

HUNGARY

GDP per capita continues to converge on that of the best performing countries, but the gap remains large due to relatively low levels of productivity and labour utilisation.

Priorities supported by indicators

Reduce the tax wedge on labour income

A relatively high tax wedge on labour is hindering job creation. The wedge reflects the large revenue requirements needed to cover high level of government spending, but also narrow tax and contribution bases due to significant shadow-economy activity.

Actions taken: The employers' lump-sum healthcare contribution and other employer contributions for certain groups of workers have been reduced, personal income taxes have been cut and special tax allowances introduced. However, the wedge will increase in 2006 and 2007 as part of a revenue-based effort to bring down the large government deficit.

Recommendations: Reduce tax wedges over the medium term and finance the reduction by cutting public spending. The special tax allowances have made marginal tax incentives too complex and a universal tax allowance would be a better solution. Less costly ways of reaching family policy objectives than the currently very high support via taxes and benefits are needed.

Further reform the disability benefit system

The disability benefit system has ended up providing welfare to a much wider group than originally intended because eligibility conditions have been too light or inadequately enforced, contributing to the low employment rate, especially among older cohorts.

Actions taken: Assessment of disability has been centralised following a bribery scandal and medical guidelines have been streamlined.

Recommendations: Take more account of remaining abilities when assessing the extent of disability and reduce the stock of disabled by increasing the emphasis on rehabilitation.

Improve the efficiency of the education system

Tertiary-level educational attainment in the working-age population is relatively low, restraining productivity advances and the capacity to introduce new technology. However, tertiary enrolment rates are rising rapidly, but this has put considerable pressure for change in both tertiary and secondary education.

Actions taken: In tertiary education, new three-year bachelor-level courses with more vocational content have been introduced. In secondary education, there is more emphasis on work-related skills, including languages, and a new school and pupil evaluation system is being implemented. Future reform plans include the introduction of tuition fees in tertiary education.

Recommendations: Implement the planned tuition-fee system and continue with curricula reform. Address incentive problems in teachers' pay scales but also cut back on the level of job protection which undermines efforts to address underperformance and prevents a rejuvenation of the profession.

Other key priorities

- Increase public spending efficiency by moving ahead with plans to make the public administration more accountable and to ensure the cost efficient delivery of public services. At the municipal level, there is scope to strengthen co-operation by reinforcing the joint provision of services.
- Reduce shadow-economy activity by tying access to health care services to the payment of contributions, re-balancing social benefits towards more employment-friendly forms and raising sanctions to deterrent levels. Reconsider the recently introduced system of minimum wages according to educational achievement. The new system discourages the use of cash payments, but undermines labour market efficiency.