

COOPERATION FOR A MORE COMPETITIVE AND SUSTAINABLE HUNGARY



2024 | 2025

COOPERATION FOR A MORE COMPETITIVE AND SUSTAINABLE HUNGARY 2024-2025

The American Chamber of Commerce's strategic-level recommendations
to drive the economy forward

INTRODUCTION

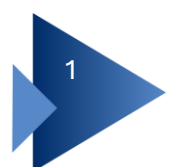
The American Chamber of Commerce (AmCham Hungary) is a politically independent nonprofit community funded by its members, representing Hungarian and international business interests. Within our expansive network of over 300 member companies 38% are from the USA, 36% representing Hungarian origins and 26% stemming from other international backgrounds. What they have in common is their strong integration in both domestic and international value chains, regardless of their country of origin. Therefore, since our foundation in 1989, we have been striving to contribute as much as possible to improve Hungary's competitiveness and to maintain the dialogue and cooperation between the business sector and the government based on our common interests.

In the framework of our advocacy work, we have prepared various position papers, advocacy propositions, and recommendation packages since our foundation, dealing with a specific industry segment, social sub-system or even the economy as a whole. The views expressed in these papers are those of our member companies that effectively support the competitiveness of the Hungarian economy through their investments, analysis, and extensive international experience.

One key element of maintaining a dialogue between government and business stakeholders is our "*Cooperation for a More Competitive and Sustainable Hungary*" recommendation package, which we have presented every year since 2016.

The Recommendation Package follows the structure set out in AmCham's Strategic Work Plan 2021-25, which also corresponds to the main directions of our advocacy activities:

- **Business environment**
- **Human capital**
- **Smart growth**



The packages of recommendations in recent years have primarily aimed at translating existing and emerging government strategic goals on competitiveness into actions. This publication differs from its predecessors, as instead of a technical focus, we are presenting aspects and considerations that affect Hungary's competitiveness and global economic integration at a strategic level, which our members believe are vital for the sustainability and long-term development of the Hungarian economy. Our concrete recommendations for practical implementation in each of these areas will be presented to stakeholders in further papers, depending on their relevance, in constructive cooperation with government policy officials.

We would like to emphasize that *Cooperation for a More Competitive and Sustainable Hungary* is not a study or a scientific analysis. Our aim remains to present the framework through which our members and current and potential investors assess the Hungarian business and socio-economic environment.

We believe that maintaining and improving Hungary's competitiveness is our common interest. AmCham will continue to be a strategic partner of the government in this regard and is committed to an ongoing constructive dialogue. We trust that our government partners will be open and that our recommendations will help to strengthen our cooperation.

Budapest, April 8, 2024

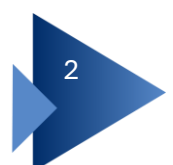
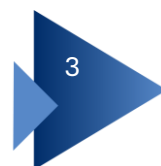


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I. BUSINESS-INVESTMENT ENVIRONMENT

INVESTMENT CONSIDERATIONS FOR FOREIGN INVESTORS

Foreign investors can look at a wide range of specific criteria when choosing a destination country, depending on the characteristics of their industry. However, there are some general dimensions relating to the political, economic and social environment of the country that are of particular importance in the assessment. Such as the destination country's:

1. market size and potential;
2. infrastructure;
3. labor market;
4. taxation environment;
5. the stability of its economic and political environment, and;
6. the development of its legal, political and social institutions.

In addition to the endogenous factors of market size and potential (population, internal demand, etc.), access to markets linked to the home market (notably the European common market) is equally important.

In the case of infrastructure, we mainly refer to the extent of coverage by utility and telecommunication networks, the cost of connecting to them, and the capacity and reliability of the networks deployed. Additionally, the quality of the mobility capacities of goods and persons is also an important factor.

In the labor market, the key considerations are productivity, wage levels and skills, i.e. the availability of labor that produces as much economic output as possible at the best value for money. It is important for growth that the labor market has some spare or expansionary capacity.

The tax system is primarily concerned with the level of taxes (mainly corporate and sectoral). Furthermore, the overall simplicity, stability and predictability of the tax system is a major consideration.

Predictability in the economic and political environment is similarly of crucial importance. Businesses are concerned about the frequency and predictability of changes in the laws that apply to them, the independence of market processes from politics, and the degree of corruption in the economy.

Furthermore, another imperative consideration is institutional sophistication, by which investors mean, among others, the characteristics of the public policy and regulatory environment that are not strictly codification, general legal provisions (such as the

existence of intellectual and industrial property frameworks that provide adequate guarantees, judicial independence and objectivity), On the other hand, the ability to meaningfully consult with government stakeholders, innovation capacity, and many other factors that affect the industry are also critical.

INVESTOR PERCEPTION OF CENTRAL-EASTERN EUROPEAN COUNTRIES

For investors looking for a global or European destination, the countries of the Central-Eastern European region form a relatively homogeneous group. In addition to favorable geostrategic factors, an attractive environment is provided by a more highly skilled workforce than in South-East Asia, cheaper than in Western Europe, and a physical infrastructure capable of adequately serving mainly medium value-added production. The membership of the countries of the region in the European Union is of utmost importance, which provides access to the common market and a degree of institutional and legal guarantees for companies.

In addition to the general advantages, similarities and homogeneity of perception mean that there is intense competition for foreign direct investment (FDI) between countries in the region, so even small comparative advantages or disadvantages can be critical when making an investment decision.

HUNGARY'S SITUATION

Hungary is one of the most open economies in Europe, and therefore one of the most exposed to global processes. According to the National Bank of Hungary, the stock of foreign direct investment stood at around €99 billion in 2022, or nearly 60 percent of GDP, more than double the net value of all EU assistance disbursed to Hungary between 2012 and 2022. FDI inflows not only generate capital surpluses, but also boost productivity and competitiveness, and have an indirect multiplier effect in the Hungarian SME sector. It is therefore essential that Hungary remains an attractive destination for foreign investors.

In the competition for FDI, it is crucial that Hungary is seen in a more favorable light than its neighbors in the pre-decision analysis comparing countries in the region. At this stage, the risks are particularly high in the case of extreme negative macroeconomic divergences (e.g. inflation), the absence of important international treaties (e.g. a double taxation treaty with the US) or the lack of access to key financial resources (e.g. suspension of EU subsidies).

It is also important that both inflation and the HUF-EUR exchange rate remain stable and predictable, as excessive volatility is a major source of uncertainty for both.

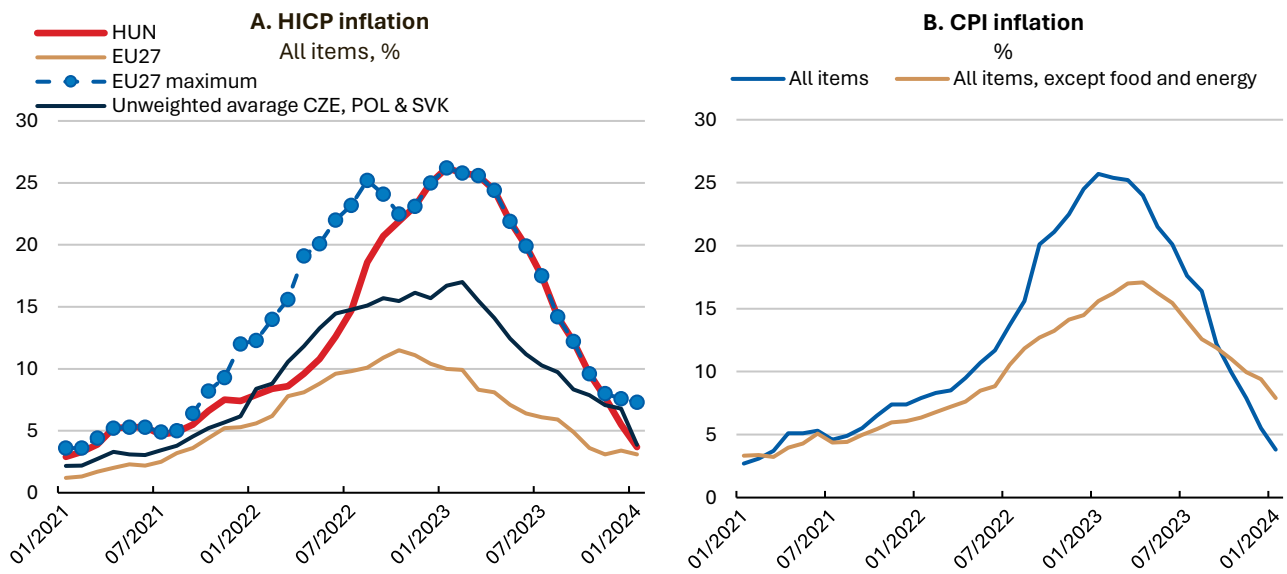


Figure 1A, 1B: General inflation has declined, but core inflation remains high, Source: Eurostat Database on Harmonized Indices of Consumer Prices (HICP), OECD Database on Consumer Price Indices

Hungary's overall international image in moderate, economic-technocratic media tends to be on the whole negative, and this can result in a competitive disadvantage. Although business decisions are not primarily made based on daily news, they do reach the foreign headquarters of multinational companies and can influence investment decisions. The situation could be significantly improved by highlighting the country's achievements and economic advantages, as well as by more positive, or at least more neutral, political communication and negotiated settlements of disputed economic and foreign policy issues behind closed doors.

A stable and predictable regulatory environment would also greatly improve the willingness of existing foreign companies to develop and reinvest. It is critical for business actors to be informed of legislative and tax changes affecting them sufficiently in advance to prepare. It is equally important that changes are preceded by a sufficient depth and duration of social consultation, as frequent and sudden public interventions in the functioning of the market seriously undermine investor confidence, even for companies that are not directly affected by the measure.

The negative effects resulting from economic risk assessment and subjective perceptions can be partially offset by targeted measures that help attract investment to Hungary. Here we would like to highlight the investor-friendly system of the Individual Government Decisions (IGDs) and the excellent work and constructive attitude of the Hungarian Investment Promotion Agency (HIPA), which is highly appreciated by our member companies. However, it is also important to point out that similar support schemes and government agencies with the same function exist in other countries in the region (e.g. Czechinvest, Polish Investment & Trade Agency, InvestRomania, etc.), and this may moderate the positive impact.

TRANSITION TO A HIGHER ADDED VALUE ECONOMY

In the face of fierce international competition, Hungary must create its investment and industrial strategy from a regional perspective. For many years, our Chamber has argued that to maintain Hungary's long-term competitiveness, it is essential to significantly increase the productivity of the economy and shift the focus of economic policy from quantity to quality. These changes can only be achieved with strong government commitment and effective action. Unless these are achieved, we risk being overtaken in the medium term by our regional competitors in terms of capital absorption capacity.

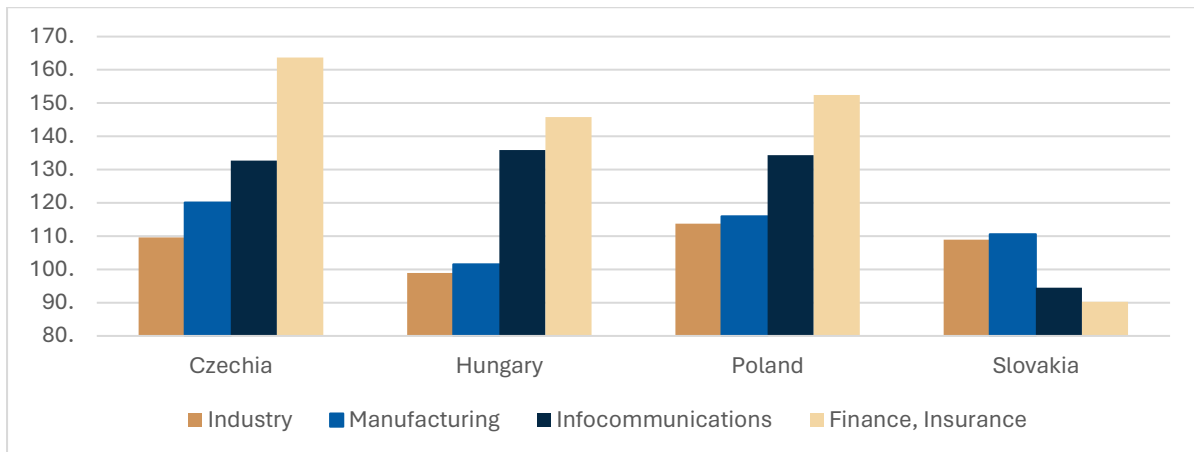


Figure 2: Volume change in value added per worker for the V4 countries in some sectors in 2022 (2015=100), Source: OECD Database on Productivity Statistics

The current economic and FDI strategy has long favored manufacturing sectors over services. Although manufacturing capacities constitute an essential part of a diversified modern economy, it is important to emphasize that this stage in the value chain of products adds the least value.

