2000 Country Reports on Economic Policy and Trade Practices
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HUNGARY

Key Economic Indicators 1/

(Billions of U.S. dollars unless otherwise indicated)

	1998	1999	2000	
Income, Production and Employment:				
Nominal GDP	47.03	48.45	47.39	2/
Real GDP Growth (pct)	4.9	4.5	5.6	
GDP by Sector: 3/				
Agriculture	2.29	2.06	2.00	
Manufacturing	11.68	11.78	12.52	
Construction	1.89	1.93	1.86	
Services	25.51	26.34	25.07	
Government	N/A	N/A	N/A	
Per Capita GDP (US$)	4,651	4,808	4539	2/
Labor Force (000s)	6,368	6,200	6,402	
Unemployment Rate (pct)	9.1	9.6	6.5	3/
Money and Prices (annual percentage growth):				
Money Supply Growth	18.1	18.84	17	4/
Average Consumer Price Inflation	14.3	10.0	9.8	
Official Exchange Rate (HUF/$ annual average)	214.45	237.29	280	
Balance of Payments and Trade:				
Total Exports FOB	23	25	26.6	
Exports to U.S. (US$ millions)	1,567	1,893	2,020	5/
Total Imports CIF	25.7	28	30.4	
Imports from U.S. (US$ millions)	482	504	452	5/
Trade Balance	-2.7	-3	-3.8	
Balance with U.S. (US$ millions)	-1,085	-1,389	-1,568	5/
Current Account Deficit/GDP (pct)	4.8	4.3	3.4	
Net External Public Debt	4.4	2.9	2.6	6/
Debt Service Payments/GDP (pct)	10.3	9	8.5	
Fiscal Deficit/GDP (pct)	4.6	3.9	3.4	
Gold and Foreign Exchange Reserves	9.3	10.9	10.6	7/
Aid from U.S. (US$ millions)	9.9	4.0	0	
Aid from All Other Sources	N/A	N/A	N/A	

1/ Source: Central Statistical Office and National Bank data available through October 2000, except where otherwise noted.

2/ Apparent inconsistency with the growth figures is due to the considerable strengthening of the dollar against the Hungarian forint.

3/ The Central Statistical Office changed the method of calculation of the unemployment rate as of 2000. The new figure is calculated according to the ILO recommendation.

4/ August-on-August M1 growth in 2000 (no M2 data available since 1998).

5/ Source: U.S. Department of Commerce; 2000 projected from January-October data. Note that U.S.-source and Hungarian-source bilateral trade figures differ markedly, due largely to country-of-origin distinctions in exports whose final assembly occurs in Hungary.

6/ July 2000.

7/ Sept 2000.

1. General Policy Framework

Hungary has been transformed into a middle-income country with a market economy and a well elaborated but still developing Western-oriented legal and regulatory framework. The first post-communist government (1990-94) began significant economic reform, but was unable to privatize many state enterprises and implement systemic fiscal reforms, which led to large imbalances in Hungary's fiscal and external accounts. A successor government (1994-98) achieved economic stabilization through an IMF-coordinated austerity program adopted in March 1995, and accelerated privatization and economic reform. In 2000 Hungary continued to post solid increases in industrial output, exports, and overall output. Continued economic restructuring under the current government (elected in May 1998) is expected to allow for sustainable growth in the medium term. Regional disparities exist in Hungary, though they will likely narrow in the future.

A revised privatization program enacted in 1995 gave new momentum to sales of government enterprises and assets, largely to Western companies. Privatization contributed to a rapid transformation of the energy, telecommunication, and banking sectors. Currently, over 80 percent of the country's GDP is derived from the private sector, and Hungary has lowered government expenditures as a percentage of GDP. Other significant reforms include means testing of social-welfare payments (partially reversed by the current government) and partial privatization of the pension system (implemented in January 1998). The unfinished reform agenda includes rationalizing health care and local government financing.

Privatization revenues have reduced Hungary's foreign debt burden substantially. The government has an unblemished debt payments record and its foreign-currency obligations have been rated investment grade by all major rating agencies since late 1996. Foreign currency reserves stood at $10.56 billion through September 2000, enough for more than four months of imports.

