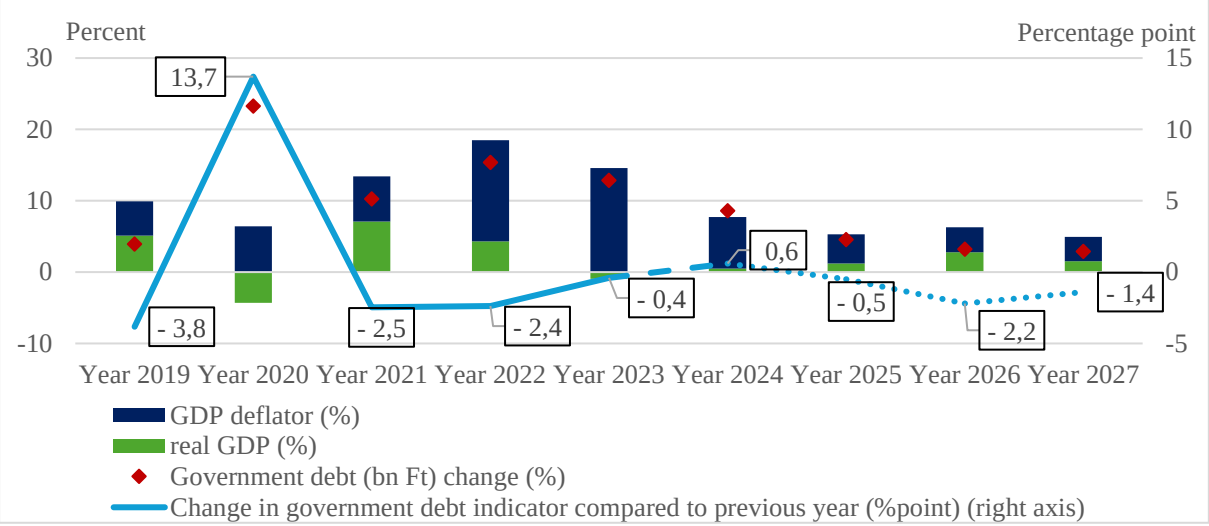
**The increase in the public debt ratio in 2024 does not violate the debt rule of the Constitution.** The provision states that only in times of special legal order or in the event of a sustained and significant downturn in the national economy may borrowing be used to

implement the central budget, which would result in an increase in the debt ratio compared to the previous year[15] . In view of the armed conflict in a neighbouring country, the government has declared a state of emergency, which constitutes a special legal order[16], thus providing an exemption from the debt rule of the Fundamental Law. Moreover, apart from the exempting factors, if the debt ratio were to increase during the implementation of the budget, the calculation of the debt ratio should not take into account, inter alia, the surplus of public debt resulting from the time needed to reimburse EU funds subsequently not accounted for in the budget, or from exchange rate fluctuations in transactions that create debt in foreign currency.[17]

### 4.1.1 The impact of real GDP and GDP deflator developments on the government debt indicator

The components of the public debt indicator have contributed/are contributing differently to the evolution of the indicator over the period analyzed, as illustrated in Figure 15.

**Figure 15: Change in the amount of government debt and nominal GDP[18] , and change in the value of the government debt indicator from the previous year, 2019-2027, in percentages**




*Note: 2024-2027 data are calculated from Plan data*

*Source: KSH STADAT 21.1.1.1., EDP report (2023, 2024), Plan (2025) based on SAO calculation and editing.*

It can be seen that in 2020, due to the adverse macroeconomic and budgetary effects of the coronavirus epidemic, the amount of public debt increased more than the value of nominal GDP (based on the combined effect of the GDP deflator and real GDP) compared to the previous

[15] Fundamental Law of Hungary, Articles 36 (6), 37 (2)-(3)
[16] Fundamental Law of Hungary, Article 51 (1)
[17] Act CXCIV of 2011 on the Economic Stability of Hungary, § 4 (3a), § 6 (1)
[18] GDP in real terms and GDP deflator

year, and therefore the value of the public debt indicator increased by 13.7 percentage points. However, from 2021 onwards, nominal GDP has increased, or is projected to increase, by more than the amount of government debt compared to the previous year, so the value of the debt indicator is projected to decrease year on year (except for the increase in 2024).

The graph shows that the improvement in the public debt indicator in the period 2021-2023 was mainly driven by a rapid increase in nominal GDP, above 10.0% year-on-year, and in 2023 only by the effect of the GDP deflator, with the economy contracting by 0.9% (real GDP). In 2024, the rate of inflation slowed significantly compared to 2022-2023, so that, overall, nominal GDP did not increase at the same rate as the amount of public debt (0.9 percentage points higher than nominal GDP compared to the previous year), due to the effect of the GDP deflator and modest economic growth (0.5 percent according to preliminary data). As a result, the government debt ratio is projected to rise from 73.4 percent at the end of 2023 to 74.0 percent at the end of 2024 (73.6 percent based on preliminary financial account data, according to the MNB's data release).

The Plan projects the debt ratio to decline over the period 2025-2027, with nominal GDP growth of around 5-6 percent (coupled with subdued economic growth) and the amount of public debt increasing at a declining annual pace. This would allow the debt ratio to be on a declining path in the years 2025-2027, with a stable but moderate economic growth rate of around 2 percent, and with a planned (moderate) increase in net nationally financed primary expenditure.

### 4.1.2 Correlations between the implicit interest rate on government debt and the planned and actual evolution of the GDP deflator

*The implicit interest rate on government debt (the average interest rate on the financial instruments (government bonds, loans) that finance government debt over a year) is basically determined by the nominal cost of financing (interest expenditure), which can be influenced by a number of factors. Among these factors, the evolution of benchmark yields in the government bond market and the average maturity of government debt are noteworthy. Reference yields in the government bond market are indirectly pushed up by higher inflation, which increases the implicit interest rate on government debt in future periods through higher interest rates on newly issued government bonds and floating rate government bonds. For newly issued government bonds, the repricing of debt starts with the rise in benchmark yields, with the increase in the implicit interest rate on government debt not occurring immediately but with a lag. When inflation declines, the process is reversed, but the effect of falling inflation is also*

