

**THE HUNGARIAN
LABOUR MARKET
IN 2008-2009**

ZSOMBOR CSERES-GERGELY

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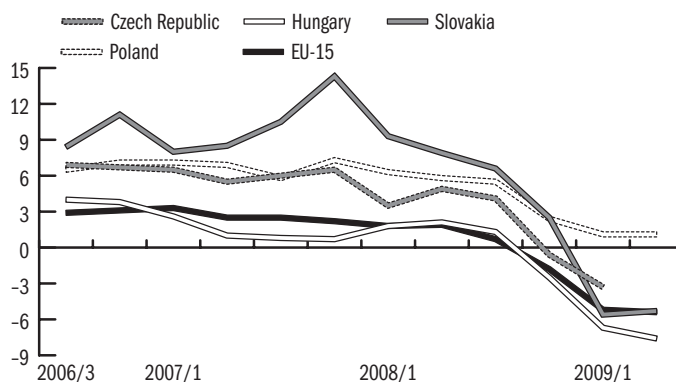
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Following several years of stagnation, employment entered a course of decline towards the end of 2008. This chapter examines the first year of the economic crisis, with special emphasis on labour market processes and the policies affecting these processes. As will soon become clear, the factors contributing to the decline in 2008 included not only the crisis but also various demographic processes and structural problems that had been left unresolved for decades. It should be noted that the slump in employment was not at that time accompanied by a drop of similar magnitude in economic activity. This was probably in large part due to employment policies focusing on the reduction of inactivity just as much as on the tackling of unemployment, which had not been the case during the years following the regime change.

1. THE ECONOMIC SCENE

The global financial crisis emerging during the second half of 2008 gave rise to a substantial decline in both production and consumption in the economies of the European Union, which led to a major shrinkage in both internal and external market trade. Among the Visegrád countries, Slovakia and Hungary suffered the greatest drop in GDP (*Figure 1*). By the second half of 2009 there was some improvement thanks to recovery measures in the central budgets and the reserve banks. The decline in public consumption was somewhat slower than in investment or export, which immediately reacted to the disturbances in the financial markets, but it is expected to persist longer as a result of the rise in unemployment.

**Figure 1: The development of real GDP in the Visegrád countries
(percentage changes relative to the corresponding period in the previous year)**



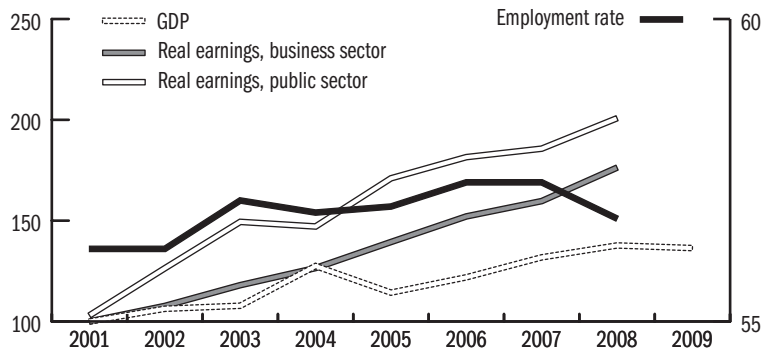
Source: EUROSTAT on-line database (teina011).

Hungary felt every effect of the crisis that other countries felt. The paradigm change in credit and funding practices constituting the root of the crisis deserves special mention. The credit sources previously within easy reach have been blocked one after another and enterprises relying on these loans have been forced into a very tight corner (MNB, 2009a). Circumstances specific to Hungary have meant, however, that the country has had to face further challenges. The insecurity surrounding the change of Prime Minister and the substantial government debts had an adverse effect in more ways than one on the business environment and, thus, the position of enterprises. The exchange rate of the Hungarian forint floating since February 2008 immediately reacted to the finance position of the country and to the market's level of confidence in the government. As a result, starting in the summer of 2008, the exchange market value of the forint fell by about a quarter in half a year, which meant another blow for those having foreign currency loans, including enterprises. Once its initial struggles were over, the newly formed government pledged to carry through a series of long overdue structural reforms. In parallel with its activities, the intensive stock market conjuncture, the financial turmoil and the convulsions of the exchange rate settled, and in August 2009 the economy was characterised by relative calm and a confident outlook.

Looking at the entire year, over the first three quarters the Hungarian GDP displayed an increase of about 2 per cent compared to the same period of the previous year, which was then followed by a sharp decline. By the second quarter of 2009 the reduction had reached 7.6 per cent and there were few signs of positive change. *Figure 2* displays the Hungarian GDP values (left axis) and wages and employment (right axis) over recent years. While the changes of the past few months are of a magnitude not seen for a long time, the annual figures unequivocally indicate that the decline started earlier in Hungary – in parallel with the Gyurcsány government's stabilisation programme of 2006.

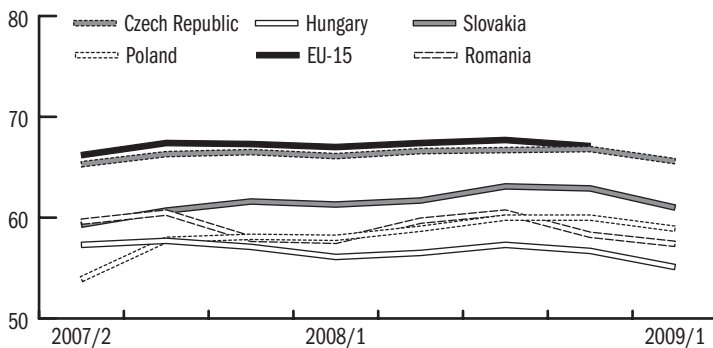
The employment figures displayed in *Figure 3* are also suggestive of a deeper and earlier crisis. Across the EU-27, the employment rate among the 15–64 year-old population increased fairly dynamically from 62.9 in 2005 all the way to 65.5 per cent in 2008. In the Visegrád countries, especially in Poland and Slovakia, the employment rate showed an almost uninterrupted rise during the post-2006 boom preceding the collapse of the financial markets. For Hungary, however, the figures show continued stagnation over the same period.

In Hungary, the slump in consumption and especially in export demand at the beginning of 2009 brought about a clear decrease in employment reaching well beyond general seasonal effects. This meant that the modest improvement experienced over the preceding decade was essentially nullified: the employment rate in the first quarter of 2009 was once again at 55 per cent, where it had been in the first quarter of 1999.

Figure 2: Macroeconomic indicators in Hungary, 2001–2009

Note: GDP value of 2009 is a Eurostat estimate. GDP volume: 2001 = 100, earnings: average earnings in the business sector in 2001 = 100, real earnings deflated according to the consumer price index. Employment rate on the right scale.

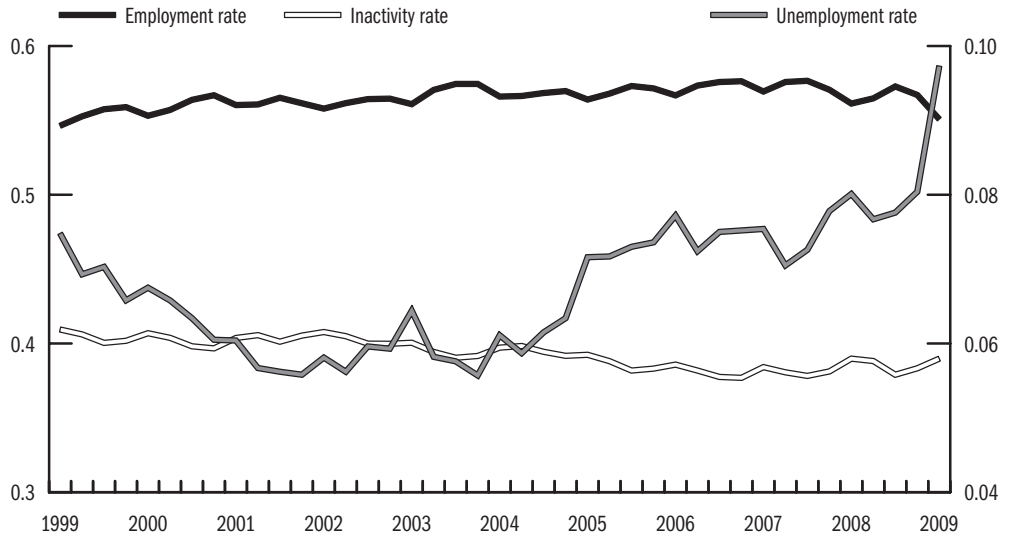
Source: Earnings, employment: authors' calculations based on Hungarian Central Statistical Office data. GDP: Eurostat on-line database (nama_gdp).

