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COUNCIL RECOMMENDATION

of 21 October 2024

on economic, budgetary, employment and structural policies of Hungary

(C/2024/6824)

THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 121(2) and Article 148(4) thereof,

Having regard to Regulation (EU) 2024/1263 of the European Parliament and of the Council of 29 April 2024 on the effective coordination of economic policies and on multilateral budgetary surveillance and repealing Council Regulation (EC) No 1466/97 ([1]), and in particular Article 3(3) thereof,

Having regard to Regulation (EU) No 1176/2011 of the European Parliament and of the Council of 16 November 2011 on the prevention and correction of macroeconomic imbalances ([2]), and in particular Article 6(1) thereof,

Having regard to the recommendation of the European Commission,

Having regard to the resolutions of the European Parliament,

Having regard to the conclusions of the European Council,

Having regard to the opinion of the Employment Committee,

Having regard to the opinion of the Economic and Financial Committee,

Having regard to the opinion of the Social Protection Committee,

Having regard to the opinion of the Economic Policy Committee,

Whereas:

(1) Regulation (EU) 2021/241 of the European Parliament and of the Council ([3]), which established the Recovery and Resilience Facility ('the Facility'), entered into force on 19 February 2021. The Facility provides financial support to the Member States for the implementation of reforms and investments, entailing a fiscal impulse financed by the Union. In line with the priorities of the European Semester for economic policy coordination, the Facility helps achieve the economic and social recovery and implement sustainable reforms and investments, in particular reforms and investments to promote the green and digital transitions and to make the Member States' economies more resilient. It also helps strengthen public finances and boost growth and job creation in the medium and long term, improve territorial cohesion within the Union and support the continued implementation of the European Pillar of Social Rights.

(2) Regulation (EU) 2023/435 of the European Parliament and of the Council ([4]) ('the REPowerEU Regulation'), which was adopted on 27 February 2023, aims to phase out the Union's dependence on Russian fossil-fuel imports. This would help achieve energy security and diversify the Union's energy supply, while increasing the uptake of

([1]) OJ L, 2024/1263, 30.4.2024, ELI: http://data.europa.eu/eli/reg/2024/1263/oj.
([2]) OJ L 306, 23.11.2011, p. 25, ELI: http://data.europa.eu/eli/reg/2011/1176/oj.
([3]) Regulation (EU) 2021/241 of the European Parliament and of the Council of 12 February 2021 establishing the Recovery and Resilience Facility (OJ L 57, 18.2.2021, p. 17, ELI: http://data.europa.eu/eli/reg/2021/241/oj).
([4]) Regulation (EU) 2023/435 of the European Parliament and of the Council of 27 February 2023 amending Regulation (EU) 2021/241 as regards REPowerEU chapters in recovery and resilience plans and amending Regulations (EU) No 1303/2013, (EU) 2021/1060 and (EU) 2021/1755, and Directive 2003/87/EC (OJ L 63, 28.2.2023, p. 1, ELI: http://data.europa.eu/eli/reg/2023/435/oj).

renewables, energy storage capacities and energy efficiency. Hungary added a new REPowerEU chapter to its national recovery and resilience plan in order to finance key reforms and investments that will help achieve the REPowerEU objectives.

(3) On 16 March 2023, the Commission issued a communication entitled 'Long-term competitiveness of the EU: looking beyond 2030', in order to inform policy decisions and create the framework conditions for increasing growth. The communication frames competitiveness in terms of nine mutually reinforcing drivers. Among those drivers, access to private capital, research and innovation, education and skills, and a functioning single market emerge as paramount policy priorities for reform and investment to address current productivity challenges as well as to build up the long-term competitiveness of the Union and its Member States. On 14 February 2024, the Commission issued a communication entitled 'The 2024 Annual Single Market and Competitiveness Report'. That communication details the competitive strengths and challenges of the European single market, tracking yearly developments according to the nine competitiveness drivers identified.

(4) On 21 November 2023, the Commission adopted the 2024 Annual Sustainable Growth Survey, marking the start of the 2024 European Semester for economic policy coordination. On 22 March 2024, the European Council endorsed the priorities of the 2024 Annual Sustainable Growth Survey, which are centred around the four dimensions of competitive sustainability. On 21 November 2023, on the basis of Regulation (EU) No 1176/2011, the Commission also adopted the 2024 Alert Mechanism Report, in which it identified Hungary as one of the Member States that may be affected, or may be at risk of being affected, by imbalances and for which an in-depth review would be needed. The Commission also adopted a recommendation for a Council recommendation on the economic policy of the euro area and a proposal for the 2024 Joint Employment Report, which analyses the implementation of the Employment Guidelines and the principles of the European Pillar of Social Rights. The Council adopted the Recommendation on the economic policy of the euro area ([5]) ('the 2024 Recommendation on the euro area') on 12 April 2024 and the Joint Employment Report on 11 March 2024.