The government has pledged to continue reducing fiscal deficits and inflationary wage increases. The consolidated budget deficit in 2000 will equal about 3.4 percent of GDP, down from 3.9 percent in 1999. Hungary finances its state deficit primarily through foreign and domestic bond issues. The market expects a current account deficit of under $1.7 billion in 2000, less than the $2 billion in 1999. Foreign direct investment has slightly exceeded the current deficit through the end of September 2000, in contrast to only 82 percent by the end of

1999. Following a cumulative decline of 17 percent from 1995 to 1996, net real wages are expected to increase 1.5 percent in 2000, after an estimated 2.5 percent increase in 1999.

Hungary is a leader in attracting foreign direct investment, with an estimated $23 billion in cumulative inflows since 1989. The United States is a leading investor in Hungary with over $8 billion in cumulative FDI since 1989. Tax incentives and related credits are available for foreign investments, especially in underdeveloped regions. Hungarian law currently permits the establishment of companies in customs-free zones, which are also exempt from indirect taxation tied to the turnover of goods. These zones, the engines of Hungarian industry and foreign trade, will face significant changes after Hungary's accession to the EU, but until then there are no plans to reduce the preferences guaranteed to them.

A signatory to the Uruguay Round Agreement and a founding member of the World Trade Organization, Hungary joined the Organization for Economic Cooperation and Development (OECD) in May 1996 and, as a part of that process, is further liberalizing capital account transactions. Hungary has harmonized many laws and regulations with European Union standards and has oriented economic policy towards the earliest possible accession date of January 1, 2003.

2. Exchange Rate Policy

The revised Foreign Exchange Law, effective January 1, 1996, made the Hungarian forint legally convertible for current account transactions. Foreigners and Hungarians can maintain both hard currency and forint accounts. The forint exchange rate is managed within a ± 2.25 percent band ("crawling peg") pegged 100 percent to the euro. In October 2000 the rate of devaluation was 0.3 percent a month. A 0.1 percent cut in this devaluation rate is expected in the first quarter of 2001. Improved macroeconomic performance has helped slow average annual inflation from 28.3 percent in 1995 to a projected 9.8 percent for 2000.

The Hungarian National Bank's principal policy target is a sustainable decline in inflation within the constraints of the foreign exchange regime. Commercial banks can conclude foreign exchange swap transactions with the MNB.

3. Structural Policies

The market freely sets prices for most products and services. User prices for pharmaceuticals, public transport, and utilities are set in some cases by the state. The government offers a wholesale floor price for many agricultural products. Public opposition and regulatory intervention have prevented utility prices (e.g., natural gas for heating and cooking) from reaching market levels, causing energy companies to receive less than the cost-plus-eight percent return stipulated in privatization contracts.

Starting in 1997, successive governments have reduced income tax rates and employer social contributions in an effort to cut inflation, spur job growth, and shrink the gray economy. Corporate tax remains low at 18 percent. A ten-year corporate tax holiday applies to investments of at least $33 million, as of October 2000, or $10 million in less developed regions, and a five-year, 50 percent tax holiday applies to investments of at least $3.3 million. Other incentive programs exist, including some offered by counties and municipalities. Consult the Country Commercial Guide for additional information.

Major structural budget reform has been implemented and further legislation is expected in this area. In January 1998 a new “three pillar” pension system was introduced in which private funds initially augment and gradually supplant more of the current state-funded, pay-as-you-go public system. The next areas of government finance reform are health care and local government financing. Health care costs are emerging as a drain on the budget and a source of fiscal indiscipline. The government continues to control pharmaceutical prices in order to limit health spending. Wholesale reforms are unlikely until after the 2002 election, which could also induce a bout of spending.

4. Debt Management

Hungary is a moderately indebted country with gross foreign debt expected to be $30.4 billion at the end of 2000. Net public domestic debt was $20.1 billion at the end of July 2000. Hungarian governments have consistently met external debt service payments. Moody's has upgraded the foreign currency ceilings for bonds and bank deposits in Hungary from Baa1 to A3. A standby credit arrangement with the IMF ended in February 1998 by mutual agreement. Hungary is expected to have reserves of $10.4 billion at the end of 2000.