Figure 3: Quarterly employment rates in the Visegrád countries, population aged 15–64

Source: Eurostat on-line database.

But the situation is not as bad as it seems. The ten-year improvement in employment was primarily grounded in a steady decrease in inactivity, a rise in the statutory retirement age and an improvement in schooling, and these trends are expected to persist in the future. Importantly – as shown in *Figure 4* – in contrast with previous shocks, the slump in employment has not so far been accompanied by a significant increase in inactivity, but has mainly been realised as an increase in unemployment (right axis). The micro-level data of employment leavers are concordant with this observation. As can be seen in *Figure 5*, the first quarter of 2009 was marked by a sudden rise in the percentage of people becoming unemployed, while the increase in the proportion of people exiting employment for inactivity was only slightly higher than is usual at the beginning of a new year.

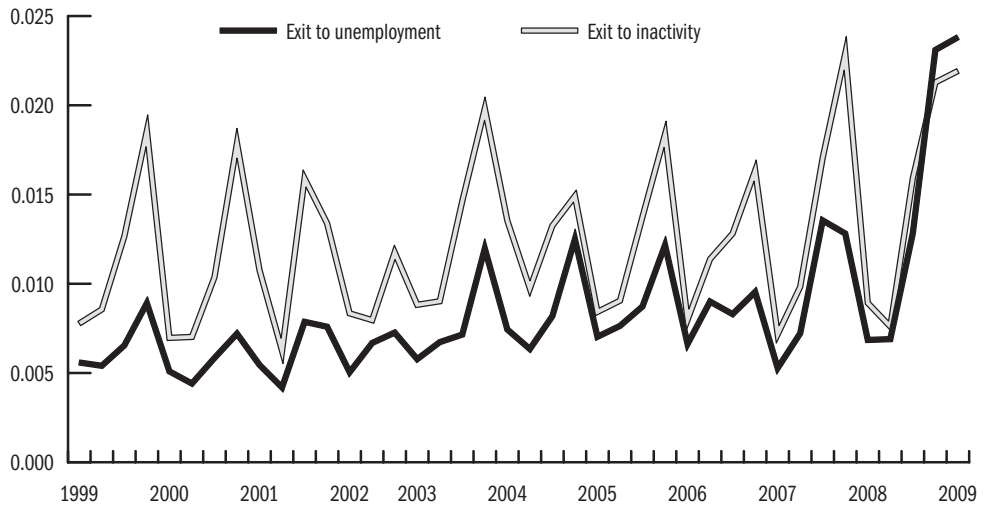
Figure 4: Main labour market indicators, 1999–2009



Note: Unemployment rate displayed on the right axis.

Source: Authors' calculations based on the HCSO Labour Survey data, the 15–64 year-old population.

Figure 5: Quarterly exit rate from employment, population aged 15–64



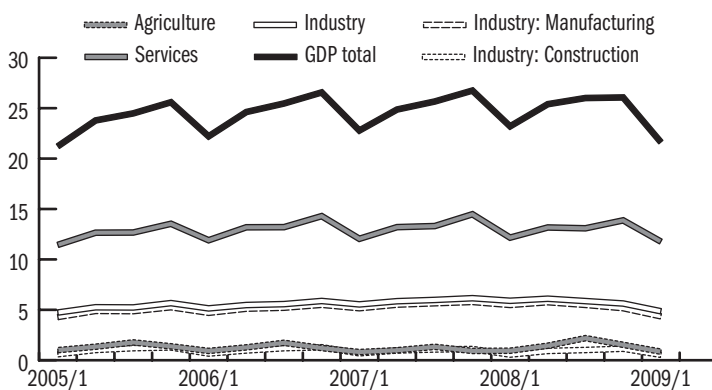
Source: Authors' calculations based on the HCSO Labour Survey panel, unemployment as defined by the ILO.

2. LABOUR DEMAND

The labour demand effects of the economic crisis

The global crisis started as a credit and finance crunch, but its effects soon spread out to the real economy. The sectors most deeply affected by the financial market turmoil were the automotive industry, the various services and retail businesses selling high-value goods. In Hungary these sectors were hit by the crisis through three different channels: local consumption decreased both because of the constrained credit market and as a result of the drop in incomes, and as the European (especially the German) market was also in crisis for similar reasons, the demand for export also plummeted (MNB 2009a, 2009b). Given the decline in investments on account of increasingly limited credit options and failing prospects, and the fall in incomes among the population, the effects of a financial turmoil will sooner or later be felt by every sector of an economy. As can be seen in *Figure 6*, agriculture was left largely undisturbed by the crisis until the end of the first quarter of 2009. While in the construction industry there was a decline in demand, this was part of a longer-term process. The sectors showing the strongest signs of decline were the heavily export-oriented industries, especially the manufacturing industry.

Figure 6: Quarterly change in real output in selected sectors, 2006-2009



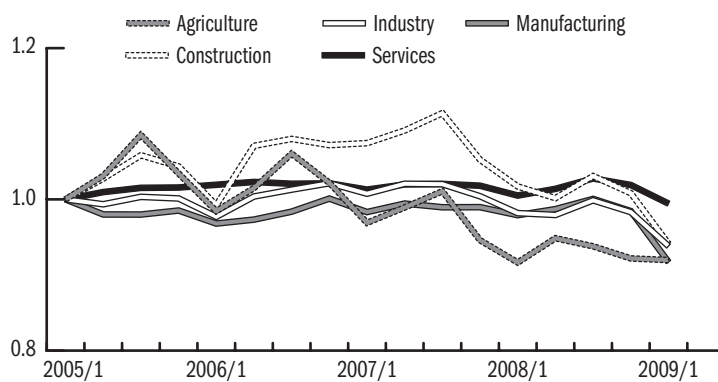
Notes: At year 2000 prices, the GDP of agriculture in Quarter 1 of 2005 = 100. The figure displays the GDP of individual sectors relative to agriculture: the figures for the beginning of 2005, for instance, show that the contribution of the service sector to the gross Hungarian output was more than ten times that of agriculture, and the manufacturing industry contributed more than four times more.

Source: Authors' calculations based on HCSO data.

Figure 7 displays changes in the workforce sizes compared to the first quarter of 2005 in the different sectors. In the construction industry and in agriculture the downward trend began, respectively, in 2007 and 2005, i.e., well ahead of the crisis, as a result of sector-specific business cycles and, presumably, of their capital intensive restructuring. In industry, especially in manu-

facturing, and in the service sector, in contrast, the decline in employment clearly developed in parallel with the crisis.

Figure 7: Quarterly change in employment in five main sectors (Quarter 1 in 2005 = 100)



Source: HCSO.

