Hungary
A continuous shrinking of the unemployment benefit system

Béla Galgóczi*

Introduction

Unemployment was an unknown phenomenon under state socialism; being without an official job was even seen as criminal and was subject to sanctions. In reality, 'unemployment' was kept hidden behind the company gates in the form of over-employment. Correspondingly, unemployment benefit, as with any other labour market policy instrument, was non-existent before 1989 in Hungary.

The collapse of the state socialist regime in 1989 resulted in a disintegration of the regional political economy by the early 1990s. In Hungary, as in most Central and Eastern European countries, this period was marked by a huge decline in GDP and by a collapse of industrial output. As a result of rapid market liberalisation, Western products started to flood the market, pushing a large number of domestic products out. This situation was further aggravated by an early privatisation of trade, the food industry and other industries producing consumer goods.

Emerging mass unemployment and rapidly declining purchasing power of wages came as a huge shock for the population. The rise in the number of people unemployed in Hungary from 10,000 to 600,000 (corresponding to a 12% unemployment rate) between 1989 and 1992 had in some respects a harsher impact than the Great Depression.

This dramatic emergence of mass unemployment was a new experience and the hastily established labour market institutions were totally unprepared to deal with a problem of this scale and nature. The establishment of fully fledged labour market policy measures and institutions was completed by 1991. Although unemployment had

* Senior researcher at the ETUI (European Trade Union Institute), Brussels, Belgium.

stabilised below the level of 10% from the mid 1990s onwards, employment rates remained persistently low until very recently.

This article focuses on labour market policy measures and institutions in Hungary, and reviews past and current practices. It also gives a short background on labour market developments specific to Hungary, and briefly addresses the impact of the recent economic crisis on employment, examining specific labour market policy tools to deal with the repercussions of the crisis on employment.

General labour market trends in Hungary in the past decade

In the past decade the Hungarian labour market has been characterised by persistently low employment rates. Table 1 shows the development of the employment rate over the last ten years in Hungary. Average growth rates of 4% in the period 1997-2006 were not sufficient for job creation as most of the growth was generated through an increase in productivity. The declining growth rate in 2007 and 2008 was accompanied by a slight decrease in the employment rate mainly due to job cuts in the public sector.

The employment rate of around 57% of the population aged 15 to 64 falls substantially short of the corresponding EU27 average of 65.9% for the last year. The female employment rate lags behind male employment by 13 percentage points over the whole period, making the gender gap in employment larger than the EU average and showing similar patterns to most southern European countries.

Table 1 **Employment rate (%) by gender for the population aged 15-64 between 1997 and 2008 in Hungary**

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
HU total	52.4	53.7	55.6	56.3	56.2	56.2	57.0	56.8	56.9	57.3	57.3	56.7
- Men	59.7	60.5	62.4	63.1	62.9	62.9	63.5	63.1	63.1	63.8	64.0	63.0
- Women	45.4	47.4	49.0	49.7	49.8	49.8	50.9	50.7	51.0	51.1	50.9	50.6
EU27 (total)	60.7	61.2	61.8	62.2	62.6	62.4	62.6	63.0	63.6	64.5	65.4	65.9

Source: Eurostat (2009)

Another weakness of the Hungarian labour market lies in the low employability of older people. Disability pensions and a variety of early retirement schemes have absorbed a large proportion of individuals leaving the labour force. In the 45-60 age group, over 40% of the unemployed receive disability benefit *(Bálint and Köllő, 2007)*.

The very low participation and employment rate of individuals in the 15-24 age group is also a factor behind the overall low employment rate. The activity rate of the Hungarian 15-24 age group lags behind the EU15 average by 20 percentage points. The reason for the low activity rate is that very few students – at least according to statistical observations – are willing to enter the labour market during their studies and even fewer find a job *(OECD, 2007)*.

