

Hungary is the most corrupt Member State of the European Union

**Corruption Perceptions Index results and the corruption
situation in 2022**

Transparency International Hungary report

Budapest, 2023

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Executive summary

For the 28th time, the Berlin-based Secretariat of Transparency International (TI) has compiled the Corruption Perception Index, which ranks the countries of the world based on their exposure to corruption in the public sector (Corruption Perceptions Index - CPI) as rated by business people and experts. In 2022, Hungary scored 42 points on a scale from 0 (most corrupt) to 100 (least corrupt), ranking 77th out of 180 countries, down 1 point and 4 places from a year earlier. This can be considered a medium performance globally, but within the European Union, Hungary has slipped to the last place.

Hungary's results are significantly lower than those of the countries that are considered our direct regional competitors. Czechia and Slovenia, together with other European countries, reached 41st place with 56 points. Poland ranked 45th with 55 points, Slovakia 49th with 53 points, and Croatia 57th with 50 points in TI's corruption ranking. The two countries with which Hungary was tied for last place in the European Union in the 2020 CPI ranking have moved up somewhat: Romania is 63rd with 46 points and Bulgaria is 72nd with 43 points in the 2022 Corruption Perceptions Index.

Hungary's bottom position in the European Union is the culmination of a process that has been going on for more than a decade, involving the erosion of the rule of law, state capture, and the development of systemic corruption. While in 2012 Hungary was ranked 19th in the then EU-27, its performance deteriorated in a trend-like fashion, and in 2019 and then in 2021, only Bulgaria ranked lower. (In 2020, there was a three-way tie for last place between Hungary, Romania, and Bulgaria). By 2022, Hungary lost the minimal lead it had a year earlier after Bulgaria improved its position somewhat and Hungary lost ground.

In parallel to the presentation of the Corruption Perception Index, Transparency International Hungary (TI Hungary) published its annual report on corruption, which comprehensively analyzes the state of the rule of law, public procurement, and the use of EU funds, as well as the impact of corruption on economic performance.

One of the most significant developments in 2022 is that for the first time in the history of the EU, the European Commission has launched a rule of law procedure against Hungary after the parliamentary elections in April, tying the availability of EU funds to conditions - says the Rule of Law section of the report. This indicates that, after a decade, a change of attitude has taken place in the European Union, and neither the EU institutions nor the key Member States are standing idly by as infringements and systemic corruption are occurring in some Member States - primarily in Hungary and Poland.

As of January 2023, under the rule of law mechanism, Hungary will not have access to 55 percent of the funds from the three operational programs for the 2021-2027 budget cycle, i.e., EUR 6.3 billion (about HUF 2,500 billion, almost 30 percent of the total cohesion funding), until it meets the 17 conditions ("milestones") set by the European Commission. The EU also tied the de-blocking of EUR 5.8 billion (approximately HUF 2,300 billion) in direct grant from the Recovery Fund (RRF) to 10 additional requirements, mainly related to the independence of the judiciary. Thus, Hungary has to meet a total of 27 so-called "super-conditions". The latest information suggests that the Commission is gradually raising the stakes: in addition to the requirements known so far, the enforcement of the values set out in the Charter of Fundamental Rights of the European Union is also a prerequisite for obtaining cohesion funds. Due to the long lead time of the survey, the impact of the government measures to free up EU funds is not yet reflected in the latest CPI results just published.

The report details some of these anti-corruption measures. The analysis covers the Integrity Authority, changes in the freedom of information and the asset declaration system, the review of the functioning of public interest asset management foundations carrying out public duties (KEKVA), and the provisions on private prosecution in corruption cases. The report concludes that the steps taken under EU pressure and designed to curb the misuse of EU funds can be considered the only serious anti-corruption measures of the NER (System of National Cooperation) period, although the government's real aim is to obtain funds, not to restore the rule of law. According to TI Hungary, the package is not even suitable for the latter, since corruption permeates the state structure and abuses have become part of the system. State capture was already complete by the middle of the previous decade. Nevertheless, if the Commission rigorously monitors the implementation of the new rules, misuse of EU funds can be expected to decrease in the future, but the institutional destruction of the last decade will not be undone and the rule of law will not be restored "in one fell swoop".