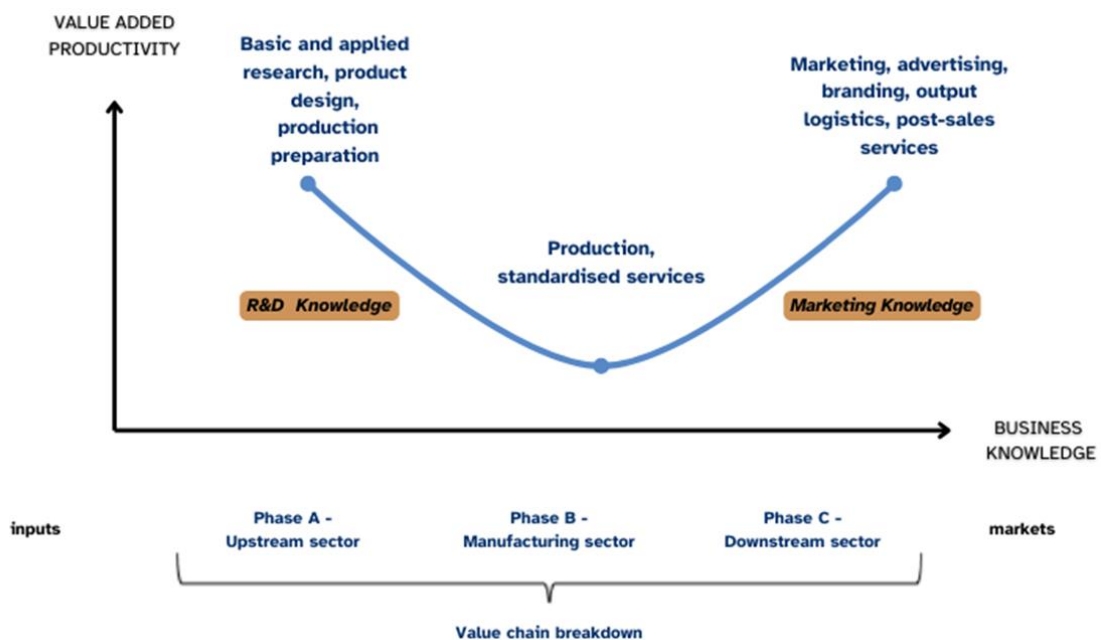


Figure 3: Smile Curve, Source: Schematized diagram by György Boda based on Davide Del Prete's 2017 study "The "Smile Curve": where Value is Added along Supply Chains

Consequently, if the manufacturing sector becomes overly massive in the country's economy, it will also result in Hungary's macroeconomic commitment to the lower value-added stage of international value chains in the long run. A significant number of companies have recently set up service centers in Hungary, with the sector employing nearly 160,000 people in 2021, typically in higher-paid, higher value-added jobs than the market average. Therefore, it would be worth raising the development of the sector to a strategic level.

Increasing the efficiency and performance of the SME sector is also a key factor, as SMEs generate almost half of Hungary's added value. In almost every country in the world, the competitiveness of SMEs lags behind that of multinationals, but in the case of Hungary, the gap is particularly wide. This is partly due to the tight labor market conditions in Hungary, where competition with large capital-intensive companies usually lags behind in the competition for quality labor. With access to adequate EU funds, we propose the continuation of aid schemes similar to those of the previous budgetary cycle and the launch of new ones, specifically with the aim of making Hungarian SMEs more demand-driven, agile, digital and attractive to employees, and thus stable suppliers to players in international value chains. For the new subsidy schemes, we propose a predominance of reimbursable forms of subsidy and financial instruments, as they are more attractive to businesses than non-reimbursable solutions. A key selection criterion in the tendering process should be to ensure that subsidies go to SMEs that are internationally viable and have good growth potential. In addition to grants and subsidies, it is also essential that the business lending environment can stimulate development and investment at the right interest rates.

We see five closely related sets of problems as obstacles to a transition towards higher value-added domestic production:

1. The often changing and unpredictable legal and tax environment,
2. The unavailability of properly educated and trained human resources,
3. The need to improve the efficiency of the R&D&I ecosystem,
4. The low competitiveness of the start-up and SME sector and
5. The backlog of the country's infrastructure development.

The challenges in these areas are described in more details below.

II. TAX REGULATION FROM A COMPETITIVENESS PERSPECTIVE

THE IMPACT OF FISCAL PLANNING AND THE SPECIFICITIES OF THE TAX SYSTEM ON INVESTOR CONFIDENCE

The fundamental function of the tax system is to provide the revenue needed to carry out the tasks of the state budget. Considering that this inevitably involves interference in the functioning of market conditions, it is important to monitor the extent to which each measure weakens the efficiency of product and capital markets, worsens competitive conditions and increases uncertainty among market participants, as these all affect the pace of economic growth.

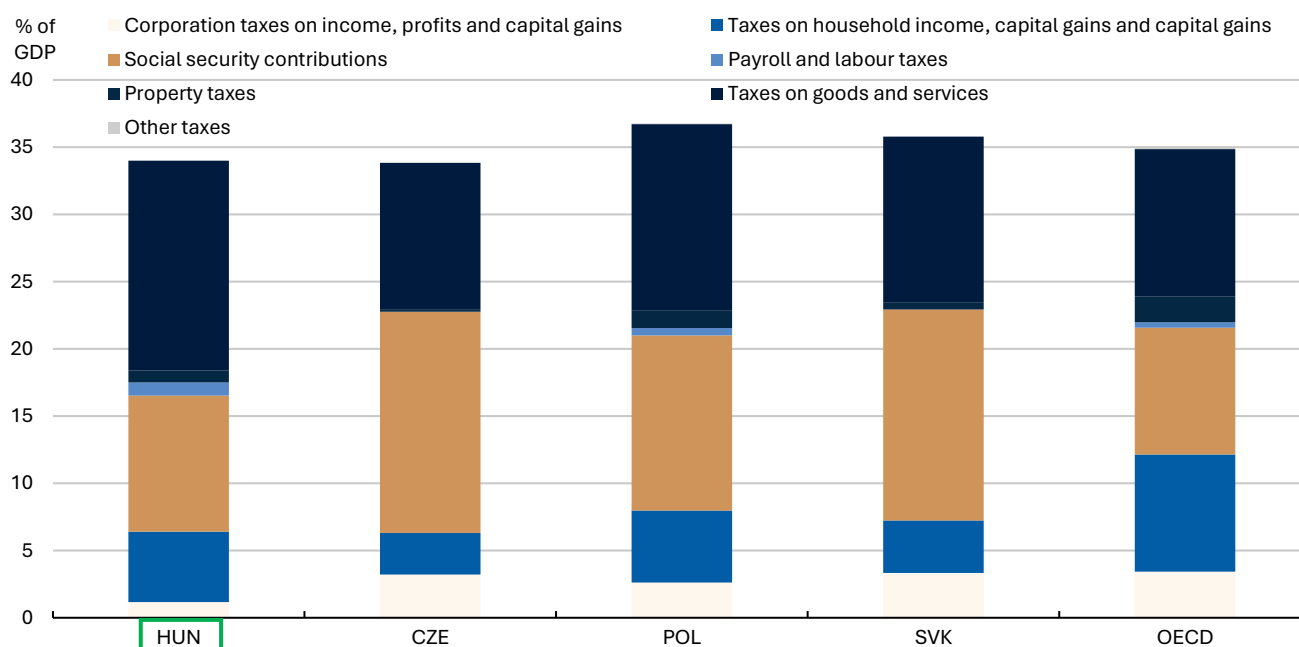


Figure 4: Hungary relies more on VAT and less on income tax than other regional and OECD countries, Source: OECD Database on Revenue Statistics.

In Hungarian fiscal planning practice, the budget law is traditionally presented in the spring, but the highly volatile global economic environment means that the initial calculations are subject to significant corrections almost every year, and the government regularly resorts to special taxes to compensate for the resulting shortfalls. While the easiest and quickest way to address the revenue needs of the state budget is indeed to impose special taxes, this leads to unpredictability and instability in the tax system in the long run. Special taxes can have a disruptive effect on entire sectors of the economy, reduce productivity, discourage development and reinvestment, and are a negative factor in the risk assessment of new investors.

A significant number of economic agents would have a much more favorable view of the domestic economic-tax environment if the government were to abandon the practice of imposing special taxes altogether, however, some recurrent features of actual tax practice make the situation worse.

In regard to sector-specific taxation, the trend to tax certain industries raises competition concerns too. The practices discourage foreign investment, reduce competition within the industry and ultimately to products and services that offer poor value for money for Hungarian consumers.

Investors also identify the quasi-retroactive legislation that is common in the imposition of special taxes as a further country risk, whereby the legislator ties a tax liability for the current year to a specific number or tax base of a previous tax year. In addition to the general uncertainty, given that these tax burdens are typically introduced unexpectedly during the year, they also cause difficulties in reporting to parent companies, stock exchanges or in the course of other data provisions.

The current tax system is characterized by the fact that the same tax subject is simultaneously regulated at different levels of the legal hierarchy. This makes the application of the laws considerably more difficult, as the content of an apparently valid regulation currently in force may be contradicted by a lower-ranking special tax provision. As a result, following and interpreting the law and monitoring the current rules of the norms can only be ensured at the cost of considerable time and energy. In the course of the legislative process, it would be important to have a professional dialogue between the government and the sectors concerned, which would also help to prevent future legislative change initiatives and problems of interpretation.

We welcome government plans to abolish several windfall taxes from 2025 onwards. Our member companies are looking forward to the forthcoming measures and are calling for the complete abolition of the special tax regime and a move to more predictable tax solutions. If the system of special taxes is not planned to be phased out by the government for the time being, we propose consolidating the standards and freeing them from content errors or restructuring them to ensure that the special taxes are considered taxes covered from the aspect of the global minimum tax.

When designing the tax system, it is already worth taking into account long-term macroeconomic aspects such as the sustainability of some of our country's social subsystems. Economic analysts are almost unanimous that the current funding model for pensions and healthcare in particular is unsustainable and heading for collapse without major reform. Therefore, there is a need for a significant increase in self-care in both areas, which could be boosted by [appropriate](#) and supportive tax rules.

THE IMPACT OF THE TAX SCHEME'S GENERAL STRUCTURE ON PRODUCTIVITY

The current tax system is too complex and bureaucratic, leading to lower productivity for both the state and the companies. There are currently 61 different taxes, contributions and special taxes, while 91% of the central budget's tax revenue is generated by only 7 tax types.

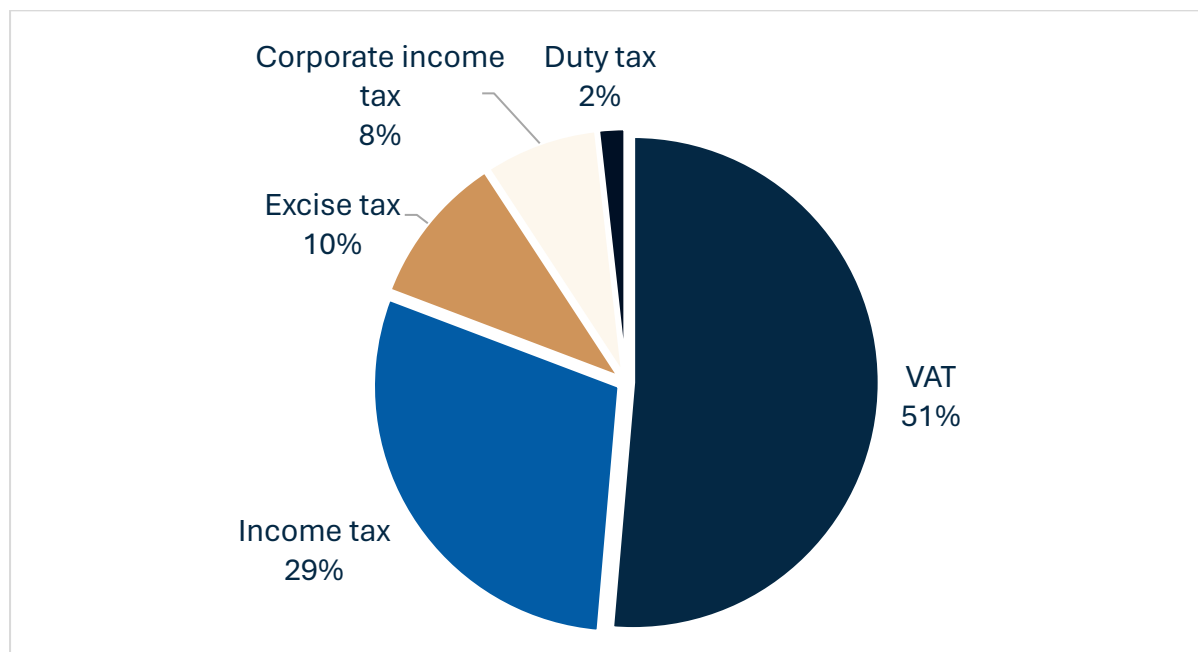


Figure 5: Distribution of revenues by main tax categories in the central budget, December 2023, Source: Hungarian National Treasury

Reducing the number of taxes is an EU commitment, as well as it could also lead to a more attractive investment environment. A general technical revision might also create the opportunity for other bureaucracy-reducing measures.