Table 2 **Unemployment rate (%) by gender in Hungary between 1997 and 2008**

	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008
HU total	9.0	8.4	6.9	6.4	5.7	5.8	5.9	6.1	7.2	7.5	7.4	7.8
- Men	9.7	9.0	7.5	7.0	6.3	6.2	6.1	6.1	7.0	7.2	7.1	7.6
- Women	8.1	7.8	6.3	5.6	5.0	5.4	5.6	6.1	7.4	7.8	7.7	8.1
EU15 (total)	9.8	9.3	8.5	7.7	7.2	7.6	7.9	8.1	8.1	7.7	7.0	7.1

Source: Eurostat (2009)

The unemployment rate fluctuated within a relatively narrow range around 7% in the last decade, as Table 2 shows. It was slightly below the EU15 average until 2007 and used to be much more favourable than in most Central and Eastern European new member states (CEE NMS), where double digit unemployment rates were more the rule than the exception until 2006. On the other hand, Hungary did not see an improvement in unemployment between 2006 and 2008, when NMS with previously high unemployment, such as Poland, the Baltic states and Slovakia, experienced a spectacular decrease in unemployment rates. It was, in fact, the opposite as the unemployment rate had even increased slightly due to lower growth rates caused by the government's stabilisation measures. There were no substantial differences between the male and female unemployment rates for the whole period, although the previously lower female unemployment rate changed to a slightly higher level than male unemployment from 2005, as the austerity measures primarily affected the public sector, where are women traditionally overrepresented.

While unemployment among young people in Hungary was slightly lower than the EU15 average until 2006, by 2008 the unemployment rate of the 15–24 age cohort had risen to 3 percentage points higher than the EU15 average.

The duration of unemployment in Hungary is long. In 2006 only 4.3% of the unemployed succeeded in finding a job within one month following their job loss. In 2007 this increased slightly to 4.5 per cent. The proportion of those looking for a job for more than one year, however, increased between 2006 and 2007 from 41.2% to 44.1%.

Over half of the unemployed population does not receive unemployment benefit. The proportion of job-seekers quickly decreases with age over the age of 40 – the majority of those who receive unemployment benefit but are in fact inactive are found in this age group.

The impact of the crisis on the Hungarian labour market

The deepening crisis, caused primarily by the sharp drop in exports and aggravated by falling investments and household demand due to tight fiscal policy and the credit crunch, had shown its effect on the Hungarian labour market within a short time (for more details on the effects of the crisis in CEE, cf. Galgoczi, 2009). In contrast to the rest of Europe, the Hungarian labour market was already showing signs of contraction in 2007.

Compared to 2008, the number of persons employed has decreased by 85,000, bringing the already low employment rate down further to 55.3% by April 2009. The number of unemployed people grew by 88,000 between May 2008 and May 2009, an increase of 32%. The unemployment rate increased from 7.5% to 10.2% in this period, as Table 3 shows. The proportion of men has increased among the unemployed, as male unemployment grew by 2.8 percentage points, while female unemployment rose by 1.3 percentage points. At the same time the average duration of unemployment has decreased somewhat.

The highest decrease in employment was observed in the manufacturing industry, where it fell by 9.3%, representing 76% of total job losses in Hungary between May 2008 and May 2009. Public administration and public services which had suffered substantial job losses in the previous years were only slightly affected in this period.

Table 3 **Unemployment rate (%) in Hungary between May 2008 and May 2009**

	May 2008	Nov 2008	Dec 2008	Jan 2009	Feb 2009	Mar 2009	Apr 2009	May 2009
HU	7.7	8.1	8.4	8.8	9.2	9.7	10.0	10.2
EU27	6.8	7.5	7.6	8.0	8.3	8.5	8.7	8.9

Source: Eurostat (2009-1), (seasonally adjusted monthly figures)

A review of Hungarian labour market institutions and employment policy with particular regard to passive measures

The legal background of labour market regulations in Hungary

After labour market policy measures were hastily introduced in 1989, the legal foundations of a comprehensive system were established by the Employment Promotion Act in 1991. Legislation on employment relationships consists of three major parts; the Labour Code covers the competitive sphere; the Civil Servants Act covers public administration employees; and the Public Servants Act covers employees in public services (education, health, etc.).