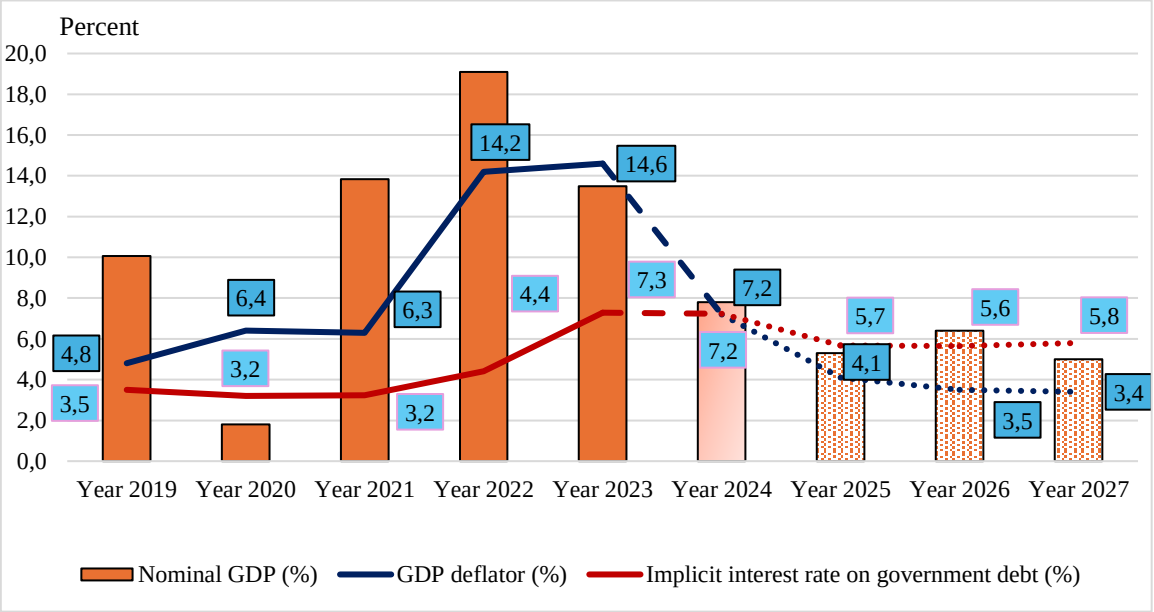
*delayed in the implicit interest rate. In addition, the implicit interest rate is also affected by the real yield available and the risk premium.*

The optimal level of the implicit interest rate on government debt varies across countries due to the complexity and the number of parameters involved, but in the case of Hungary, the optimal level was 3.5% in 2019 (when the debt ratio fell to 65.0% and a relatively low interest rate environment prevailed).

The GDP deflator and the implicit interest rate on government debt have opposite effects on the government debt indicator. While a higher GDP deflator lowers the value of the debt indicator due to a higher level of nominal GDP in a given year, an increase in the implicit interest rate on government debt raises the amount of government debt in a given year, which increases the value of the debt indicator.

The evolution of the GDP deflator and the implicit interest rate on government debt, as well as nominal GDP, is shown in Figure 16 for 2019-2027.

**Figure 16: Evolution of GDP deflator, implicit interest rate on government debt and nominal GDP in 2019-2027 in percent**




*Note: 2024-2027 figures are Plan values.*

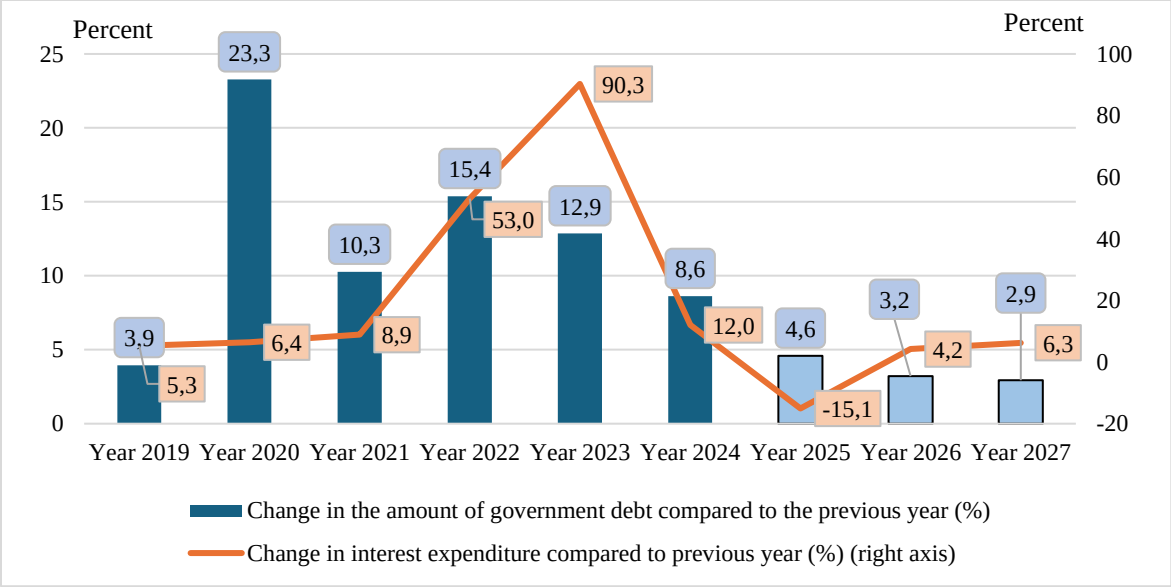
*Source: based on KSH STADAT 21.1.1.1., KP2020, KP2021, Plan (2025), SAO ed.*

The GDP deflator started to rise in 2021, as inflation and the exchange rate deterioration accelerated in the second half of 2021, and peaked in 2023. In contrast to the GDP deflator, the implicit increase in the interest rate on government debt shows a more subdued dynamic, but also a prolonged increase over time, as explained above.

The milestone for the two indicators was 2024, when the GDP deflator was just equal to the implicit interest rate on government debt (7.2 percent), according to the Plan data. The higher value of the GDP deflator than the implicit interest rate on government debt contributed to the decline in the debt indicator between 2020 and 2023, but from 2025 onwards, the implicit interest rate on government debt increases government debt at a higher rate than the GDP deflator increases nominal GDP, according to the Plan data. The result of these two effects would be an increase in the government debt ratio, which could be offset in other ways, partly by an improvement in the primary balance and partly by dynamic economic growth (with some minor items).

Although the implicit interest rate on government debt is expected to decline significantly from 2024 to 2025 (from 7.2% to 5.7%), thereafter, until the end of 2027, the implicit interest rate on government debt is projected to be higher than the GDP deflator and also higher than nominal GDP growth in 2025 and 2027 (which includes real growth in addition to the GDP deflator).

