

**LABOUR MARKET TRENDS  
IN HUNGARY, 2005**

**ÁLMOS TELEGDY**



## 1. INTRODUCTION

2005 was a successful year for Hungary by most macroeconomic indicators. GDP growth was about 4.3 percent, higher than in the previous two years, when it was 3.8 and 3.4, respectively.<sup>1</sup> Inflation was as low as 3.6 percent (measured by the consumer price index). The volume of investment also increased (by 6.4 percent), and industrial productivity grew by 10.7 percent. The success suggested by these figures, however, is somewhat tarnished by the very high budget deficit of over 2 percent, which shows the need for a correction in the very near future.

Concerning the labour market, three changes can be traced in 2005: the unemployment rate was high compared to previous years, and continued to increase during the year; the number of public sector employees continued to decline; real wages continued to rise and the increase was driven by the public sector. The growing economic activity, however, was not accompanied by a significant shift in the traditionally low participation rate, and the employment rate also remained stable at a low level.

The purpose of this report is to document the changes in the labour market indicators during 2005, and consider what can be the source of the change. The next section focuses on the employment and inactivity rate. Section three presents the unemployment rate. The last section documents changes in the real wages.

## 2. EMPLOYMENT AND INACTIVITY

Labour force participation has been low in Hungary since the beginning of the transition, and this has not changed in 2005. Table 1. shows that among the working age population (15–74 years old) the participation rate was 54.5 percent, less than one percent higher than in 2004.<sup>2</sup> This figure is 56.9 percent in the 25 European Union (EU) countries, showing that Hungary is a low

1 The figures presented in this chapter come mostly from the Hungarian Statistical Office Statdat system.

2 These rates are defined according to the International Labour Organization (ILO) definition. The participation rate (or activity rate) is defined as the number of working and unemployed over the total population (aged 15–74). Unemployment rate is defined as the number of unemployed over the number of active population. All those who are not active, are classified as inactive.

participation country, although the difference between the country and the EU average is not so great. The number of the active population was also quite stable, increasing only by 52 thousands on average between 2004 and 2005.

**Table 1: Economic Activity in 2005**

	Emp.	Unemp.	Active	Inactive	Emp. Rate	UE rate	Part. rate
<b>Total</b>							
2004	3,900.4	252.9	4,153.3	3,567.9	50.5	6.1	53.8
2005	3,901.5	303.9	4,205.4	3,517.1	50.5	7.2	54.5
<b>Quarterly</b>							
Q1 2005	3,870.6	297.4	4,168.0	3,556.0	50.1	7.1	54.0
Q2 2005	3,891.5	299.5	4,191.0	3,532.4	50.4	7.1	54.3
Q3 2005	3,927.6	308.6	4,236.2	3,485.7	50.9	7.3	54.9
Q4 2005	3,916.4	309.9	4,226.3	3,494.4	50.7	7.3	54.7

Source: *Hungarian Statistical Office* Statdat system. The figures refer to population 15–74 years old. The numbers are expressed in thousands, the rates in percents of the total.

The employment rate in 2005 was 50.4 percent, exactly the same as in the previous year. On average, 1,100 jobs were created on the net, the number of employed reaching 3,901.5. Over the year, the employment rate was quite stable, as the quarterly data in Table 1. show. The employment rate varied between 50.1 and 50.9 percent, and the participation rate between 54 and 54.9 percent. Across genders, however these rates are rather different: The male participation rate was 61.7 percent, while only 47.8 percent of the females were active in the labour market (shown in Table 2.). The employment rate shows a similar pattern across genders: it was 57.4 percent across males and only 44.2 percent across females. This difference of 13 percentage points in the male and female employment rates is not unusual: in the EU it was 15.2 percent among the population aged 15–64 (Eurostat).