(5) On 30 April 2024, the Union's new economic governance framework entered into force. The framework includes the new Regulation (EU) 2024/1263 on the effective coordination of economic policies and multilateral budgetary surveillance, the amended Council Regulation (EC) No 1467/97 ([6]) on speeding up and clarifying the implementation of the excessive deficit procedure, and the amended Council Directive 2011/85/EU ([7]) on requirements for the budgetary frameworks of Member States. The objectives of the new economic governance framework are to promote sound and sustainable public finances, sustainable and inclusive growth and resilience through reforms and investments, and prevent excessive government deficits. The new economic governance framework also promotes national ownership and has a greater medium-term focus, combined with more effective and coherent enforcement. Each Member State has to submit to the Council and to the Commission a national medium-term fiscal-structural plan. A national medium-term fiscal-structural plan contains the fiscal, reform and investment commitments of a Member State, covering a planning horizon of 4 or 5 years, depending on the regular length of the national legislative term. The net expenditure ([8]) path in the national medium-term fiscal-structural plans has to comply with the requirements of Regulation (EU) 2024/1263, including the requirements to put or keep general government debt on a plausibly downward path by the end of the adjustment period, or for it to remain at prudent levels below 60 % of gross domestic product (GDP), and to bring and/or maintain the general government deficit below the 3 %-of-GDP Treaty reference value over the medium term. Where a Member State commits to a relevant set of reforms and investments in accordance with the criteria set out in Regulation (EU) 2024/1263, the adjustment period can be extended by up to 3 years. For the purpose of supporting the preparation of those national medium-term fiscal-structural plans, on 21 June 2024, the Commission published guidance on the information to be provided by Member States in their national medium-term fiscal-structural plans and in their annual progress reports. In accordance with Articles 5 and 36 of Regulation (EU) 2024/1263, the Commission transmitted to the Member States reference trajectories and technical information, where applicable. Member States have to submit their national medium-term fiscal-structural plans by 20 September 2024, unless the Member State and the Commission agree to extend the deadline by a reasonable period of time. In accordance with their national legal

([5]) Council Recommendation of 12 April 2024 on the economic policy of the euro area (OJ C, C/2024/2807, 23.4.2024, ELI: http://data.europa.eu/eli/C/2024/2807/oj).

([6]) Council Regulation (EC) No 1467/97 of 7 July 1997 on speeding up and clarifying the implementation of the excessive deficit procedure (OJ L 209, 2.8.1997, p. 6, ELI: http://data.europa.eu/eli/reg/1997/1467/oj).

([7]) Council Directive 2011/85/EU of 8 November 2011 on requirements for budgetary frameworks of the Member States (OJ L 306, 23.11.2011, p. 41, ELI: http://data.europa.eu/eli/dir/2011/85/oj).

([8]) Net expenditure as defined in Article 2, point (2), of Regulation (EU) 2024/1263: 'net expenditure' means government expenditure net of (i) interest expenditure, (ii) discretionary revenue measures, (iii) expenditure on programmes of the Union fully matched by revenue from Union funds, (iv) national expenditure on co-financing of programmes funded by the Union, (v) cyclical elements of unemployment benefit expenditure, and (vi) one-offs and other temporary measures.

frameworks, Member States may debate their draft medium-term plans with their national parliaments, may ask the independent fiscal institutions to issue an opinion, and may conduct a consultation of social partners and other national stakeholders.

(6) In 2024, the European Semester for economic policy coordination continues to evolve in line with the implementation of the Facility. The full implementation of the recovery and resilience plans remains essential for delivering the policy priorities under the European Semester, as the plans help effectively address all or a significant subset of challenges identified in the relevant country-specific recommendations issued in recent years. The 2019, 2020, 2022 and 2023 country-specific recommendations remain equally relevant for the recovery and resilience plans which have been revised, updated or amended in accordance with Articles 14, 18 and 21 of Regulation (EU) 2021/241.

(7) On 11 May 2021, Hungary submitted its national recovery and resilience plan to the Commission, in accordance with Article 18(1) of Regulation (EU) 2021/241. Pursuant to Article 19 of Regulation (EU) 2021/241, the Commission assessed the relevance, effectiveness, efficiency and coherence of the recovery and resilience plan, in accordance with the assessment guidelines set out in Annex V to that Regulation. On 15 December 2022, the Council adopted its Implementing Decision on the approval of the assessment of the recovery and resilience plan for Hungary ([9]), which was amended on 8 December 2023 pursuant to Article 18(2) of Regulation (EU) 2021/241 to include the REPowerEU chapter ([10]). The release of instalments is conditional on the adoption of a decision by the Commission, in accordance with Article 24(5) of Regulation (EU) 2021/241, stating that Hungary has satisfactorily fulfilled the relevant milestones and targets set out in the Council Implementing Decision.