**Figure 17: Year-on-year change in government debt and interest expenditure between 2019 and 2027, percentage**




*Note: 2024-2027 figures are calculations based on the Plan.*

*Source: based on EDP (2024), Eurostat (2025) and Plan data, edited and calculated by SAO.*

Figure 17 shows that while the change in the amount of public debt was highest in 2020, the year of the COVID outbreak, interest expenditure increased only marginally during this period (despite the significant nominal debt increase) due to the low inflation environment. Interest expenditure growth was lower than debt growth until 2022, but this trend was reversed in 2022, with interest expenditure in 2023 90 percent higher than in the previous year as a result

of rising yields on inflation-linked government bonds due to high inflation. In 2025, the Plan projects interest payments to fall by 15.1 percent, with a rise from 2026 onwards, which could exceed the growth rate of the amount of debt (relative to the previous year).

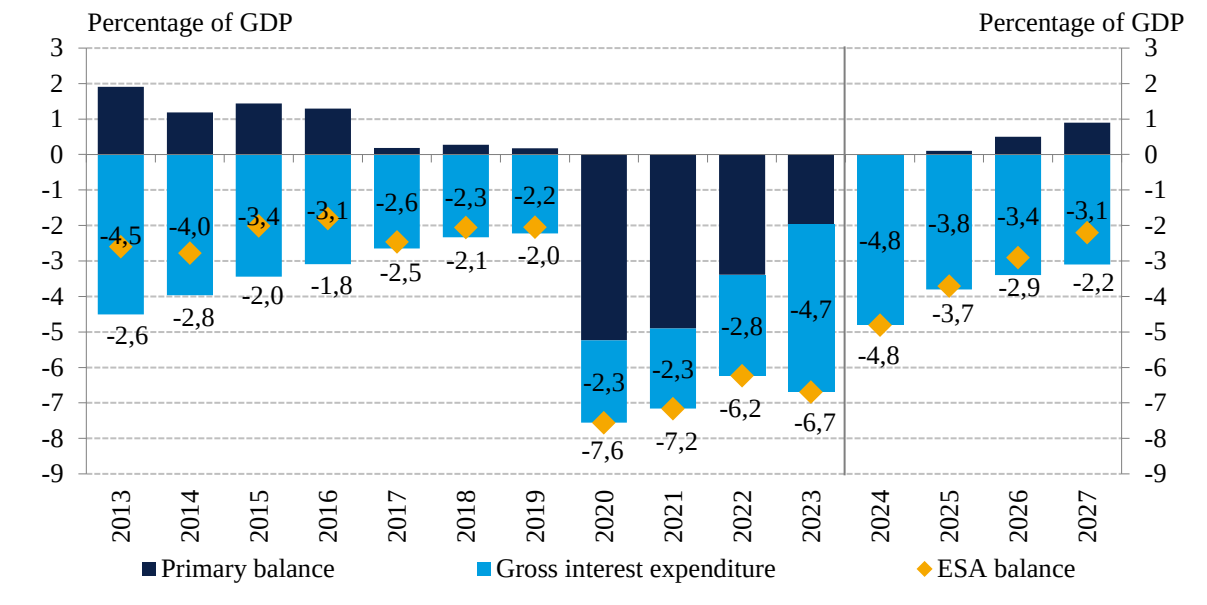
In addition to the above, changes in the exchange rate also affect the evolution of government debt. Given that the share of central foreign currency debt in government debt is close to 30 percent at the end of 2024, a more favorable evolution of the exchange rate of foreign currency debt than envisaged in the Plan would make it difficult to reduce the government debt ratio.

Conclusion: the challenge for the reduction of the public debt ratio between 2025 and 2027 is that the implicit interest rate on public debt is projected to be higher than the GDP deflator and even higher than the nominal GDP growth rate in 2025 and 2027. Therefore, a significant improvement in the primary balance is needed to improve the government debt ratio, as envisaged in the Plan.

**Reduced interest expenditure significantly supports deficit reduction**

**Between 2025 and 2027, the main driver of the decline in the budget deficit is a reduction in government interest expenditure.** Interest payments in the budget as a share of GDP on an accrual basis jumped in 2023, remained high in 2024 and could start to decline sharply in 2025. In 2025, however, interest payments could fall by 1 percent of GDP, leading to a similar improvement in the overall balance, while the primary balance could remain unchanged (Figure 18). Overall, the expected 1.9% improvement in the fiscal deficit-to-GDP ratio between 2024 and 2026 is mainly driven by a 1.4% decline in interest expenditure. This projection is broadly in line with the medium-term fiscal structural plan originally submitted in October 2024.

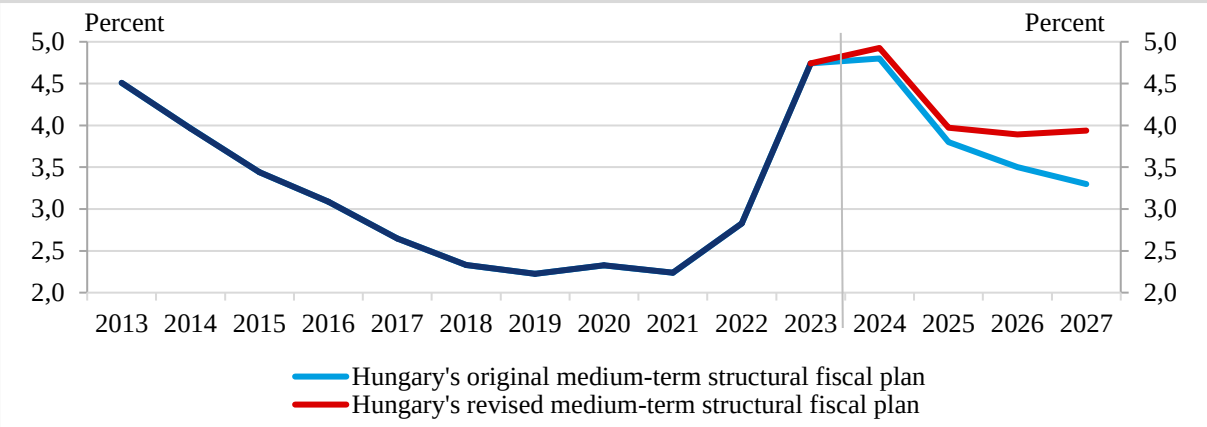
**Figure 18: Primary balance and accrued interest expenditure and ESA balance as a percentage of GDP**




*Source: HCSO, Convergence Programme, Budget Act 2025, Ministry of National Economy January 2025 announcement, MNB forecast*

**Hungary's revised medium-term fiscal structural plan expects substantially higher interest expenditure over the entire horizon than the originally submitted medium-term plan.** The plan, submitted in October 2024, projected government interest expenditure to fall to 3.8% of GDP this year, and to 3.1% by 2028. The revised plan, however, suggests that interest expenditure could stagnate at around 4 percent of GDP (Figure 19). The increase is driven by higher yield expectations, as short yields are expected to be close to 6 percent instead of 4-5 percent as previously expected, while long yields are expected to be around 6.5-7 percent instead of 5-6 percent, according to the new expectation.