**Table 2: Economic Activity in 2005 by Gender**

	Men			Women		
	Emp. Rate	UE rate	Part. rate	Emp. Rate	UE rate	Part. rate
Total	57.4	7.0	61.7	44.2	7.5	47.8
Q1	56.8	7.0	61.1	44.0	7.3	47.5
Q2	57.2	6.9	61.5	44.1	7.4	47.7
Q3	57.9	6.9	62.2	44.4	7.7	48.1
Q4	57.7	7.1	62.2	44.3	7.6	48.0

Source: *Hungarian Statistical Office* Statdat system. The figures refer to population 15–74 years old.

Of the employed, about 70 percent were employees (2,729 thousand) and the remaining 30 percent self-employed (1,172.5 thousand). The proportion of public sector employees in all employees was 29.5 percent.

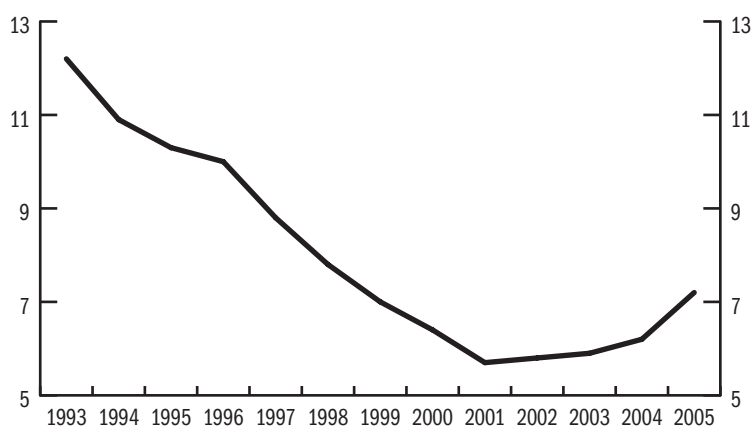
Net job creation had opposing trends in the corporate and public sector. Between 2004 and 2005, the number of corporate jobs increased by 4,200. On the contrary, the number of public jobs declined by 10,700, which shows that the number of employees declined in the whole economy by 6,500.<sup>3</sup> Therefore, the number of self-employed must have increased by 7,600 in order to reach the figure of 1,100 jobs created in the economy.

Job creation and destruction also varied among industries. The largest proportion of net job destruction took place in agriculture, industry (2.9 percent in each) and health and social services (2.3 percent). The sectors with the highest increase in the number of employees were financial intermediation (5 percent) and real estate and business services (7.4 percent), while the number of employees in the other sectors of the economy was quite stable.<sup>4</sup>

### 3. TRENDS IN UNEMPLOYMENT

The most important change over the last several years concerned the unemployment rate, which, after a steady decline from its highest level of 12.1 percent in 1993 reached a low of 5.7 percent in 2001, as Figure 1 shows. After 2001 it started to climb slowly until 2004, increasing during this three year period by only less than half a percentage point. The year of 2005, however, added more than one percentage point to the unemployment rate, reaching 7.2 percent. While the Hungarian unemployment rate is still smaller than the average EU 25 rate of 7.8 percent in 2005, its trend is of concern together with the fact that unemployment increased during a period when the economy was growing quite quickly.<sup>5</sup>

Figure 1: Unemployment Rate, 1993–2005



Source: *Hungarian Statistical Office* Statdat system.

Table 2. shows the unemployment rate by gender for 2005, totals and by quarter. The unemployment rate is 7 percent among men, and half a percentage

<sup>3</sup> The average number of public sector jobs increased in 2002 by approximately 18,000, then it started to decline in the following year, but at a very small pace (2,000 jobs).

<sup>4</sup> These figures exclude the self-employed.

<sup>5</sup> The latest data reveal that the unemployment rate continued to increase, reaching 7.8 percent in February 2006.

point higher among women. Quarterly data reveal that men’s unemployment rate was stable over 2005, but women’s increased by 0.3 percentage points.

