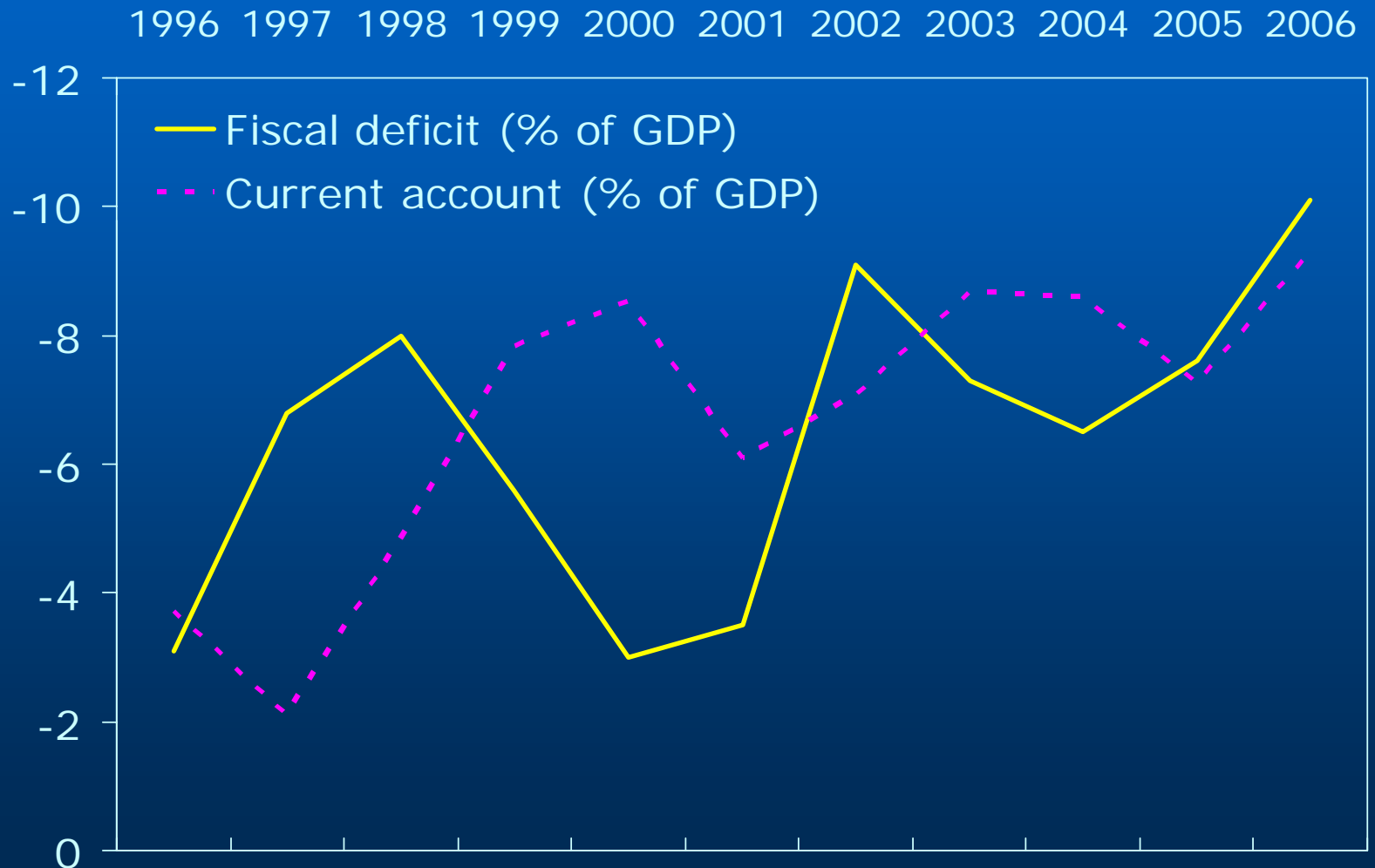


# Hungary: Some Thoughts on Why and How to Adjust Fiscal Policy

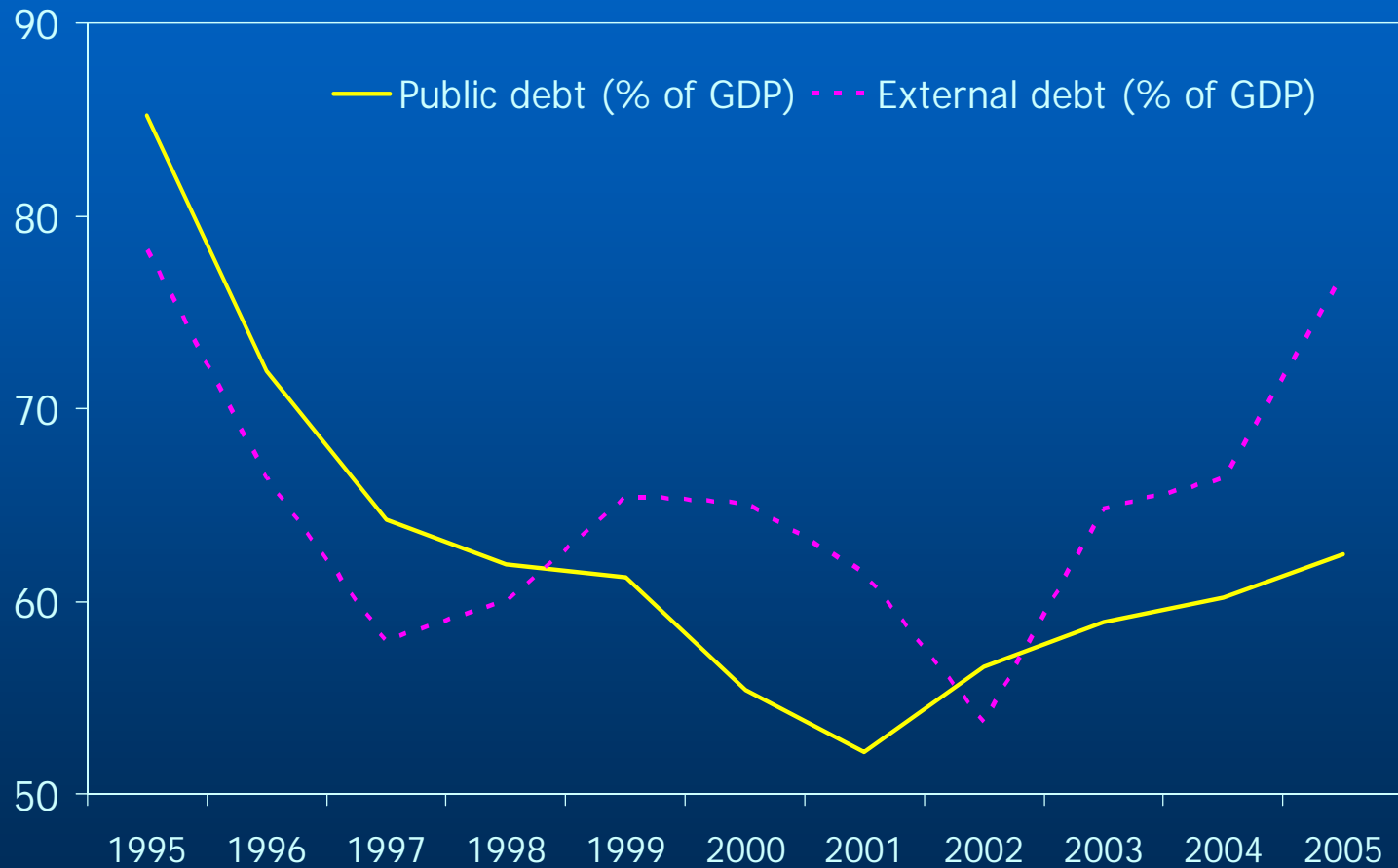
Christoph B. Rosenberg  
International Monetary Fund

August 2006

# The twin deficit problem is worsening...



... accompanied by worrying dynamics in public and external debt.