Due to the geographical distribution and the specialised labour demand of the enterprises involved, the sector-specific demand shock concentrated in the western part of Hungary and among skilled workers. Although a decrease was observed in the country's overall employment rate as well as for each educational group, the drop was markedly steeper, and statistically significant, among skilled workers in the Northwest and West border regions (*Table 1*). This may also explain the fact that men and women were affected differently by the crisis, since the manufacturing industry employs men in considerably larger proportions. While the employment rate among women fell by half a percentage point, from 50.1 per cent in the first quarter of 2008 to 49.6 per cent in the first quarter of 2009, the corresponding change among men was more than 1.5 percentage points, from 62.5 to 60.8 per cent.

Table 1: Changes in employment rates between the first quarter of 2008 and the first quarter of 2009 (percentage points)

Region	Primary	Vocational	Secondary	Tertiary	All
Central Hungary	0.00	-0.02	-0.01	-0.01	<i>-0.01</i>
Northwest	0.00	<i>-0.05</i>	0.00	0.02	<i>-0.01</i>
West border	-0.03	<i>-0.06</i>	0.00	-0.01	<i>-0.02</i>
Southwest	-0.02	0.02	0.03	-0.01	0.02
Northern Hungary	-0.03	-0.03	0.01	-0.02	<i>-0.01</i>
Northeast	-0.03	-0.02	-0.02	-0.02	<i>-0.02</i>
Southeast	-0.02	-0.03	-0.02	0.00	<i>-0.02</i>
All	-0.02	-0.03	-0.01	-0.01	<i>-0.01</i>

Note: Statistically significant changes are marked in italics.

Source: Authors' calculations based on the HCSO Labour Survey.

The labour market impact of the global crisis also surfaces in the Hungarian Employment Service records of workforce reductions and vacancies. The period when the number of employees laid off as part of an announced workforce reduction increased to a level well above previous years' average was between December 2008 and May 2009. As we can see in *Table 2*, dismissed employees do not immediately appear among the customers of job centres, and those living in regions characterised by higher levels of unemployment are more likely to register.

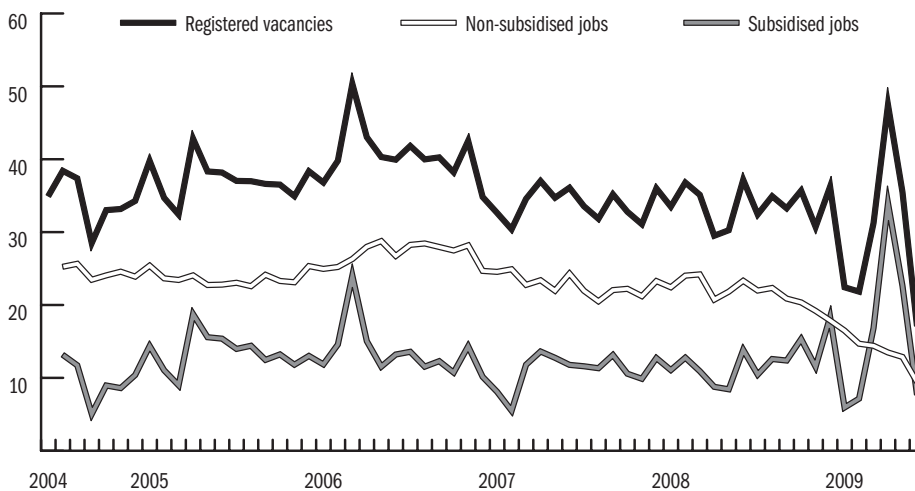
Table 2: Workers registering as job seekers after being laid off as part of mass layoffs by region

Region	Announced lay-offs,* N	Of those registering as unemployed, N			Ratio of registering workers to announced lay-offs
		October-December 2008	January-March 2009	April-June 2009	
Central Hungary	5 927	6	190	851	13.2
Southeast	2 129	6	317	304	35.8
Northwest	6 845	15	1 255	1 750	38.9
Northern Hungary	3 105	7	394	795	44.9
West border	4 924	22	569	1 880	56.2
Southwest	2 921	45	216	1 205	59.9
Northeast	3 770	356	693	620	63.1
All regions	29 621	457	3 634	7 405	38.8

* The number of people affected by layoffs following 1st October 2008 whose notice period ended by 30th June 2008. Classified according to the laid-off workers' place of residence (rather than the job location).

Source: Hungarian Employment Service.

Figure 8: Number of registered subsidised and non-subsidised vacancies

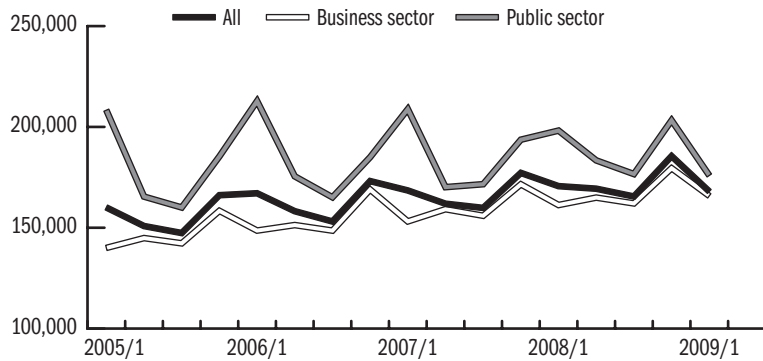


Source: MNB (2009b) Hungarian National Bank figures based on Hungarian Employment Service data.

The number of announced non-subsidised jobs entered a phase of steady decline in the summer of 2008 (Figure 8). The *Pathway to Work* programme was launched during the first quarter of 2009 with the goal of counteracting this trend, and while it has improved employment and unemployment figures, it cannot alleviate the effects of the crisis – more will be said about this later.

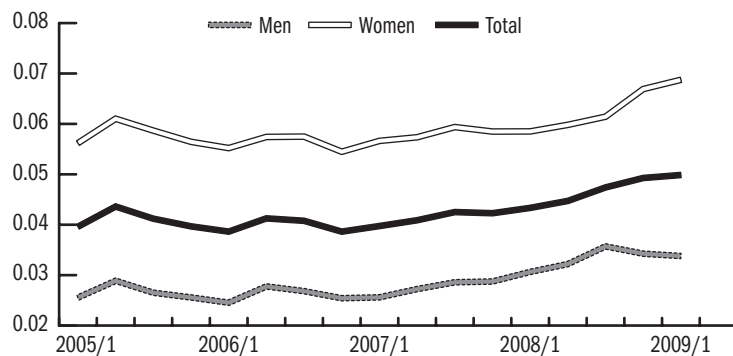
The decline in labour demand resulting from the increasingly poor profit prospects is reflected not only in mass layoffs but also in wage levels, although wage responsiveness appears to be slowing down for the moment (Figure 9). The average wage continued to fall but the figures of the last quarter indicate a slower rate of decrease. The interpretation of the trends remains uncertain, however, given the increase in part-time employment displayed in Figure 10 (MNB, 2009b).¹

Figure 9: Gross real wages in the public and the private sectors, 2005–2009 (at Quarter 1, 2005 prices)



Source: HCSO on-line database.

Figure 10: Proportion of part-time employment, 2005–2009



Source: HCSO Labour Survey.

¹ HCSO statistics indicate that the wages of full-time workers decreased to a lesser extent than the overall trend. We cannot tell, however, whether this reflects an improvement or an effect of compounding.

There may be a number of (not incompatible) explanations for the increasing share of part-time employment: a general upward trend in more flexible atypical employment models; the introduction of increasingly stringent measures

fighting the shadow economy from 2006 onwards; confidence in the temporary nature of the demand reducing effects of the global crisis; or the crisis life belt offering cash incentives to employers having employees changing to part-time employment.

Policies

Governments in every country in the world have developed some strategy of fighting the impact of the crisis. At the rather late date of May 2009, the *Employment Summit* was held by the European Union in Prague. The Summit agreed on strategies related to the tackling of the crisis and to employment policies, several elements of which involve the triggering of a positive shock – relying on government expenditure – to counteract the negative shock of the crisis. Since the proposals were made almost three quarters of a year into the crisis, a considerable share of the strategies agreed on had already been implemented in the various member states and were now granted funding.

