

## **IMF: The Orbán-package may fail due to the austerity measures**

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- *Actions plans, “big announcements”, Szell Kalman Plan, Convergence Programme, Hungarian Labor Plan – there are many events in connection with the government’s economic policy. How consistent do you think the announced or already delivered measures are?*
- Consistent with what, the IMF’s expectations or something else?
- *Also with them or with the promises of the election campaign. But it can also be interesting to compare each of these to each other (IMF-expectations, election promises, actions).*
- As I am not an elector, I would not like to make any comment on campaign promises, and I would also like to look forward rather than into the past. We know that there have been difficulties and we did not agree in some issues in the past. But the announcement of the Szell Kalman Plan and some related measures brought a 180 degree turnover in the government’s economic policy.
- *Compared to what has it brought a 180 degree turnover?*
- We clearly expressed our criticism last October and in January, so let me only say that we did not have the same opinion about several economic policy measures before the adoption of the 2011 budget. But we welcome the developments happened since then. As we underlined in the recent IMF Staff Report, the direction and targets of the Szell Kalman Plan and the Convergence Programme are very welcome in general and most of them are consistent with our policy recommendations expressed last year or even earlier. Finally, there are structural measures on the agenda. But of course we have to wait for the implementation.
- *Do you think the targets and measures of the Szell Kalman Plan, the Convergence Programme or the Labor Plan contain consistent targets and measures?*
- The first two do, while we have only recently got to know the Labor Plan, thus before forming an opinion, it looks like a framework for further specific measures, so I would like to know the detailed measures related to the plan before forming an assessment. The details are the most important here as well – this is the real test of how the government plans to achieve the otherwise good goals (growth and higher employment).

- *Look at growth first: the government calculates with a “dynamic” and a “conservative” growth path but there are some people who consider even the latter projections as questionable. Do you think the planned growth rate is achievable?*
- We are in the conservative camp: we project growth of 2.6% in 2011. In 2012, the growth is projected at 2.5% in 2012, mainly because fiscal adjustment affect domestic demand negatively in 2012 before boosting growth to around 3% later.
- *We can hear many numbers on how many jobs will be created in the next couple of years. What is your projection until 2014?*
- I think we do not have enough information as of now to give you a definite answer. The government itself projects to be the main driver of the job creation in the coming few years, which is a temporary solution. The most important source of job creation should be the private sector.
- *This is one of the main source of criticism in Hungary against the government’s plans: it is not clear how people getting used to digging ditches or doing jobs which do not need high qualification under the public works will be able to find a job. Do you see any chance of this?*
- This is one of the big challenges of the program. It is important to have a strategy which shows how the transition from public works to private employment happens, so that there are clear goals and expectations of the government’s labor market programs. We do not know yet how the government wants to go through this transition process. Boosting employment sustainably is a challenge, there have been multiple approaches in international practice.
- *For example?*
- For example differentiated minimum wage, let’s say to allow for regional differentials. The key is to align real wages with productivity improvement – that would bring motivation for both employees and employers. Labor market programs also included training component, which, if well-focused, can be especially important in Hungary – since here, as you mentioned – an important problem is that there are many less qualified among long-time unemployed, and it is difficult to qualify them for new areas.
- *It seems that the government is going in the opposite way: they would issue a decree on wage hikes. What do you think of this?*
- I would not like to pre-comment the proposals since they are still proposals. We will see what the final version being at the Parliament contains. But it is true in general that flexible wage policy is favorable for the labor market in the long term. The Hungarian economy and economic growth is still weak, wage growth is contained, and economic

participants need to be able to accommodate to the situation – if they perceive wage pressures, they may react with lay-offs. The most important issue for each enterprise is to be able to grow, thereby also increasing employment – to achieve this, they need to cur their expenditures (even their wage bill). This is especially true for SMEs who in general do not have a lot of “fat” to cut and hence are the most price- and cost- sensitive segment.