As for the Integrity Authority, the report states that its powers are undersized. For example, it cannot launch investigations, it cannot be a party to legal proceedings, and in general, if it detects any kind of irregularity, it cannot act on its own, but is forced to refer them to the competent authority. It has somewhat stronger powers concerning public procurement processes, as it can suspend a specific procurement procedure if it suspects an infringement. It can also investigate asset declarations, but it has no power to sanction the irregularities detected, nor can it force other authorities to do their job. The Integrity Authority is therefore likely to be (and will be) reliant on the willingness of other authorities to cooperate, and its effectiveness will primarily depend on the extent to which it is able or willing to engage in conflict with the captured institutions of the state and the government itself to break systemic corruption and curb corrupt practices. Much will therefore depend on the commitment of the Authority's leadership and apparatus, and whether they are ready to distance themselves from the government in their role - taking advantage of the Authority's reporting obligation to the EU - or whether they operate as a de facto government body.

TI Hungary – along with several other independent organizations fighting corruption, such as K-Monitor and Atlatszo.hu – applied for and was selected as a member of the Anti-Corruption Task Force, consisting of 10 government representatives and 10 civil society members and working alongside the Integrity Authority (but not part of it). TI Hungary reiterates that its participation is subject to predetermined conditions, and it will remain a member of the Task Force only as long as there is a chance for meaningful work.

Regarding public procurement and the use of EU funds, the report notes that the mitigation of risks related to public procurement is a central element of the negotiations between the European Union and the Hungarian government to obtain EU funds. In Hungary, the economic weight of public procurement remains significant, while the public procurement market is highly exposed to corruption. The total value of public procurement procedures in 2022 amounted to HUF 4,590 billion, an increase of 9 percent compared to the previous year, and well above the values of the years before the coronavirus epidemic.

According to data from the Public Procurement Authority, while in the first three quarters of 2022, there was a 48 percent increase in prices compared to the same period of the previous year, by the end of the year purchases were cut back so much that only a 6 percent price increase could be detected

for the full year in terms of the average price of individual purchases. At the same time, compared to the period before the epidemic (2019), the average amount of public procurement procedures increased by 67 percent, reflecting the severe overpricing of public procurement in addition to inflation.

The European Commission has made several findings on the irregularities in public procurement in Hungary. The Commission has repeatedly drawn attention to the high rate of single-bid public procurement, which reduces the intensity of competition in the public procurement market and therefore poses a significant risk of corruption. Although the rate of single-bid public procurement is decreasing, at 35 percent (for procurements above the EU threshold) it remains well above the EU target of 15 percent. (Hungary promised to reduce the proportion of single-bid procedures as part of the anti-corruption package.) The competitive conditions for obtaining public contracts are further worsened by the fact that the most important procurements are regularly exempted by the government from traditional public procurement procedures, for example on the pretext of the coronavirus epidemic, or for reasons of national security. Last year was no exception: concessions launched in previous years that went against EU legislation were closed, usually with winners close to the government (for example, two concessions for waste management and the operation of freeways, both for 35 years).

In the new funding period that started in 2021, not a single euro has been received so far due to the suspension of the funding. Nevertheless, the distribution of funds has already started in 2021. According to data from the government's tender portal, 193 tenders received non-reimbursable grants of about HUF 528 billion by the end of 2022 - approximately 20 percent of total funding – from the Recovery Fund launched in the meantime. Most of the money has already been paid out to the applicants. However, for the time being, all of this is financed by the Hungarian budget, i.e., the taxpayers, and it is questionable whether the Commission will ever accept these invoices.

Looking at the longer-term trends in the utilization of EU funds, it appears that although Hungary has been one of the largest beneficiaries of the EU budget, the inflow of money has not contributed to increased efficiency or economic prosperity measured by the growing number of businesses, and inequalities have not decreased, while corruption has increased.

The economic chapter of the report concludes that in 2022, as in previous years, the correlation between economic performance as measured by Gross Domestic Product (GDP) per capita and the anti-corruption performance as measured by the Corruption Perception Index score remains strong in the European Union. It is true that the regression coefficient of 0.81, which indicates the strength of the relationship, is slightly lower than in 2020 and 2021 (0.83 in the previous two years). Hungary is stuck in the EU's lower house of corruption-ridden Member States with low national income by EU standards, even though it experienced strong economic growth in the seven years preceding the coronavirus epidemic (averaging more than 4 percent per year). According to data from the International Monetary Fund (IMF), GDP per capita increased from USD 13,666 in 2013 to USD 18,983 in 2022, an overall increase of no less than 39 percent. As mentioned above, the CPI for 2022 shows Hungary as the most corrupt country in the EU, while in terms of GDP per capita, Hungary has outperformed only three EU countries (Bulgaria, Romania, Croatia) and it is essentially on par with Poland.