The publication summarising the strategies of the European Union (*Shared commitment for employment*) proposes three main policies in addition to other measures related to the crisis: 1) to save existing jobs, create new jobs and encourage mobility, 2) to provide training and improve the match between labour market demand and supply, and 3) to improve employment odds.

The Hungarian government's policies have approached the task of tackling the crisis from two major directions. First, credit opportunities, export arrangements and guarantees were expanded in an effort to counterbalance the turmoil in the financial market.² These large-scale support programmes offering hundreds of billions of forints (billions of Euros) are primarily aimed at saving enterprises hit by the crisis, and if they are successful, the jobs at risk will also be saved – careful research will be needed, however, to assess the impact of these measures in the future.

The other strain of policies involves a substantial boost in the resources allocated directly for job preservation and creation. In the first phase of the programme locally financed funds were opened: a job preservation fund with a 1.5 billion forint (about 5.5 million EUR) budget devoted to the prevention of mass layoffs; a variety of job preservation funds mediated by regional job centres (wage subsidies, training, temporary services for people about to be laid off) with a budget of 10 billion forints available until the end of 2009; and three competition-based grant schemes maintained by the Hungarian Employment Foundation and open to enterprises. The three grant schemes, which were announced in February 2009, and depleted by March, distributed more than seven billion forints in total a) to prevent the loss of the jobs of employees threatened by layoffs (*Preservation* programme); b) to secure a humane arrangement for those who could not avoid layoffs and help them find and start a new job (*New Prospects* programme); and c) to provide support for

² http://www.kormanyszovivo.hu/page/valsagkalauz_vallalkozasoknak.

enterprises that were in a position to employ those whose jobs fell victim to the crisis (*On to Work* programme). The quick depletion of the funds suggests that they were highly popular – it will be the task of future studies to assess their effects together with the effects of other job preservation programmes.

The local sources of financing the intervention measures suggested by the European Commission are supplemented by the more substantial source offered by the European Social Fund. This provides the financial support for the large-scale Social Renewal Operational Programme No. 2.3.3. A launched in May 2009³ with aims similar to those of the *Preservation* programme. With a budget of 20 billion forints (about 75 million Euros) in total, the programme offers grants to micro-, small and medium-sized businesses and is open to applications until December 2009. The grants are intended to allow businesses shaken by the crisis to reduce the working week of their employees and use the remaining time to provide in-service training. Currently there are government plans to create a 10 million forint fund and extend the programme to large businesses starting this autumn (Social Renewal Operational Programme No. 2.3.3.B).

These intervention programmes are certainly not of a negligible scale. It is worth mentioning, however, that the policy they support is the most defensive kind of strategy proposed by the EU: job preservation without any need for labour market flexibility. This contrasts with the risk taking nature of the locally funded *New Prospects* and, especially, the *On to Work* programmes. None of the grant schemes using the EU funds were aimed at improving flexibility and only meagre support was available for job creation (such as the support offered to firms with high value added totalling 1.5 billion forints, or the 480 million forint fund for job creation).

It is difficult to predict, however, how successful or efficient direct labour market interventions may turn out to be. Although the message sent by the Hungarian media in August 2009 is that the job preservation programme had helped save the jobs of 46 thousand employees, this figure in fact refers to the number of people participating in the programme. Grants of this kind are difficult to target with precision and thus they remain prone to operating with a substantial dead loss, i.e., the risk of supporting employers that could also have saved those jobs in the absence of support. This risk may be reduced in the Social Renewal Operational Programme No. 2.3.3, where a new tool – an assessment system modelled on the enterprise credit scoring system developed by the International Training Center for Bankers – was used to screen businesses which, while hit by the crisis, were nevertheless likely to survive without support. The effects of the programme will, once again, need to be evaluated in a comprehensive research study carefully comparing the development of participating and non-participating companies at an aggregate and at an individual level.

³http://www.nfu.hu/informacios_nap_a_tamop_2_3_3_09_munkahelymegorzo_tamogatas_kepzessel_kombinalva_palyazathoz_kapcsolodoan.

The government resources allocated for business support programmes were substantially surpassed by the funds directly invested into public sector job creation. From 2007 onwards, a number of blueprints were worked out for the expansion of the public employment programme, which were then used to develop the *Pathway to Work* programme launched in the spring of 2009, scaled, in response to the crisis, even larger than originally planned. The programme is an umbrella name for the reform package enacted in Act CVII of 2008 revising the obligations of those participating in the *regular social assistance* scheme. With respect to employment, the primary aim of the programme is to identify those *regular social assistance* participants who have the physical capability of working, and transfer them to a *work availability support* scheme, where support is tied to an obligation to perform paid public benefit work organised by their local governments. According to the figures for July 2009, around 70 thousand participants were working as part of the scheme: that is, a new sector of a size comparable to the workforce size of the entire Hungarian chemical or finance industry. As a direct effect, the programme decreases the number of the registered unemployed and also improves the employment rate because the participants' unemployed status is suspended for the period while they are performing public work. One important structural change is that the programme calls for closer co-operation between job centres and local governments, which work together in building a shared *employment and welfare database* containing all the relevant personal details of the participants.

Other effects of the programme triggered heated professional debates even before its launch. The participants employed within the *Pathway to Work* programme are not *de facto* participants in the country's labour market. They are recruited from among the long-term unemployed population, most of them are uneducated and live in regions where work is difficult to come by in any event. It is the intended aim of the programme to help this long-term unemployed population to return to the open labour market, but an outcome of this type has not been verified either by studies looking into similar programmes run in other countries or by the scattered experiences of previous Hungarian public employment schemes. The usual limitations of public employment programmes may be reduced as a result of a proposed modification to the law⁴ introducing the requirement that each *regular social assistance* claimant must contact their job centre before offering to perform public work. This way, those with a potential to find employment in the open labour market may have a better chance of doing so.

The positive impact of the programme on the crisis also appears to be of a superficial nature. Although it improves both employment and unemployment figures, it cannot improve the prospects of those recently becoming unemployed since they will have to wait for quite a long period of time before

⁴ Oral communication by Leó Lőrincz, head of the Employment and Service Development Department of the Hungarian Employment and Welfare Agency.

they can be eligible for the programme. Also, by reducing the number of active job seekers, it constrains one of the basic mechanisms of labour market adaptability. The reason being that the more people are willing to work – at least temporarily – for lower than usual wages, the quicker the market will recover from the rising unemployment effected by the declining labour demand and return to the original (or a higher) level of employment.⁵ And this willingness is likely to be greater if there are several competitors for each job. The artificial suppression of unemployment may therefore allay social tensions but it also hinders recovery from the recession.

Finally, we should also mention the wage and tax policies of recent years, which in part were developed independently of crisis relief measures, but which may have played an important role in the development of the current employment figures and wages. Some of the most important issues are the level of the minimum wage, the tax and contribution brackets and the measures aimed at clamping down on the informal economy. The real value of the total cost of the minimum wage has decreased in 2009, as has the guaranteed wage minimum payable to *skilled workers*: this may mitigate the decline in labour demand (*Figure 11*). For the regular minimum wage, the primary cause of the decrease was the reduction of contributions put into effect in July, while for the qualified workers' wage minimum, the decrease in real value can be attributed to its moderate, below-inflation increase.

Figure 11: Real value of the total cost of employment at the minimum wage, 1997-2009



⁵ As the current crisis originates in the financial market, the significance of wage responsiveness is even greater than usual. The insecurity generated by the crisis leads to an increase in interest rates and in the relative price of capital, and thus the chances of capital-intensive growth and flexibility will be reduced. The lower the costs of labour become, the faster will adjustment and recovery occur.