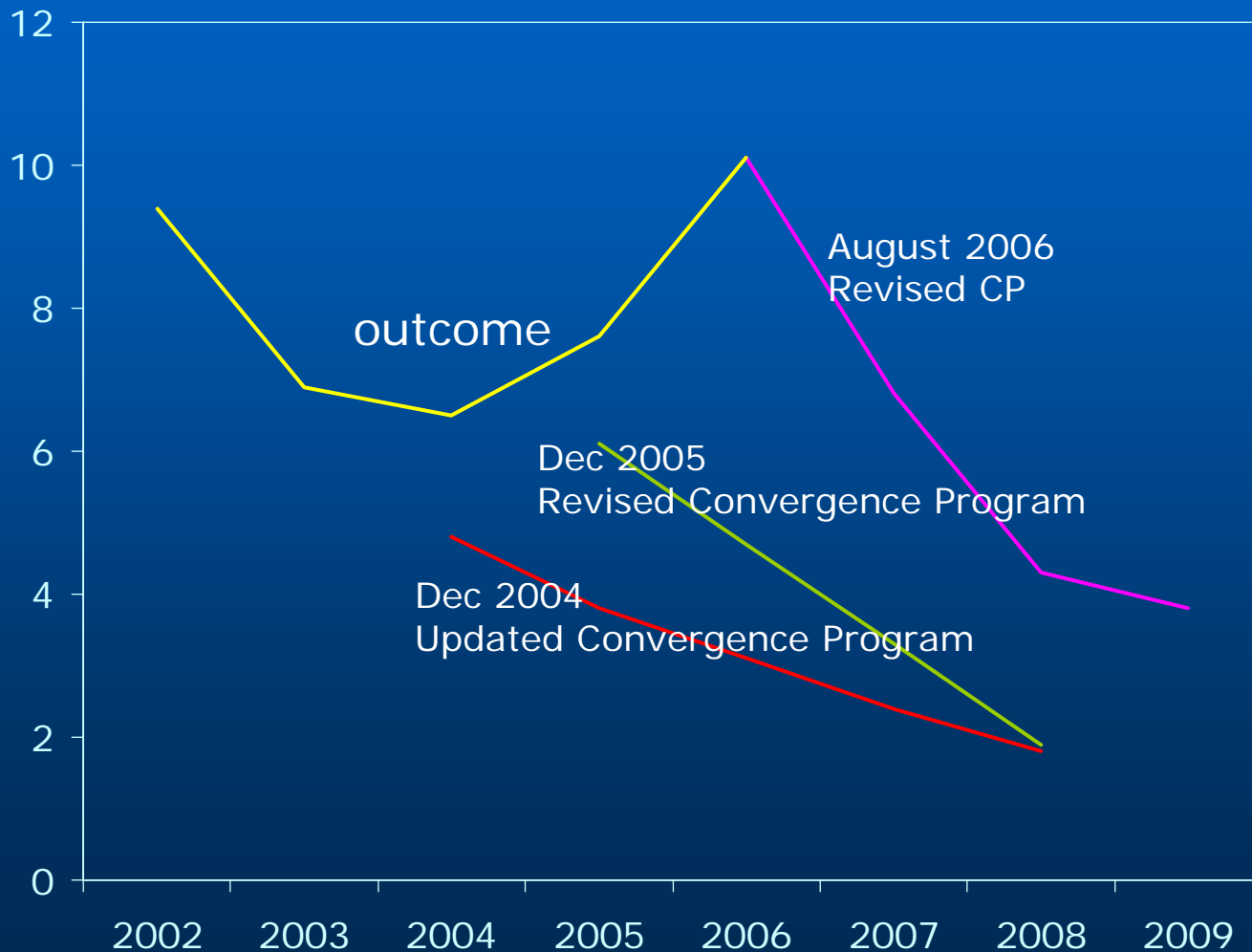
Hungary now appears more vulnerable than other key emerging market countries.