5. Significant Barriers to U.S. Exports

On July 1, 1997 Hungary joined the Pan European Free Trade Zone and Cumulation System. Combined with tariff reductions stipulated in Hungary’s 1993 EU Association Agreement, imports from EU members and associated states face declining tariffs (dropping to zero on January 1, 2001). Goods from the United States are subject to Hungary’s MFN tariff rates until Hungary adopts the EU common external tariff. This increasing differential between tariffs on EU goods and on U.S. goods has disadvantaged many U.S. exporters. Duty must be paid on imports from outside the Pan-European Zone, which may then be exported duty-free to other countries within the Pan-European Zone. Duty paid on inputs processed and then exported within the zone is no longer refundable, a problem that the Hungarian government has addressed on a case-by-case basis for U.S. firms exporting from Hungary to European markets.

Although 95 percent of imports (in value terms) no longer require prior government approval, quota constraints apply to some 20 product groups, including cars, textiles, and precious metals (the quotas, however, are not actually reached in most of these areas). Under WTO rules, Hungary will phase out quotas on textiles and apparel by 2004. As a result of the WTO Agricultural Agreement, quotas on agricultural products and processed foods have been progressively replaced by tariff-rate quotas. In 1997 Hungary eliminated an import surcharge imposed as part of the March 1995 austerity package.

Importers must file a customs document (VAM 91 form) with a product declaration and code number, obtained from the Central Statistical Office. Upon importation, the importer must present Commercial Quality Control Institute (KERMI) certified documentation to clear customs. This permit may be replaced by other national certification and testing agency documents, such as those of the National Institute for Drugs. Hungary participates in the International Organization for Standardization (ISC) and the International Electro-Technical Commission (IEC).

Foreign investment is allowed in every sector open to private investment. Foreign ownership is restricted to varying degrees in civil aviation, defense, and broadcasting. Only Hungarian citizens may own farmland, but this restriction is slated for elimination upon EU accession.

Under the November 1995 Law on Government Procurement, public tenders must be invited for purchases of goods with a value over $33,000. As of October 2000, the same is true of construction projects worth $66,000 or designs and services worth over $16,500. Bids that contain more than 50 percent Hungarian content receive a 10 percent price preference. This process does not apply to military purchases affecting national security, or to gas, oil, and electricity contracts. Hungary is not a party to the WTO Government Procurement Code, and some U.S. firms have taken legal action against non-transparency and procedural irregularities involving government tenders.

6. Export Subsidies Policies

The Hungarian Export-Import Bank and Export Credit Guarantee Agency, both founded in 1994, provide credit and/or credit insurance for less than ten percent of total exports. There are no direct export subsidies on industrial products, but some agricultural products receive export subsidies from the state. After 1993, agricultural export subsidies exceeded Hungary's Uruguay Round commitments in the range and value of products subsidized; in October 1997 the WTO approved an agreement in which Hungary committed to phase out excess subsidies and not to expand exports of subsidized products to new markets. Hungary is abiding by the terms of that agreement in phasing out subsidies, despite continued political pressure from domestic constituencies.

7. Protection of U.S. Intellectual Property

Intellectual Property Rights laws in Hungary are generally good, but insufficient resources, court delays, and light penalties hamper enforcement. In 1993 the United States and Hungary signed a comprehensive Bilateral Intellectual Property Rights Treaty. Hungary also belongs to the World Intellectual Property Organization; Paris Convention on Industrial Property; Hague Agreement on Industrial Designs; Nice Agreement on Classification and Registration of Trademarks; Madrid Agreement Concerning Registration and Classification of Trademarks; Patent Cooperation Treaty; and Bern and Universal Copyright Conventions. The 1995 Media Law makes broadcast transmission licenses conditional upon respect for international copyrights. In 1997 legislation strengthened access to legal injunctions in infringement cases. In 1998 Hungary ratified the new WIPO Copyright Treaty and Performances and Phonograms Treaty. In compliance with its TRIPS obligations, Hungary enacted a new copyright law that went into effect on September 1, 1999. This replaced the

1969 Copyright Law and introduced modern copyright legislation. There is some question of whether sufficient legal authority exists for civil ex parte search procedures. Hungary is currently on the Special 301 Watch List, mainly due to confidential data protection and enforcement issues.

Patent protection exists for both products and processes, but problems exist with the protection of data submitted to regulatory authorities in the process of applying for and registering pharmaceutical products for marketing authority. The Hungarian government claims that its unfair competition legislation is adequate to prevent the use of data submitted by multinational research pharmaceutical firms from being used by domestic, generic drug manufacturers, but examples exist where generics have actually come to market prior to or very soon after the original product. Hungary is working on a data exclusivity protection provision in its revised Medicine Act, but it may not give the same level of protection available in the United States and the European Union. Hungary has requested derogations of data exclusivity protection and of supplemental protection certificates for pharmaceutical products in its EU accession negotiations. Hungary has been invited to join the European Patents Agreement beginning July 1, 2002.