(8) On 30 April 2024, Hungary submitted its 2024 National Reform Programme and its 2024 Convergence Programme, in line with Article 8(1) of Council Regulation (EC) No 1466/97 ([11]). In accordance with Article 27 of Regulation (EU) 2021/241, the 2024 National Reform Programme also reflects Hungary's biannual reporting on the progress made in achieving its recovery and resilience plan.

(9) On 19 June 2024, the Commission published the 2024 country report for Hungary. It assessed Hungary's progress in addressing the relevant country-specific recommendations adopted by the Council between 2019 and 2023 and took stock of Hungary's implementation of the recovery and resilience plan. On the basis of that analysis, the country report identified gaps with regard to those challenges that are not addressed or only partially addressed by the recovery and resilience plan, as well as new and emerging challenges. It also assessed Hungary's progress in implementing the European Pillar of Social Rights and in achieving the Union headline targets on employment, skills and poverty reduction, as well as progress in achieving the United Nations Sustainable Development Goals.

(10) The Commission carried out an in-depth review under Article 5 of Regulation (EU) No 1176/2011 for Hungary. The main findings of the Commission staff's assessment of macroeconomic vulnerabilities for Hungary for the purposes of that Regulation were published in April 2024. On 19 June 2024, the Commission concluded that Hungary is experiencing macroeconomic imbalances. In particular, Hungary faces vulnerabilities related to price pressures and external and government financing needs, which remain relevant, although an improving external environment has mitigated some short-term risks. The large current account deficit closed in 2023 as domestic demand shrunk amid a recession in Hungary and as a result of lower energy prices. Together with tighter monetary policy, those factors helped reduce the very high inflation rate. Nevertheless, core inflation has remained among the highest in the Union, and unit labour costs have continued to grow strongly, exerting pressure on competitiveness The current account is expected to revert to a small deficit in 2024 as domestic demand recovers, while the economy and its external financing remain exposed to developments in energy prices and risk premia. House prices slowed down and overvaluation eased in 2023 against the backdrop of higher interest rates. The large budget deficit persists on account of expansionary policies in previous years and weaker than expected growth in 2023. The deficit is forecast to narrow somewhat, but to remain significant and to continue contributing to inflation and adding to external borrowing needs. The government debt-to-GDP ratio and the interest burden are set to remain elevated. Policy progress has been limited across all areas, particularly fiscal and structural ones, contributing to the persistence of the identified vulnerabilities. A fiscal adjustment would contribute to reducing core inflation and strengthening the external position as well as containing rises in government debt; the launch of an excessive deficit procedure should underpin such an adjustment. The timely and effective implementation of the recovery and resilience plan is

([9]) ST 15447/22 INIT and ST 15447/22 ADD 1.

([10]) Council Implementing Decision of 8 December 2023 amending the Implementing Decision of 15 December 2022 on the approval of the assessment of the recovery and resilience plan for Hungary (ST 15964/1/23 REV 1 and ST 15964/23 ADD 1).

([11]) Council Regulation (EC) No 1466/97 of 7 July 1997 on the strengthening of the surveillance of budgetary positions and the surveillance and coordination of economic policies (OJ L 209, 2.8.1997, p. 1, ELI: http://data.europa.eu/eli/reg/1997/1466/oj).

expected to help reduce vulnerabilities, which would be reinforced by the phasing-out of distortive interventions in markets and by reforms that support fiscal consolidation.

(11) According to data validated by Eurostat, Hungary's general government deficit increased from 6,2 % of GDP in 2022 to 6,7 % in 2023, while the general government debt fell from 74,1 % of GDP at the end of 2022 to 73,5 % at the end of 2023. As announced in the Commission's communication of 8 March 2023 entitled 'Fiscal policy guidance for 2024', the Commission is taking the first step for the opening of deficit-based excessive deficit procedures on the basis of the outturn data for 2023, in line with existing legal provisions. On 19 June 2024, the Commission issued a report under Article 126(3) of the Treaty. That report assessed the budgetary situation of Hungary, as its general government deficit in 2023 exceeded the 3 %-of-GDP Treaty reference value. The report concluded that, in light of that assessment, and after considering the opinion of the Economic and Financial Committee formulated pursuant to Article 126(4) of the Treaty, the Commission intends to propose in July 2024 to open an excessive deficit procedure for Hungary, by proposing that the Council adopt a decision under Article 126(6) of the Treaty establishing the existence of an excessive deficit situation in Hungary.