**Figure 19: Changes in interest expenditure in Hungary's medium-term structural fiscal**

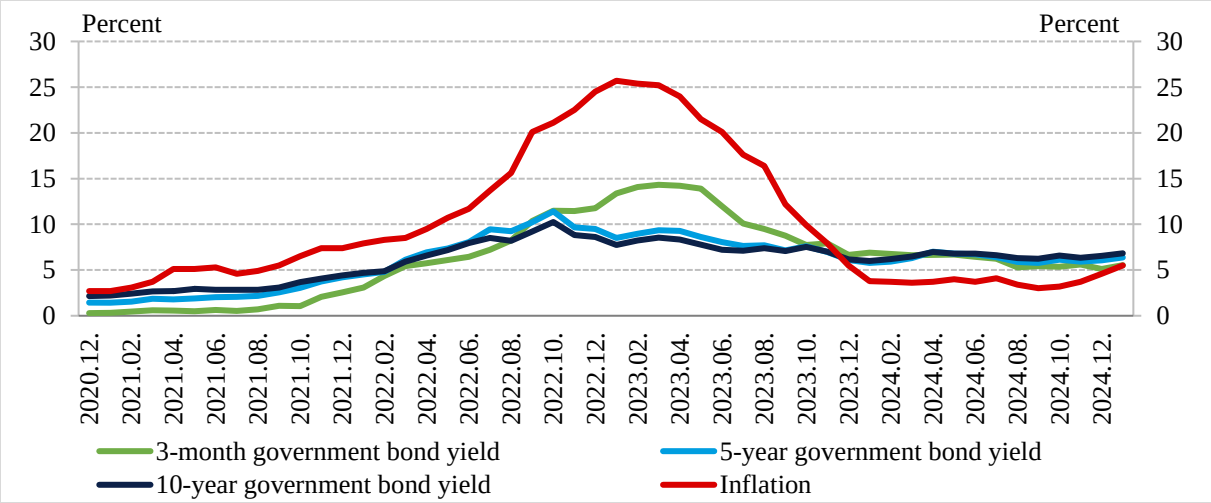



*Source: Hungary's original and amended medium-term structural fiscal plan*

**The cost of government debt is influenced by a number of factors based on its structure, these factors include inflation, inflation expectations, country risk perceptions, exchange rate developments and yields in domestic and international sovereign debt markets.** The structure of government debt is complex, consisting of a variety of liabilities and mainly debt instruments, government securities, which may have different interest rates, maturities and denominations. By looking at the structure of debt, we can estimate the share of interest expenditure that each factor affects.

**The evolution of government interest expenditure is mainly influenced by Hungary's risk perception, inflation and forward-looking inflation expectations.** According to data for 2024, inflation directly determines the interest rate on inflation-linked retail bonds, which represent 14% of the total stock of government bonds. In addition, the interest rate on long-term and fixed-rate securities, which account for almost half of government securities (46%), is determined by the developed market interest rate environment, inflation expectations and country risk perceptions, while the interest rate on foreign currency bonds, which account for 26% of government securities, is determined by the external interest rate environment and risk perceptions. The interest rates on short-dated discount notes (SDRs) and floating rate notes, which account for a smaller share of government bonds, 14%, depend on short-term interest rates.

**Figure 20: Inflation and benchmark government bond market yields**




*Source: ÁKK, KSH*

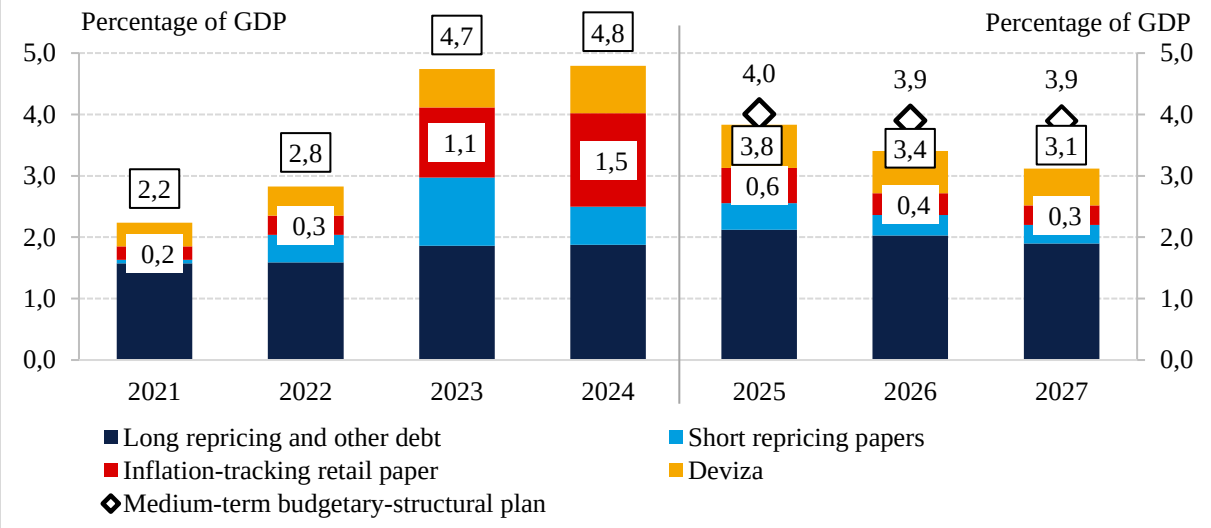
**The rise in interest expenditure has been mainly driven by the surge in inflation in recent years.** After a steady decline since 2013, government interest expenditure as a share of GDP rose to 2.8% of GDP in 2022 and further increased to 4.8% of GDP in 2024. Inflation developments play a significant role in the variation of interest expenditure. Inflation-linked

interest expenditure increased sharply from 1.1% of GDP in 2023 to 1.5% in 2024. Inflation has contributed to the increase in interest expenditure not only directly, but also indirectly, through the impact of the increase in holdings due to the popularity of inflation-indexed government bonds. Demand for inflation-linked retail paper has been strong, with the holdings of Premium Hungarian Government Securities and Baby Bonds rising from HUF 4,500 billion at end-2022 to close to HUF 7,360 billion at end-2024.