Of the taxes in force in January 2024, the following taxes were introduced only in years 2022/2023:

- insurance surtax,
- retail extra tax,
- credit institution special tax,
- special tax for petroleum product manufacturers,
- special tax of Mandatory Takeover Tariff/Renewable Subsidy System producers,
- special tax on the provision of balancing capacity,
- extra profit tax on pharmaceutical manufacturers,
- (securities) financial transaction tax (regulated by a specific law),
- telecommunication extra tax,
- airlines' contribution (regulated by a specific law),

- extension of the Social Contribution Tax to interest-related incomes,
- extension of local business tax to airlines,
- carbon-dioxide quota tax,
- transaction fee (payable to the climate protection authority).

In addition to the new taxes mentioned above, the Extended Producer Responsibility scheme (EPR) based on EU directives, the Carbon Border Adjustment Mechanism (CBAM) in 2023, then the mandatory Deposit Return System (DRS) was introduced in 2024. EPR, DRS and CBAM pose particular difficulties for companies because they have to comply with the requirements following only a short preparation period, with limited information and without the possibility of prior planning, which might even require to replace the company's current structure.

The introduction of the Extended Producer Responsibility (EPR) scheme and the Deposit Return System (DRS) will significantly reduce the environmental product tax payment burden of the affected business entities. It is therefore expected that the product tax will not generate significant budgetary revenue, but will also create a significant administrative burden for the tax authorities and companies. We propose to conduct a cost-benefit analysis of the two taxes to simplify and manage them in a uniform system. Since the cessation of the obligation to pay the product tax does not mean the simultaneous cessation of the product tax obligation, it is worth to consider reducing the administrative burden in such cases. As a first step, we propose to carry out a cost-benefit analysis of the two tax types to simplify and manage them in a single system.

The consolidated tax base of individuals may be subject to several exemptions, some of which are based on age or marital status. Such exemptions might lead to wage tension, with a younger employee receiving a higher net wage for the same work compared to slightly older colleagues without children. Moreover, reaching a certain age leads to a loss of benefits, which, irrespective of productivity, also results in wage reduction. The system might also strengthen the bad practice where some employers target the tax-exempt age group when addressing the labor market and then dismiss employees upon becoming 25 years old. While we understand the considerations behind the measures, which are partly demographic and partly aimed at promoting early employment, we consider the use of tax instruments to achieve this objective to be of questionable effectiveness and therefore recommend that consideration be given to phasing out these tax exemptions. If the removal of these discounts is not currently in the government's plans, we propose the examination of the process evaluation and implementation fidelity regarding the original objectives and publish the results of the impact assessment.

We welcome the change whereby an employee or an executive officer who acquires a business share in a start-up company does not mean receiving income under Act CXVII of 1995 on Personal Income Tax. Sharing in the business is a popular and effective way of building employee motivation and ownership, thus reducing turnover and providing employees with access to sustainable passive income. This leads to an increase in the overall standard of living and the level of well-being. For this purpose, we propose to extend the benefit to all employee business share acquisitions.

From both a social and economic perspective, it is essential that investing in human capital becomes a long-term strategy, as part of which the working-age population must make efforts to avoid negative health and social consequences. The working population also needs to be motivated to understand and master the digital technologies that permeate their daily lives and workplaces. A fringe benefit scheme can act as an appropriate incentive in areas where there is a need to increase well-being. The fringe benefit can be used for school and adult education, health insurance, and voluntary pension schemes. With proper planning, these processes can even lead to a positive fiscal balance, increase the competitiveness of the economy and generate savings in some public subsystems.

Hungary has made a commitment to the European Union to implement a major pension reform in the coming years to access the repayable resources and reimbursable loan of the Instrument for Recovery and Resilience, which we welcome. As this is a very important issue for our member companies, we call on the government to consult with economic actors on this issue as well and to put the plans for the restructuring to public debate beforehand.

Enhancing digitalization, reducing the administrative burden on taxpayers and simplifying procedures remain a direction that is essential for a client-friendly administration. We welcome the efforts made in the field of digitalization and recommend that this trend be maintained. In this context, we endorse that consideration be given to a wider adoption of the SAF-T standard in the future. To reduce the administrative burden, it would be worth examining whether the various data reports to be submitted to tax authorities could be consolidated.

THE EFFECTS OF THE LACK OF A DOUBLE TAX TREATY BETWEEN THE UNITED STATES AND HUNGARY

The termination of the double taxation treaty between the United States of America and Hungary creates a significant competitive disadvantage in the regional competition for US working capital. The comparative disadvantage of the effects of uncertainty on firms' strategic planning and the increased administrative costs of operations is clear.

The negative impacts are particularly large in the reverse case, when the US subsidiaries of Hungarian, typically innovative companies and start-ups are affected. The primary market for technology companies is still the US, so with the end of the treaty, these companies will, in the long run, be forced to set up their headquarters in a neighboring country instead of Hungary, which also deteriorates our comparative advantage.

We would also like to highlight a secondary impact, mainly on human resources. On the one hand, US citizens (expatriates) working in Hungary face significant additional administrative burdens and potentially additional taxation as their US-sourced income becomes taxable in Hungary in the absence of treaty protection. When corporate

headquarters are looking for investment locations, the tax and other costs of seconded executives are considered to a significant extent when making the final decision.

On the other hand, the absence of a tax treaty also has significant disadvantages for Hungarian employees. A good example of this is the additional tax burden arising from the share-based compensation schemes of US companies, which in the case of companies already operating in Hungary affects not only senior executives but a wide range of employees. If a US parent company wishes to grant shares or stock options to employees working in Hungary, the benefits may be subject to a 30% US withholding tax.

The termination of the treaty will also have adverse consequences for Hungarian individuals who invest part of their savings in US markets, as the 30% US withholding tax mentioned above may significantly reduce the return on their investments. For separately taxable income, the tax paid abroad can be offset, but the offset cannot make up for the increase in the US tax burden, and in any case, these individuals will have to pay 5% of the tax base to the Hungarian budget.

In conclusion, the lack of an agreement significantly reduces the country's competitiveness, contributes to higher costs for domestic subsidiaries and may ultimately lead to an outflow of highly skilled labor.

We would like to emphasize that, due to the specificities of the US legislature, no hypothetical scenario or political promise should be expected to lead to a quick solution. A new agreement requires a certain degree of bipartisan consensus on the US side. On the Hungarian side, the resolution of the issue could be facilitated by bringing the matter to a technical level as soon as possible and by actively reducing diplomatic tensions.

III. FACTORS DETERMINING HUMAN CAPITAL

THE IMPACT OF WORKFORCE ON COMPETITIVENESS

There is a unanimous consensus among our members that there is no discussion on competitiveness that cannot ultimately be traced back to the nature of a country's human capital, its defining characteristics.

Automation and digital transformation, in particular the spread of artificial intelligence-based solutions, will also cause a major shift in the labor market. Rather than performing simpler, unskilled or entry-level tasks, the focus is shifting towards higher value-added work that manages the complexity of processes, across all job functions. This also requires continuous learning and self-training on the part of employees. We are confident that the government needs to support policy measures to prepare today's employees for the challenges of the future through appropriate education, retraining programs and targeted support for employees.

SPECIFICITIES OF THE HUNGARIAN LABOR MARKET

Hungarian labor market data shows that the work-based society, which is considered a basic principle by the Hungarian government, is reflected in near-full employment. According to November 2023 KSH data, the average number of employed persons aged 15-74 was 4 million 736 thousand. Among 15-64 year olds, 4 million 629 thousand were in employment, with an employment rate of 75.2%. The number of employed men was 2 million 435 thousand (employment rate: 79.0%), while the number of employed women was 2 million 194 thousand (employment rate: 71.3%). The employment rate for the so-called prime working age, i.e. the population aged 25-54, was 88.4%.

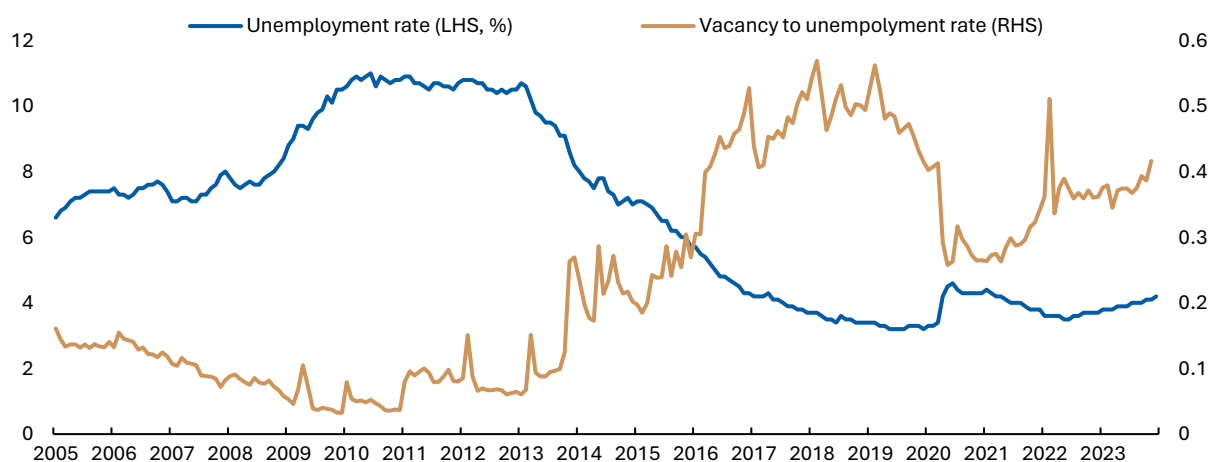


Figure 6: Despite the fall in economic activity, the labor market remains historically tight. The typically opposing curves have tended to move together in recent years. Source: OECD database on Short-Term Labor Force Statistics.

The number of job vacancies in the national economy as a whole was 78,574 (2.4%) in Q3 2023, 11 thousand less than a year earlier.

The above ratios in terms of their scale (not counting pandemic fluctuations) have been characteristic for several years.

Based on the above data, the labor market situation in Hungary is characterized by a duality, showing both persistent labor shortages and a certain degree of unemployment. The main reason for labor shortages is the mismatch between employers' needs and jobseekers' qualifications, skills and even intentions. Skills shortages, particularly in the case of people with lower qualifications, prevent them from finding a job in the primary labor market, which can lead to social tensions that accumulate beyond the under-utilization of resources. Moreover, the available labor supply and the new jobs created are situated in different locations. Furthermore, in sectors facing persistent labor shortages, the high inflationary wave of the past period, among other factors, has led to strong wage competition, which has resulted in Hungary losing its labor cost advantage in some sectors of the economy compared to its regional competitors.

This is aggravated by negative demographic trends, which together call for active labor market intervention.

There has been no radical turnaround in demographic trends, despite strong government intentions. The most optimistic outcome resulting from these measures in the foreseeable future is a slowdown in population decline. Thus, there are two ways to meet labor demand: from the country's internal reserves (e.g. young people, people over 50, women with small children or large families, people with disabilities, etc.) or from foreign hires. Opening up internal reserves requires targeted programs, budgetary resources and shaping social attitudes. There is international competition for foreign employees, so the quality of the available talent pool depends to a large extent on the opportunities, circumstances and perceptions of each country and the possibilities of working in Hungary.

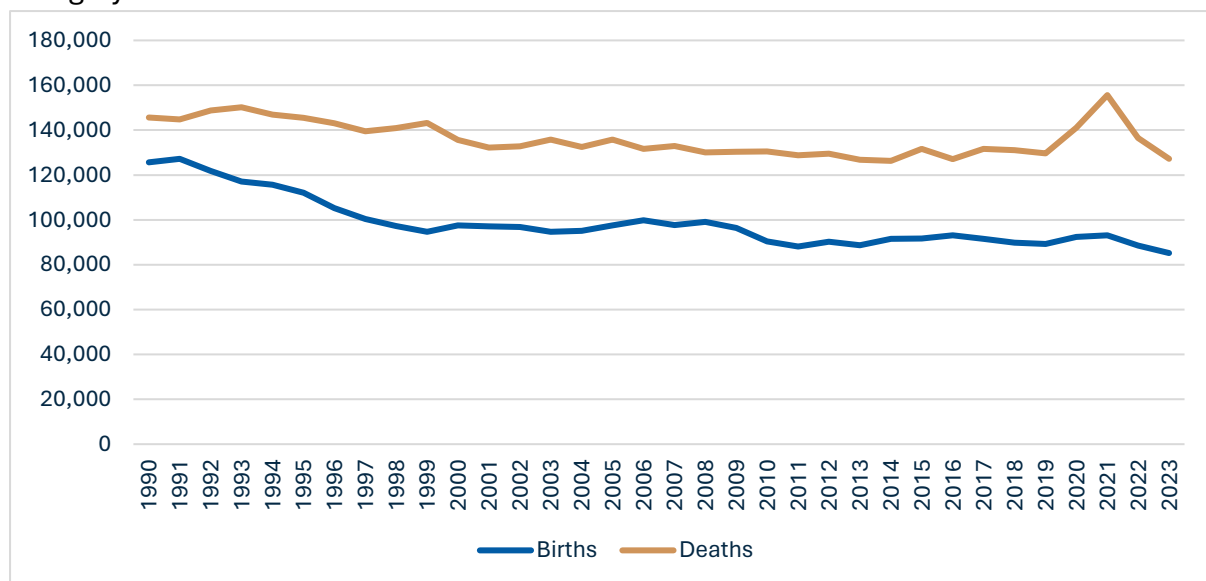


Figure 7: Number of births and deaths in Hungary. Source: Central Statistical Office

Budget spending on education and health is a profitable investment in the country's human resource capacity, if allocated and used efficiently. In order to progress, it is therefore necessary to increase these expenditures above the European average as a share of GDP. The reforms undertaken in both areas can be effective, but only if adequate financial resources are available to implement them.

