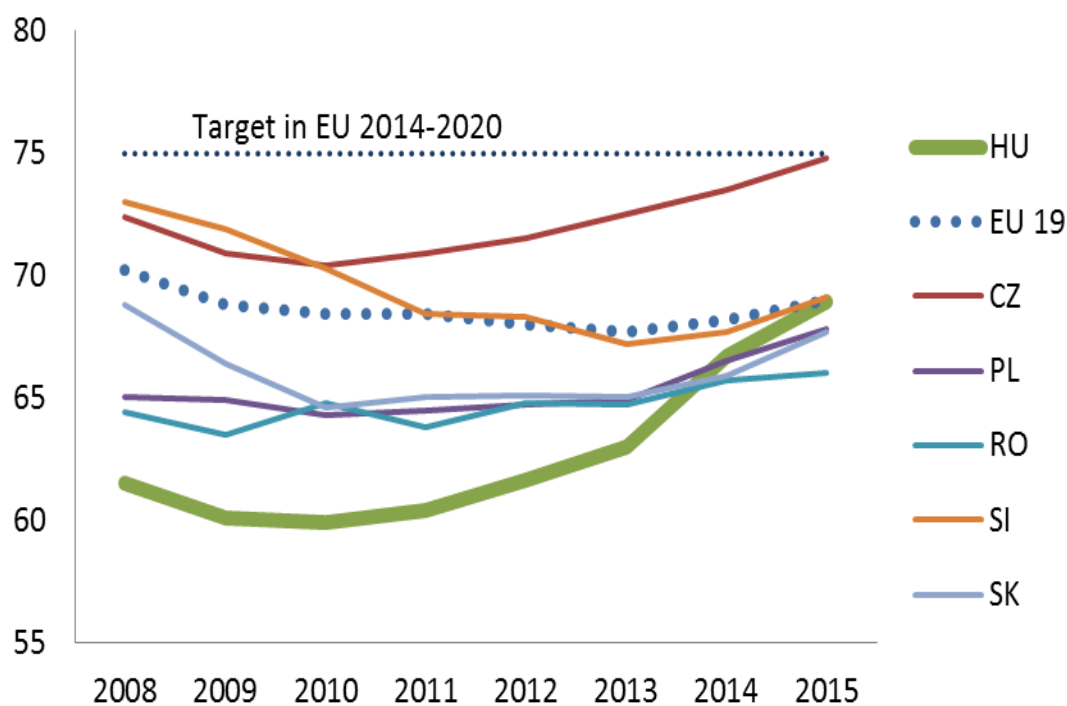


Labour market outlook is improving

Parallel to GDP growth, employment trends have been positive since 2010, thanks also to the Government's labour market policy and other measures. In July-September 2016, the number of people in employment increased, and the unemployment rate fell to a 30-year low. Wages have also risen in the June-August period (July-September data not available yet), boosting consumer demand. Due to rising employment figures, higher tax revenues and favourable macro-economic data, the Government is weighing options to reduce payroll taxes in order to boost wages and, consequently, the standard of living in Hungary.

Since the recession in 2008-2009, Hungary has come a long way in terms of employment trends. In 2008, the employment rate among those aged 20-64 years – compared to other countries in the region – was by far the lowest, 61.5 percent, and repercussions of the crisis pushed this indicator even slightly below 60 percent by 2010, whereas neighbouring countries have not seen such meagre figures even during the midst of downturn.

Employment rate among people aged 20-64 years (percent)