**Public ESA interest expenditure could fall to 3.8% of GDP in 2025 from 4.8% in 2024.** The reduction of 1 percentage point of GDP is mainly due to the repricing of inflation-linked government bonds to a lower inflation base in 2024. Interest expenditure on inflation-tracking government inflation-linked securities is less than halved in both nominal and GDP terms in 2025 compared to the previous year (from 1.5 percent of GDP to 0.6 percent) (Figure 21).

**Over the outlook horizon, interest expenditure will continue to decline to close to 3 percent of GDP.** The annual decline of 0.3-0.4 percent is mainly due to lower inflation and government bond market yields. The decline in inflation and short yields is reflected more rapidly in the decline in interest expenditure, while the decline in long yields is reflected more slowly in the decline in interest expenditure, due to different repricing times.

**Figure 21: Breakdown of accrued interest expenditure as a percentage of GDP**

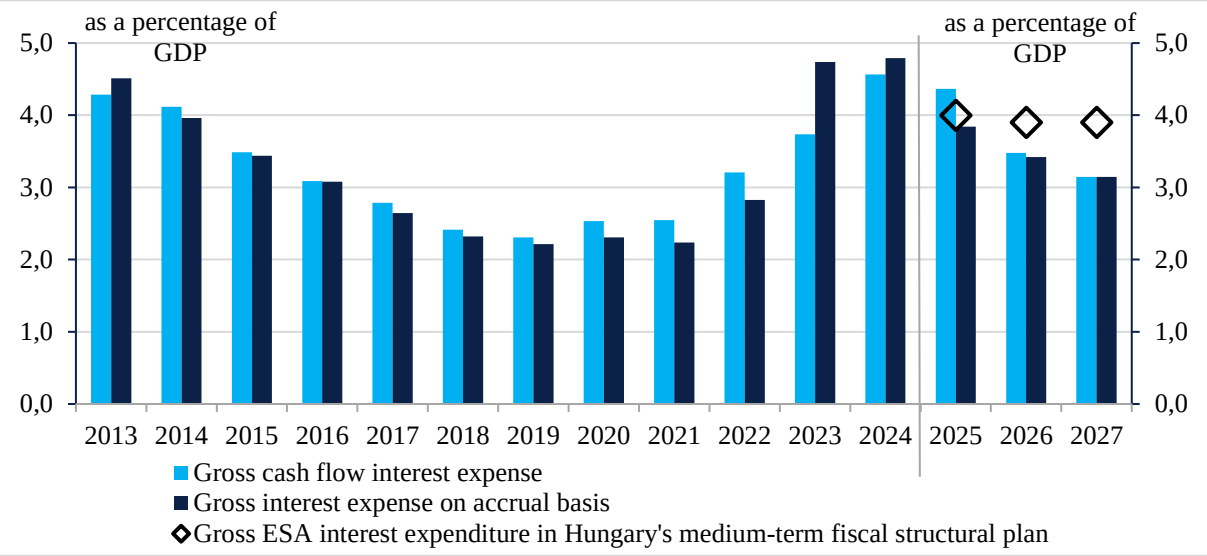



*Source: ÁKK, Eurostat, Hungary's medium-term fiscal-structural plan, 2024-2027 MNB forecast*

**The high interest expenditure due to inflation is already accounted for in the accrual balance in 2024, but will actually be paid in 2025, which will significantly increase the cash deficit in 2025.** There is a time lag between interest expenditure on a cash basis and on an accrual basis (Figure 22). On a cash basis, interest expenditure is recorded at the value date when the interest is actually paid. In accrual accounting, the yield paid for the period is spread

equally over each day of the year. Therefore, for the ESA interest expense, the effect of inflation in 2023 is already recorded in 2024, while the related interest payments are made in 2025.

**Figure 22: Evolution of gross cash flow and gross accrued interest expenditure as a percentage of GDP**




*Source: HCSO, Closing Accounts Acts, Hungary's Medium-Term Fiscal-Structural Plan and MNB Inflation Report based on MNB calculation and forecast*

# 5. THE RISKS ASSOCIATED WITH THREE MAJOR SPENDING AREAS OF THE GOVERNMENT

## 5.1 Evolution of public sector wages compared to the dynamic growth of competitive wages

The high wage dynamics that have characterized the competitive sector in recent years were also observed in the public sector, with average gross earnings in the competitive sector increasing by 50.9% and average gross earnings in the public sector by 51.5% between 2021 and 2024 (HCSO data). Meeting the Plan's commitment to increase net nationally financed primary expenditure (which the Plan expects to be a maximum of 4.3, 4.0 and 3.9 percent in 2025, 2026 and 2027, respectively) could be at risk if high wage dynamics persist over the next three years.

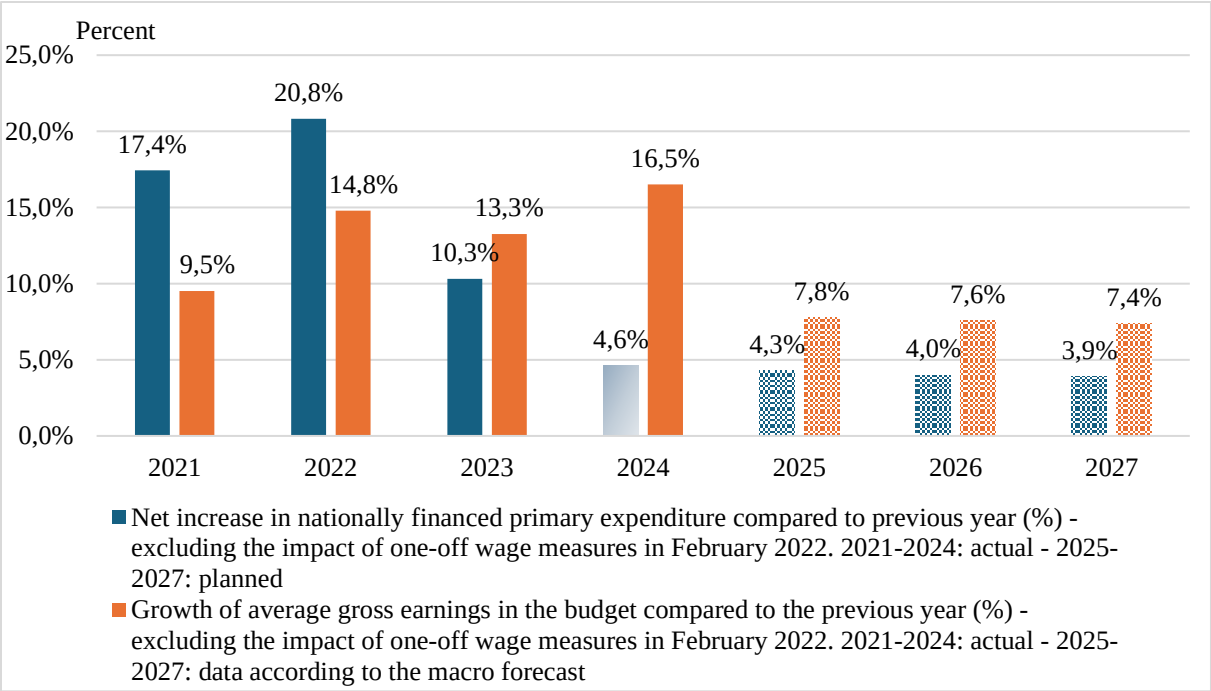
### 5.1.1 Trends in net nationally financed primary expenditure and changes in public sector wages