The Civil Servants Act and the Public Servants Act contain detailed and rigid prescriptions on job classification, wage scales and promotion. The relatively low level of pay in the public sector is compensated by better protection against lay-offs and by guaranteed promotion.

The Labour Code regulates the market sphere and follows a free market philosophy: the employment relationship is based upon individual and/or collective bargaining between employees and employers, with government intervention limited to setting minimum standards.

Working hours are fixed at eight hours per day. Overtime, special working hours, multiple shifts, work on public holidays, paid leave and the protection of minors and women (pregnant or with a child under a year old) are also regulated by the Labour Code. The Labour Safety Act provides for health and safety, and physical conditions at work.

It can be concluded that labour market regulations are rather liberal in Hungary, particularly in the private sector. Dismissal costs and severance payments are also regulated in a rather liberal manner. Laid-off employees are provided with a period of notice and a severance payment. The employer is required to justify the lay-off and employees have the right to defend themselves against the reasons stated. Notice periods and severance payments are dependent on tenure within the firm.

Labour market policy institutions

Government bodies

Most labour-related issues were integrated under the authority of the Ministry for Employment and Labour, although the Ministry of Social and Health Affairs and the Ministry for Education retain some labour-related responsibilities.

Public Employment Service

The Public Employment Service (PES) consists of the Labour Office and a regional network of labour market centres, and operates under the authority of the Ministry for Employment and Labour. The Labour Office is responsible for ensuring the professional background and direction of the regional centres (in terms of methodology, information and statistical background, etc.). These centres operate both passive (the unemployment benefit system) and active (e.g. re-training) labour market instruments. Financial resources are provided by the Labour Market Fund, which succeeded the Employment Fund and The Solidarity Fund in 1996. The legal foundations of this system are given in the 1991 Employment Promotion Act.

The social partners can participate in the application of employment policy, and its adaptation to specific and regional conditions via the tripartite Labour Market Fund (LMF) Steering Committee. This forum was created in 1997 and is responsible for managing the Labour Market Fund. The right of disposal over the Fund is formally granted to the Minister of Employment and Labour Affairs (previously, the Minister of Labour) but, according to the law, the Minister exercises this right jointly with the LMF Steering Committee. This means that the Fund is actually managed by the tripartite body. The Committee has extensive powers with regard to the financial issues of the LMF, such as drafting its annual budget; deciding on re-allocation between the sub-funds; and deciding on the co-financing of national programmes for economic and regional development.

At the decentralised level, the county employment offices and labour councils bear the same joint responsibility over the decentralised funds. The extent of decentralisation varies. In the case of the Employment sub-fund it is almost 90% of the total. In 1997, the Labour Mediation and Arbitration Service was established to assist in firm-level wage conflicts or other labour-related disputes.

Employment policy measures

Labour market policy in Hungary is based on the same instruments as in most of the EU15 countries, consisting of active and passive labour market policy instruments (here we will discuss passive instruments only).

Labour market policy is based on combined financing: unemployment benefit and the active measures are insurance-based, while income support and social assistance are budget-financed.

Contributions are paid by both employers and employees. The levels of contributions gradually increased until the mid 1990s, but have decreased somewhat since then (with a further decrease from July 2009).

Expenditure on employment policy decreased significantly in terms of its share of GDP throughout the whole period (from 2.81% of GDP in 1992 to 0.64% of GDP by 2006). This very low level is still among the highest in the CEE NMS. In comparison, labour market policy expenditure in the EU15 was on average 2% of GDP in 2006.