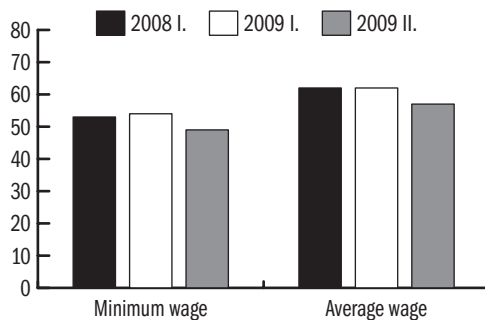
Note: At 1997 forint value, in 2009 according to the last inflation projection of 4.5% estimated by the Hungarian National Bank (*MNB*, 2009b). The values for 2009 were weighted to take the mid-year changes in contributions into account. The skilled worker wage minimum is the lowest wage payable for jobs requiring at least general or vocational secondary education (up till July 2009: the wage could be somewhat lower for employees with less than 2 years' work experience).

The objectives of encouraging the less highly educated to work and of moderating the negative effects of the financial crisis would easily justify bolder measures than that, such as nominally freezing the minimum wage, abolish-

ing the skilled workers' wage minimum, or relaxing some of the measures introduced at the end of 2006, especially the rule that set a minimum for the basis of compulsory social security contributions at twice the amount of the minimum wage.⁶ According to *MNB* (2008), the increase in the minimum wage payable to skilled workers may have contributed to the decline of employment in 2008, partly because the increase had a stronger effect on higher wage categories than expected (employers tried to preserve the relative proportions within their wage scales). *Kátay* (2009) even proposes that the skilled workers' wage minimum should be abolished altogether in order to improve wage flexibility and thus competitiveness.

In an effort to stimulate labour demand, a government decision was made to lower contribution rates as part of the crisis relief package: in July 2009 standard health care and employers' contributions were reduced from 32 to 27 per cent of the portion of the wage up to twice the amount of the minimum wage, above which the rate of 32 per cent remains. The special employers' contribution rate was also reduced by 5 percentage points (also up to twice the amount of the minimum wage). This special rate applies to young first-time employees within the first two years of their careers, employees over the age of fifty returning to work from unemployment and employees returning to work after a period of child rearing or taking care of a relative. As shown in *Figure 12*, these steps brought about a substantial decrease in the tax wedge, i.e., the tax burden on wages dropped to a lower percentage of the gross wages.

Figure 12: The tax wedge at the minimum wage and the average wage in manufacturing, 2008–2009 (per cent)



Note: Figures for Quarter 1, 2008: 137,931 forints per month before tax, Quarter 1, 2009: 137,379 forints; projection for Quarter 2, 2009: 137,104 forints.

Source: Taxes and contributions from Hungarian Tax Authority data, gross wages from HCSO institutional data and the projections of the Hungarian National Bank, assuming slower wage decline in the second quarter.

The decrease in the tax wedge is somewhat smaller at the level of the minimum wage because the upper threshold of tax credits has not been adjusted to follow the increases in the minimum wage since 2008, i.e., a little bit more of the once entirely tax-free minimum wage has been claimed back by the cen-

⁶ An employer may request exemption from the rule of double contributions base. The request is assessed with reference to the firm's profitability, that is, paying contributions after less than the double base considerably increases the risk of an extended audit by the tax authorities.

tral budget each year. Further contribution reductions are planned for 2010, the most important of which is that the fixed health care contribution will be scrapped, which is expected to lower the tax wedge at the level of the minimum wage by about 2.7 percentage points. Some of the remaining changes will leave the low-wage segments of the population unaffected, while others may or may not affect them.⁷

The reduction of wage costs and especially the contributions burden on low wages has long been among the recommendations of both Hungarian and international experts. This step is indisputably one of the wisest decisions the Hungarian government could choose to make. It could be a step not only towards recovery from the global crisis but also towards recovery from the older internal structural crisis and towards dislodging the economy from the persistently low level of employment.

3. LABOUR SUPPLY

In Hungary the employment rates are especially low among the uneducated, the young and the old populations and among women rearing young children, while the employment rates of middle-aged and relatively highly educated people approach the EU average (*Table 3*). The size of these groups relative to the total population is primarily a function of demographic processes – the best that policies can do is exert their influence on the level of economic activity in each group.

Table 3: Employment rate across various sub-groups in the Visegrád countries, 2008

Country	Aged 15–24 (men and women)	Women aged 25–39	Aged 55–64 (men and women)	Uneducated aged 25–64	Aged 25–64 (men and women)	Aged 15–64 (men and women)
Hungary	20.0	63.6	31.4	38.7	64.7	56.7
Poland	27.3	72.2	31.6	43.0	67.5	59.2
Slovakia	26.2	67.9	39.2	32.3	72.1	62.3
Czech Republic	28.1	66.0	47.6	46.5	75.1	66.6
Slovenia	38.4	85.4	32.8	55.0	75.2	68.6
EU-15	41.0	72.4	47.4	57.9	72.9	67.3

Source: Eurostat on-line database.

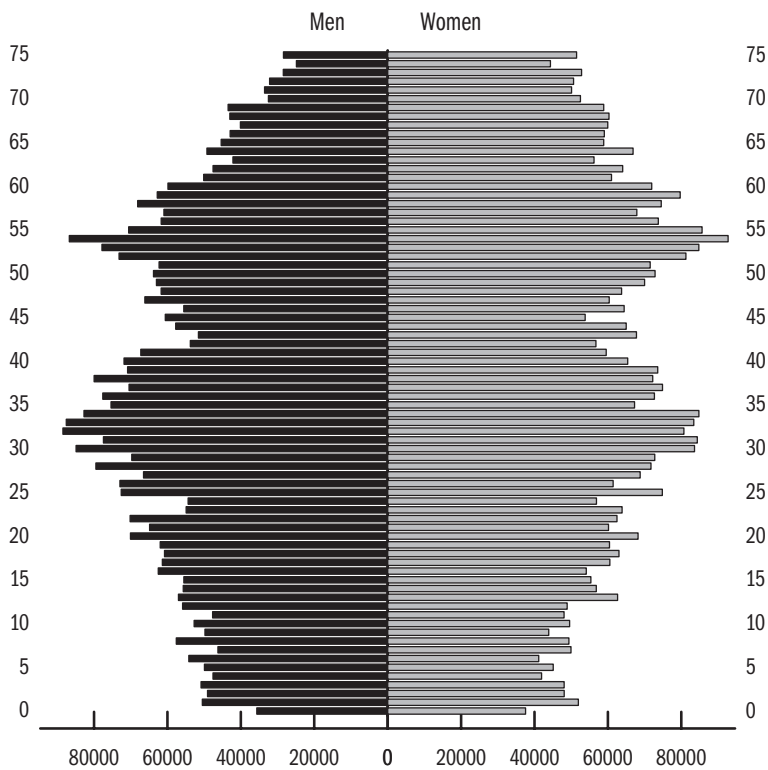
⁷ The decrease in contributions in effect from July 2009 is planned to be extended to wages above the double of the minimum wage threshold from 2010. There will also be changes in the rules of calculating the tax base of the personal income tax, which will be counterbalanced to some extent by adjustments to the tax rates and brackets

Compared to demand, the supply of labour is in several respects shaped by slower and longer-term processes. It is grounded in demographic processes, which determine not only the size of the working-age population as a whole but also the sizes of age cohorts of special significance with respect to the labour market. The age structure diagram of the Hungarian population in the first quarter of 2009 is displayed in *Figure 13*.