(12) On 12 July 2022, the Council recommended ([12]) that Hungary take action to ensure in 2023 that the growth of nationally financed primary current expenditure is in line with an overall neutral fiscal policy stance, taking into account continued temporary and targeted support to households and firms most vulnerable to energy price hikes and to people fleeing Ukraine. At the same time, the Council recommended that Hungary stand ready to adjust current spending to the evolving situation. It also recommended that Hungary expand public investment for the green and digital transitions, and for energy security taking into account the REPowerEU initiative, including by making use of the Facility and other Union funds. In 2023, according to the Commission's estimates, the fiscal stance ([13]) was contractionary, at 4,7 % of GDP, in a context of high inflation. The growth in nationally financed primary current expenditure (net of discretionary revenue measures) in 2023 provided a contractionary contribution to the fiscal stance of 1,7 % of GDP. The growth in nationally financed primary current expenditure in 2023 was in line with the Council Recommendation of 12 July 2022. However, it is important to note that this was largely driven by the very high level of net expenditure in 2022 compared to 2023, including untargeted expenditure in several areas, which contributed to macroeconomic imbalances, financed by a windfall profit and sectoral taxes levied on companies mainly in the energy, financial and retail sectors. Nationally financed investment amounted to 4,6 % of GDP in 2023, representing an increase of 0,2 percentage points as compared to 2022. Hungary financed public investment for the green and digital transitions and for energy security, such as energy-efficiency enhancements and digitalisation in healthcare and education. Hungary has not yet submitted a payment request under the Facility.

(13) In the 2024 Convergence Programme, the macroeconomic scenario underpinning the budgetary projections projects real GDP growth at 2,5 % in 2024 and 4,1 % in 2025, while projecting inflation measured by the harmonised index of consumer prices (HICP) at 4,2 % in 2024 and 3,6 % in 2025. The general government deficit is expected to decrease to 4,5 % of GDP in 2024 and stand at 3,7 % of GDP in 2025, while the general government debt-to-GDP ratio is set to decrease to 73,2 % by the end of 2024 and 72,1 % by the end of 2025. After 2025, the general government deficit is projected to decrease gradually to 2,9 % of GDP in 2026, to 2,4 % in 2027 and to 1,9 % in 2028. Therefore, the general government balance is planned to go below the 3 %-of-GDP Treaty deficit reference value in 2026. In turn, after 2025, the general government debt-to-GDP ratio is projected to decrease gradually to 68,8 % in 2026, to 66,0 % in 2027 and to 62,8 % in 2028.

(14) The Commission's 2024 spring forecast projects real GDP to grow by 2,4 % in 2024 and 3,5 % in 2025, and inflation measured by HICP to stand at 4,1 % in 2024 and 3,7 % in 2025.

([12]) Council Recommendation of 12 July 2022 on the 2022 National Reform Programme of Hungary and delivering a Council opinion on the 2022 Convergence Programme of Hungary (OJ C 334, 1.9.2022, p. 136.).

([13]) The fiscal stance is defined as a measure of the annual change in the underlying budgetary position of the general government. It aims to assess the economic impulse stemming from fiscal policies, both those that are nationally financed and those that are financed by the Union budget. The fiscal stance is measured as the difference between (i) the medium-term potential growth and (ii) the change in primary expenditure net of discretionary revenue measures (and excluding temporary emergency measures related to the COVID-19 crisis) and including expenditure financed by non-repayable support (grants) under the Facility and other Union funds.

(15) The Commission's 2024 spring forecast projects a government deficit of 5,4 % of GDP in 2024, while the general government debt-to-GDP ratio is set to increase to 74,3 % by the end of 2024. The decrease in the deficit in 2024 mainly reflects a gradual recovery of tax revenues, lower spending on subsidies to utility companies for the losses incurred due to caps on residential energy prices, and a decrease in public investments. The increase in the debt-to-GDP ratio is driven by a high headline deficit, lower nominal GDP growth and additional debt-increasing transactions, such as the expected acquisition of the Budapest airport by entities classified in the general government sector and the implementation of financial instruments supported under REPowerEU loans. According to the Commission's estimates, the fiscal stance is projected to be contractionary by 1,0 % of GDP in 2024.

(16) Expenditure amounting to 0,8 % of GDP is expected to be financed by non-repayable support ('grants') under the Facility in 2024, compared to 0,3 % of GDP in 2023, according to the Commission's 2024 spring forecast. Expenditure financed by grants under the Facility will enable high-quality investment and productivity-enhancing reforms without a direct impact on the general government balance or debt of Hungary. Expenditure amounting to 0,4 % of GDP is expected to be backed by loans from the Facility in 2024, compared to 0,0 % of GDP in 2023.