Table 4 **Public employment policy expenditure 1992-2006 as % of GDP**

	1992	1995	1998	2000	2006
Total expenditure in % of GDP	2.81	1.33	1.01	0.86	0.64

Source: Hungarian Ministry of Labour, 2005, Eurostat 2009.

The three most important passive instruments are unemployment benefit, income support and early retirement. The system of unemployment benefit is earnings-linked (an insurance device), but the latter two measures are provided as social assistance.

Unemployment benefit

This form of assistance is available if an unemployed person is not entitled to a pension, is both capable of and available for work, co-operates with the labour office (i.e. visits the centre within given time limits and accepts job offers made by the centre) and has made contributions to the Labour Market Fund (for at least 360 days over the last four-year period). Job offers made by the labour office must correspond either to the qualification level of the job-seeker, or to the qualification level acquired through the training programme offered by the labour office, or to the qualification level of the job in which the person was employed at least six months before unemployment. The job offered must be accessible by public transport, and involve no more than a three-hour daily commute, (in the case of job-seekers with children under 10, a two-hour daily commute).

The unemployment benefit system has gradually become less generous: in 1993-94, the entitlement period became one year instead of two years, and it decreased to nine months in 1998. On the other hand, unemployed people can become eligible for benefits again after certifying 180 days of work. In those days the level of unemployment benefit was between 65% and 75% of previous earnings, with a maximum level of twice the minimum old-age pension. From 2002 the duration of unemployment benefit was reduced from nine months to 180 days and at the same time its maximum level was adjusted to double the national minimum wage (otherwise 60% of previous average wage). The current national minimum wage is 71,000 HUF (approximately 250 Euro) and is exempt from personal income tax.

Income support for the unemployed

After exhausting unemployment benefit, income support for the unemployed is 40% of the national minimum wage for a further 90 days. The entitlement period for this support was also reduced in two stages from an initial two years to the current 90 days.

This support is jointly financed by local government (25%) and the Labour Market Fund (75%). It must be emphasised that this measure is only available to those who are long-term unemployed and that it also differs from general social assistance because it is mainly financed from the Labour Market Fund.

Early retirement

Since retirement ages have changed and early retirement had some disincentive effects, it was replaced in 1998 by pre-retirement unemployment benefit. Employees with at least 20 years of service are entitled to this support until they become eligible for an old-age pension, or participate in a disability pension scheme (but for a maximum of 5 years). This provides the same amount as income support and can be seen as a continuation of income support for unemployed people for a maximum of five years before they reach retirement age.

Job market entrants

Young unemployed school leavers were entitled to receive unemployment benefits at 75% of the minimum wage until 1995. In 1996, this type of assistance was replaced, also on the grounds of its potential disincentive impact, by wage subsidies for their employment. The scheme is in fact a combination of wage subsidies and on-the-job training. In this case, therefore, a passive measure was exchanged for an active one.

Specific labour market policy tools to tackle the effects of the crisis

Although Hungary did not launch a large-scale discretionary stimulus package for the economy due to the fiscal constraints in line with the IMF-EU agreement, there are a few measures available for the actors involved in the real economy to cushion the immediate effects of the downturn.

As a general measure to stimulate employment, the government has decreased the level of social security contributions paid by employers by 4 percentage points and the personal income tax level for employees on low to average incomes from July 2009, but has offset these measures through an increase in VAT to keep the fiscal discipline within external constraints.

Hungary was the only new member state (except Bulgaria) to hastily adopt a specific labour market policy measure to cope with the impact of the crisis on employment. In January 2009, following western European examples, the Labour Ministry developed a public labour market policy instrument to support reduced working time in companies affected by the crisis. The job creation pillar of the Labour Market Fund (previously used to subsidise firms that made major investments involving job creation) was redesigned into a pillar for 'maintaining employment'. Companies applying for this support can run production on a four-day week basis, while compensation for the lost working hours is financed by the Labour Market Fund, providing up to 80% of the lost income with a maximum level of double the statutory minimum wage. The initial expectation of the government was that this support measure could save around 20% of threatened jobs during the crisis. According to media reports and anecdotal evidence, the use of this support scheme has been popular among enterprises and the special fund devoted to its financing will soon be exhausted. The Labour Minister has promised to extend the fund in the future. There is no statistical information available on the number of employees covered by the scheme up until now.