## Public Debt and External Debt and Deficits, 2005, % of GDP.

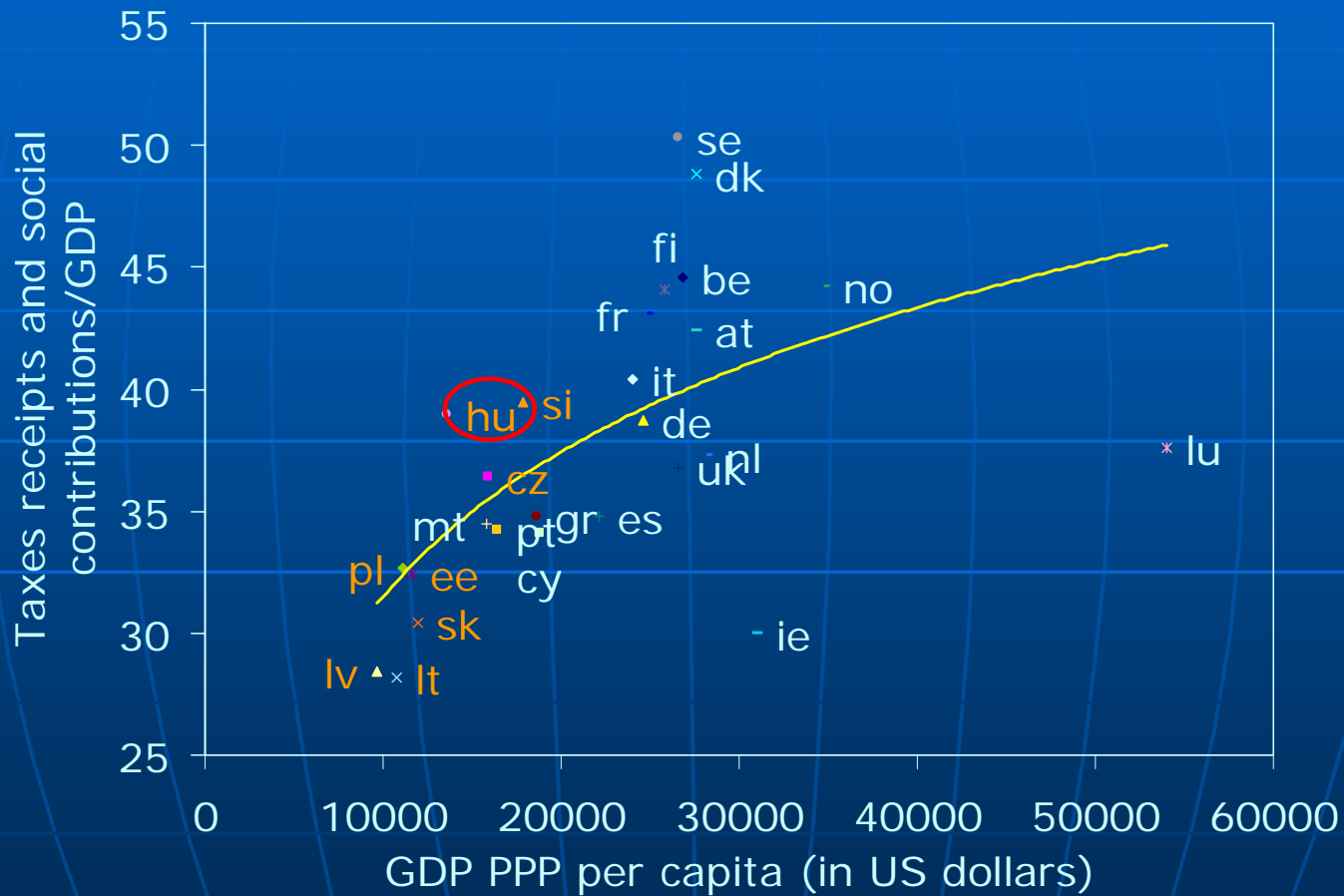
	Fiscal deficit	Public debt	CA deficit	External debt
<b>Hungary</b>	<b>-7.6</b>	<b>62.4</b>	<b>7.3</b>	<b>75.3</b>
Argentina	-2.5	85.9	-1.8	74.4
Uruguay	0.8	69.9	2.0	68.4
Turkey	3.1	67.9	6.3	49.5
Brasil	3.3	75.1	-1.8	21.3

Source: IMF staff estimates.