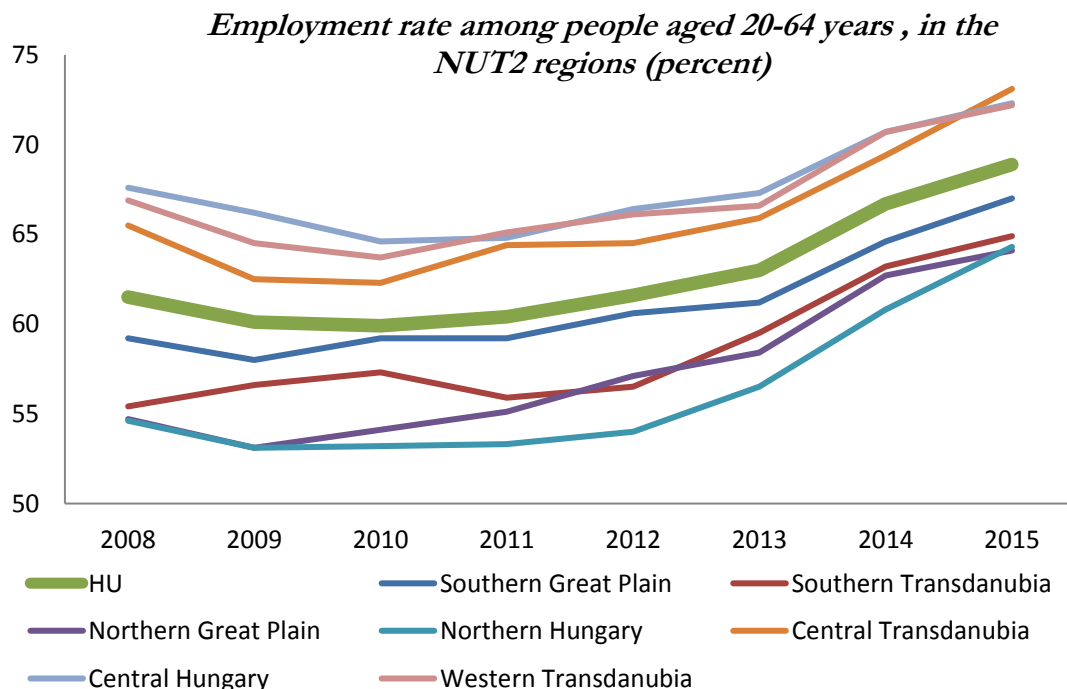




Source: Eurostat

The breakthrough in employment trends had come in 2011, by 2013 employment and unemployment data reached the V4 average, and after that growth momentum has remained robust. The most marked upturn was registered in 2014, but the number of people in employment rose by some 110 thousand even in 2015, of which three-fifths was recorded in the private sector. In Q4 2015, the number of people with a job totalled 4 million 259 thousand, while the annual average of people employed was 4 million 210 thousand, the highest figure in the past 25 years.

According to the latest labour market flash report of the Hungarian Central Statistical Office (KSH), the number of people in employment was 4 million 391 thousand in the period July-September within the national economy, up by 126 thousand year-on-year. The private sector added some 127 thousand jobs to the overall increase. The number of public work employees dropped by 0,5 percent. The number of employees posted abroad also felt by some 1000. The employment rate of those aged 15-64 years rose to 67.1 percent.

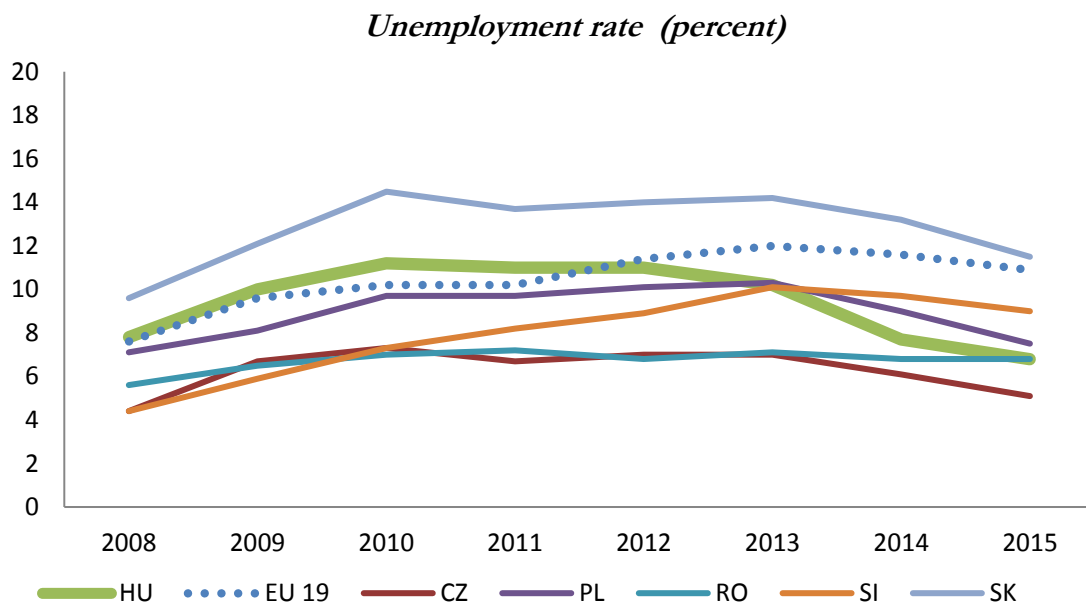


Source: Eurostat



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The inflow of formerly economically inactive people to the labour market has, albeit slowly, showed up in rising employment data, and it helped reduce the unemployment rate to 6.8 percent already in 2015. According to the latest unemployment flash report of the KSH, in July-September, compared to the same period in the previous year, unemployment rate was down by 1,5 percentage point to 4,9.