(17) On 14 July 2023, the Council recommended ([14]) that Hungary ensure a prudent fiscal policy, in particular by limiting the nominal increase in net nationally financed primary expenditure ([15]) in 2024 to not more than 4,4 %. When executing their 2023 budgets and preparing their budgets for 2024, Member States were invited to take into account that the Commission would propose to the Council the opening of deficit-based excessive deficit procedures on the basis of the outturn data for 2023. According to the Commission's 2024 spring forecast, Hungary's net nationally financed primary expenditure is projected to increase by 3,6 % in 2024, which is below the recommended maximum growth rate. However, net expenditure in 2023 was higher than expected at the time of the recommendation (by 1,8 % of GDP). Had net expenditure in 2023 been the same as expected at the time of the recommendation, the resulting growth rate of net expenditure in 2024 would have been above the recommended growth rate by 1,5 % of GDP. Therefore, according to the Commission, taking into account the base effect resulting from higher-than-expected net expenditure in 2023, there is a risk that net nationally financed primary expenditure will not be fully in line with what was recommended by the Council.

(18) Moreover, the Council recommended that Hungary take action to wind down the emergency energy support measures in force, using the related savings to reduce the government deficit, as soon as possible in 2023 and 2024. The Council further recommended that, if renewed energy price increases necessitate new or continued support measures, Hungary ensure that such support measures are targeted at protecting vulnerable households and firms, are fiscally affordable, and preserve incentives for energy savings. According to the Commission's 2024 spring forecast, the net budgetary cost ([16]) of energy support measures is estimated at 1,6 % of GDP in 2023 and projected at 0,9 % in 2024 and 0,4 % in 2025. In particular, subsidies to utility companies for the losses incurred due to caps on residential energy prices are assumed to remain in force in 2024 and 2025. If the related savings were used to reduce the government deficit, as recommended by the Council, those projections would imply a fiscal adjustment of 0,6 % of GDP in 2024, whereas net nationally financed primary expenditure provides a contractionary contribution to the fiscal stance of 1,9 % of GDP in that year. According to the Commission, the emergency energy support measures are not projected to be wound down as soon as possible in 2023 and 2024. There is a risk that this will not be in line with what was recommended by the Council. However, the related savings are projected to be fully used to reduce the government deficit. This is in line with the Council recommendation. The budgetary cost of emergency energy support measures targeted at protecting vulnerable households and firms is estimated at 0,0 % of GDP in 2024 (0,1 % in 2023), of which 0,0 % of GDP preserves the price signal to reduce energy demand and increase energy efficiency (0,1 % in 2023).

(19) In addition, the Council also recommended that Hungary preserve nationally financed public investment and ensure the effective absorption of grants under the Facility and of other Union funds, in particular to foster the green and digital transitions. According to the Commission's 2024 spring forecast, nationally financed public investment is projected to decrease from 4,6 % of GDP in 2023 to 4,0 % of GDP in 2024. This is largely due to the cuts and postponements in nationally financed investment projects announced by the authorities in light of the high projected deficits. There is a risk that this will not be in line with what was recommended by the Council. In turn, public expenditure financed from revenues from Union funds, including grants under the Facility, is expected to increase from 0,8 % of GDP in 2023 to 1,7 % of GDP in 2024. This increase is due to a projected pickup in the

([14]) Council Recommendation of 14 July 2023 on the 2023 National Reform Programme of Hungary and delivering a Council opinion on the 2023 Convergence Programme of Hungary (OJ C 312, 1.9.2023, p. 155).

([15]) This contribution is measured as the change in general government primary expenditure, net of (i) the incremental budgetary impact of discretionary revenue measures, (ii) one-offs, (iii) cyclical unemployment expenditure and (iv) expenditure financed by non-repayable support (grants) under the Facility and other Union funds, relative to the medium-term (10-year) average potential nominal GDP growth rate, expressed as a ratio to nominal GDP.

([16]) The figure represents the level of the annual budgetary cost of those measures, including revenue and expenditure and, where applicable, net of the revenue from taxes on windfall profits of energy suppliers.

absorption of the Union cohesion policy funding from the 2020-2027 programming period and higher expenditure on investments supported by the Facility.

(20) On the basis of the policy measures known at the cut-off date of the forecast and on a no-policy-change assumption, the Commission's 2024 spring forecast projects a government deficit of 4,5 % of GDP in 2025. The decrease in the deficit in 2025 mainly reflects higher value-added tax and personal income tax revenue supported by stronger growth, a further decrease in subsidies to utility companies for the losses incurred due to caps on residential energy prices, and lower interest expenditure due to decreasing coupon payments on inflation-linked retail bonds. At the same time, the planned phasing-out of temporary windfall-profit and sectoral taxes levied since 2022, in line with their sunset clauses, is set to have a debt-increasing impact. The general government debt-to-GDP ratio is set to decrease slightly to 73,8 % by the end of 2025. Prudent fiscal policy should contribute to reducing core inflation, which is well above the Union average and could lead to competitiveness losses if persistent, and should also contribute to strengthening the external position.