In addition to the 304 thousand unemployed the number of discouraged workers (those who do not work and are available but do not search) is also rather high at 110.8 thousand. As in most countries, these people are categorized in Hungary as inactive, as the search criteria is not satisfied and thus they cannot be considered unemployed. The Bureau of Labour Statistics (BLS), however, regularly publishes “measures of labour under-utilization.”<sup>6</sup> One of these measures includes discouraged workers as unemployed. Had the Hungarian statistics categorized these people as unemployed, the unemployment rate would have been boosted to 9.6 percent.<sup>7</sup>

One important feature of unemployment is its duration. While short term unemployment can be attributed to job search – and it may well have a disciplinary role – long term unemployment is detrimental for several reasons: people may get discouraged and stop actively looking for a job, their skills may deteriorate or even become obsolete over long spells, and stigmatization can also be associated with long term unemployment. The structure of unemployment duration did not change much between 2004 and 2005 as Table 3. shows. The proportion of people looking for a job for over one year actually increased slightly (from 40 percent to 41.6 percent) and the proportion of shorter spells declined somewhat.

**Table 3: Length of Job Search of Unemployed in 2004 and 2005**

UE. spell	2004		2005	
	Thousands	Percent	Thousands	Percent
< 1 month	13.0	5.2	14.8	5.0
1-3 months	42.0	16.8	48.9	16.5
4-6 months	39.9	15.9	44.1	14.9
7-12 months	55.3	22.1	65.4	22.1
13-18 months	33.4	13.3	41.0	13.9
19-24 months	19.6	7.8	27.4	9.3
> 25 months	47.2	18.8	54.3	18.4
Total	250.4	100.0	295.9	100.0

Source: *Hungarian Statistical Office* (2005, 2006). The figures refer to population aged 15–74. Unemployment spell is measured in months. Unemployed who start working in 90 days are excluded.

<sup>6</sup> The Bureau of Labour Statistics is the main agency of the US Federal Government that collects statistics on American employment.

<sup>7</sup> The number of discouraged workers was as high as 117.6 thousand in 2002, the following year it declined to 100 thousand, and in the last two years it was at around 110 thousand.

Who are the unemployed and which demographic category suffered from its increase in 2005? Table 4. presents the unemployment rates for 2004 and 2005 by gender, education and age. Male and female unemployment rates were equal in 2004, but female unemployment increased by half a percentage point more than male unemployment. Among education groups, those with at most 8 classes experienced the sharpest increase in the number of unemployed: this group’s unemployment rate rose from 12.3 to 15.6 percent in a

year. Among those with vocational training, the unemployment rate was half a percentage points higher in 2005 than in 2004 (it rose from 6.9 to 7.4 percent), while high school graduates' unemployment rate increased only slightly, from 4.7 to 4.9 percent. Among the population with a higher education, the unemployment rate did not change but remained at 2.3 percent.

**Table 4: Unemployment Rates by Gender, Education, Age and Region, 2004, 2005**

	2004	2005	Change
Total	6.1	7.2	1.1
<b>Gender</b>			
Men	6.1	7.0	0.9
Women	6.1	7.5	1.4
<b>Education</b>			
≤ 8 classes	12.3	15.6	3.3
Vocational	6.9	7.4	0.5
High school	4.7	4.9	0.2
University	2.3	2.3	0.0
<b>Age</b>			
15–19	34.9	37.8	2.9
20–24	13.4	17.5	4.1
25–29	6.5	8.2	1.7
30–39	6.0	6.8	0.8
40–49	5.0	5.7	0.7
50–59	3.9	4.8	0.9
<b>Region</b>			
Central Hungary	4.5	5.2	0.7
Central Transdanubia	5.6	6.3	0.7
Western Transdanubia	4.6	5.9	1.3
Southern Transdanubia	7.3	8.8	1.5
Northern Hungary	9.7	10.6	0.9
Northern Great Plain	7.2	9.1	1.9
Southern Great Plain	6.3	8.2	1.9

Source: *Hungarian Statistical Office* (2005, 2006). The figures on gender education and region refer to population aged 15–74.