# Fiscal outcomes have fallen short of targets, suggesting a fundamental rethink of fiscal accountability



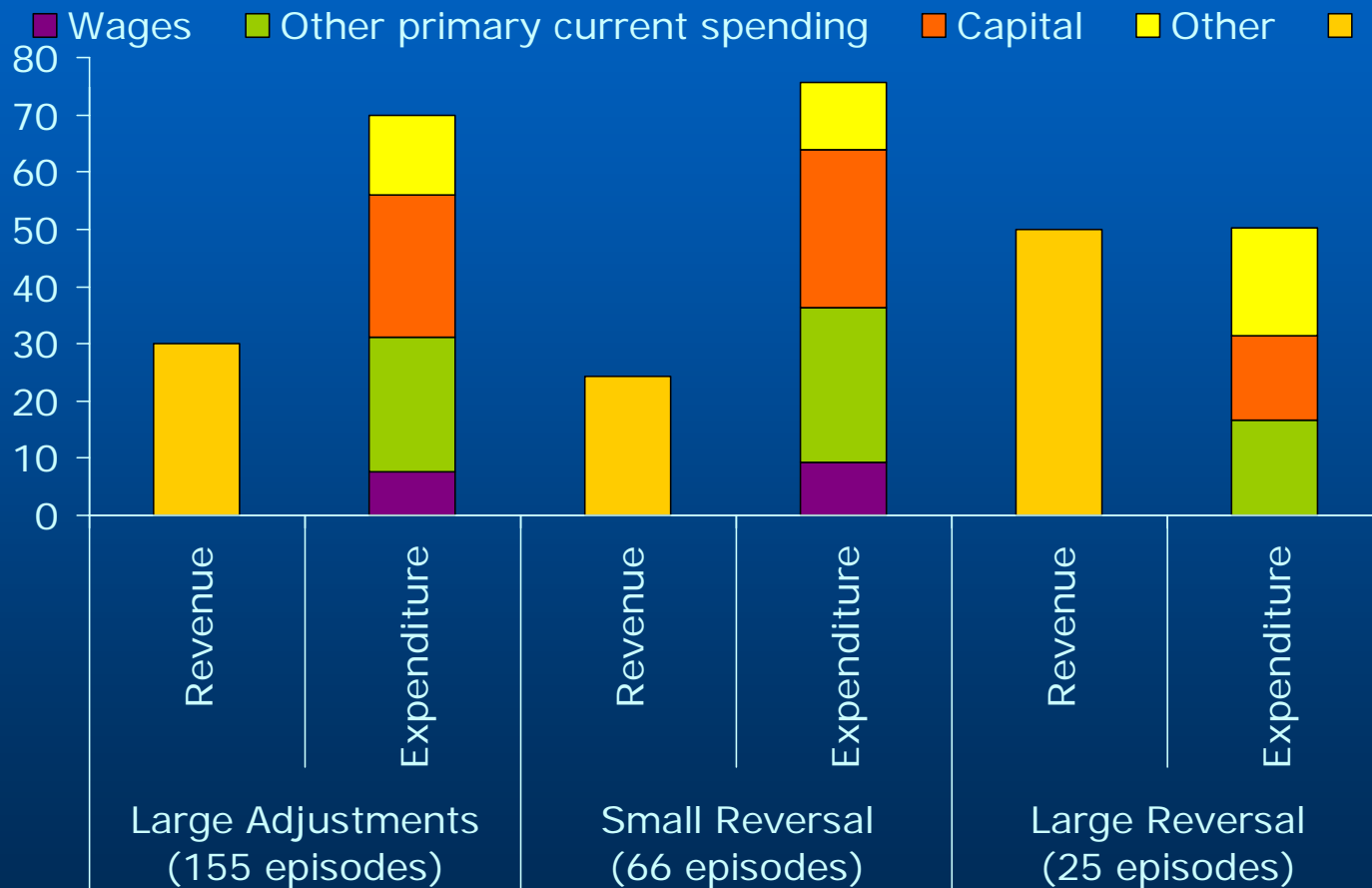
# Tax Burden and GDP per capita in Europe



# IMF Study: Experience with Large Fiscal Adjustments

- Examined about 300 episodes of fiscal adjustment 1971-2001 (in 165 countries)
- 155 “large” adjustments (top 1/3, with adjustment  $> 6.3\%$  of GDP and  $>22.8$  of expenditure)
- 63 “front-loaded” adjustments (2/3 of adj. in the first year)
- Large adjustments are implemented under more difficult macro circumstances than small adjustments.