The role of the social partners in formulating employment policy

The regular institutions of social dialogue are the most important terrain for the involvement of the social partners in policy formulation, including employment policy issues in Hungary.

The key institution of national-level tripartism is the Interest Reconciliation Council (IRC), established in 1988 by the then Reform Communist government, which went through several institutional and organisational changes over the two decades but has remained the key institution of national-level social dialogue until today. Depending on the actual political climate it had a varying impact, not only on employment-related public policy formulation and legislation, but also on the whole process of political and economic transformation.

The social partners are also central actors in the implementation of employment policy, and its adaptation to specific and regional conditions, through their role in the tripartite Labour Market Fund Steering Committee. As mentioned before, the Fund is actually administered by the tripartite body and the Committee has extensive powers with regard to the Fund's financial management.

Within and besides their institutional role, the social partners and especially trade unions have had an impact on the formulation and application of labour market policy. Although they have managed to influence decisions, they have not been able to counteract the successive cuts (as described above) in the unemployment benefit system. It counts as a partial success, however, that the severe austerity measures of the 2006-2008 period did not seriously affect social welfare and labour market policy provisions. The current debate is, however, aimed precisely at the alleged negative impacts of this policy. There is a consensus among experts, media analysts and politicians that the current social welfare system in Hungary is too generous and has adverse effects on the level of employment. This view is widely supported by the European Union and the International Monetary Fund. There is mounting pressure for further streamlining and targeting of benefits and welfare provisions with a focus on activation and promoting employability while eliminating perceived disincentives of a 'generous' welfare system for employment. The likely victims of such a policy would be groups in society with multiple disadvantages. The trade unions are fighting against this process on all levels; their capacity to have a successful impact, however, seems to be rather limited.

Conclusions

Hungary introduced the whole range of labour market policy instruments that are common in the EU15 at the beginning of the 1990s. As far as the general situation of the labour market is concerned, unemployment has never reached alarming levels; it was slightly below the EU15 average for most of the period under consideration. The real problem has been and continues to be the low participation and employment rate.

Labour market policy measures were cut back from relatively generous levels in the early 1990s in successive stages over the period under consideration, in line with a continuously shrinking share of GDP expenditure. Cutbacks mostly affected the entitlement period for unemployment benefit, its level having in fact been increased over time.

The tightening of passive measures has aggravated the situation of the long-term unemployed and led to the growing social exclusion of the social strata most affected by long-term unemployment (low-skilled employees, people living in structurally weak regions, and the Roma minority).

Beside the low employment rate in general, this is the most serious problem affecting the labour market in Hungary.

References

Bálint M. and Köllő J. (2007) *The Hungarian labour market: review and analysis*, Budapest, Economic Research Institute of the Hungarian Academy of Sciences.

European Commission (2009) *Spring Economic Forecast*, May, Brussels.

Eurostat (2008) *Statistics in Focus*, 94/2008, Luxembourg.

Eurostat (2009) *Online database*. http://epp.eurostat.ec.europa.eu/tgm.

Eurostat (2009-1) *News release – Euroindicators,* 97/2009, Luxembourg.

Galgóczi B. (2009) "Central Eastern Europe five years after: from 'emerging Europe' to 'submerging' Europe?", EEEPB 2009/4, Brussels, ETUI.

Glassner V. and Galgóczi B. (2009) "Plant-level responses to the economic crisis", ETUI Working Paper 2009/1.

OECD (2007) Economic Survey of Hungary, *Improving reconciliation between work and family*. http://oecd,org/document/29/.