The report also draws attention to the fact that, despite the destruction of the rule of law and systemic corruption, the Hungarian economy has seen intense investment activity since 2016, not only in public but also in private investments as well (the investment paradox). This is explained by several interrelated factors. First, the concentrated public procurement market, as well as the generous state support for crony companies and oligarchs trickle down later as private investments through the various reinvestments by these government-loyal actors. Second, inflation has consistently exceeded the base rate of the central bank after 2016, so the abundance of resources caused by the negative real interest rate has helped investments. Third, the systemic overpricing of public procurement and EU resource allocation improves investment and growth statistics. Fourth, since the second half of the

last decade, a significant number of economic actors have accommodated the disruption of the rule of law and systemic corruption, accepting it as a kind of "new normal".

World Map of Corruption

1.1. Hungary's place in the corruption ranking

For the 28th time, Transparency International's Berlin-based Secretariat has published the Corruption Perceptions Index (CPI¹), which ranks countries according to their level of protection against corruption in the public sector.

Hungary scored 42 points on a scale from 0 (most corrupt) to 100 (least corrupt) in 2022, ranking 77th out of 180 countries, down 1 point and 4 places from a year earlier. In 2012, Hungary was ranked 46th with 55 points. Since then, Hungary's score on the Corruption Perceptions Index has steadily declined by 13 points, and the country has dropped 31 places in the global corruption ranking. No other country's ranking has fallen so much in the last decade. The Hungarian government's anti-corruption record is increasingly poor, and this is particularly striking when compared to the European Union, as in 2022 Hungary was the most corrupt Member State in the EU.

According to the CPI, Hungary ranks globally on a par with Kuwait, Burkina Faso, Solomon Islands, Timor-Leste, Trinidad and Tobago, and Vietnam in terms of corruption severity, as these countries, like Hungary, scored 42 on the Corruption Perceptions Index in 2022. Mechanical comparisons of the anti-corruption performance of countries that differ significantly in social, economic, or even cultural terms can be misleading, as expectations of the countries' ability to resist corruption can differ significantly. It is therefore more important to look at longer-term trends and to compare the anti-corruption performance of countries with comparable institutional arrangements and cultural specificities, rather than year-on-year comparisons using just a single score. A comparison of the EU Member States fully satisfies these requirements.

¹ The Corruption Perceptions Index (CPI) is prepared by the Secretariat of Transparency International (TI) in Berlin based on 13 surveys and analyses performed by 12 organizations. They measure corruption in the public sector by surveying the opinion of experts and businessmen on the corruption exposure of the public institutional system, the economy, and society. Corresponding data were available on 180 countries in 2022, and Hungary was assessed based on 10 different subfactors. TI defines the scores of the subfactors on a scale from 0 to 100, where 0 marks highly corrupt countries and 100 those least affected. The secretariat of TI in Berlin calculates the index by weighting the average of the scores. In the Corruption Perceptions Index, a score of "0" indicates the most corrupt country, and a score of "100" indicates the least corrupt country (for a detailed description of the CPI methodology, see www.transparency.org/research/cpi/overview). The CPI is based on a compilation of surveys and research from the African Development Bank Country Policy and Institutional Assessment, Bertelsmann Foundation Sustainable Governance Index, Bertelsmann Foundation Transformation Index, Economist Intelligence Unit Country Ratings, Freedom House Nations in Transit, Global Insights Country Risk Ratings, IMD World Competitiveness Yearbook, Political and Economic Risk Consultancy Asian Intelligence, Political Risk Services International Country Risk Guide, Varieties of Democracy (VDEM) Project, World Bank Country Policy and Institutional Assessment, World Economic Forum Executive Opinion Survey (EOS), World Justice Project Rule of Law Index. The 2022 Corruption Perceptions Index data for Hungary is compiled from ten different surveys, excluding data from the African Development Bank Country Policy and Institutional Assessment and the World Bank Africa Country Policy and Institutional Assessment, and the Political and Economic Risk Consultancy Asian Intelligence surveys for obvious reasons. Hungary is assessed by all sub-indices of the Corruption Perceptions Index that are relevant to Europe. The CPI survey covered on average 50-80 countries in the years 1995-2000, 100-130 countries between 2001-2005, and 160-180 countries between 2006 - 2016. Since 2017, the number of countries surveyed has been 180 every year. Hungary has been included in the CPI survey every year since 1995. Transparency International's Secretariat in Berlin has calculated Hungary's CPI score based on data from 10 surveys every year since 2017. The survey has been criticized from time to time, and in response, Transparency International asked the European Commission for a credibility (robustness) test in 2018. The Joint Research Center (a background institution of the Commission) has audited the CPI and found it to be a suitable tool for measuring corruption (the report is available at https://www.transparency.org/files/content/pages/2018_CPI_2017_StatisticalAssessment.pdf).