If wage growth, without any change in the number of public sector employees, persistently exceeds the increase in net nationally financed primary expenditure, it must be compensated by a reduction in other expenditure, as the additional expenditure cannot be financed by revenue increases.

In the following, it is assumed that between 2025 and 2027, the average gross public sector wage bill will evolve in line with the macro forecast used for the 2025 budget, so that public sector wages may increase by 7.8% in 2025, 7.6% in 2026 and 7.4% in 2027, and the number of employees is assumed to remain stagnant.

Figure 23 illustrates the growth in net nationally financed primary expenditure over the period 2021-2023 and the growth in net nationally financed primary expenditure over the period 2024-2027 under the Plan. The figure also shows the annual increase in average gross public sector earnings between 2021-2024 and the annual increase under the macro projection between 2025-2027.

**Figure 23: Growth in net nationally financed primary expenditure and average gross public sector compensation in [19]**




*Source: European Commission (2024) and based on KSH STADAT 20.1.1.41., edited by SAO*

The graph shows that in 2021 and 2022, the growth in net nationally financed primary expenditure exceeded wage growth, but in 2023 wage growth was slightly higher. In 2024 and later years, the Plan assumes that the growth in net nationally financed primary expenditure will be lower than in previous years, so that the growth in average gross earnings in the public sector would be significantly higher than the growth in average gross earnings in 2024 and later years under our assumption.

If wage growth substantially exceeds expenditure growth, the surplus must be saved elsewhere. Figure 23 illustrates that there would be a serious tension between dynamic public sector wage growth under the given assumption and subdued net expenditure growth. Therefore, the impact of the different dynamics has been quantified. Table 7 summarizes the amounts of increase in net nationally financed primary expenditure over the period 2025-2027 under the Plan and the amounts of increase in government expenditure on wages and public benefits under different wage increases. The baseline version of this is the macro forecast used as the basis for planning the 2025 budget, which projects average gross earnings in the budget to increase by 7.8 per cent in 2025, 7.6 per cent in 2026 and 7.4 per cent in 2027. However, we

[19] Actual data between 2021-2024, and Plan and macro forecast data between 2025-2027.

have also quantified fictitious growth rates in the table to illustrate the associated budgetary burden. The calculations in the table are based on projected values for 2024.

**Table 7: Growth in net nationally financed primary expenditure as committed in the plan and growth in expenditure on wages and public charges for different public sector wage increases between 2025 and 2027**

| Year | Net expenditure growth (HUF billion) | Amount of wage increase corresponding to the growth rate of net expenditure (HUF bn) | Amount of wage growth by macro level (HUF billion) | Amount of increase in wages and public charges (HUF billion) | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | | | | 4% | 5% | 6% | 7% | 8% | 9% |
| | | | | in the event of a wage increase | | | | | |
| 2025 | 1 461 | 367 | 667 | 342 | 427 | 513 | 598 | 684 | 769 |
| 2026 | 1 417 | 357 | 700 | 356 | 449 | 544 | 640 | 738 | 838 |
| 2027 | 1 437 | 362 | 734 | 370 | 471 | 576 | 685 | 797 | 914 |
| Total. | 4 315 | 1 086 | 2 101 | 1 068 | 1 347 | 1 633 | 1 923 | 2 219 | 2 521 |

*Source: Plan (2025) and KSH STADAT 21.2.1.26, and calculation and editing based on the macro forecast*

In the calculations, to determine the total increase in expenditure on wages, we have estimated the amount of expenditure on wages in 2024 based on preliminary data for the first three quarters of 2024, and increased this by the amount corresponding to the different wage growth paths, while for net nationally funded primary expenditure we have used the Plan figures. The figures in the table show that even with wage dynamics of 5 percent, the commitment to restrain spending is under strain.

Table 8 shows the amount of expenditure saved on wages and salaries and on expenditure other than public charges for different average annual wage increases. The figures in the table are calculated as the difference between the wage increases corresponding to the growth rate of net nationally financed primary expenditure and the expenditure increases on wages corresponding to each wage growth path.

**Table 8: Amount to be saved annually from non-wage expenditure of net nationally financed primary expenditure between 2025 and 2027 for different wage increases**

| Year | Amount to be saved from net expenditure other than wages and public charges (HUF bn) | | | | | |
|---|---|---|---|---|---|---|
| | In the case of a wage increase under the macro-pathway | 5 % | 6% | 7% | 8% | 9% |
| | | in the event of a wage increase | | | | |
| 2025 | 300 | 60 | 146 | 231 | 317 | 402 |
| 2026 | 343 | 92 | 187 | 283 | 381 | 481 |
| 2027 | 372 | 109 | 214 | 323 | 435 | 552 |
| Total | 1 015 | 261 | 547 | 837 | 1 133 | 1 435 |

*Source: Plan (2025) and KSH STADAT 21.2.1.26, and calculation and editing based on the macro forecast*

If spending on wages and their public charges increases by an average of 5 percent per year over the period 2025-2027, then HUF 261 billion in non-wage spending should be saved between 2025 and 2027, based on a ratio of wage spending to net nationally financed primary expenditure of 25.2 percent in 2024. Assuming that budget wages between 2025 and 2027 evolve according to the macro forecast used for the 2025 budget planning, savings of HUF 1 015 billion in non-wage expenditure are needed. An average annual wage increase of 9 percent over the period 2025-2027 would require total savings of HUF 1 435 billion at the expense of non-wage expenditure.