Trademark infringement is a problem in Hungary, with various counterfeit goods (e.g. perfumes, clothing) available on the local market. These goods appear to be entering Hungary from other countries rather than being manufactured here. The number of civil actions brought before the Budapest Metropolitan Court (the exclusive court of competence for these cases) is up dramatically since 1997, but the enforcement of sanctions against the sale of pirated goods is still lacking. There are no available estimates of the losses incurred by the various industries due to either black or gray market activities. This area of IPR infringement is receiving increased attention from Hungarian and international law enforcement, however, due to the involvement of organized crime and connections with money laundering schemes.

Copyright protection is weak in Hungary, with pirated CDs, tapes, videos and software available on the local market. Many of these products are produced in Hungary. Video and cable television piracy is widespread, and local television and cable companies regularly transmit programs without authorization. Local groups such as the Business Software Alliance and the Hungarian Anti-Piracy Association are funded in part by manufacturers associations (e.g., Motion Picture Association) and are working to reduce the level of piracy, in cooperation with Hungarian law enforcement. There are about 1,000 software copyright court cases tried each year. Government cooperation has been good, but not enough resources are available to effectively stop copyright infringement. The International Intellectual Property Alliance estimates that total losses due to piracy in 1999 were $30 million, down significantly from an estimated $74 million in 1998. Some estimates suggest, however, that over half of the business software in use nationally is illegal and could represent annual losses of over $50 million.

In addition to the direct losses noted above, the lack of data exclusivity protection in Hungary might deter U.S and multinational pharmaceutical companies from bringing new products to the Hungarian market. The Pharmaceutical Research and Manufacturers Association is compiling estimates of the losses incurred by the pharmaceutical industry due to this lack of IPR protection.

8. Worker Rights

a. *The Right of Association:* The 1992 Labor Code, as amended in 1999, recognizes the right of unions to organize and bargain collectively and permits trade union pluralism. Workers have the right to associate freely, choose representatives, publish journals, and openly promote members' interests and views. With the exception of military personnel and the police, they also have the right to strike.

b. *The Right to Organize and Bargain Collectively:* Labor laws permit collective bargaining at the enterprise and industry levels. The Economic Council (formerly the Interest Reconciliation Council), a forum of representatives from employers, employees, and the government, sets the minimum and recommended wage levels in the public sector. Trade unions and management negotiate private wage levels. Special labor courts enforce labor laws. Affected parties may appeal labor court decisions in civil court. The 1992 legislation prohibits employers from discriminating against unions and their organizers.

c. *Prohibition of Forced or Compulsory Labor:* The government enforces the legal prohibition of compulsory labor.

d. *Minimum Age for Employment of Children:* The Labor Code forbids work by minors under the age of 14, and regulates labor conditions for minors age 14 to 16 (e.g., in apprenticeship programs).

e. *Acceptable Conditions of Work:* The Labor Code specifies conditions of employment, including: working time, termination procedures, severance pay, maternity leave, trade union consultation rights in management decisions, annual and sick leave entitlement, and conflict resolution procedures.

f. *Rights in Sectors with U.S. Investment:* Conditions in specific goods-producing sectors in which U.S. capital is invested do not differ from those in other sectors of the economy.

Extent of U.S. Investment in Selected Industries—U.S. Direct Investment Position Abroad on an Historical Cost Basis—1999

(Millions of U.S. dollars)

Category	Amount	
Petroleum		-22
Total Manufacturing		610
Food & Kindred Products	-56	
Chemicals & Allied Products	144	
Primary & Fabricated Metals	(1)	
Industrial Machinery and Equipment	363	
Electric & Electronic Equipment	-19	

Transportation Equipment	(1)	
Other Manufacturing	34	
Wholesale Trade		139
Banking		(1)
Finance/Insurance/Real Estate		(1)
Services		-37
Other Industries		640
TOTAL ALL INDUSTRIES		1,425

(1) Suppressed to avoid disclosing data of individual companies.
Source: U.S. Department of Commerce, Bureau of Economic Analysis.