Table 1: Corruption Perceptions Index scores in the European Union, 2022

Placement within the EU	Country	Score		Placement within the EU	Country	Score	
1.	Denmark	90	↑	15.	Latvia	59	=
2.	Finland	87	↓	16.	Czechia	56	↑
3.	Sweden	83	↓		Italy	56	=
4.	Netherlands	80	↓		Slovenia	56	↓
5.	Germany	79	↓	19.	Poland	55	↓
6.	Ireland	77	↑	20.	Slovakia	53	↑
	Luxembourg	77	↓	21.	Cyprus	52	↓
8.	Estonia	74	=		Greece	52	↑
9.	Belgium	73	=	23.	Malta	51	↓
10.	France	72	↑	24.	Croatia	50	↑
11.	Austria	71	↓	25.	Romania	46	↑
12.	Lithuania	62	↑	26.	Bulgaria	43	↑
	Portugal	62	=	27.	Hungary	42	↓
14.	Spain	60	↓				

Source: TI Hungary calculations based on the Corruption Perceptions Index 2022. The column showing the ranking of countries shows the ranking within the European Union, not the global ranking, and the arrows indicate the direction of change relative to the country's score in the Corruption Perceptions Index in 2021.

As shown in Table 1, Hungary was the most corrupt Member State in the European Union in 2022. Although this is not the first time that Hungary finished last place in the EU, it has never been the sole country at the bottom position, i.e., not in a tie with any other Member States.

The country's performance against corruption has steadily deteriorated over the past decade. In 2012, Hungary was the 19th most corrupt member of the then 27-member European Union. By 2017, Hungary had fallen from this rather weak position to 26th-27th place (in a tie) in the now EU-28, only ahead of Bulgaria.² Although 2018 saw a slight improvement in the ranking - with a gain of 1 point, it managed to get ahead of Greece, which temporarily dropped significantly - in 2019, once again, only

² Transparency International Hungary: *A Korrupció Értékelési Index 2017-ben – Korrupció, jogállamiság és gazdasági teljesítmény Magyarországon, nemzetközi összehasonlításban [The Corruption Perceptions Index 2017 - Corruption, rule of law and economic performance in Hungary in international comparison]* (available at https://transparency.hu/wp-content/uploads/2018/12/CPI_2017_narrativ_final_final.pdf)

Bulgaria ranked lower.³ Hungary⁴ tied with Bulgaria and Romania for the last place in the EU ranking in 2020, but lagged behind Romania in 2021, after the latter improved its score by 1 point. Last year, Hungary's ranking dropped even further, as even Bulgaria, which improved its resistance to corruption by 1 point, overtook us in 2022.

Hungary has been ranked the second most corrupt Member State in the European Union three times in the last eleven years - in 2017, 2019, and 2021 - and last year, for the second time after the year 2020, Hungary finished in last place, this time not sharing this position with any other Member State.

The Hungarian government's weakening anti-corruption record is particularly striking when compared to the performance of Central and Eastern European countries. In terms of anti-corruption performance, the former Socialist bloc has split in two. At the forefront of the region are the Baltic States, having improved their credibility in the fight against corruption virtually uninterruptedly: Estonia and Latvia increased their Corruption Perceptions Index scores by 10 points each, and Lithuania by 8 points over ten years. While Estonia, which started the decade with a much higher initial score than Hungary, has moved closer to the European and global leaders in the CPI, Hungary, which has been on a steady decline, has fallen back to the level of the Balkans and Eastern Europe. The 9-point gap measured in 2012 in the CPI scores of Estonia, the regional leader, and Hungary, which fought its way down to last place in the EU, has widened to 32 points by 2022. The gap between the two countries' anti-corruption performance has therefore more than tripled in 11 years.