The continuation of the status quo is a long-term barrier to moving towards a higher value-added economy, and we urge stakeholders to make serious and broad-based investments in the country's human capital capacity, including in the country's economic strategy planning:

- Train and retain more highly qualified professionals within the country;
- Attract more highly skilled foreign employees to Hungary;
- Revise the operating and approach of the Hungarian public education system in order to ensure the supply of new talents;
- Fine-tune higher education, vocational education and adult training systems;
- Increase the number of years of life lived in good health by properly restructuring and resourcing the health system.

RETAINING SKILLED HUNGARIAN WORKFORCE, ATTRACTING FOREIGN EMPLOYEES

A priority demand from companies is to address general labor market problems, in particular the migration of skilled labor or the lack of skills and competences (e.g. digital competences). One of the reasons for migration of young, highly skilled Hungarian employees is the fact that their incomes are below EU average. The main source of the pay gap is that, although a layer of employees compete with their Western European counterparts in terms of both skills and productivity, but they are not available in sufficient numbers to allow international companies to bring their truly high value-added operations to Hungary. Economic growth and public initiatives support innovative sectors and the creation of higher value-added jobs and are necessary to realize wage improvements and maintain higher wage levels. Without quality jobs that offer both professional challenge and development, the most qualified professionals will leave the country, and the critical mass of highly skilled employees that are able to elevate the Hungarian economy out of the middle-income trap will not be created.

In the case of foreigners, the recently promulgated Act XC of 2023 on the General Rules for the Entry and Residence of Third-Country Nationals and the related regulations we welcome the legislative intention to regulate employees with different qualifications and life situations. However, in many cases the regulation imposes disproportionate burdens on both employees and employers. The legislation does not allow foreign employees to settle permanently in Hungary and is therefore not suitable to meet the labor needs of

investors coming to Hungary for the long term. Companies need to ensure constant labor supply, which requires a significant amount of resources, both in terms of time spent on training and the cost of intermediaries. The model is still feasible in low value-added sectors, in terms of physical labor, but not in jobs requiring high qualification or special knowledge. Moreover, people with certain qualifications are not allowed to work higher-skilled jobs, and foreign employees cannot be employed in various sectors, thus, the detailed rules need to be adjusted. This regulation could put Hungary at a competitive disadvantage in the long run.

The issue of diversity is worth mentioning, as it is not only socially but economically significant. To this end, strengthening equality and inclusion in the workplace for different social groups is important not only for companies but also for the national economy.

Thorough analysis and empirical evidence of the value of diversity and acceptance in the workplace shows that there are many business advantages to investing in diversity:

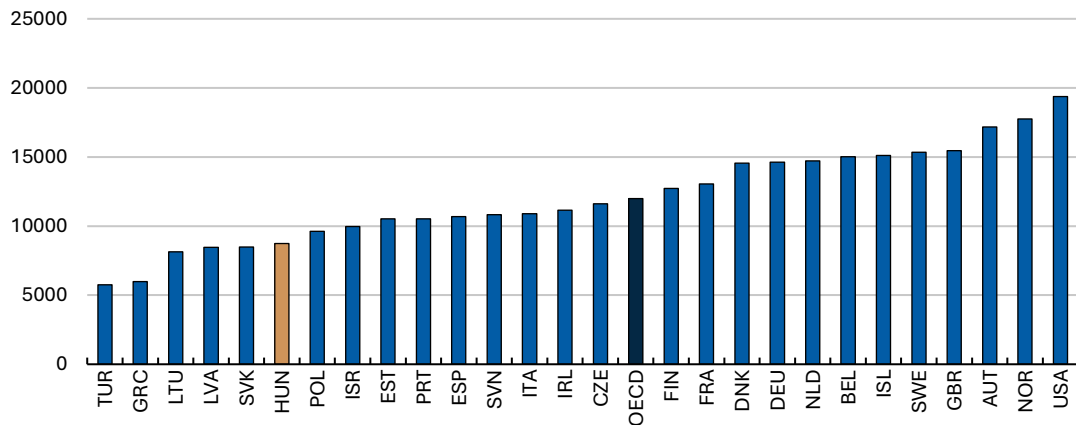
- businesses can more easily recruit and retain talented employees, especially in areas requiring high expertise;
- employees' productivity increases as they become more engaged in their work, their workplace relationships improve, as well as teams in the workplace cooperate more effectively;
- higher levels of creativity and innovation are fostered, which leads to a key competitive advantage;
- compliance with ESG criteria facilitates the integration of SMEs as suppliers in global value chains.

As our members include both multinational and Hungarian companies, we assume it is of the utmost importance to raise awareness of the economic and business advantages of diversity and acceptance in Hungary. It is not enough to motivate and support employers based on time-limited tenders; a government strategy and initiatives are needed to promote a long-term diverse workplace culture.

THE EFFECTIVENESS OF THE PUBLIC EDUCATION SYSTEM FROM THE EMPLOYERS' PERSPECTIVE

The key to Hungary's future and competitiveness lies in the development of human resources. In the upcoming years, countries that focus on innovation and high value-added production, with a skilled and creative workforce, will have an advantage in international competition. An effective and future-oriented education system is essential to ensure economic development, prosperity and social cohesion. High-quality public education that is consistently prioritized, is one of the most important and long-term investments in the country's success.

A. Total education expenditure per full-time student
2019, USD PPP



Average reading performance (PISA 2022)

B. Education expenditure and outcomes

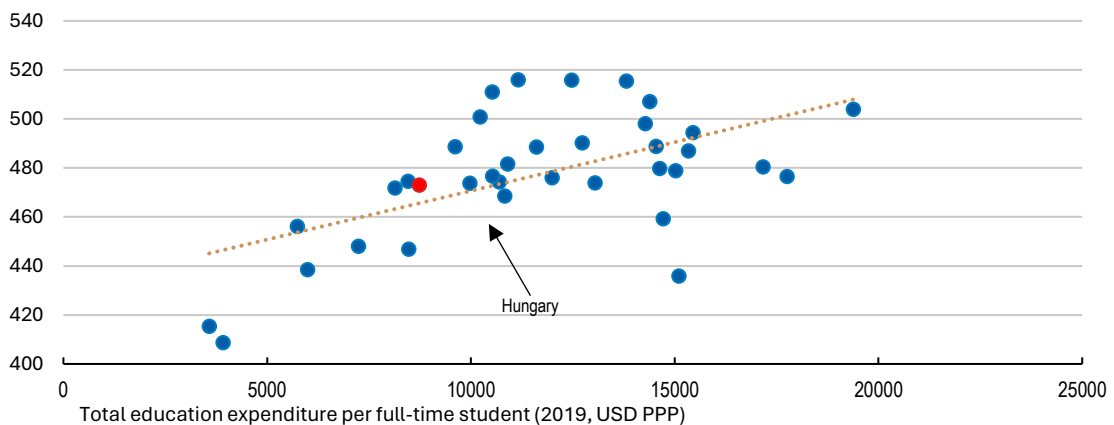


Figure 8A, 8B: Lower education spending contributes to lower educational outcomes, source: OECD Education at a Glance and 2022 PISA Survey

From a corporate perspective, the efficiency of the education system is primarily measured by the extent to which it can prepare young people for labor market opportunities as well as the added value of future employees in the labor market. A highly skilled workforce with modern knowledge is essential not only to increase but also to maintain the competitiveness of the economy. The education system, as the entry point to both higher education and the labor market, works to open doors and prepare young people for the labor market in the present and future, and to equip students with the skills needed to be an informed and competent citizen.

Based on the results of the 2022 PISA survey, which also measures the basic knowledge and competencies required for further education or to enter the labor market, Hungary is in the midfield of OECD countries.

The PISA results observed between 2012 and 2022 show a decrease in all three areas - Mathematics, Reading comprehension and Science. Based on the average 10-year trend, the biggest fall is in students' reading comprehension skills, which show a drop of almost 12 points. In science, the performance of Hungarian students worsened by 5.5 points, while Mathematics results declined by almost 3 points.

In our view, the current education system needs to be further improved to ensure that, in addition to providing the appropriate knowledge, emphasis is placed on developing the competences and skills required by the labor market as well as the transferring modern skills.

Today's labor market is increasingly volatile, and it is difficult to predict which jobs and professions will emerge and if their demand will increase or decrease. As a result, we do not know exactly what knowledge we need to equip future employees with. Therefore, it is of utmost importance that schools successfully transfer adaptability, the skills constant learning and innovation to students.

| PISA test results among Hungarian students | | | | |
|---|--------------------|------------------------------|-----------------|----------------|
| | Mathematics | Reading comprehension | Sciences | Average |
| 2000 | | 480 | | 480,0 |
| 2003 | 490 | 482 | | 486,0 |
| 2006 | 491 | 482 | 504 | 492,3 |
| 2009 | 490 | 494 | 503 | 498,7 |
| 2012 | 477 | 488 | 494 | 486,3 |
| 2015 | 477 | 470 | 477 | 474,7 |
| 2018 | 481 | 476 | 481 | 479,3 |
| 2022 | 473 | 473 | 486 | 477,3 |

Source: OECD

Figure 9: PISA survey results among Hungarian students, Source: OECD

This is feasible if the compulsory lexical curriculum is reduced and students have the following key competences, in addition to a sufficiently solid basic knowledge:

- high writing-reading skills,
- multilingualism,
- basic skills in mathematics and science, technology and engineering (STEM),
- digital and technological literacy,
- interpersonal skills and the ability to acquire new competences,
- skills for active citizenship,
- entrepreneurial spirit,
- basic self-awareness,
- cultural awareness and expression.

We welcome the government's recognition of the importance of these skills to succeed in today's world, and the way they are being applied in elite training, but their impact on the economy as a whole is not sufficient. We therefore propose to extend at least some of the approaches already present in elite education to the whole of Hungarian public education. To develop key competences, the following aspects need to be mainstreamed in public education:

- high quality education and training that prepares people for lifelong learning,
- the systematic use of more pragmatic competence-based and experience-based teaching and learning methods,
- in addition to individual performance, encourage and value cooperation,
- to encourage alternative learning methods and environments,
- to identify and lay down methods for assessing and measuring key competences,
- building modern and relevant career guidance support and programs.

THE OPPORTUNITY FUNCTION OF THE EDUCATION SYSTEM

The basic function of a well-functioning public education system is to level out social inequalities. The current structure does not promote equal opportunities, but rather hinders them, by segregating students from different cultural, social backgrounds or abilities. Moreover, the quality of education varies considerably between regions, which is particularly pronounced in peripheral areas.

This is also supported by the results of the 2022 PISA survey, in which the scores of Hungarian students were strongly influenced by their socio-economic background. This leads to the conclusion that the education system has a low equity performance. Students from higher socio-economic backgrounds (i.e. those in the top quartile of students in terms of socio-economic status) scored 121 points better than students from disadvantaged backgrounds (bottom quartile). This difference is well above the OECD average of 93 points. Hungary is the third worst performer in terms of inequality among the 73 countries.