- *It is clear that there are budgetary constraints, mainly because the introduction of the flat PIT system resulted in revenue shortfall of HUF 500 bn per year while the government's expectations have not been achieved, i.e. the new system is not favorable for everybody. What do you think of the flat PIT system?*
- We have expressed concerns last fall that the tax changes will produce a structural revenue shortfall which will have to be compensated. We also saw risks that the tax reform could produce smaller boost to consumption growth than expected by the government last Fall , Anyway, it is all water under the bridge now, the tax reform has already been implemented it does decrease the taxation of higher labor incomes, and let's see whether it will result in sizeable employment gains. This is the most important –we have to look forward and pay attention to how growth can be increased.
- *The IMF's most recent report criticizes the Szell Kalman Plan in many points and considers many steps risky. What are the most important sources of danger according to you?*
- I would highlight one of them: the sustainability of the measures as they affect the most vulnerable groups of the society. While we are fully supportive of the objectives to boost labor participation, at the same time several of the measures such as the reduction in welfare benefits, , together with the tax reform will affect the lowest-income groups. This could generate social tensions which can make the implementation of the programme more challenging, since if there are social tensions, the planned measures may also have to be amended.
- *What are your proposals instead of these?*
- Uor key advise has been instead of the across-the-board cuts in social benefits, they should be better targeted (in terms of incomes) to protect the vulnerable, those who really need social support. By taking the benefits away from those who do not need it—I mean higher-income groups, the funds would be freed for other purposes, such as protecting the vulnerable or active labor programs, or debt reduction.
- *It is interesting what you are saying, as electors not familiar with the IMF usually think that the IMF always wants to cut welfare benefits. And now it turns out that you consider this as one of the most important problems. Does the Szell Kalman Plan contain so tough austerity measures that you think there will be social tensions?*

- I can imagine why people may have such opinions about the IMF, but it is not true. We never appear in a country because its economy performs very well but rather because the situation is bad. And we do not advise cuts for the sake of cuts, only when there is a problem which needs a fiscal restructuring – for example, the most important vulnerability of Hungary through the recent crisis has been its high level of public debt. How can one fight against this? With budget savings or growth. For this, reforms are necessary but there is no big maneuvering room. As in a war: you do what you have to do. But even with these, we always pay attention to social issues and political risks, and looking for the right mix of fiscal measures that can produce savings in the long-term, in a sustainable way. A programme has to be socially sustainable as well, then it has a higher chance of being implemented and followed through. That is why we are always wary about across-the-board expenditure cuts – instead we would like to see targeted, multi-year savings. Especially as in the case of across-the-board cuts, expenditures usually start to increase in the longer term.
- *Interesting that you used the word ‘war’ similarly to PM Orban recently...*
- I did not want to plagiarise anybody...I meant when the crisis hits, one needs to do what needs to be done.
- *I did not assume it. I just mentioned this, as the PM argues that the most important goal is to reduce public debt. Should this really be the main focus?*
- Debt reduction, growth, employment increase – these goals are all important together, and they are interconnected. Without employment, there is no growth and while debt is so high, the economy is vulnerable. These goals are very reasonable, but I can only repeat myself: we have to wait for the implementation.
- *What do you think of the nationalization of private pension system? Is it an appropriate tool?*
- We have analyzed this in details earlier, thus I would rather not go into details again on this issue. If these funds are at least partly used for debt reduction, it is better than to use them to finance current spending. The main question is what will happen to the funds not used for debt reduction, what are the structural deficit targets, and whether they bring debt to GDP ratio down – the Szell Kalman plan goes in the right direction, but one needs to analyze the 2012 budget in detail to understand this.
- *What do you think of China purchasing Hungarian government bonds?*
- We do not have any information on this, thus I cannot comment it.

- *The IMF also wrote in its report that “the government reversed most of its fiscal achievements reached during the programme” (those achieved during the Bajnai-government – the editor) What do you mean under that?*
- We mean the change in the structural budget deficit, which is an important concept from the point of view of fiscal sustainability. To be very specific: structural deficit declined by almost 3% during 2008-2009, while it is expected to increase by 1.6% over 2010-2011, thus undoing part of the earlier reduction.
- *What chance do you see for the government’s expectations being achieved until 2014?*
- This is not a question of optimism or pessimism. We have published our projections based on the assumption that the government implements the Szell Kalman Plan and delivers measures in time.
- *How long time does the government have?*
- The government set deadlines for itself. They are ambitious (brave), have been met with a lot of optimism from the markets, which is positive but also creates a pressure to meet those high expectations.
- *Greece is on the edge of default, there are other EU countries which may default, the US has a record-high debt, China is fear of increasing inflation – do you think that there may come a crisis even bigger than the 2008 one?*
- This is the 1-million dollar question and I would be happy if I knew the exact answer. Both governments across the world and international institutions learnt a lot from the 2008 crisis, thus everybody is working hard on preventing a new crisis and finding a sustainable growth solution. Coming back to my favorite country, Hungary, these turbulences you mentioned yet again highlight that the global economy is still vulnerable, thus a small and open economy as Hungary have to be cautious and follow the most responsible policies.
- *Will the eurozone survive these years?*
- I do not want to answer this question.
- *And do you think the government’s announcement that it does not want to join the eurozone until 2020 was a smart idea?*
- As an IMF-employee, I would not like to comment on this, as it is a purely national decision,--but I think – whenever the euro adoption happens – one has to use this period as an extra incentive to implement or complete all the reforms which make the country able to comply with the conditions of the euro adoption, and be at its most competitive.