Hungary's severe decline is also clearly visible within the Visegrad Group. In 2022, Hungary finished last in the V4 for the seventh consecutive year. Although Poland's anti-corruption performance deteriorated by 1 point in 2022, Czechia improved by 2 points, and Slovakia improved by 1 point. Together, they are well ahead of Hungary. The newest 1-point drop in Hungary's performance is also a sign that it is moving further away from its direct regional competitors.

Comparing the results, we can conclude that Poland, with a CPI score higher than Hungary's every year, has seen a 3-point drop in performance compared to 2012, but still far outperforms Hungary. Over the same period, Slovakia and Czechia both improved their scores by 7 points. Meanwhile, Hungary's resistance to corruption has fallen by a total of 13 points, showing an uninterrupted deterioration since 2012. This is a very poor result not only regionally, but also globally.

Cyprus, another EU Member State, has fallen even more sharply, by 14 points in a decade in the CPI survey. Unlike Hungary, however, the deterioration in the anti-corruption performance of Cyprus, which started with a score of 66 in 2012 and reached 52 in 2022, is far from a straight line, and the Mediterranean country still finished a full ten points ahead of Hungary in the latest survey.

Table 2 shows the change in the results of Central and Eastern Europe since 2012, Figure 1 shows the regional trend, and Figure 2 shows the comparison of the Visegrad Group.

³ Transparency International Hungary: *Korrupció, gazdasági teljesítmény és jogállamiság Magyarországon – A Korrupció Értékelési Index eredményei 2018-ban* [Corruption, economic performance and rule of law in Hungary - Results of the Corruption Perceptions Index 2018] (available at https://transparency.hu/wp-content/uploads/2019/01/CPI_2018_narrativ_20190128-1.pdf)

⁴ Transparency International Hungary: *Korrupció Magyarországon a koronavírus-járvány árnyékában A Korrupció Értékelési Index eredményei 2020-ban* [Corruption in Hungary in the shadow of the coronavirus epidemic - Corruption Perceptions Index results in 2020] (available at https://transparency.hu/wp-content/uploads/2021/01/TI-Magyarország_CPI-2020_jelentes.pdf)

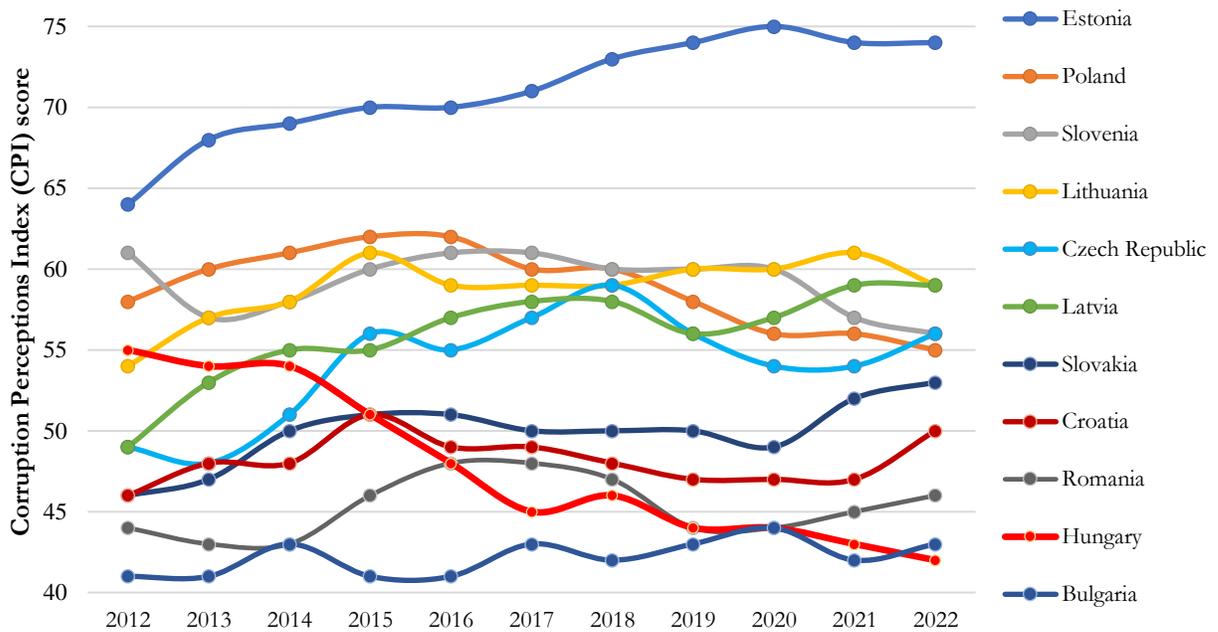
Table 2: Corruption Perception Index scores in Central and Eastern Europe, 2012-2022