# Components of sustained vs. reversed fiscal adjustment (in percent of contribution to the change of primary balance)



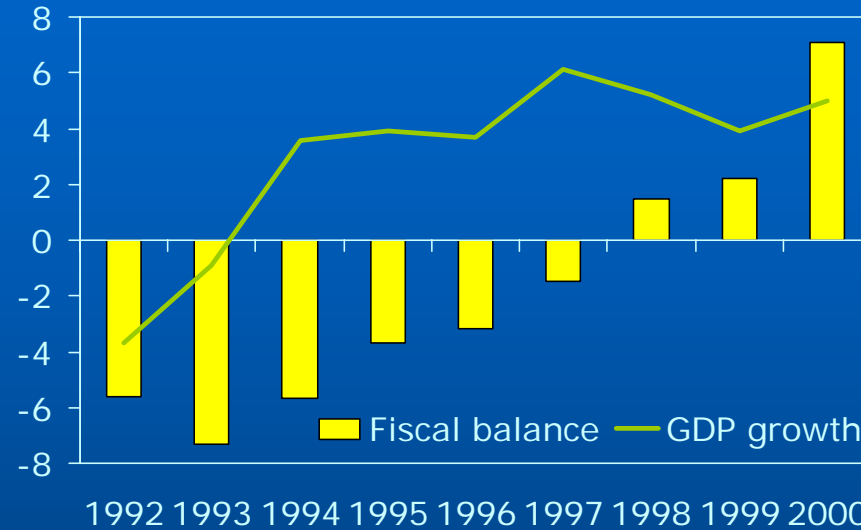


# Key Findings

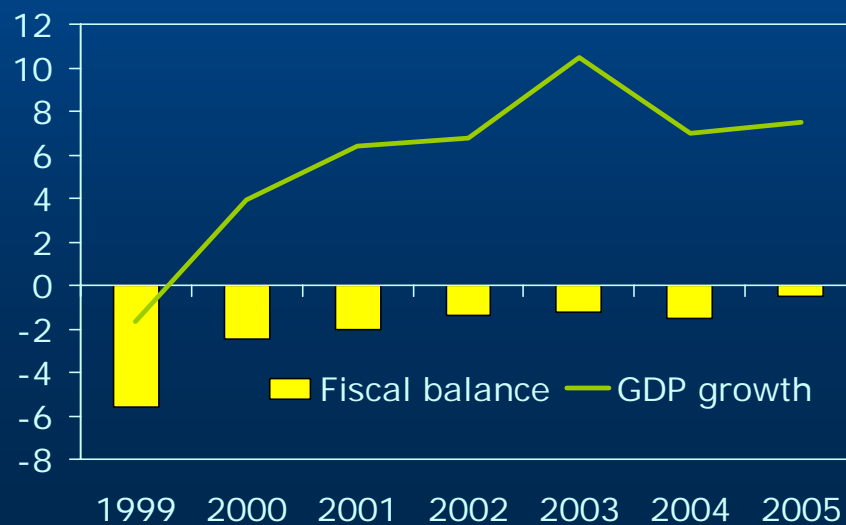
- Expenditure-based consolidations are more likely to be sustained
- Cuts in current spending (wage bill, subsidies) are particularly effective and may also have positive side-effects
- Failed adjustments rely primarily on revenues, especially PIT and trade taxes
- Adjustments during crisis are more likely to be reversed
- Large and sustained adjustments are associated with positive macro effects (on growth, C/A deficit)

# Large Fiscal Adjustments And Growth: Some Recent Country Cases

Finland 1992-2000



Lithuania 1999-2003



# Conclusions

- The government is rightly committed to strong fiscal effort, which is necessary to reduce vulnerabilities.
- International experience suggests that adjustment should rely on budgetary savings rather than tax hikes.
- There is a need to create binding and multi-year fiscal commitments, transparency and accountability.