One of the most notable features of the age pyramid of the Hungarian population is the large number of so called *Ratkó children* of about 55 years of

age and *Ratkó grandchildren* of about 33 years of age.⁸ Both of these generations are close to life stages that have special significance in terms of labour market participation. The *Ratkó grandchildren* have just entered the best working age, which is, however, also the most active period of child bearing. In the short run, the rising trend in the number of births beginning in 2004 (the *Ratkó great grandchildren*) has the effect of lowering the activity of the working-age population. The youngest of the *Ratkó children* are about to reach the typical age of retiring with a disability pension while the oldest of the group are approaching the statutory old-age retirement age. On average more than 140 thousand people will reach the age of retirement between 2009 and 2013 while there are only around 120 thousand 18–22 year olds likely to enter the labour market.

Figure 13: Age structure of the Hungarian population



Source: Authors' calculations based on HCSO Labour Survey data.

The temporarily negative population processes are somewhat counterbalanced by the improvement in educational attainment. The expansion of education in the 1960s has now reached the pre-retirement cohorts – the increase in the employment rate among those over 50 is to some extent explained by the higher activity rate of people having at least upper secondary qualifications.

⁸ The *Ratkó period* is named after Anna *Ratkó*, Hungarian health secretary between 1950 and 1953, and refers to the period between 1950 and 1956 characterised by population policies prohibiting abortion and introducing a tax on childlessness. The generation of children born during this period are called the *Ratkó children* and their children are the *Ratkó grandchildren*.

The expansion of higher education in the 1990s surfaces in a similar way when looking at the middle-aged cohorts. Among the total population, the percentage of 15–64 year-olds having at most primary education decreased from 33.5 per cent in 2000 to 25.8 per cent in 2008, while the percentage having tertiary education increased from 11.7 to 16.5 per cent over the same period. This is likely to account for the fact that as a result of changes in the composition of the population the average employment rate has increased since 2000 even though the employment rate of each individual educational group has decreased.

Table 4 also shows, however, that the positive influence of improved education on employment is extremely slow. Moreover, notwithstanding the overall improvement in education, there still remains a large proportion of people leaving the education system with only primary qualifications. That is, in the absence of competent government interventions, the Hungarian economy is unlikely to grow out of the problem of low employment even among the uneducated.

Table 4: Employment rates of 15–64 year-olds by educational attainment, 2000–2008

Year	At most primary	Vocational secondary	General secondary	Tertiary	Total
2000	28.9	71.7	62.9	82.1	56.0
2001	29.1	71.8	62.5	82.2	56.2
2002	28.6	71.6	62.1	81.6	56.2
2003	28.4	70.5	62.9	82.0	57.0
2004	27.6	69.7	61.9	82.2	56.8
2005	28.0	68.7	61.7	82.5	56.9
2006	27.6	69.2	61.6	81.2	57.3
2007	27.3	68.6	61.6	80.0	57.3
2008	27.2	66.4	60.7	79.5	56.7

Source: authors' calculations based on HCSO Labour Survey data.

The level of activity among individual groups is strongly influenced by transfers. Welfare payments, pensions and generally any cash transfer not coming from work activities have the effect of lowering people's inclination to work, as has been empirically confirmed in Hungarian studies.⁹ Recognising the significance of this phenomenon – and complying with the expectations of the European Union – Hungarian policies have undergone gradual changes over recent years: while immediately following the regime change the reduction of unemployment and the social tensions stemming from it was the first priority, in recent years increasingly more attention has been paid to the level of economic activity among the working-age population both in terms of objectives and in terms of measures.

⁹ For an overview of empirical studies in Hungary, see: *Bódis et al* (2005) on unemployment benefit schemes, and *Cseres-Gergely and Scharle* (2007) on maternity benefits, pensions and social assistance.

Maternity benefits

In Hungary, the employment rate among mothers caring for children under the age of six lags 35 percentage points behind the employment rate among women having older children or no children. The corresponding difference is 20 percentage points in Germany and 1.6 percentage points in Denmark. Mothers' labour supply is discouraged both by the relatively generous cash transfers available to parents with young children and by the low accessibility and insufficient capacity of day care facilities.

In line with the shift in objectives, the development of children's day care facilities returned to the government agenda in 2004: the maintenance requirements imposed on local governments have been tightened, the funding rate per child has been increased for nursery schools, the regulations on starting and running alternative day care facilities for under 3s (family day care, integrated kindergarten) have been simplified and more resources have been allocated for institutional investments. Attempts at expanding the capacity of nursery schools have remained at a modest level, however. As part of the crisis relief measures – but clearly not with the intention of short-term expenditure reduction – a decision was made to reduce the maximum period of claiming maternity benefit: the first generation affected by this decision will be those whose children have their second birthday in 2012.

Pension-type transfers

In Hungary one in three people among the 55–64 year-old population works, which is not an especially low figure in the Visegrád region but falls far behind the EU average of 47 per cent and even further behind the Lisbon objective of 50 per cent. The gap is, to some extent, attributable to the relatively poor general health of the Hungarian population but is mainly explained by the low statutory retirement age and the regulations on eligibility, which were relaxed after the regime change and still offer relatively favourable terms of early retirement.

These regulations have been tightened in recent years. The new reform of the disability pension scheme endorsed in July 2007 focused on improving employment odds and left the system of incentives determining the likelihood of claims essentially untouched. The new regulations state that each claimant's health and *remaining* work capability must be thoroughly assessed, and health, welfare and employment rehabilitation services are offered based on the results of the assessment. Claimants are entitled to a rehabilitation allowance for the duration of the rehabilitation period, for a maximum of three years. The amount of the allowance matches, or slightly exceeds, the claimant's future pension but its payment is conditional on the claimant's uninterrupted co-operation with the job centre. An amendment endorsed last year also specifies the obligation of co-operation for persons receiving regular so-

cial assistance but judged to be ready for rehabilitation, although the requirement only applies to those having more than ten years before they reach the statutory retirement age. The tighter regulations on disability pension claims and the introduction of the rehabilitation allowance presumably accelerated the downward trend in early retirement beginning in 2002. This trend may come to a halt, however, as a result of the crisis – the rising number of claims seems to point in this direction, although up till now it has not been accompanied by an increase in the positively assessed claims of disability or similar allowance.

Looking at old-age pensions, the gradual increase of the statutory retirement age to 62 years initiated by Act LXXXI of 1997 has been completed in 2009. Although the option of early retirement with no loss of pension is still available provided that the required years of service have been completed, the increase in the statutory retirement age has made its contribution to the rise in economic activity over the past decade. In May 2009, taking advantage of the crisis, one of the first actions of the Bajnai government was to raise the retirement age in steps from 62 to 65 years over the period between 2012 and 2017, and to increase the minimum service period required for full-pension early retirement to 40 years. While the effects of these measures are obviously unobservable in 2009, both are highly important and well calibrated since, although the decision to retire is influenced by a number of factors, the statutory age is decisive (*Cseres-Gergely, 2007*).

The increase of the retirement age cannot, of course, have the intended positive effects unless the elderly remain not only active but also employed. Although we have limited experiences in this area, the raise implemented after 1997 suggests promising results. The Labour Survey results of the Hungarian Central Statistical Office show that the employment rate among women aged 55–59 increased from 13.6 per cent in 1998 to 38.7 per cent in 2008, while their unemployment rate rose from 4.8 to only 5.5 per cent (the male population is characterised by a similar pattern although with less gain). The significance of these results is not limited to the age cohorts involved but extends to the entire population: the rise in employment over the past decade is to a considerable extent attributable to the increase of the retirement age, although the effect substantially faded after 2005 (*Kátay, 2009*). While an increase from 55 to 62 years is not at all equivalent to a change from 62 to 65 years, the latter is also likely to be successful provided that suitable services, working week regulations, training and incentives are available to assist the elderly in their continued employment, and that the unemployment programmes are prepared for this special group of customers.