Source: Eurostat

The Government's employment policy has identified five priority fields to be improved in the period 2014-2020: 1, stimulating unemployed and inactive people to seek and find a job; 2, promoting jobs for youth; 3, improving labour competitiveness; 4, improving the adaptability of employees and enterprises; 5, developing the social economy. Accordingly, several Government strategies have been created and implemented in order to attract more people to the labour market and retain existing labour force. Thus, labour market and employment trends have also been shaped by certain structural changes other than shifts in macro-economic supply and demand.

The potential labour pool in the age bracket of 15-64 years has been shrinking, but the process has been mitigated by the rise in retirement age. Thus, the retiring of the generation born in the



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early 1950s has been delayed, and more labour force was made available within the economy. On the other hand, since 2011 women have been allowed to retire after 40 years of employment, and up to 2015 some 150 thousand women have exercised this option. The raising of the retirement age had been determined already in 2009, but the measure took effect only in 2014, when former early retirement schemes were also restricted.

The age limit for compulsory education was reduced – in accordance with the practise in the majority of EU member states – from 18 years to 16 years. Those, however, who leave the educational system without having gained proper work skills find it hard to get a job. A reform process aimed at the overhaul of the vocational and adult education systems has been launched to assist job-seekers and potential employers as well. The new system is designed to improve the job prospects of potential labour through education and cooperation with economic stakeholders.

The period when jobseekers are entitled to unemployment benefits was cut to three months, to stimulate jobseeker activity. Another measure with even larger impact was the replacement of certain social benefits with public work wages. Public work schemes have activated some long-term unemployed or economically inactive people, who used to do only temporary or black jobs for years. The scheme aims to lead able-bodied but long-term inactive people back to a steady job and steady income and replace social benefits requiring zero efforts. The scheme, however, is now viewed as contradictory, even as a stumbling block in the adaptability of the labour force, but the “workfare instead of welfare” principle is still considered to be valid.

At the time of introduction, the scheme was designed as an alternative employment form which was believed to mitigate repercussions in the crisis-hit country. Nowadays, as the country is facing structural labour shortages the programme must be reconsidered. In terms of statistics, the scheme has certainly improved the country’s economic activity index, a major factor in global competitiveness rankings, and overall employment data.

It has to be noted that certain external factors have also underpinned the favourable labour market trends in recent years, such as the acceleration of the transfer of EU funds, low global oil prices and robust economic growth at our major economic partners.

Rising wages and standard of living



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Following a flat wage growth trend at the end of the 2000s, average wages had soared within the national economy and in 2015 they reached EUR 800 level in gross terms. Thanks to lower taxes on labour, net wage growth exceeded gross wage growth in the 2010s. In 2015, net wages averaged EUR 524.

According to the latest KSH flash report, in August 2016 the average gross wage was EUR 834, up by 6.9 percent year-on-year. In January-August 2016, gross wages increased by 6 percent, compared to the same period of the previous year. Wage growth has also been fuelled by the 5.7 percent rise in the minimum wage and the guaranteed minimum wage, wage hikes at armed forces and complementary wage hikes at welfare sector employees. In the first eight months of 2016, the increase of net wages – 7.6 percent -- exceeded that of gross wages, due to the 1 percentage point cut in the personal income tax rate.

Lower payroll taxes for higher wages

As a consequence of rising employment, higher tax revenues and favourable macro-economic data, the Government is contemplating the reduction of payroll taxes in order to boost wages and the standard of living. Government analyses estimate that 250 thousand people still do not have a steady job, while there are 50 thousand vacancies across the country. The fact that several regions and professions are affected by labour shortages shows robust economic growth. On the other hand, factors such as inadequate labour skills, high payroll taxes and lack of mobility are working as disincentives to offer and impediments to take a job, although the economy could absorb several thousands of people.

The planned payroll tax reform measures include a progressive tax reduction scheme for the next 2-3 years, which would be tied to a rise in net wages.

Besides securing the improvement of the standard of living, wage hikes are also essential for retaining labour force. One of the key reasons for labour shortages has been migration driven by better-paid jobs in Western European countries and this has put Hungarian enterprises at a disadvantage in the competition for highly skilled labour.