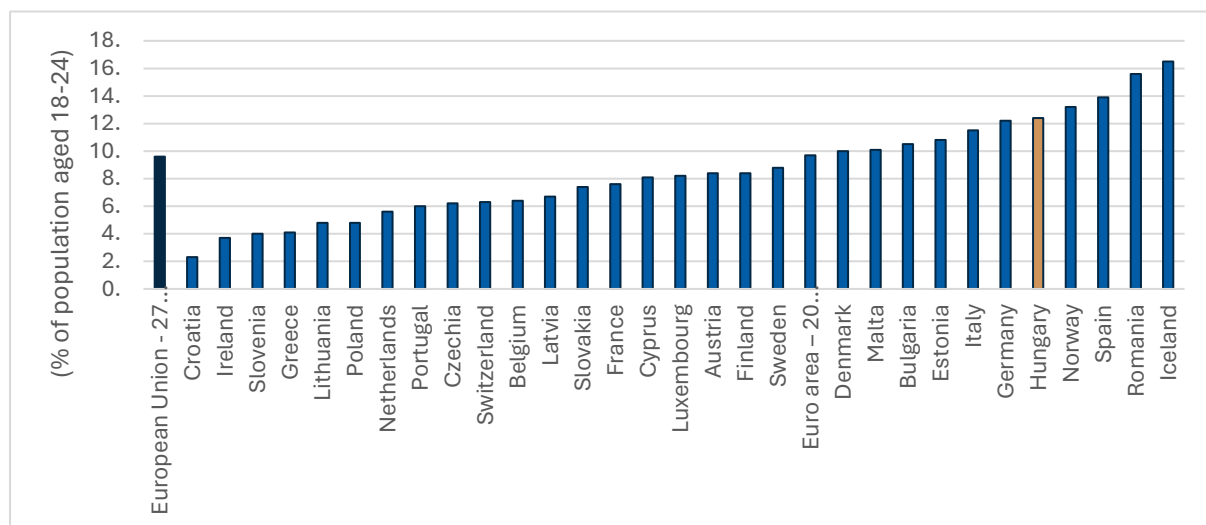


Figure 10: Early leavers from education and training (2022), Source: Eurostat

There is a very high number of drop-outs from the public education system (i.e. those with no more than a basic education), which is a barrier to opportunity. In 2022, the percentage of young people aged 18-24 with no more than primary education, no further education or training was 12.4%, compared to an average of 6.1% in the Visegrád region.

Over the last two decades, the unskilled population has been excluded from employment for the most part, increasing social and territorial disparities and reducing social mobility. This trend will continue in the future unless the education system is able to equip disadvantaged students with the outlook and competences needed in the labor market.

Alleviating labor market problems is implausible in the short run without integrating young people who drop out of education into the workforce after adequate training. This is not only a societal need, but an economic need. Every Hungarian student should leave public education with at least a full secondary education, thus increasing their chances in the labor market. While there is a debate among education experts about the impact of bringing the age limit of compulsory education back to 18, from an employer's perspective, we think that it is not feasible to acquire the skills and competences necessary to thrive in a modern economy up until the age of 16.

SUSTAINABLE TEACHER SUPPLY IS THE BASIS FOR COMPETITIVE EDUCATION

The continuing decline in the number of working age teachers and the general ageing of the profession signals the dilemma of the future sustainability of the education system. In our view, the three main issues in the teacher training system are as follows:

1. the lack of attractiveness of the career;
2. low entry requirements for teacher training;
3. fragmented teacher education.

We consider it particularly important to ensure the human resources of education, because without motivated and professionally prepared teachers, the transformation of the education system cannot succeed. Emphasis should be placed on attracting the best talent to post-secondary education, thus, we call for government action to facilitate this, reflecting the recognition as well as the socio-economic weight and importance of teachers. Wage realignment is a vital but insufficient step in this process. In order to attract professionals with the right skills and motivation, we propose to take education out of the realm of day-to-day politics and put it back into the framework of the social minimum.

While it is the duty of the state to ensure access to education of equal quality, it is also necessary to avoid excessive uniformity of education, which is risked by overly centralizing education. Granted, we do not dispute the need for a core curriculum that sets out the knowledge and skills framework that all students should acquire, however,

designing individual learning pathways, and that teachers have sufficient autonomy are essential to help students choose the learning methods that best suit them. Greater freedom and methodological flexibility in teaching can also lead to the development of new good practices, such as the appropriate place of new digital technologies (e.g. generative AI) in the education system. This requires the government to commit to modern, digital teaching methods that ensure that teachers and schools have access to digital solutions and tools. The organizational autonomy of schools can assure teachers' autonomy and professional freedom.

Additionally, it is important to expand the network of educational support professionals, such as school psychologists, development educators, mental health professionals, career counsellors, etc. They are necessary in all institutions, but especially in schools in lagging regions.

Hungary's economic competitiveness is closely linked to the ability of the education system to effectively convey, translate into practice, and meet the needs of the economy. Skills such as problem-solving, creativity, communication and digital literacy not only affect personal fulfilment, but also determine a country's economic and innovation potential. Accordingly, the education system needs to adapt dynamically to current and future labor market requirements in order to contribute to the country's competitiveness and growth. A coherent and comprehensive reform would have detectable positive effects within ten years, and in the long run would create the basis for a more competitive and prosperous Hungary.

THE LINK BETWEEN HEALTH AND COMPETITIVENESS

The health of the population has an impact on all aspects of society and the economy, so improving the health of the population by preventing and detection chronic diseases early is of national strategic interest. Regrettably, life expectancy in Hungary is 76.2 years, the 5th lowest in the EU, and has dropped by two years during the Covid19 pandemic.

Citizens in adequate health conditions place smaller burdens on the healthcare system; moreover, good health indicators directly affect productivity and, therefore, Hungary's competitiveness in general. Increases in the number of years spent in health have been shown to be associated with higher productivity and GDP growth. Thus, spending on healthcare should be regarded as an investment in human resources rather than an expense.

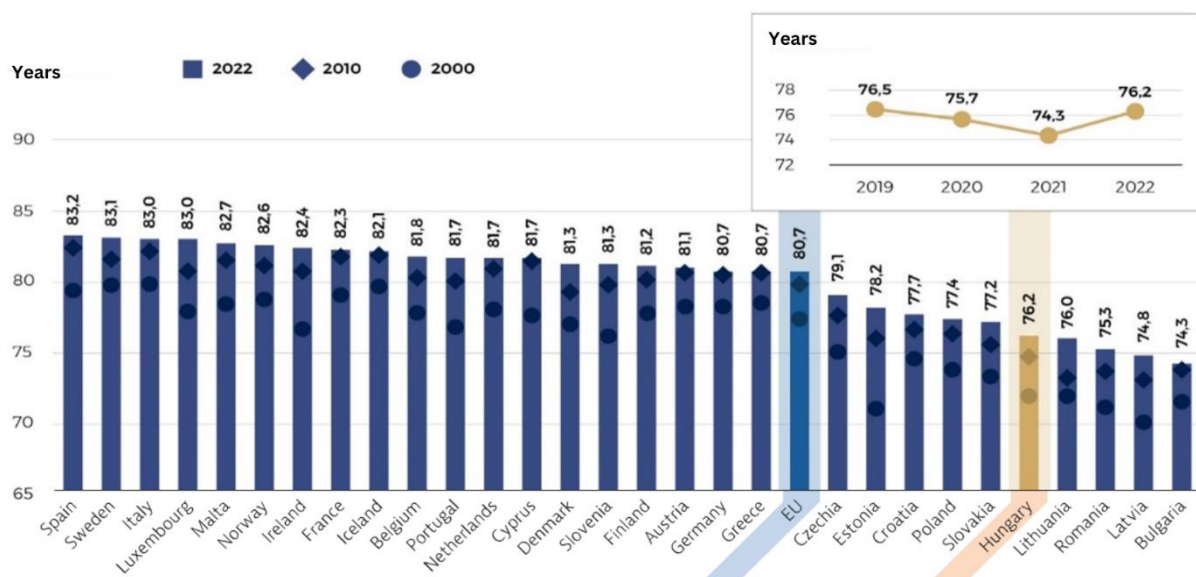


Figure 11: Life expectancy down by more than 2 years after the start of the Covid19 pandemic Source: OECD: State of Health in the EU; Hungary, health country profile 2023

Currently, the ageing population in all EU countries, including Hungary, is making it increasingly expensive to maintain welfare systems. Concurrently, the number of new entrants to the labor market is regularly lower than the number of retirees. This fiscally and competitiveness-wise negative impact can be mitigated by importing labor or, in the long run, by increasing the birth rate. However, this needs to be accompanied by the maintenance of the health of the working-age population.

The labor needs of the Hungarian economy cannot be met by guest workers or young people entering the labor market alone. This is clearly indicated by the fact that the number of employees aged 65 and over, i.e. those working beyond retirement age, has tripled over the past ten years.

The share of people aged 65 and over in employment is projected to rise from 19% in 2018 to 29% in 2050. Therefore, in beyond the physical health of working age people, the mental and physical health of this age group alone has a significant impact on the country's economic performance. The health of the population is a critical strategic factor that can only be improved through quick and effective action. Additionally, a reason for concern is that surveys show that nearly 17% of employees over 45 years of age have a 'moderate' or 'poor' Work Capacity Index, indicating the need for urgent intervention to address the risk of losing their ability to work.

Hungary has one of the highest rates of years of life lost due to avoidable mortality among OECD countries. This negative ranking applies to both preventable mortality (which could be prevented by public health and primary prevention interventions) and treatable mortality (which could be avoided by timely screening and appropriate treatment). Avoidable mortality has a particularly large impact on the competitiveness of the economy, as the loss of the deceased means the permanent loss of a significant human resource.

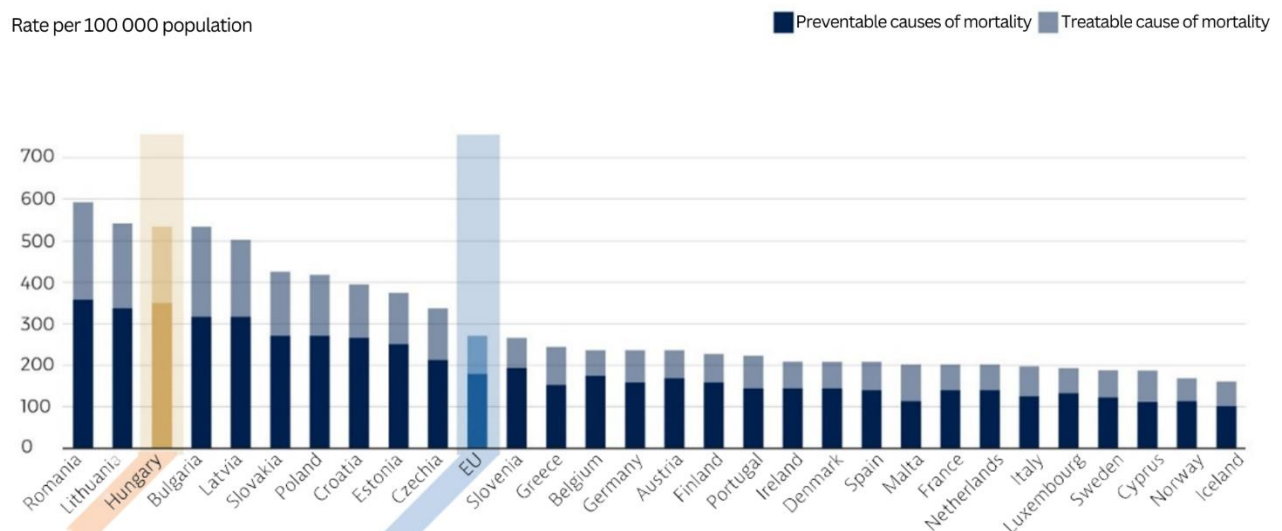


Figure 12: The avoidable death rate in Hungary is the 3rd highest in the EU. Source: OECD: State of Health in the EU; Hungary, Health country profile 2023

The close link between the health of the population and the competitiveness of the economy means that strategic planning for health must consider its impact on the economy. We would like to stress our support for efforts to improve the organizational, cost and resource efficiency of the sector and urge that changes be introduced as soon as possible. Granted, a lasting positive change in the healthcare system can only be achieved if public spending on health as a share of the GDP is increased significantly and sustainably.

The following aspects of the health ecosystem are of particular importance to our members. However, as it would be beyond the scope of this document to cover the full range of issues, we suggest reviewing our position statement [Healthy Nation, Competitive Country](#) published in 2022 for a detailed overview.

Hungary lagged behind the Czech Republic, Slovakia and Poland until the end of the last decade. Although Hungary approached the V4 average in 2020, this progress can be attributed to sectoral wage increases and exceptional items related to the fight against COVID. Efforts to build an active, working-age society that succeeds, and for Hungary to catch up with at least the European average, the level of public health expenditure as a share of GDP needs to sustainably and substantially exceed the V4 average.

INTERNATIONAL VALUE CHAINS SERVING MODERN HEALTHCARE

The Covid pandemic has highlighted the need to increase self-sufficiency in healthcare, but mainly in basic hygiene equipment (masks, gloves, hand sanitizers, etc.) and essential medicines. In modern healthcare, complex medicines and devices are produced in global value chains worldwide due to their diversity and technological needs, and it is not practical or realistic for even the largest and most economically powerful countries to produce the entire roster exclusively domestically. Moreover, in the case of complex medicines and devices, the shortening of value chains even on a limited scale can only be achieved in a pan-European context and through cooperation.