Placement within a region	Country	CPI 2012	CPI 2013	CPI 2014	CPI 2015	CPI 2016	CPI 2017	CPI 2018	CPI 2019	CPI 2020	CPI 2021	CPI 2022	Change (2012→2021)
1.	Estonia	64	68	69	70	70	71	73	74	75	74	74	+10 ↑
2.	Lithuania	54	57	58	61	59	59	59	60	60	61	62	+8 ↑
3.	Latvia	49	53	55	55	57	58	58	56	57	59	59	+10 ↑
4.	Slovenia	61	57	58	60	61	61	60	60	60	57	56	-5 ↓
5.	Czech Republic	49	48	51	56	55	57	59	56	54	54	56	+7 ↑
6.	Poland	58	60	61	62	62	60	60	58	56	56	55	-3 ↓
7.	Slovakia	46	47	50	51	51	50	50	50	49	52	53	+7 ↑
8.	Croatia	46	48	48	51	49	49	48	47	47	47	50	+4 ↑
9.	Romania	44	43	43	46	48	48	47	44	44	45	46	+2 ↑
10.	Bulgaria	41	41	43	41	41	43	42	43	44	42	43	+2 ↑
11.	Hungary	55	54	54	51	48	45	46	44	44	43	42	-13 ↓

Source: TI Hungary calculations based on the Corruption Perceptions Index 2012-2022

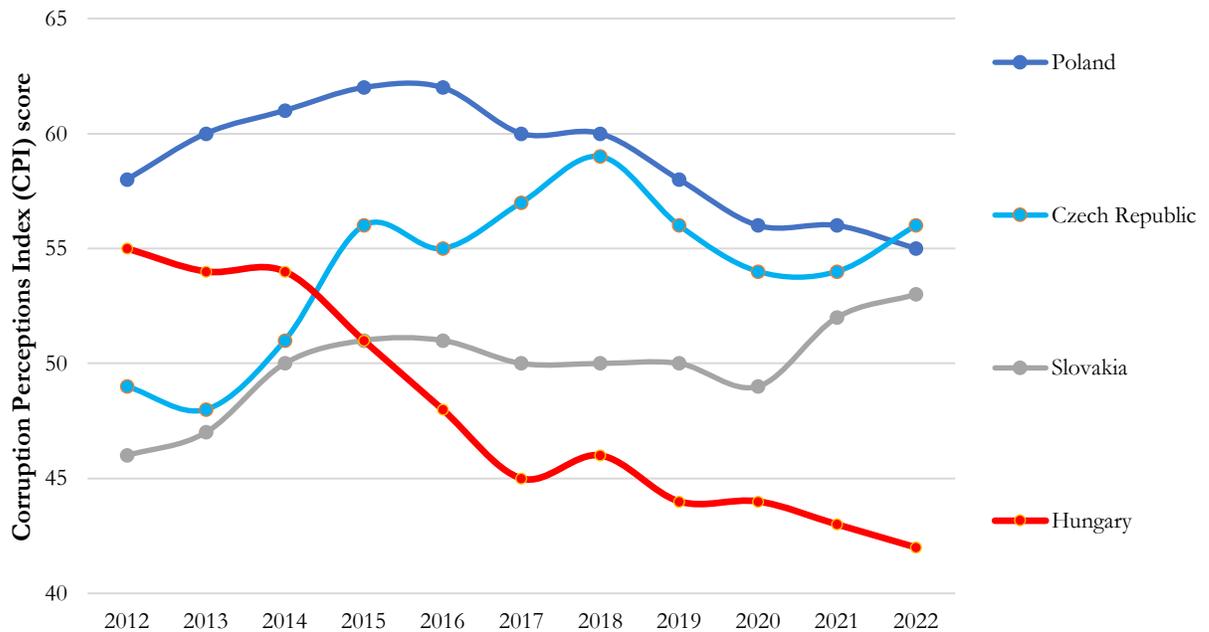
Note: The higher the score, the better the perception of corruption. The number in the last column represents the difference between the country's score in the Corruption Perceptions Index in 2012 and 2022. The ranking in the first column shows the relative - not global - ranking of countries in the region.