(21) Weaknesses in budget planning and execution have increased the expansionary bias of the fiscal policy and added to current macroeconomic challenges. The very early adoption of annual budgets between 2016 and 2023 reduced the reliability of macroeconomic and budgetary forecasts. Various budget flexibility rules and large budget reserves allowed for higher discretionary spending. Ad hoc spending decisions were often made at the end of the budget year or were enacted by government decrees throughout the year without adequate parliamentary oversight and public consultation, in turn reducing budget transparency. The national fiscal framework has not led to a more prudent fiscal stance because of shortcomings in the design of domestic fiscal rules, in particular a debt rule with procyclical features and the weak enforcement of medium-term budget planning, further eroded by the special provisions of the 'state of danger' regime. Frequent and significant revisions of fiscal targets have undermined the role of the budget as an anchor for market participants and have called into question the credibility of the medium-term fiscal plans. Basing medium-term fiscal planning on multiannual spending ceilings, as set out in the revised Union fiscal rules, may help address the expansionary bias of the fiscal policy. The effectiveness of the national fiscal council in steering public discussions on fiscal issues remains constrained by its limited mandate and resources.

(22) In accordance with Article 19(3), point (b), of Regulation (EU) 2021/241 and criterion 2.2 of Annex V to that Regulation, the recovery and resilience plan includes an extensive set of mutually reinforcing reforms and investments to be implemented by 2026. Those reforms and investments are expected to help effectively address all or a significant subset of challenges identified in the relevant country-specific recommendations. Within this tight timeframe, proceeding swiftly with the effective implementation of the recovery and resilience plan, including the REPowerEU chapter, is essential to boost Hungary's long-term competitiveness through the green and digital transitions, while ensuring social fairness. To deliver on the commitments of the recovery and resilience plan by August 2026, it is essential for Hungary to significantly accelerate the implementation of reforms and investments, first by swiftly implementing the necessary measures to ensure the protection of the Union's financial interests. The systematic involvement of local and regional authorities, social partners, civil society and other relevant stakeholders remains essential to ensure broad ownership for the successful implementation of the recovery and resilience plan.

(23) As part of the mid-term review of the cohesion policy programmes, in accordance with Article 18 of Regulation (EU) 2021/1060 of the European Parliament and of the Council ([17]), Hungary is required to review each programme supported by the European Regional Development Fund (ERDF), the European Social Fund Plus (ESF+), the Cohesion Fund and the Just Transition Fund (JTF) by March 2025, taking into account, among other things, the challenges identified in the 2024 country-specific recommendations, as well as its national energy and climate plan. That review forms the basis for the definitive allocation of the Union funding included in each programme. Hungary has made progress in implementing cohesion policy programmes and the European Pillar of Social Rights, but challenges remain and significant social and regional disparities persist between the least and most developed districts of the country, as well as between urban and non-urban areas. It is crucial to accelerate the implementation of the cohesion policy and to strengthen administrative capacity at the sub-national level. The priorities agreed in programmes remain relevant. It is of particular importance to rapidly implement the investments in the digital and green transitions, including the development of basic digital skills, the digital transformation of businesses, and the

([17]) Regulation (EU) 2021/1060 of the European Parliament and of the Council of 24 June 2021 laying down common provisions on the European Regional Development Fund, the European Social Fund Plus, the Cohesion Fund, the Just Transition Fund and the European Maritime, Fisheries and Aquaculture Fund and financial rules for those and for the Asylum, Migration and Integration Fund, the Internal Security Fund and the Instrument for Financial Support for Border Management and Visa Policy (OJ L 231, 30.6.2021, p. 159, ELI: http://data.europa.eu/eli/reg/2021/1060/oj).

take-up of smart city solutions, nature-based and net-zero technologies and water management, as well as the territorial just transition plans. Hungary should also continue to work on integrated territorial development in functional areas and the least developed districts. Equally, the implementation of investments in social inclusion and poverty reduction, focusing on children and the most deprived districts, and the comprehensive strengthening of basic skills and improving access to quality mainstream education and lifelong learning remain a priority. In that regard, structural reforms of the education system, including by improving access to quality early-childhood education and care, as well as targeted actions to address labour market challenges for vulnerable groups and to build the capacity of social partners remain key. Resolving pending issues on enabling conditions and the general regime of conditionality is necessary for Hungary to make full use of the cohesion policy funds.