The distribution of the unemployment rate by age group shows that unemployment increased the most among the population aged 20–24 (from 13.4 to 17.5 percent, or by 4.1 percentage points). The second largest increase was experienced by the youngest cohorts (15–19 years old), among whom the unemployment rate increased by 2.9 percentage points, from 34.9 to 37.8 percent. Among people 25–29 years old the increase was of 1.7 percent (from 6.5 to 8.2 percent). Among older cohorts the unemployment rate increased by 0.7–0.9 percent.

Finally, we investigate changes in regional unemployment rates. The largest increase between 2004 and 2005 did not always take place in already high unemployment regions. The two regions comprising the East of the country

(the Northern and the Southern Great Plain) experienced the largest increase of almost two percentage points. The second group – Western and Southern Transdanubia – had an increase of 1.3 and 1.4 percent, respectively. The central part of the country (comprising Central and Northern Hungary and Central Transdanubia) had an increase of less than one percent. It is worth noting that although Northern Hungary had the largest unemployment rate both in 2004 and 2005, the change in its regional rate is not high.

To summarize, the 1.1 percentage point increase in the unemployment rate was not distributed equally among demographic groups. Groups traditionally considered as disadvantaged – females, those at the bottom of the skill ladder and young workers, among them many new entrants to the labour market – had a disproportionately greater chance to become unemployed during 2005. Already high unemployment regions were not hit more by the increase than those which had a relatively low unemployment rate.

What can the reasons be for the increase in unemployment while the Hungarian economy was growing by over 4 percent? Without a thorough analysis one can only speculate, and there are several possibilities. On the demand side it is possible that some form of skill biased technological change took place, as the economic growth was accompanied by an increase in the volume of the investment. This is supported by the fact that unemployment increased mostly among the young and uneducated. Second, it is possible that despite the overall growth of the economy, industries traditionally employing low skilled workers shrank. There is some evidence for this hypothesis: in agriculture about 11 thousand jobs were destroyed, another 10 thousand in transport, storage and communication, and 24 thousand jobs in industry (*Hungarian Statistical Office* 2006). Other sectors which also employ low-skilled workers grew, however. In trade and reparations 40 thousand jobs were created, and in hotels and restaurants another five thousand.

On the supply side economic growth could motivate people to switch from inactivity to unemployment if they believed that more jobs are available now than in the past or if they decided to start searching for some other reason. A piece of regulatory change in 2004 could also increase the willingness to start searching (Law 123/2004). If an employer hires an unemployed elderly person or somebody who has recently been on maternity leave, he can benefit by a reduction of up to 50 percent of the social security payment. If the disadvantaged inactive believe that this tax reduction made it more likely for them to get a job, they might start actively searching and thus become unemployed.

The data support these hypotheses to some extent: between 2004 and 2005 the number of inactive persons declined by 50.8 thousand, while the number of unemployed increased by the same amount (see Table 1.). Discouraged workers, however, are the group most susceptible to become active (start to search) if they believe it is worthwhile doing so. Thus, the number



of discouraged workers should also decrease if the increasing unemployment rate is due to supply side factors. But we do not observe this in the data. Actually, the number of discouraged workers increased slightly between 2004 and 2005, from 109.2 to 110.8 thousand. In conclusion, there is probably no simple story behind the increase in the unemployment rate. More could be said about its causes only by looking at the number of people transiting across types of labour force status.

In conclusion, labour force activity and employment did not change much during 2005. The unemployment rate, however, after a steady decline between 1993 and 2001, and a small increase between 2001 and 2004, grew quite substantially, by over one percentage point. This growth was disproportionately distributed in the population, affecting mostly women, the young and the uneducated. The increase in unemployment is also worrying because the economy was on a growth path during this period. I have outlined several factors that could have had a role in the growing unemployment, but to choose among them a more elaborate analysis is necessary.

