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Hungary External Relations briefing:

Hungarian Interests in the EU- Budget Negotiations

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Hungarian Interests in the EU- Budget Negotiations

Negotiations on the new EU-budget have already started behind the scenes over the last months and several EU-members have already pointed out their proposals or their key interests. In recent weeks, the new Germany government was formed, thus, it is very likely that negotiations on the new EU-budget will speed up in the coming weeks. As we pointed out in our earlier analyses, it is a strategic goal of the Hungarian foreign policy to ensure financial capital and foreign direct investments to the needs of economic development, and technological progress. **That is why the negotiations on the next EU-budget (the multiannual financial framework – hereafter: MFF) are crucial to Hungary and they stand in the focus of the Hungarian foreign policy. This briefing focuses on main questions of the Hungarian negotiations strategy and the crucial fault lines among the member states at this question.**

In order to understand the significance of these negotiations, it suffices to point out **that a financial hole of around 90-95 billion euros** – left by Britain leaving the EU – **must be filled by the new MFF**, at the same time there are new challenges as well, like terrorism, border security, global warming etc. the EU must find answers to and tackle them. The discussions must be concluded this year – at least that is the plan of the European Commission. During the negotiations, the following practical and more theoretical aspects should be considered by the Hungarian foreign policy:

The first question which must be settled in this framework, **is whether all countries agree on the need to increase the budget significantly**. That is the goal of the European Commission and several countries already gave their consent to the plan, however, there are also countries (France, Austria, Spain, and Finland) who explicitly expressed their disagreement on this question.

So, on the one side, **Hungary must consider the likelihood of decreasing EU-transfers after 2020. On the other side, Hungary must find allies in its efforts at least to keep the size of the MFF on the current level.**

— Traditionally, Central European countries and Mediterranean countries (Spain, Greece and Portugal) would prefer generous EU-transfers.

— However, two of the Baltic countries (Estonia and Lithuania) are about to leave the position of least advanced regions, thus they will benefit less from the MFF than between 2014 and 2020.

— Even in the Czech Republic, regions are to be found that don't belong any more to the most favored regions.

— There are different scenarios as for the cohesion fund and regional support presented by the European Commission. Spain will be supported, if cohesion fund and regional support would remain the same, however, in the second scenario, only a few Spanish regions would receive cohesion fund support, in the third scenario none of the Spanish regions would get any support.

— **So, it is very likely that the support of the mentioned Baltic-countries, Spain and the Czech Republic for maintaining the level of subsidies will decrease over time, it won't be easy to win them to this case.**

So, our conclusion is the more the structure of the budget changes, the more difficult it will be to find the support of former net recipients.

Of course, it can be added, that the largest net contributor, Germany will be decisive in keeping the level of support, and they already signaled their willingness to increase the contribution to 1.3 percent of GNI. (Between 2014 and 2020 this figure was 1.0 percent.)

From a broader point of view, it could be argued as well, that **budget surpluses on country-level could counterbalance an eventual decrease of the EU-transfers.** This aspect is not only important to Hungary, but to other countries as well. Hungary seems to be preparing for this period, since the plan to launch a balanced budget is again in the Hungarian media outlets. **The**

Ministry for National Economy underlines in its plans that zero-deficit budget is already feasible in 2020 and 2021.

— However, there is only one of the scenarios, the second one would be to decrease the income tax and to make it to a single digit tax, as influential decision makers close to the government and the central bank argued making their point clear what to do, when increasing Hungary's international competitiveness.

— The third option would be to simply reduce public debt.

In our understanding, the aggregate sum of the MFF won't change significantly, because there is slight majority for increasing contributions, however, the Hungarian foreign and economic policy must be prepared for a different structure of the budget. In the following, we look at the structure changes proposed by the European Commission and the possible effects on Hungary:

1. **It is most than likely that the share of agriculture will diminish in the MFF, since the mainstream thinking seems to support the decrease for the time being.** That doesn't support the goals of the Hungarian economic development. The European Commission depicts three scenarios in its proposal, the first scenario starts off by keeping the budget on the same level, the second forecasts 30 percent cut, the third scenario 15 percent decrease of expenditures. Although the Hungarian agriculture generates less than 5 percent of the GDP, it has clear competitive advantages over most EU-members and proportionally Hungary will be one of the larges losers in this change.

   a. Traditionally, Poland and France are staunch supporters of generous agricultural subsidies,

   b. Poland will most likely remain in this camp.

   c. However, France that is traditionally a though opponent on this issue, already signaled its willingness to make compromises in this question. The French opposition goes further, since they object to go above the 1.0 percent of GNI. At the same time, they also support the abolition of the complicated system of rebates. **The change in the French standpoint increases the likelihood of a smaller agricultural budget.**

2. At the same time, it is very likely that the new MFF will increase spending on European border and coast guard, the European Commission delineates three scenarios ranging from 8 billion to 150 billion euros dedicated to this purpose for seven years. From the later version, **Hungary would benefit economically most, since the burden of the cost would fall on the MFF, however, it also would mean compromises in issues of sovereignty.**

3. It is very likely that the countries will establish a new line in the EU-budget since the European Defense Policy (EDP) was launched last year, and it is going to be built up slowly in the coming years. The proposal of the European Commission would mean 40-billion-euros earmarked for the EDP, however, **it mainly includes the development of cutting-edge technology and defense industry. Hungary would not be a beneficiary since it doesn't possess technology and capacities in this area.**

4. Increased investment in digital information and research and digitalization are also on the agenda, these investments are important to Hungary, **however, firms, universities and research centers usually compete for these financial sources and the V4 countries have very low success indicators in this area.**

5. The European Commission also proposed to **underpin the eurozone by the EU-budget**, that is an area in addition where Hungary would not be necessarily a winner. **This item could evolve into a means to give incentives to Central European countries to join the euro zone.** (Poland, the Czech Republic and Hungary already fulfil the Maastricht convergence criteria by and large, but for the time **they prefer keeping their domestic currencies.** The French proposal for the EU-budget underlined the importance of a euro zone budget. It was not clear what purposes would this budget serve: to rescue countries if it is needed or provide financial incentives to countries to join the euro zone.

6. Financial resources dedicated to external actions of the EU were 66 billion euro between 2014 and 2020. That is the sum where agreement on increasing expenditures seem to be growing. In addition to the 66 billion, the budget of the European Development Funds is 31 billion euro which is outside the EU-budget. The main argument for the increase in this area is to counterbalance migratory pressures by helping poor regions locally. **The eventual increase of this item won't affect Hungary directly, however, it must be made clear that underpins the standpoint of the Hungarian foreign policy to solve the migration crisis locally, and not in Europe.**

By and large, the new EU-budget will force the Hungarian government to make some strategic decisions, since:

— it is very likely that the amount of the budget will decrease along with substantial changes in the structure as well;

— Hungary will still benefit from the EU budget, however the 4.6 percent as of GDP subsidy level (the average sum as of GDP between 2014 and 2017) cannot be reached again;

— thus, economic policy must prepare for a more balanced public budget, however, a balanced budget won't suffice to ensure the necessary capital to economic development there are more thing to be done, if the international competitiveness of the Hungarian economy is to be improved;

— therefore, it is possible that Hungary will choose to decrease taxes and invest more in education and research and development;

— it might also turn out that the level of subsidies can be kept, however, the economic policy planning must sacrifice own currency on order to secure subsidies, but that would lead to ending the Hungarian own path in many questions.