(24) In the context of the mid-term review of the cohesion policy programmes, the need to address energy poverty and intergenerational poverty through integrated interventions, with a focus on the least developed districts and municipalities, and the need for a strengthened governance and differentiation of the smart specialisation strategy are areas that merit further attention. Hungary could leverage the Strategic Technologies for Europe Platform, established by Regulation (EU) 2024/795 of the European Parliament and of the Council ([18]), to boost investments in deep and digital technologies (e.g. the Internet of Things, big data and artificial intelligence), clean and resource-efficient technologies (e.g. renewable energy and geothermal energy) and biotechnologies (pharmaceuticals and medical products), while also investing in the skills and qualifications required to meet the labour demand in those sectors.

(25) Beyond the economic and social challenges addressed by the recovery and resilience plan and other Union funds, Hungary faces several additional challenges related to the business environment, the skills levels and integration of disadvantaged groups into the labour market, social assistance and social dialogue, and reliance on Russian fossil fuels.

(26) The business environment continued to deteriorate, primarily due to increasing state interventions in the economy and frequent ad hoc changes to the regulatory framework. Hungary performs poorly in indicators that measure competitiveness and regulatory quality. The high number of taxes increased in 2024. In recent years, the number of sector-specific taxes levied on certain sectors and firms has increased. Those taxes tend to be in sectors where foreign ownership is high (for example: retail, cement, construction and ceramic materials), creating a disproportionate burden on the firms concerned and affecting the single market. Firms complain about unequal treatment and arbitrariness when authorities conduct administrative inspections or decide on permits. There is a general perception that various state interventions are used to force foreign owners to sell their firms, facilitating the creation of public or government-connected national champions. The government increasingly declares certain investment projects to be of 'strategic importance for the national economy' to speed up and lighten the administrative process. The criteria used by the government are not transparent and cannot be challenged in court. The government continues to use its power to exempt certain transactions from merger control. The criteria for those exemptions are not transparent, and no formal procedure exists to contest them. The government also continues to make extensive use of its mandate to issue emergency decrees under the 'state of danger' regime. Many of those decrees do not seem to relate to the invoked emergency situation, which weakens legal certainty and interferes with normal business activity.

(27) Despite certain relevant initiatives and a high overall employment rate, some disadvantaged groups, such as the low-educated, Roma and persons with a disability, still face barriers in accessing upskilling opportunities and entering the labour market. The same disadvantaged groups also tend to be low achievers in basic skills at school, leave school early, become unemployed or inactive and rarely enter higher education. Inequalities are rooted in the way the education system is organised, characterised by the concentration of socio-economically disadvantaged pupils at certain schools. Between 2014 and 2022, significant amounts of Union cohesion policy funds were allocated to preventing early school leaving and implementing active labour market measures. While the employment rate of the low-skilled and Roma increased significantly over that period, it remains much lower than the overall employment rate. The disability employment gap remains well above the Union average. Several sectors face skills shortages, which makes it difficult for Hungary to shift its economy to a high value-added growth model. The share of tertiary graduates is one of the lowest in the Union, which poses challenges in meeting the growing demand for a highly skilled workforce. The short duration of unemployment benefits makes it difficult for people to

([18]) Regulation (EU) 2024/795 of the European Parliament and of the Council of 29 February 2024 establishing the Strategic Technologies for Europe Platform (STEP), and amending Directive 2003/87/EC and Regulations (EU) 2021/1058, (EU) 2021/1056, (EU) 2021/1057, (EU) No 1303/2013, (EU) No 223/2014, (EU) 2021/1060, (EU) 2021/523, (EU) 2021/695, (EU) 2021/697 and (EU) 2021/241 (OJ L, 2024/795, 29.2.2024, ELI: http://data.europa.eu/eli/reg/2024/795/oj).

participate in reskilling and upskilling and to find better-matching jobs that could improve productivity and competitiveness. While there has been a significant increase in the number of foreign workers in recent years, this may not fully match the needs of sectors facing skills shortages and labour shortages.

(28) In the past decade, poverty indicators have improved markedly in line with the increase in the employment rate. However, the severe material and social deprivation rate is still among the highest in the Union and has worsened among children, Roma and in remote areas. The poverty-reducing impact of social transfers, while still comparable to other Member States, has decreased in recent years. Despite the high inflationary economic environment, some social benefits, such as minimum income, family benefit and family tax benefits, have remained nominally unchanged. The adequacy of the minimum income and unemployment benefits is one of the lowest in the Union. The total tax burden on low earners and the reliance on value-added tax are high, which has a disproportionate effect on low-income groups in the context of non-progressive, flat-rate personal income taxation. The share of people who spend more than 40 % of their household income on housing costs has also increased due to inflation, energy and housing price hikes, and the lack of targeted support measures. Addressing those challenges would also contribute to supporting upward social convergence, in line with the Commission's second-stage analysis based on the features of the Social Convergence Framework, which was piloted in 2024. In line with Article 3(3), point (b), of Regulation (EU) 2024/1263, the European Semester is to include the surveillance of the implementation of the employment guidelines by the Commission, inter alia via a framework to identify risks to social convergence.