Conclusion: Based on the Plan, there is a risk for public sector wage growth, as either public sector wage growth will fall short of the macro forecast used for the 2025 budget planning - and thus also short of the dynamic wage growth of the competitive sector resulting from the three-year wage agreement - or a large reallocation of other budgetary expenditure will be necessary to raise public sector wages to a higher level.

### 5.2 Differences between pension and wage growth

The Plan includes the estimated pension expenditure as a share of GDP, which will decline steadily from 7.9% in 2024 to 7.8% in 2025, 7.7% in 2026 and 7.6% in 2027. Based on the Plan, Table 9 shows the evolution of pension expenditure and pension expenditure as a share of GDP estimated by the SAO for 2025-2027:

**Table 9: Projected pension expenditure as a share of GDP in 2025-2027[20]**

| | Title | Year 2024 | Year 2025 | Year 2026 | Year 2027 |
|---|---|---|---|---|---|
| 1 | Nominal GDP, HUF billion | 80 943,3 | 85 233,3 | 90 688,3 | 95 222,7 |
| 2 | Pension expenditure, HUF billion<br>(Previous year pension expenditure + line 12) | 6 209,6 | 6 552,4 | 6 862,4 | 7 173,3 |
| 3 | Inflation, percentage | | 3,2 | 3,0 | 3,0 |
| 4 | Inflation-linked increase in pensions, year/year, % | | 3,2 | 3,0 | 3,0 |
| 5 | Inflation-linked increase in pensions, HUF bn<br>(Previous year pension expenditure line 2 x line 4) | | 198,7 | 196,9 | 205,9 |
| 6 | Change in average net earnings, percentage | | 8,7 | 7,6 | 7,4 |
| 7 | Change in average net earnings - compared to previous year, percentage | | | 86,9 | 98,4 |
| 8 | Effect of replacement (% of previous year's base amount)<br>(% replacement rate in the previous year x row 7/100) | | 1,6 | 1,39 | 1,37 |
| 9 | Increase in pensions due to the replacement effect, HUF bn<br>(Previous year pension expenditure line 2 x line 8) | | 99,4 | 91,1 | 93,9 |
| 10 | Rate of change, percentage | | 0,8 | 0,4 | 0,2 |
| 11 | *Impact of changes in headcount on pension expenditure, HUF bn*<br>*(projected increase in pensions in the previous year due to staff changes, line 11 / change in staff in the previous year x line 10)* | | 44,7 | 22,4 | 11,2 |
| 12 | Increase in pension expenditure, HUF bn (line 5 + line 9 + line 11) | | 342,8 | 310,0 | 310,9 |
| **13** | **Pension expenditure as % of GDP (row 2 / row 1)** | | 7,7 | 7,6 | 7,5 |

*Sources: the Plan (2025), the 2025 Act on the Macro-Pension Expenditure, PM and MÁK data, based on the STADAT 21.2.1.1. of the Hungarian Central Statistical Office, the table of the 12th month of the 2024 budget, the 2025 Act on the Macro-Pension Expenditure, and the explanatory memorandum, SAO calculation and editing*

In calculating pension expenditure as a share of GDP, pension expenditure in the previous year was increased by the inflation-adjusted pension increase, the replacement effect and the

[20] The calculation was based on the actual nominal GDP in 2023 increased by the nominal GDP growth in the Plan 2024-2027, and the expected inflation and net nominal average earnings change based on the Macro Path 2025 provided by the PM. The estimate was based on the pension benefit expenditure from the Pension Insurance Fund in 2024. The pension expenditure in the previous year was increased in each year by the projected inflation rate as the pension increase in that year and by the estimated pension growth from the replacement effect. The percentage replacement effect for 2026-2027 was determined by adjusting the 2025 rate. The rate and amount of the 2025 staffing change were taken from the explanatory memorandum sent to the CCA for its opinion. The 2026-2027 rate of staffing change was the change (in percentage terms) in the number of people over retirement age expected in the 50-year demographic projection from the 2025 explanatory memorandum to the MFA Act. The additional expenditure for 2026-2027 due to the change in the number of employees was calculated using the formula: projected pension increase in 2025 (previous year) due to the change in the number of employees/rate of change in the number of employees in the previous year x rate of change in the number of employees in the current year.

change in the number of employees. The table shows that the rate of pension expenditure as a percentage of GDP calculated by the Fiscal Council is similar to the Plan rate for years 2025-2027, but 0.1 percentage points lower in each year, which is within the margin of error. Both the Plan data and our calculations indicate that savings as a share of GDP are only 0.1% per year.

However, if the increase in existing pensions follows inflation, the increase will be significantly below the projected increase in wages. At the same time, the replacement effect will significantly increase pension expenditure because of the increase in wages at a much higher rate than pensions, with about one third of the increase in pension expenditure being due to the replacement effect. This, together with the increase in the number of employees, will result in the growth rate of pension expenditure exceeding the growth rate of net nationally financed primary expenditure, albeit at a decreasing rate (1.2 - 0.7 - 0.6 percentage points).

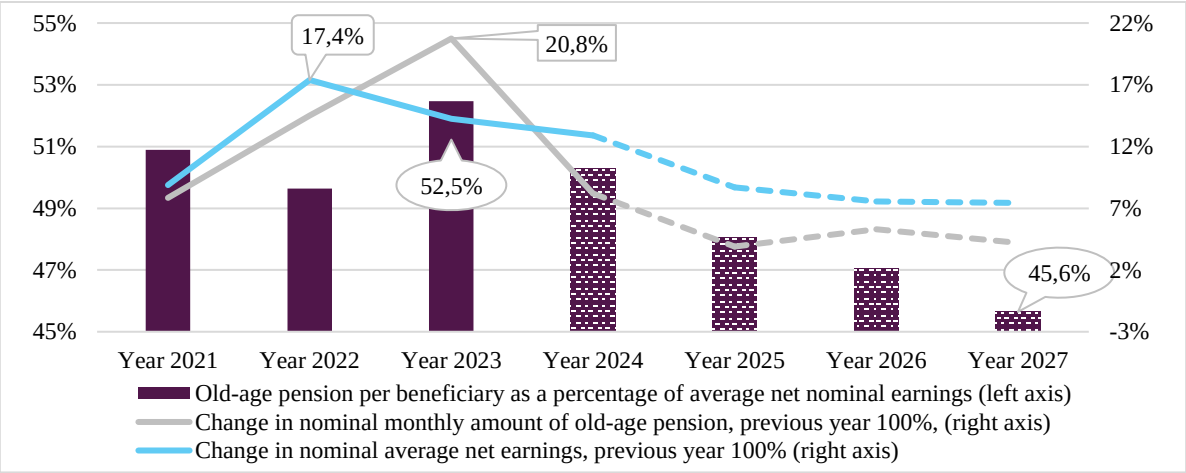
**Table 10: Change in net nationally financed primary expenditure by plan and estimated pension expenditure, in percent**