#### 4. WAGES

The average gross wage of full time employees in 2005 was HUF 158 thousands, which represents an 8.8 percent increase compared to the previous year, as Table 5. documents.<sup>8</sup> The real wage increase was 5 percent (deflating with the consumer price index [CPI] = 103.6 percent). The average net wage was equal to HUF 103 thousand, 10 percent higher in nominal terms than in 2004. The real net wage increase was 6.2 percent. The 1.2 percent difference between the gross and net wage increase indicates a small decline on the tax burden of the average wage.

**Table 5: Average Earnings of Full-Time Employees**

	Total		Corporate		Public	
	Level	Percent Change	Level	Percent change	Level	Percent change
<b>Gross Earnings</b>						
Total	158,315	108.8	148,520	106.9	182,172	112.8
Blue Collar	102,668	106.9	102,651	106.0	103,737	112.4
White Collar	222,768	109.6	238,213	107.1	207,981	112.7
<b>Net Earnings</b>						
Total	103,134	110.1	98,421	108.4	114,583	113.7
Blue Collar	76,016	108.3	75,981	107.6	77,217	112.7
White Collar	134,544	111.0	142,477	108.7	126,879	113.8

Source: *Hungarian Statistical Office* Statdat database. Earnings are expressed in current HUF. Percent change refers to values in the previous year.

The gross (net) average wage of blue collar workers was HUF 103 thousand (76 thousand) and of white collar workers 223 thousand (135 thousand). The

<sup>8</sup> The HUF/Euro average exchange rate was 248.05 in 2005, hence the average real wage was Euro 638.

nominal gross wages of blue collar workers increased by 6.9 percent (the net by 8.3 percent), whilst that of the white collar workers by 9.6 percent (the net by 11 percent). The increase in the skill premium indicates that the gap between lower and better educated people further increased during 2005.

The dynamics of wages was very different for the corporate and public sectors. While gross wages in the first increased by 6.9 percent and net wages by 8.4 percent, public sector employees enjoyed an increase of gross 112.8, and net 113.7 percent. Looking at the corporate sector only, the wage dynamics of blue and white collar workers is very similar: the difference between the growth rates is only about 1 percent (for the benefit of white collar workers). In the public sector the change in the skill premium is also 1 percent. Overall, the figures show that the large rise in skill premium measured in the overall economy masks a public sector wage premium increase.

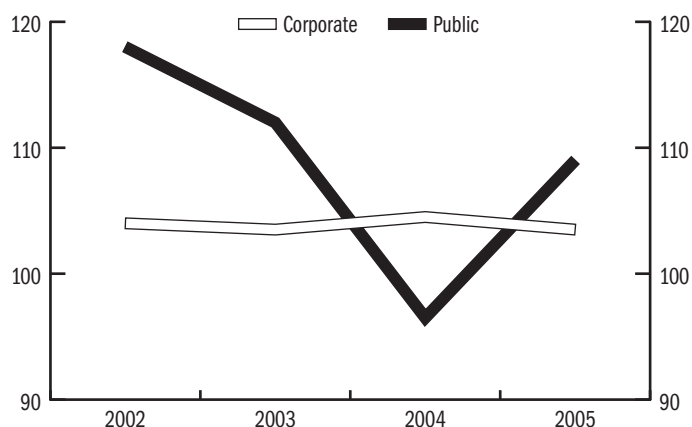
Different wage dynamics in the public and corporate sector are not surprising in the light of the earlier years' developments, and taking into consideration the fact that the driving forces changing wages in the two sectors are very different: market forces in the corporate sector, and political considerations in the public sector. Figure 2, which presents the annual change of average real wages in the corporate and public sector, documents the diverse behaviour of the two sector's wages. In the corporate sector wages grew each year by between 3 and 4.5 percent. In the public sector, however, one can track rather large changes in the wage dynamics. Between 2001 and 2002, real wages in the public sector increased by 18 percent, which was the consequence of the increase of all public sector employees by 50 percent. The following year, average wages increased by 12 percent (still showing the effect of the same policy).<sup>9</sup> In 2004, probably under the pressure of a high budget deficit, the government started to inflate away wages, which had the effect of a 4 percent wage decline in the public sector. Finally, in 2005, in the pre-election year, wages again increased significantly, by nine percent in real terms.