(29) Despite some improvements, social dialogue remains weak and fragmented. The tripartite forum in the private sector, which comprises the government, trade unions and employers' associations, has limited possibilities to influence or change the government's plans. Limited social dialogue puts employees in a disadvantaged position, including in wage bargaining, especially in the public sector. The establishment of a separate employment status for certain groups of public employees has weakened their ability to defend their collective interests. In some cases, it has led to collective agreements becoming void and having to be renegotiated. Measures such as limiting teachers' right to strike or the abolishment of collective bargaining in the health sector have gradually eroded workers' rights. The new legislation on the collection of trade-union membership fees in the public sector could further erode trade union representativeness. The relevant fora in the public sector had only one meeting in 2023.

(30) Hungary continues to rely heavily on fossil fuels, and its efforts to increase energy security by shifting away from dependence on Russian imports are slow. Hungary's share of renewable energy sources amounted to 25,7 % in 2023, 18 percentage points below the Union average. The share of Russian crude oil and gas imports amounted to 64 % and 75 % in 2021 and 2023, respectively. Oil and gas account for two thirds of its energy consumption. Hungary has one of the highest figures in the Union for fossil fuel subsidies as a share of GDP on account of subsidised energy prices for households.

(31) In light of the Commission's in-depth review and conclusions on the existence of imbalances, recommendations under Article 6 of Regulation (EU) No 1176/2011 are reflected in recommendations (1), (3) and (4). Policies referred to in recommendations (1) and (4) help to address vulnerabilities linked to external and government financing needs and price pressures. Policies referred to in recommendation (3) help to address vulnerabilities linked to price pressures,

HEREBY RECOMMENDS that Hungary take action in 2024 and 2025 to:

1. Submit the medium-term fiscal-structural plan in a timely manner. In line with the requirements of the reformed Stability and Growth Pact, limit the growth in net expenditure ([19]) in 2025 to a rate consistent with, inter alia, putting the general government debt on a plausibly downward trajectory over the medium term and reducing the general government deficit towards the 3 %-of-GDP Treaty reference value. Wind down the emergency energy support measures before the 2024/2025 heating season. Pursue effective coordination and clear demarcation of macroeconomic policies to ensure fiscal and external sustainability. Phase out remaining price and interest-rate caps to reduce distortive effects and facilitate the smooth transmission of monetary policy. Target support measures in the housing sector to low-income

([19]) According to Article 2, point (2), of Regulation (EU) 2024/1263, 'net expenditure' means government expenditure net of interest expenditure, discretionary revenue measures, expenditure on programmes of the Union fully matched by revenue from Union funds, national expenditure on co-financing of programmes funded by the Union, cyclical elements of unemployment benefit expenditure, and one-offs and other temporary measures.

households. Strengthen the medium-term budgetary framework, align the preparation of annual budgets with the budgetary year and limit discretion in the implementation of annual budgets.

2. In light of prolonged delays, significantly accelerate the implementation of the cohesion policy programmes and the recovery and resilience plan, including the REPowerEU chapter, ensuring the completion of reforms and investments by August 2026 by swiftly implementing the necessary measures to ensure the protection of the Union's financial interests and resolving pending issues on enabling conditions. In the context of the mid-term review of the cohesion policy programmes, continue focusing on the agreed priorities, taking action to better address poverty, focusing on energy poverty and the least developed districts and municipalities, and improve the smart specialisation strategy, while considering the opportunities provided by the Strategic Technologies for Europe Platform initiative to improve competitiveness.

3. Improve the regulatory framework and enhance competition in product markets and services by avoiding arbitrary administrative interventions and the selective use of tailor-made legislation providing undue advantage or disadvantage to specific companies, by applying competition scrutiny systematically to business transactions and by reducing the use of emergency measures to what is strictly necessary, in line with the principles of the single market and the rule of law. Improve the adequacy of social assistance and unemployment benefits. Improve educational attainment levels and access to effective active labour market measures, in particular upskilling and reskilling opportunities for the most disadvantaged groups, and ensure effective social dialogue.

4. Reduce overall reliance on fossil fuels, accelerate the diversification of gas supply towards non-Russian sources and take steps to phase out fossil fuel subsidies.

Done at Luxembourg, 21 October 2024.

For the Council

The President

NAGY I.