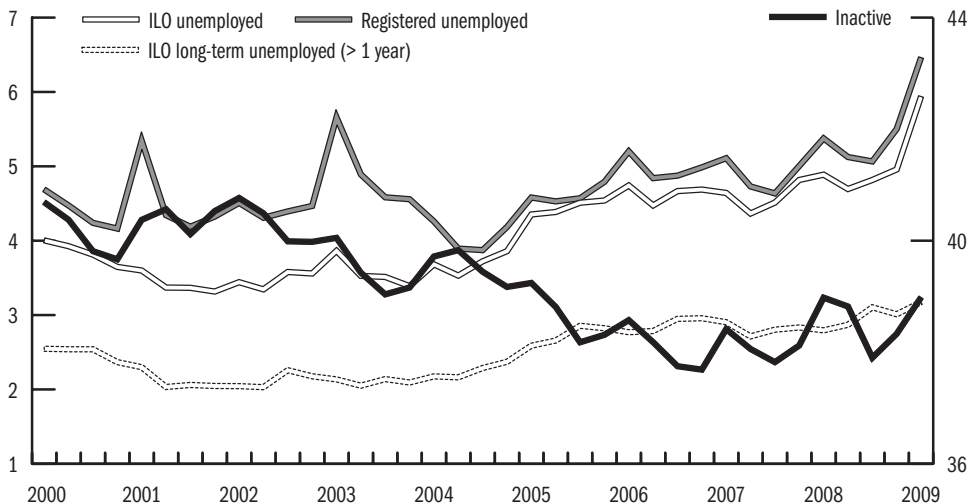
A change of considerably smaller but still measurable impact was the revision of pension formulas coming into effect in January 2008, which increased inactivity in the same year. The change involved calculating with net rather

than gross earnings, complete valorisation, the offer of extra premiums for retirement over the age of 40 and modifications to the regulations on large pensions. The first of these components encouraged a large group of people to retire at the end of 2007, before the changes took effect (*Figure 5*). Although the formula calculating the pension following early retirement remains flawed in terms of considerations of insurance mathematics, the revised formulas in combination with the raised retirement age create a fairer pension system.

Unemployment and unemployment benefits

Whatever indicator we look at, unemployment remains at a moderate level in Hungary: in the first decade of the century it remained under 5 per cent of the working-age population. As shown in *Figure 14*, from 2003 onwards the group of registered unemployed and the group of job seekers have been of about the same size among the total population. As was discussed before, this does not mean that all is well in the Hungarian labour market: the low level of unemployment is paired with a substantial inactivity rate and a low level of employment.

Figure 14: Size of various (partially overlapping) non-working groups relative to the 15–64 year-old population from 2000 by quarter (right axis: percentage of the inactive)

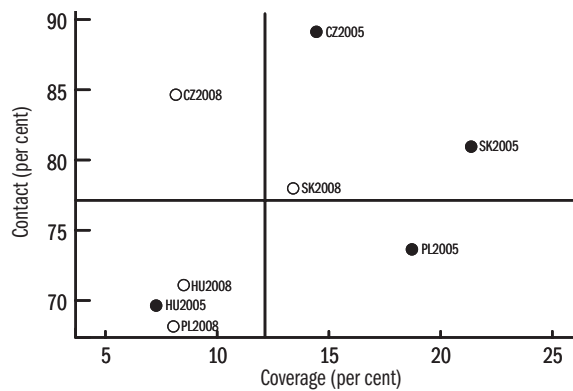


Source: HCSO Labour Survey.

In the Hungarian system a significant share of the working-age population receive welfare transfers not contingent on mandatory co-operation with job centres. In many cases the regulations may specify the condition of active job seeking but this requirement is rarely or inconsistently enforced. This phenomenon is visualised in *Figure 14*. Analysing the results of the *European Labour Force Survey* (EU LFS), *Bajnai, Hámori and Köllő* (2008) found

that in this respect the Hungarian pattern deviated from the patterns observed in other countries of the Visegrád region: while in Hungary, job centres have contact with a relatively small percentage of the non-working population and do not maintain an intensive relationship with the few who are registered, the Visegrád countries were, in contrast, characterised by high registration rates and close contact in 2005. *Figure 15* displays the changes between 2005 and 2008: although the gap between the four Visegrád countries narrowed, this was due to a decline in the other countries rather than to an improvement in Hungary.

Figure 15: Coverage and intensity of contact with the public employment services in 2005 and 2008 in the Visegrád countries for the 15–64 year-old non-employed population (reference lines mark the average of the two indices)



Coverage, displayed on the horizontal axis, shows the ratio of the registered unemployed to the total working-age non-employed population. Contact, displayed on the vertical axis, shows the percentage of those contacting their job centres within the two weeks preceding data collection. The figure differs from the graph in *Bajnai, Hámori and Köllő (2008)* in that those non-employed who are attending school are excluded here, as is the 59–64 year-old cohort. The latter exclusion has the drawback of leaving the effects of changes in the pension system uncontrolled for, but was a necessary decision as only aggregate Eurostat data are available for 2008. Source: Authors' calculations based on the Eurostat online database.

The high and rising level of long-term unemployment is explained by regulations that do little to encourage economic activity and by the persistent problem of highly limited labour market prospects the uneducated have to face.¹⁰ In Hungary the initiative of the largest scale aimed at tackling the problem of long-term unemployment is at present the *Pathway to Work* programme. As mentioned above, the official goal of the programme is to divide the population of regular social assistance recipients into two groups, and provide services and support better tailored to the needs of each in an effort to improve their economic activity. One of the groups is for those who are considered to be capable of work purely on account of their physical and intellectual abilities, disregarding the question of the competition in the labour market, and

¹⁰ See *Köllő (2009)* for details.

the other is for those who are not. The latter group continues to receive regular social assistance because the programme considers their position to be genuinely beyond help as regards employment. This presumably relatively small group is likely to remain persistently inactive. Participants aged under 35 and having less than eight completed years of schooling form a separate group: for them, the services focus on skills training, and they may satisfy the requirement of public work by attending training programmes. The potential merits of the *Pathway to Work* programme lie in the larger group of those capable of work, whose regular social assistance is replaced by *work availability support*, and who are required to accept the public work assigned to them for at least six hours a day in return for proper payment.

Public works are organised by local governments, but the administration of the move between different unemployment schemes, the transfer of payments and the task of sanctioning a refusal to co-operate are shared between the job centres and the local governments, which simplifies the maintenance of records accessible to both institutions.

It was already mentioned in connection with the crisis relief measures that although public work schemes are meant to assist the participants' return to the labour market, their success in this task remains questionable. This is a closed market, which is free from the challenges of the real market, such as job search, self-assertion, convincing the employer, securing and keeping the job, and does not involve costs (of training or travelling). While the participants may thus return temporarily to the regular rhythm of a working life, the labour market skills mentioned above will not be developed. Previous experiences suggest that the participants of public work schemes are less likely to be successful in the labour market than non-participants having the same observable abilities (*Firle and Szabó, 2007*).