Table 6. shows the level of wages by industry, as well as their relative level (compared to the average wage at the national level) and the change in the wage compared to the previous year. The lowest paid industries were hotels and restaurants, agriculture, hunting, forestry and construction, in which only 60.5, 64.9 and 67.3 percent of the average wage was paid, respectively. Workers in trade were also paid well below the national average (82.6 percent). Industries close to the national average, but still not reaching it are health, other services and industry (91, 93.5 and 95.5 percent). It is worth mentioning that mining and energy, which are parts of industry, are paid better than the national average; wages in these sectors are 6.3 and 31.3 percent higher than in the whole economy. Taken together with the industry average, it shows that the average employee in manufacturing was paid less than the average industrial employee. Sectors close to the national average but higher than it are real

9 For an analysis of the public sector wage premium following the increase, see *Telegdy (2005)*. Public sector wages were raised in September 2002, and because in Figure 2 average wages are presented, a part of the wage increase is shown between 2002 and 2003.

estate and business services (102.3 percent) and transport and postal services (107.2 percent). Finally, the best paid sectors are education with salaries 15 percent higher than the average, financial intermediation (21 percent) and public administration, defence and social security (31 percent).<sup>10</sup>

**Figure 2: Change in the Real Wage in the Public and Corporate Sector**



Source: *Hungarian Statistical Office*, Statdat database. Annual changes, expressed in percent. Nominal wages are deflated with the CPI.

**Table 6: Industrial Distribution of the Level and Change of the Real Average Gross Wage, 2005**

	Level	Relative level	Change
Agriculture, hunting, forestry	102,796	64.9	102.3
Industry, of which	151,241	95.5	103.5
Mining	168,365	106.3	100.2
Energy, water distribution	208,383	131.6	104.5
Construction	106,566	67.3	102.9
Trade	130,698	82.6	103.2
Hotels, restaurants	95,773	60.5	102.6
Transportation, postal services	169,748	107.2	103.9
Financial intermediation	350,536	221.4	104.3
Real estate, business services	161,912	102.3	101.3
Public admin., defence, social security	207,287	130.9	108.6
Education	181,448	114.6	109.6
Health	144,023	91.0	106.6
Other services	148,020	93.5	103.8
Total	158,315	100.0	105.0

Source: *Hungarian Statistical Office* Statdat database. The figures refer to full time employees.

Table 6. also shows the percentage change of the real wage compared to the previous year within each industry, and several general patterns can be drawn.

<sup>10</sup> Needless to say, these figures do not control for the quality of the workforce in the industry, and thus reflect – at least partially – the proportion of high-skilled workforce in the given industry.

First, in neither industry can one capture a wage decline. Secondly, in most industries the average wage increased less than the economy-level wage (between 2 and 4.5 percent), the exceptions being health, public administration and education. In these sectors the increase was 6.6, 8.6 and 9.6 percent, respectively. As economic units in these industries belong to the public sector to a very large extent, a high wage increase in them shows the political motivations of increasing public sector employees' wages, as discussed above.

To summarize, during 2005 nominal gross wages increased in the Hungarian economy by 8.8 percent and net wages by 10 percent. Deflation by the CPI shows that real net wages increased by 6.2 percent on average. White collar workers' wage increased by a higher proportion than that of the blue collar workers', but a closer investigation of the sectoral wage differences show that the driving force of these different dynamics was not a skill premium formed by competitive forces, but a greater increase of wages in the public sector than in corporations. As the public sector operates mostly in industries that employ a higher proportion of skilled workers, the greater public sector wage premium pushed up the average high wage of university graduates.

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