In addition, it is vital to encourage industry-specific R&D investments and higher value-added work processes in the sector. Increasing the long-term competitiveness of the domestic pharmaceutical sector is feasible by attracting international capital and knowledge. These investments play a role in increasing the country's competitiveness not only through their direct economic impact, but also through the retention of highly skilled labor, the development of areas for research (e.g. digital competences, Big Data and AI capacities, etc.) and thus, by the increase of intellectual capital. However, we believe that industrial policy considerations should be separated from issues of pharmaceutical subsidies and financing, as the two areas have different objectives. While industrial policy pursues primarily economic and strategic goals, financing should follow a value-based approach, i.e. ensuring the highest achievable health gain for the patient at the best price.

Developing a digital health infrastructure (integrating health databases, cleansing the data they contain, and introducing e-health solutions to better manage and share data) would both help improve the efficiency of care and enable more domestic research and business-based investment. In this area too, we urge the government to work with stakeholders from the market in the sector to promote digital health services.

CHALLENGES FOR THE HUNGARIAN HEALTHCARE ECOSYSTEM

Hungarian health spending is among the lowest in Europe, both in terms of GDP and population. In 2021, only 7.4% of GDP will be spent on health, compared to the European average of 11%. The need for a significant increase in spending in Hungary is illustrated by the OECD data on the number of avoidable deaths per a population of 100,000, What is more, Hungary ranks first in the European Union for cancer deaths and second after Bulgaria for cardiovascular disease deaths.

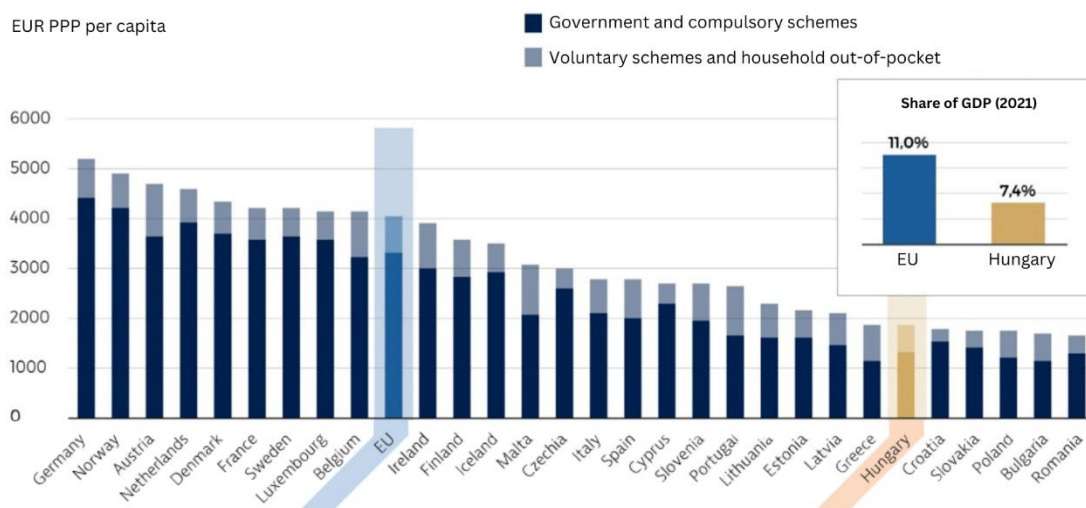


Figure 13: Health expenditure in Hungary is among the lowest in the EU. Source: OECD: State of Health in the EU; Hungary, health country profile 2023

Life sciences companies in the healthcare sector face the same challenges of an unpredictable regulatory and tax environment as those in other sectors. Moreover, due to the specificities of the sector, our member companies operating in the area are facing increasing challenges from processes that negatively affect their business and operating environment. The volatility of the Hungarian forint, its depreciation, which is still higher than desired inflation next to globally increased manufacturing and logistics costs pose a serious challenge for life sciences companies. Given their limited possibilities to compensate for these negative factors, their profitability is severely affected, influencing not only the availability of the products they sell, but also their R&D activities and other investments.

Preserving security of supply requires the introduction of price tracking mechanisms to offset the highly damaging effects of negative economic trends, raising raw material and energy prices, as well as transport costs on the businesses and operating environment of our members. The 40% special tax on pharmaceutical distributors imposed on May 31, 2023 for medicines with a producer price of more than HUF 10,000 is a particularly high burden for companies.

Hospitals' debts pose significant problems. The reasons for the recurrent accumulation of debt are well-known to health policymakers, and a detailed discussion of them is beyond the scope of this recommendation package. In addition, this is a key issue from a competitiveness perspective, thus, a solution is needed to ensure both the commitment of suppliers to Hungarian healthcare and the efficient use of available financial resources. We call for a structure to be set up whereby hospital orders are remunerated in time by a financial institution with a state mandate to suppliers. A predictable payment environment would make hospital suppliers' operations more stable and help maintain the security of supply.

THE LINK BETWEEN PUBLIC AND PRIVATE HEALTHCARE

Private healthcare is not only an alternative to public care, but it also relieves the burden on public care and provides services that fill gaps. A conscious, planned framework of cooperation between the public and private health systems can significantly alleviate many of the current systemic problems (waiting lists, underfunding, patient satisfaction, etc.). Hungary does not have enough health professionals for the two systems, but effective cooperation between the two systems could significantly improve the problem of the lack of human resources.

In Hungary, 25% of all health expenditure is paid purely out of pocket, compared to the OECD average of 18% in 2023. There is a need to create a sustainable service with a broader range of available services provided with mixed funding (from NEAK and household private resources), relying on the current purely privately funded service providers. Rather than rigidly separating and contrasting public and private funding, this model will create coexistence and will be able to help the development of the services market without reducing solidarity in the system.

STRENGTHENING PREVENTION THROUGH OCCUPATIONAL HEALTH

Modern and well-organized occupational health could become complementary to primary care, with the organizing power of companies (backed up by the right incentives) in prevention and primary specialist care, leading to public health-level gains. The impact can be maximized if legislation and incentives together can bring all employed people (~4.7 million) into contact with the occupational health system.

The situation is particularly topical given that, according to NEAK data, in January 2024 the number of GP practices permanently vacant was in the order of 900, leaving nearly 1.5 million people without a permanent GP, and the situation is expected to deteriorate further due to the average age of GPs over 60 and the lack of replacement. Occupational health providers could therefore be given a much more prominent role than at present in mobilizing for screening and thus prevention. To this end, occupational health specialists need to be granted the powers of general practitioners (e.g. referral and prescription powers). As a complement to this, we propose that the government should also allow specialists to set up a general practitioner practice without a territorial obligation.

IV. CONDITIONS OF SMART GROWTH

THE SIGNIFICANCE OF DIGITAL TRANSFORMATION

Digitalization is a comprehensive process that will fundamentally shape our entire world, including our society and economy, in the 21st century. The transition to a new operating scheme represents both an unprecedented opportunity and a challenge, as it can offer a way out of the middle-income trap and catalyze a transition towards a higher value-added economy. On the other hand, missing the digitalization window could jeopardize the economic results already achieved.

We believe that the development of a modern data economy and the creation of decision-making practices based on it are essential to increase Hungary's competitiveness. We welcome and support the government's efforts in this direction, such as programs to develop digital skills in society, the introduction of digital citizenship, or the data-driven approach to health planning and decision-making. The national data assets have significant economic and R&D&I potential, so we believe it is paramount that they are accessible to economic actors (under appropriate data protection conditions).

In our view, tying data storage to geographic location does not enhance data sovereignty, and in fact is more of a security risk. The IT protection of data can be implemented on the same level on cloud platforms as on physical servers. Due to the decentralized nature of cloud infrastructure, it is not exposed to physical risks such as theft of on-spot media, sabotage, targeted attacks on physical infrastructure, etc.

The digital transition is given a further boost by the spread of artificial intelligence solutions. Their emergence and use could bring the same revolutionary changes as the spread of electricity or the Internet. AI can be identified as perhaps the most dominant technology of our time, and some countries at the forefront of the field now see it as an infrastructure of comparable importance to telecoms or data centers. It is worth following this approach and example in our country, too, in order to avoid the trap of mediocrity.

THE SIGNIFICANCE OF DIGITAL TRANSFORMATION IN HUNGARY

The best reference system for measuring digitalization in Europe is the EU's digital economy and social development indicator, DESI. The 2022 survey ranks Hungary 22nd among the 27 EU Member States. The pace of digital transformation in recent years has been in line with the EU average, but Hungary needs to catch up in several areas:

- Digital public services (ranked 21st with 57.4 points, compared to the EU average of 67.3),

- Digital skills for human capital (ranked 23rd with 38.4 points, compared to the EU average of 45.7),
- Integration of digital technologies (ranked 25th with 21.6 points, compared to the EU average of 36.1),

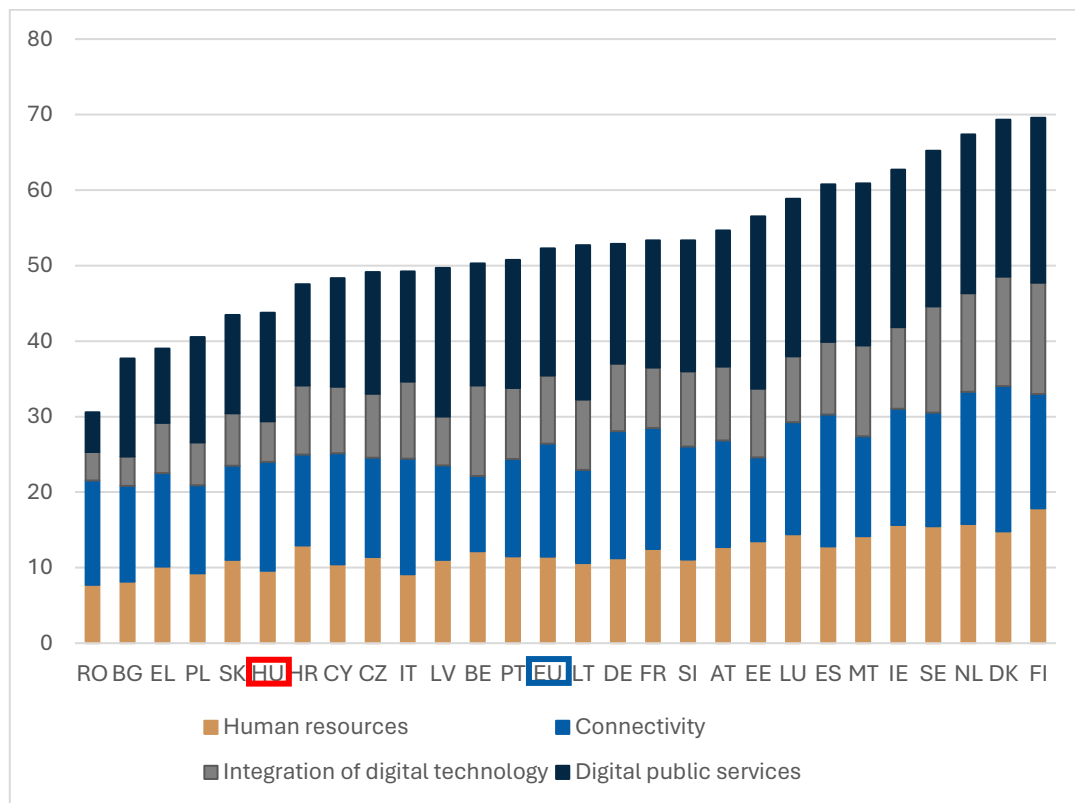


Figure 14: DESI-index 2022, Sources: European Commission

In the field of digital public services, the National Digital Citizenship Program could be a major leap forward and, if properly implemented, could provide a good basis for closing the gap. We recommend that the government engage in an intensive dialogue with domestic and multinational industry players and their representative professional organizations to ensure that the details are developed and implemented as successfully as possible. The success of the program also depends on the host side, i.e. on the confidence and ability of clients (businesses, but more importantly citizens) to use the services. We therefore recommend the launch of positive, non-political, information and education campaigns at the appropriate points of implementation.

In terms of digital skills in human capital, 49% of the population have at least basic skills, compared to the EU average of 54%, and 22% have higher skills compared to 26% in the EU. For ICT professionals, the rate is 3.9%, compared to 4.5% in the EU, and this key indicator has improved by just half a percentage point since 2019. We are afraid of that lagging behind the EU average in this area does not ensure catching up and is therefore worrying for the future competitiveness of the country. We consider digital education, improving overall digital skills, enhancing the Hungarian education system through the

benefits of digitalization, and increasing resilience to cybersecurity risks to be a top priority. We therefore urge that the situation be improved with appropriate government commitment and resource allocation.