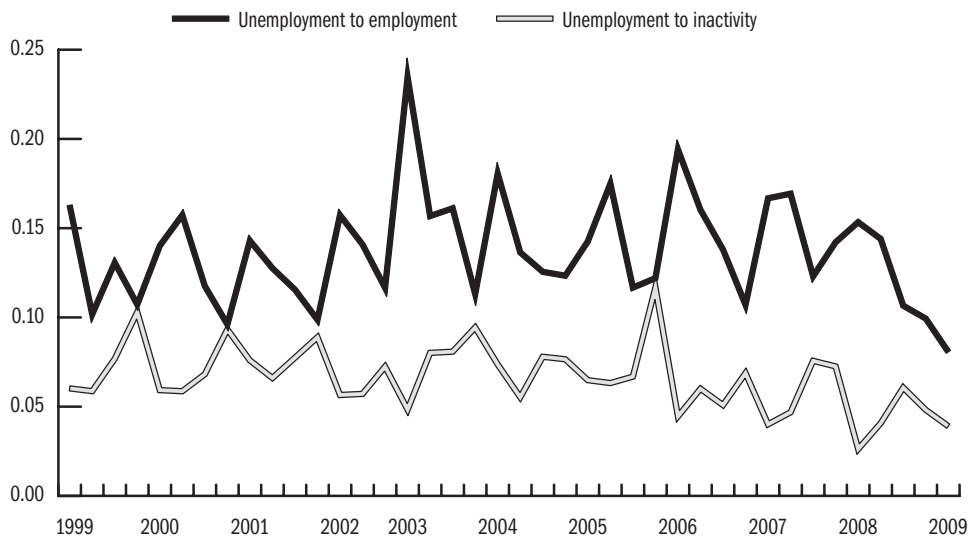
The crisis relief tasks assigned to job centres are in harmony with the government's line of policies as a whole, which is characterised by the pursuit of safe solutions, even at the expense of significant efficiency losses. Of the three approaches recommended by the EU, the Hungarian government has given priority to "job preservation" measures potentially involving an enormous dead loss, and fought to prevent the emergence of large-scale unemployment, a natural consequence of the crisis. Today, subsidised employment plays the role of the pension schemes that, a few years after the regime change, absorbed the large number of people losing their jobs – with the difference that the present solution also ensures the survival of potentially unfit enterprises. There is an important difference between the two situations, however: the resources devoted to tackling the current crisis are considerably smaller than the pension expenditure of the nineties, and they can be readily reallocated once the recession is over, since the beneficiaries of the support are not granted permanent entitlement. Although this approach is also propagated by the EU itself, the

Scandinavian countries and Great Britain, for instance, do not follow this line but relying on the purifying power of the crisis, choose to support employees leaving their unfit employers in finding another job and, thus, encourage labour market adaptability (EEO, 2009). In Hungary very little resources or attention have been devoted to this path of development, while the number of unemployed have risen sharply since the beginning of 2009.

In order to reveal the causes behind the substantial increase in unemployment in Hungary and to be able to respond to this problem with efficiently implemented policies, it is important to know the extent and direction of changes in the composition of the non-employed population: in what ways new entrants differ from previous groups of non-employed and unemployed.

Figure 16 clearly shows that in addition to the decrease in the inflow into inactivity, the probability of exiting unemployment in any direction also dropped by the first quarter of 2009. The share of the population entering inactivity has steadily decreased since 2004 and the figures for early 2009 suggest that this trend has not been reversed by the global crisis (the figure displays the data for the male population only in order to avoid inactivity due to child bearing confounding the picture). These trends indicate a further rise in the probability of long-term unemployment.

Figure 16: Percentage of people moving from unemployment into employment or inactivity relative to the size of the unemployed population in the previous period; by quarterly periods, men aged 15–64, 1999–2009

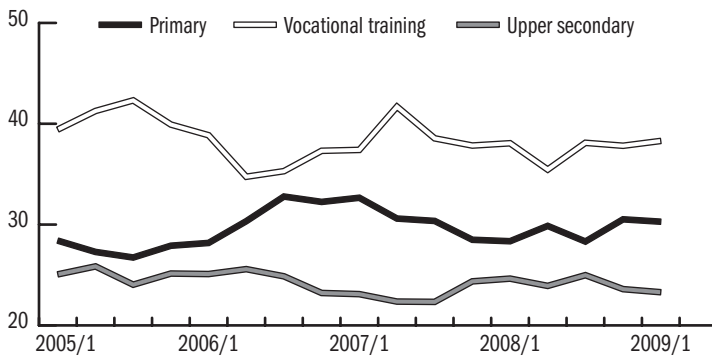


Source: Authors' calculations based on HCSO Labour Survey panel data.

For the first quarter of 2009 no major changes in the composition of new unemployment entrants are indicated by the Labour Survey figures. According to more recent data following unemployment registration up until June 2009,

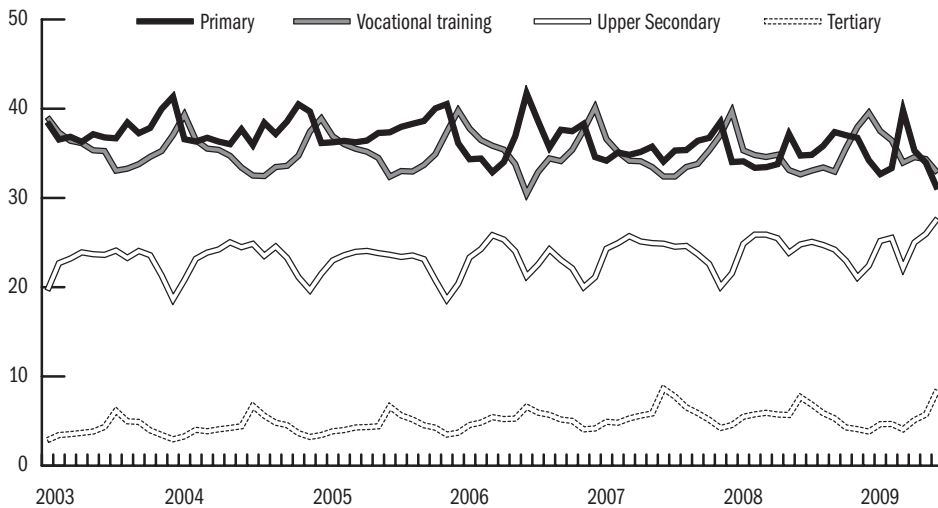
the increase appears to be significant only among those having upper secondary qualifications (*Figure 18*). Among new labour market entrants, however, the size of both the group having vocational training and the group having upper secondary qualifications has increased (*Figure 19*). The conclusion drawn from these data is that if there are significant changes in the composition of the new unemployed population, they could only be revealed by finer-grain indicators measuring productivity and vocational skills.

Figure 17: The educational composition of the new unemployed population, 2005-2009



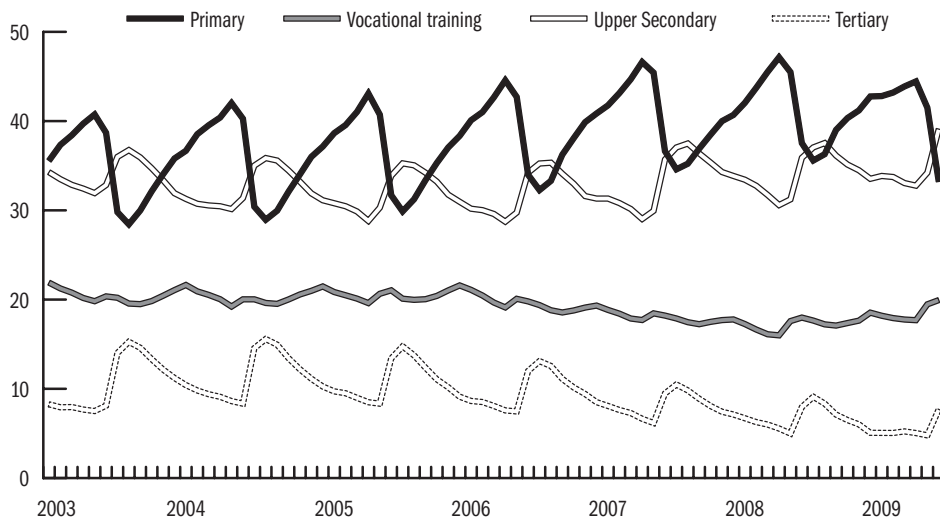
Source: Authors' calculations based on HCSO Labour Survey data, four-period moving averages.

Figure 18: The distribution of all unemployment registrations by educational attainment at monthly periods (per cent, total = 100)



Source: Hungarian Employment Service.

Figure 19: The distribution of unemployment registration among new labour market entrants by educational attainment at monthly periods (per cent, total = 100)



Source: Hungarian Employment Service.

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