| Ssz. | Title | Year 2024 | Year 2025 | Year 2026 | Year 2027 |
|---|---|---|---|---|---|
| 1. | Net increase in nationally financed primary expenditure (previous year 100%) | 4,6 | 4,3 | 4,0 | 3,9 |
| 2. | Change in pension expenditure (Table 9, line 2, previous year 100%) | | 5,5 | 4,7 | 4,5 |
| 3. | Difference (line 2 - line 1) | | 1,2 | 0,7 | 0,6 |

*Sources: the Plan (2025), the 2025 Act (Macro Forecast, Pension Expenditure), PM and MÁK data, based on the STADAT 21.2.1.1. of the HCSO, the 2025 Act and its explanatory memorandum, SAO calculation and editing*

The same can be seen in Figure 24, which shows the actual change in (net) wages and old-age pensions per capita in 2021-2023 and the estimated change in 2024-2027.

**Figure 24: Old-age pensions as a share of average net nominal earnings and their change between 2021 and 2027, in percent[21]**




*Source: KSH STADAT 25.2.1.4., 20.1.1.57., based on the Plan (2025) and the Macroplane PM 2025 data, SAO calculation and editing*

Average earnings increase more significantly in 2022 and pensions in 2023. From 2024 onwards, the nominal monthly amount of old-age pensions will increase at a decreasing rate under the Plan, which is in line with the government's projections for inflation developments as set out in other documents. However, the year-on-year increase in old-age pensions will thus be 2-5 percentage points below the increase in average earnings. The old-age pension per beneficiary (which already includes the replacement effect) as a percentage of average net nominal earnings reached its highest value (52.5 percent) in 2023, with a scissors opening from 2024 onwards.

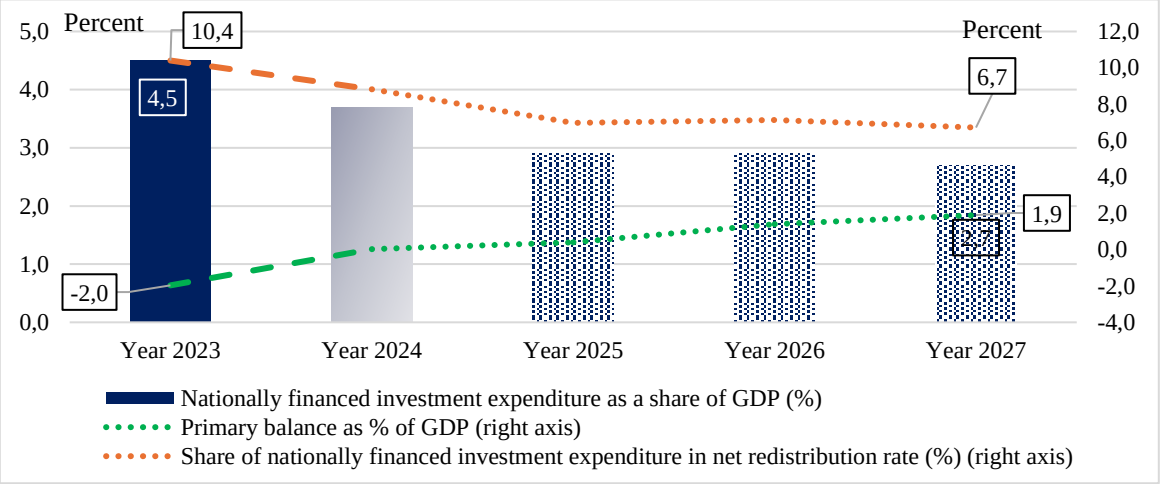
Conclusion: Despite the fact that pensions are increasing at the rate of inflation, the challenge is that budgetary expenditure on pensions is expected to increase at a higher rate than net expenditure due to the replacement effect and the increase in the number of employees, and therefore this will have to be met by below average increases in other expenditures.

### 5.3 Reduction in nationally financed public investment expenditure and its expected impact

One means of reducing government expenditure is to curb GFCF accumulation expenditure, within which the Plan details the projected evolution of nationally financed investment expenditure as a share of GDP over the period 2023-2027. The government decided to postpone or reschedule a number of investments from 2022 onwards. The government's spending restraint on investment will improve the primary balance, as shown in Figure 25.

[21] The figures for 2021-2023 are factual, the pension increase for 2024-2027 is the Plan, and the increase in net nominal average earnings for 2025-2027 is the force projected on the basis of the macro path of the 2025 budget law.

**Figure 25: Evolution of nationally financed investment expenditure and primary balance as a percentage of GDP and the ratio of nationally financed investment expenditure to the net redistribution rate, 2023-2027, in percent**




*Note: 2024-2027 figures are Plan values*

*Source: based on Plan (2024[22] , 2025), edited and calculated by SAO*

Figure 25 shows that, based on the Plan data, nationally financed investment expenditure is projected to decrease in 2024 compared to 2023, remain at the same level in 2025-2026, and then decrease slightly as a share of GDP and as a share of the net redistribution rate by 2027. The data also show that the Plan projects the weight of public investment spending to fall mainly from 2024 to 2025 (from 3.7 percent to 2.9 percent of GDP and from 8.8 percent to 7.0 percent of GDP as a share of GDP and within the net redistribution rate), while it remains essentially unchanged in 2026 and 2027. However, it is also important to highlight that nationally financed investment spending as a share of GDP in 2027 (2.7 percent) will be substantially lower than in 2023 (4.5 percent).

Conclusion: Reducing and then keeping low nationally financed investment expenditure plays a significant role in reducing the general government deficit, but it cannot yet contribute to an increase in the investment rate for the economy as a whole in the period 2025-2027. As nationally financed investment expenditure excludes EU-funded investment, a larger drawdown of EU funds than at present could significantly boost public investment.

[22] Data as at 4 November 2024 for nationally financed investment expenditure

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**EU regulations**

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