In regards the economic integration of digital technologies, although progress has been made in 2021, the majority of Hungarian businesses are still not taking advantage of the opportunities offered by digital technologies. 21% of companies use enterprise resource planning software to share information electronically (EU average: 38%) and only 13% use social media (EU average: 29%) or electronic invoicing (EU average: 32%). The situation is similar for advanced technologies: in terms of artificial intelligence, cloud services and big data, Hungary is also well below the EU average. The take-up of these services ranged between 3% and 21%, compared to the target of 75% set for the Digital Decade in 2030. Discrepancies may be due to a lack of tools, a lack of skilled human resources, or even a lack of recognition of the importance of digital technologies.

For Hungary to seize the breakthrough potential of technological development, the economy needs to be put on a consistent technology-led growth path, including industrial policy, enterprise development, innovation policy, education and training systems and public services. Professional organizations have prepared detailed recommendations for their implementation; on this topic, we would like to recommend to the attention of stakeholders the [Alliance for the Digital Hungary](#) package of recommendations published by our strategic partner, the Association of Digital Enterprises in 2022, in which our Chamber agrees with the recommendations.

THE UNIVERSITY-INNOVATION SYSTEM AND BUSINESS COOPERATION

The establishment of a well-functioning education-research-innovation ecosystem is essential to ensure Hungary's long-term competitiveness. One of the key elements of this system is the various higher education institutions, which fulfil three important functions for our member companies:

1. filling the 'talent pool', training future employees;
2. project-based innovation cooperation;
3. innovations from basic research, exploitation, collaboration with 'spinoffs'.

As discussed in the *Human Capital* chapter, the Hungarian labor market is characterized by strong employer demand, especially for skilled workers. Consequently, in accordance with the supply and demand rules of the market, a practice has developed whereby university students, even during their bachelor studies, can easily find well-paid job offers (in relation to their life situation), which is reinforced by certain tax policies, such as the exemption from income tax for people under the age of 25. While the early acquisition of work experience is welcome, the practice also means that many students do not continue their studies after obtaining a bachelor's degree, or even leave the system before they have completed it. At the societal level, the process results in fewer

than necessary highly skilled workers (with master's or doctoral degrees) leaving the system, which limits the feasibility of high value-added R&D&I investments.

In the course of 2021, the implementation of the new higher education model initiated significant changes in the lives of the Hungarian universities that underwent the model change. One of the priority goals of the restructuring was to create more favorable legislative and operating conditions for collaboration between higher education and the business sector. Although it is too early to draw conclusions on the overall balance of the model change, some observations can be made after having conducted background discussions with several stakeholders.

We welcome the government's long-term goal to create a more flexible operating environment, to raise the quality of education and to promote the market exploitation of university innovations by putting higher education institutions under foundation management. Our general experience is that the change of model has made higher education institutions more open to cooperation with industry.

In addition to the existence of openness, the effectiveness of cooperation with business actors is burdened by the fact that the structure and effectiveness of the departments responsible for corporate relations vary from one institution to another, and the effectiveness of cooperation often depends more on personal qualities. To improve this, it is necessary to set up a single and easily accessible institutional framework system to help business actors in mapping up and using the services of the given higher education institution. In line with the establishment of that single institutional framework system, it is important to develop a project management approach among staff members working in the business coordination field and to use allocated project managers in these areas. Effective market positioning of institutional capacities requires a good marketing mindset and a sales mentality. This will accelerate local operating processes, thereby promoting compliance with market deadlines. The creation of a national university knowledge base and an institutional competency map of research capacities (regardless of the funding model and updated annually) could also greatly facilitate cooperation.

At a strategic level, it would also be worth considering the criteria for assessing the success of higher education institutions. The capacity of university teachers is often fragmented between required teaching activities, innovation project work in companies and basic research activities. The question of how much resources should be devoted to basic research in the current Hungarian context is of strategic importance, given the fact that there is real global competition in this field and that the competitors are among the best-funded institutions in the world. However, it should also be considered that, while the market-oriented deployment of research resources leads to more tangible and financially rewarding results, basic research, in addition to the potential 'groundbreaking' discoveries that can be made, plays a key role in making a career in research more attractive and thus ensuring the next generation of researchers.

Hungarian higher education institutions must have unhindered access to EU and other international research and student programs (in particular Horizon and Erasmus+), as

any high quality scientific and training activity today can only be imagined in the context of international networks. If the isolation of domestic foundation-based institutions persists, it is likely that they will gradually lose competitiveness and find it even more difficult to retain highly skilled and prestigious professionals. In the longer term, such a situation may also have a negative impact on the prospects for a transition towards a higher value-added economy and may limit the scope for higher value-added FDI imports.

In order to restore the external and domestic credibility of university foundations, boards of trustees should be composed of sufficiently diverse, politically independent professionals from financial, business, legal, educational and other backgrounds.

ECONOMIC DEVELOPMENT WITHIN THE EUROPEAN GREEN DEAL

Reducing carbon dioxide emissions – is not only a central element of the European Green Deal—it is a universal goal as well. In this context, we support the commitments in Hungary's National Energy and Climate Plan. To achieve these objectives, we propose a detailed action plan, supported by impact assessments and industry consultations, and with the identification of responsible parties, setting out 5-10 year objectives, which need to be communicated consistently to society as a whole, with an educational focus. It is critical that the government monitors implementation in an ongoing and accountable way.

A gradual green transition of the economy, and industry in particular, is necessary, but it can only happen if the economic changes do not impose a disproportionate burden on society and do not undermine the competitiveness of EU businesses. We are aware of that some of the Commission's recommendations, in their current form, impose burdens and obligations on industry that jeopardize competitiveness, for example forcing early introduction of investments that are not yet economically viable and will not pay off. These investments, which are capital-intensive and high-risk, could jeopardize the economic viability of industrial actors and thus the competitiveness of European industrial capacity against US and Asian imports. Incentivizing companies and reducing the cost of switching, while respecting EU competition rules, could accelerate the achievement of the Green Deal's objectives and facilitate investment in the EU and Hungary. Reducing bureaucracy and ensuring a predictable regulatory environment would also contribute greatly to the latter. The Antwerp Declaration for a European Industrial Agreement, presented in February 2024 and supported by a wide range of sectors, reflects these issues. The objectives set out in the declaration are all designed to promote the transformation of European industry while maintaining competitiveness and resilience.

Achieving the above objectives will also be helped by an investment strategy that favors industries that can work in harmony with the country's natural resources and match its energy production capacity. It is also important to bear in mind that even if a natural

resource is currently abundant (such as the ever-increasing value of surface and groundwater resources), this does not necessarily mean that it will be so in the future. Due to the unpredictable effects of climate change, they could run out in the longer term if not used properly. A comprehensive program to modernize the country's utility infrastructure should therefore be launched alongside the investment strategy. Without significant government attention and investment, the utility infrastructure could become a serious competitive handicap, due to unrealistic capacity planned for many years ago and poor technical conditions in many places.

THE CHALLENGES OF THE TRANSITION TO A CIRCULAR ECONOMY

The circular economy model takes into account the total product life cycle in order to increase the lifetime, recycling and reuse possibilities for products. The adaptation of the model is particularly important in resource-poor regions, where it can open up new dimensions in research and development, economic growth and job creation, as well as savings.

The recycling of as much waste as possible is central to the circular economy model, which can have significant positive economic impacts in addition to environmental considerations. Although the waste concession system introduced by the government in 2023 was intended to increase recycling efficiency, contracting and other technical difficulties with subcontractors have resulted in the collection of recyclable waste falling by an average of around half since the concession started, with some types of waste (e.g. metal, batteries, etc.) almost completely out of the system for months. Although there has been some improvement, overall collection and recycling is still operating at a reduced efficiency. The dual application of the EPR system and the product charge, as discussed above, creates further difficulties. We propose that the government perform a comprehensive analysis of the current situation and set out a policy agenda to address the obstacles and shortcomings identified. The most appropriate way to do this would be to introduce legislation to make the current concession waste management system more efficient, avoiding further systemic changes.

ALTERNATIVE RECYCLING SOLUTIONS AND THE SIGNIFICANCE OF THE SUSTAINABLE CHEMICALS STRATEGY

Mechanical recycling is a well-established technology, although its efficiency has certain limitations. Therefore, other innovative technologies, such as chemical recycling, will also be needed to meet the targets set by EU legislation. The introduction of new technologies requires a competitive regulatory framework that is open to different technologies (technology openness) and facilitates their inclusion - for example in the case of the calculation of recycled content (see mass balance approach). The Chemical Strategy for Sustainability (CSS) also needs to be aligned with the criteria for ending

waste status, as some problematic substances cannot be aligned with the circular economy model. For these, a technological analysis should be carried out to see whether there is a realistic alternative to their use. Incentives and thoughtful regulatory changes are needed to kick-start these processes, so that they can be market-based and profitable in the future.

The Chemical Strategy for Sustainability was published in October 2020. A key element of the paradigm-shifting package is a move away from science-based risk management towards a general ban on substances with certain hazard labels in consumer and professional applications, and the introduction of new hazard classes under the CLP legislation.

The industry needs a transition path that provides a realistic plan to achieve the goals of the CSS. The impact of the transition from a risk-based to a hazard-based approach on the daily lives of consumers and professional users, and how this approach will look in practice, needs to be assessed. The application of the GRA (General Risk Approach), the amendments to the CLP Regulation on classification, labelling and packaging of substances and mixtures and the REACH Regulation on the Registration, Evaluation, Authorization and Restriction of Chemicals are expected to restrict the manufacture and use of products and increase their production costs. Overall, this could have a significant and potentially negative impact on the development and competitiveness of the chemicals market in EU Member States.

The chemical industry needs financial means and a sufficient timeframe for transformation, with a clear and predictable implementation path and a market for clean technologies and products to achieve the EU's sustainability goals and initiatives. The chemical industry is the cornerstone of future sustainability innovation, and continued support is essential to enable and accelerate the achievement of sustainability goals and to maintain the competitiveness of EU businesses. In 2023, the European Commission prepared the so-called 'Transition Pathway' document, which sets out the key points for the chemical industry to make the green and digital transition. There is a need for such a document at the national level, taking into account the views of Hungarian chemical companies.

POWER GENERATION, ALTERNATIVE ENERGY SOURCES

The output from photovoltaic power plants and wind turbines are not adequately predictable due to the technology and the geographical characteristics of Hungary. We assume that nuclear and gas fueled power plants will continue to be needed to ensure a stable supply and to avoid fluctuations in the future, but that they would require significant R&D&I resources to advance energy storage technologies. For alternative energy sources, such as hydrogen or Carbon Capture and Storage (CCS) solutions, where a meaningful market has not yet developed, the state needs to support investment, including through an appropriate legal framework. In implementing the

energy strategy, it is inevitable that the government considers the realities of the wider geopolitical environment alongside strictly economic considerations, and takes into account the extent to which contractor and supplier contracts will be sustainable within this framework.

A certain degree of decentralization of the currently centralized energy network should be considered, which could be accelerated, for example, by supporting small-scale household power plants (SSHPs) and by creating a legal framework that would allow energy communities to operate in a meaningful way and by promoting their establishment. The establishment and development of a 'peer-to-peer' network of energy communities focused on renewable energy, especially in small towns and rural areas, would be an effective way to aggregate small loads. The widespread dissemination of microgrids, capable of ensuring maximum localized consumption of renewable energy, schedule observation and the elimination of grid problems, is also vital. The ability to operate in isolation also represents decentralized energy security. On-site and off-site corporate PPAs (power purchase agreements) can play a key role in promoting the use of renewable energy and generating finance, and their promotion can also be a good goal for the state. Currently there is a lack of necessary legal conditions for the take-up of these solutions, and in the case of residential solutions, the fact that users are automatically excluded from the scope of those eligible for a reduction in the electricity bill is a particular obstacle. In Hungary, taxes on energy-related areas are exceptionally high and should be substantially reduced in order to improve the return on energy investments (e.g. the Robin Hood tax and the system usage fee for the use of the public electricity grid). It is important that the implementation of these innovative solutions, which reduce energy dependency locally, is subject to as few regulatory and administrative barriers as possible, which discourage investment.

ENERGY EFFICIENCY

Most of the buildings in Hungary is highly inefficient from an energy aspect. The situation is particularly bad for residential buildings, but even for major investments we are far from the target of 100% zero-emission buildings by 2030.

Around 37% of the country's final energy consumption in 2021 can be attributed to household energy consumption. In order to substantially improve the energy efficiency of the existing domestic residential sector, substantial support should be made available to the public for energy upgrades. Energy efficiency projects that contribute to reducing Hungary's energy dependence and building a more sustainable future should be supported and promoted.

Construction of zero-emission buildings to a greater extent is considerably impeded by the lack of an established and stable underlying infrastructure to rely on, there is a lack of innovative, energy-efficient technologies and smart solutions that reduce energy use and negative impacts on the environment. There is also a lack of information channels

for stakeholders (especially the public) to obtain credible information on energy efficiency in buildings. We believe that quick and effective incentive steps by the government are necessary in these areas.

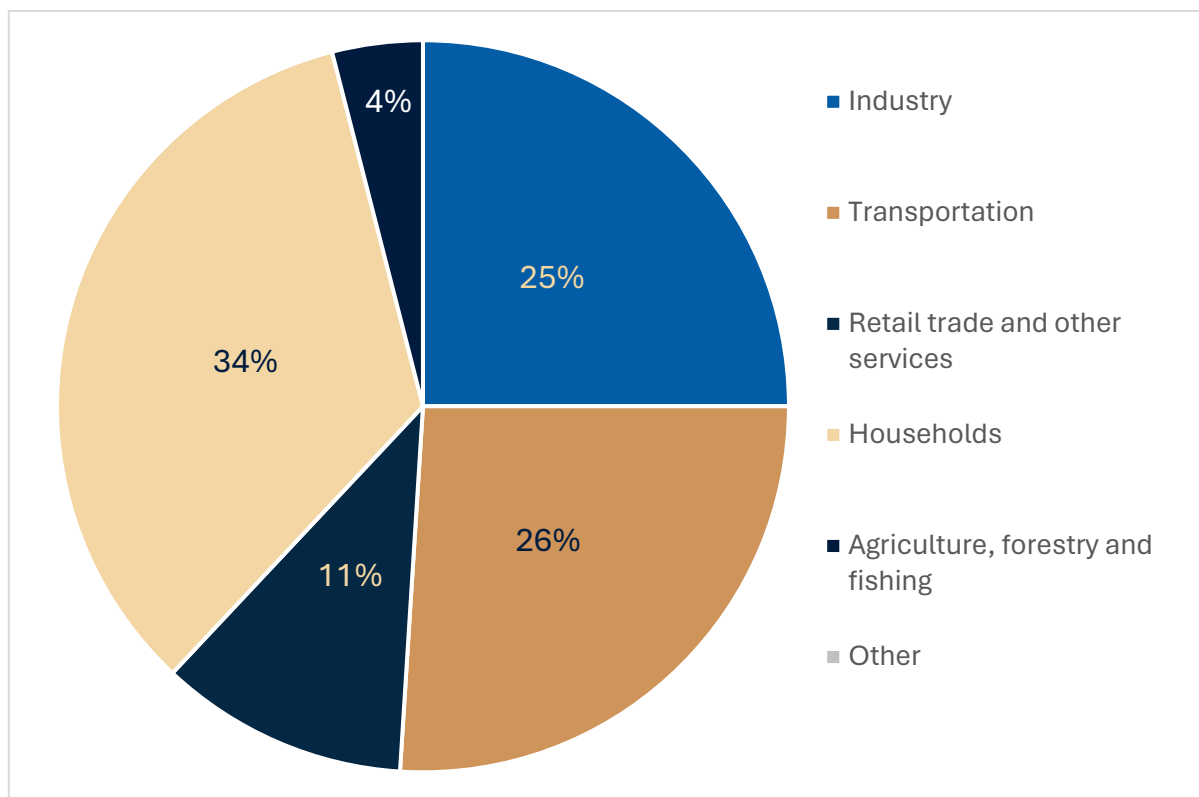


Figure 15: Distribution of final energy use. Source: Revised National Energy and Climate Plan 2023

SUMMARY

GENERAL BUSINESS AND INVESTMENT ENVIRONMENT

1. The countries of the Central and Eastern European region form a relatively homogeneous group in the eyes of investors looking for global or European destinations, so in the competition for FDI it is crucial that Hungary is seen in a more favorable light than its neighbors in the pre-decision analyzes comparing the countries of the region. Particularly high risks at this stage are the extreme negative macroeconomic divergences, the absence of relevant international treaties, the lack of access to key financial resources and the general perception of the country's economic and political environment.
2. For many years, AmCham has argued that to maintain Hungary's long-term competitiveness, it is essential to significantly increase the productivity of the economy and shift the focus of economic policy from quantity to quality. This process requires a computable legal and fiscal environment, adequately skilled and available human resources, a sufficiently efficient R&D&I ecosystem, improved competitiveness of the start-up and SME sector, and the development of the country's infrastructure. These measures can only be implemented with strong government commitment. Predictability is greatly enhanced when governments consult widely and in a timely manner on measures affecting the economy.

TAX REGULATION FROM A COMPETITIVENESS PERSPECTIVE

3. One of the greatest sources of uncertainty in the Hungarian economic and legal environment is the practice of imposing special taxes, which has a highly disruptive effect on entire sectors of the economy. Special taxes reduce productivity, can discourage development and reinvestment, and are also a negative aspect of the risk assessment of new investors. Although special taxes are an easy revenue for the budget, they have a demonstrable negative economic impact even in the medium term, and we recommend that the government should stop imposing them.
4. The current tax system is too complex and bureaucratic, leading to lower productivity for both the state and the companies. Reducing the number of taxes can also lead to a more attractive investment environment. A general tax technical revision might also create the opportunity for other bureaucracy-reducing measures.
5. The termination of the double taxation treaty between the US and Hungary will create a serious competitive disadvantage in the regional competition for US

working capital, but will particularly affect Hungarian technology start-ups, whose primary market remains the US. Hungarian individuals who have a presence in the US markets through share incentive plans or savings are at a significant disadvantage. In summary, the lack of an agreement significantly reduces the country's competitiveness, contributes to higher costs for domestic subsidiaries and may ultimately lead to an outflow of highly skilled labor. Due to the peculiarities of the US legislature, despite any hypothetical scenario and political promises, it is not worth expecting a quick solution, so the Hungarian side could help to resolve the issue by bringing the matter to a technical level as soon as possible and by actively reducing diplomatic tensions.

FACTORS DETERMINING HUMAN CAPITAL

6. The country's future competitiveness and opportunities are fundamentally determined by the nature and defining characteristics of the human resources available, and it is therefore critical that the two areas most affecting human resources, education and health, are given adequate strategic weight in stakeholders' vision for Hungary's future.
7. The Hungarian labor market is characterized by both persistent labor shortages and a certain degree of unemployment, due to a mismatch between the needs of employers and the qualifications, skills and even intentions of jobseekers. Meeting labor demand requires both opening up the country's internal reserves through targeted programs and budgetary resources, and promoting the employment of foreign workers, for whom there is international competition. The quality of the foreign workforce that can be attracted depends to a large extent on the opportunities and circumstances offered by each country, the perception of these and the possibilities of working in Hungary.
8. The measure of the effectiveness of the education system from an employer's perspective is the extent to which it can prepare young people for labor market opportunities and the added value they bring to the labor market in the future. A highly skilled workforce with modern knowledge is essential to maintain and increase the competitiveness of the economy. Public education is an input at the top of the education chain for both higher education and the labor market, so it must perform its function to the best effect.
9. The transformation of the education system cannot succeed without motivated and professionally prepared teachers. In the training of young people, emphasis should be placed on attracting the best talent. To facilitate this, we call for government measures that reflect the recognition of the socio-economic weight and importance of teachers and provide them with appropriate professional flexibility. Wage realignment is an inevitable but insufficient step in this process.

To attract a teaching workforce with the right skills and motivation, we propose to take education out of the realm of daily politics and put it back into the framework of the social minimum.

10. The health of the population has an impact on all aspects of society and the economy, so improving the health of the population and preventing and early detection of chronic diseases is of national strategic interest. Citizens in good health conditions put smaller burdens on the healthcare system; also, good health indicators directly affect productivity and, therefore, Hungary's competitiveness in general. Increases in the number of years spent in health are associated with higher productivity and GDP growth, so health spending should be seen as an investment in human resources rather than a 'cost center'.
11. Hungary has one of the highest rates of life-years lost due to avoidable mortality among OECD countries. This negative ranking applies to both preventable mortality (which could be prevented by public health and primary prevention interventions) and treatable mortality (which could be avoided by timely screening and appropriate treatment). Avoidable mortality has a particularly large impact on the competitiveness of the economy as a whole, as the loss of the deceased means the permanent loss of a significant human resource. Hungarian health spending is among the lowest in Europe, both in terms of GDP and population, so it is essential to increase spending while improving the efficiency of the public health system.
12. The Covid outbreak has highlighted the need for a degree of self-sufficiency in healthcare, but mainly in basic hygiene supplies and essential medicines. In modern healthcare, complex medicines and devices are produced in global value chains worldwide due to their diversity and technological needs, and it is not practical or realistic for even the largest and most economically powerful countries to produce the entire vertical exclusively domestically. Also in the case of complex medicines and devices, the limited shortening of value chains can only be achieved in a pan-European context and through cooperation.
13. Life sciences companies in the health sector face the same challenges of an unpredictable regulatory and tax environment as those in other sectors but have very limited possibilities to compensate for these negative factors due to the specificities of the sector. Their declining profitability affects not only the availability of the products they sell but also their research and development activities and investments. Preserving the security of supply requires the introduction of price tracking mechanisms to offset the highly damaging effects of negative economic trends, rising raw material and energy prices, and rising transport costs on the business and operating environment of our member companies.
14. Private healthcare is not only an alternative to public care, but it also relieves the burden on public care and provides services that fill gaps. A conscious, planned

framework of cooperation between the public and private health systems can significantly alleviate many of the current systemic problems. A quarter of all health spending in Hungary is purely ‘out of pocket’, so there is a need to create a sustainable, diversified, mixed-funded service, building on the current purely privately funded providers. Rather than rigidly separating and contrasting public and private funding, this model will create coexistence and will be able to help the development of the services market without reducing solidarity in the system.

CONDITIONS OF SMART GROWTH

15. Digitalization is fundamentally shaping our society and our economy. On the one hand, the transition to a new operating scheme can offer a way out of the middle-income trap and catalyze a shift towards a higher value-added economy, while missing the digitalization window of opportunity could jeopardize the economic gains already made. To increase competitiveness, it is essential to develop a modern data economy and the decision-making practices that build on it. The national data assets have significant economic and R&D&I potential, so we assume that it is important that they are accessible to economic actors (under appropriate data protection conditions).
16. A key element of the innovation ecosystem is the system of cooperation between companies and universities. In order to increase efficiency, it would be important to develop a single, easily accessible institutional framework that (with a project-oriented approach) helps business actors to map and use the services of a given higher education institution. At a strategic level, it would also be worth considering the criteria for evaluating the success of higher education institutions, as the capacity of university teachers is often fragmented between the required teaching activities, the innovation projects of companies and basic research activities. An annually updated national university competence map could provide help to address this issue.
17. It is critical that Hungarian higher education institutions can participate freely in EU and other international research and student programs, as any high quality scientific and training activity can only be imagined embedded in international networks. If the isolation of domestic foundation-based institutions persists, it is likely that they will gradually lose competitiveness and find it even more difficult to retain highly skilled and prestigious professionals.
18. A gradual green transition of the economy is absolutely necessary, but it can only happen if the economic changes do not impose a disproportionate burden on society and do not undermine the competitiveness of EU businesses. These investments, which are capital-intensive and high-risk, could jeopardize the economic viability of industrial actors and thus the competitiveness of European industrial capacity against US and Asian imports. Providing incentives to

companies and mitigating the cost of the transition could accelerate the attainment of those goals.

19. The unpredictable effects of climate change mean that the natural resources that are still abundant need to be protected. A comprehensive program to modernize the country's utility infrastructure should therefore be launched alongside the investment strategy.
20. The recycling of as much waste as possible is vital to the circular economy model, which has significant positive economic impacts in addition to environmental considerations. Although the waste concession scheme introduced in 2023 was designed to increase recycling efficiency, contracting and other technical difficulties continue to significantly reduce the effectiveness of the scheme. We propose that the government should perform a comprehensive analysis of the current situation and set out a policy agenda to address the obstacles and shortcomings identified. The most appropriate way to do this would be to introduce legislation to make the current concession waste management system more efficient, avoiding further systemic changes.
21. The output of solar and wind power plants is not easily predictable due to the technology and the geographical characteristics of Hungary, so in addition to nuclear and gas fueled power plants, significant R&D&I resources and an appropriate regulatory framework would be needed to ensure a stable service in order to develop energy storage technologies in a forward-looking way. In implementing the energy strategy, it is important that the government considers the realities of the wider geopolitical environment alongside strictly economic considerations, and takes into account the extent to which contractor and supplier contracts will be sustainable within this framework. A certain degree of decentralization of the currently centralized energy network should also be considered, by supporting small-scale household power plants and by creating a legal framework that allows energy communities to operate in a meaningful way.
22. Most of the building stock in Hungary is highly inefficient from an energy aspect, especially in residential buildings, which can be significantly improved through effective government programs. Energy efficiency projects that contribute to reducing Hungary's energy dependence and building a more sustainable future should be supported and promoted. Construction of zero-emission buildings to a greater extent is considerably impeded by the lack of an established and stable underlying infrastructure to rely on, there is a lack of innovative, energy-efficient technologies and smart solutions that reduce energy use and negative impacts on the environment. There is also a lack of information channels for stakeholders (especially the public) to obtain credible information on energy efficiency in buildings. We are confident in that quick and effective incentive steps by the government are necessary in these areas.