Figure 1: CPI scores for Central and Eastern Europe, 2012-2022



Source: TI Hungary calculations based on the Corruption Perceptions Index 2012-2022.

Figure 2: CPI scores for Visegrad Group, 2012-2022



Source: TI Hungary calculations based on the Corruption Perceptions Index 2012-2022.

1.2. Corruption rankings around the world

The countries at the top of the CPI world rankings have been the same for a long time - the Nordic countries, for example, have been at the top every year.⁵ In 2022, Denmark (90), Finland (87), and New Zealand (87) were back on top of the Corruption Perceptions Index, and Norway (84) retained its fourth place. Sweden (83) and Singapore (83) remain in a tie for fifth place, and Switzerland (82), the Netherlands (80), Germany (79), and Ireland (77) were also in the leading group.

Except for Singapore, which is considered a "benevolent dictatorship", the countries at the top of the Corruption Perceptions Index are all well-functioning democracies where impartial state power not only respects the rule of law but also serves the public good in general. In these countries, corruption is mostly successfully curbed, which contributes to their outstanding economic performance in global terms. Of course, corruption is not unknown in top-performing countries, and blatant abuses do occur. The fundamental difference, however, is that in these countries, the corruption that becomes exposed and is a by-product of the system is prosecuted by the judiciary and state authorities.

The G7 countries, which dominate the global economy, are all in the top fifth of the world corruption ranking, except for Italy, which continues to score 56 points. Overall, business people and experts surveyed rate Germany (79), Canada (74), Japan (73), the UK (73), France (72), and the US (69) as rather reliable in their commitment to fight corruption. However, the most economically developed countries do not perform equally well against corruption. For example, the CPI score of Brexit-torn Britain fell by 5 points last year, and even if only by a symbolic 1 point, Germany's score also decreased. By contrast, the United States, which fell by 8 points and 11 places in the Corruption Perceptions Index between 2017 and 2021, scored 69 points in 2022, an improvement of 2 points. Last year, the US ranked 24th in the CPI ranking, three places ahead of the global superpower's 2021 score.

Burundi, Equatorial Guinea, Haiti, North Korea, and Libya, all with 17 points, Yemen with 16, and Venezuela with 14, ranked at the bottom of the CPI in 2022, while South Sudan, Syria, and Somalia shared the last three places, with 13-13 and 12 points respectively. In the CPI's nearly three-decade history, these countries have consistently finished at the bottom of the rankings. Not only is their anti-corruption performance considered glaringly weak, but their political systems are also anarchic or dictatorial, and therefore unable or unwilling to serve the common good.

Also of interest is the ranking of the Hungarian government's decades-long friends to the East, China and Russia, in the world corruption ranking. Russia's score of 28 in last year's Corruption Perceptions Index is 1 point below its already very low score of 2021, giving the country, which launched a war against Ukraine last year, 137th place out of 180 countries surveyed. In contrast, China moved up one place in the corruption ranking in 2022 and is now consistently ahead of Hungary. In 2022, the Far Eastern superpower, which at the beginning of the 2010s was still well behind Hungary with scores between 36 and 40, maintained its CPI score of 45 and moved up to 65th place, twelve places ahead of Hungary (but is still one of the most corrupt countries in the world).

⁵ The numbers in brackets after the names of the countries listed below show their 2022 CPI score. A higher score indicates a lower corruption incidence.

2. On the rule of law in the 13th year of the NER [System of National Cooperation]

2.1. A change in the European Union's policy

Fidesz, led by Viktor Orbán, has won a two-thirds majority in the April 2022 parliamentary elections for the fourth time in a row. In contrast to the stability of the power in Hungary, the external conditions for the government to operate have changed significantly. On the one hand, Russia has launched a war of aggression against Ukraine, and on the other, the European Commission has launched a so-called rule of law mechanism against Hungary immediately after the April elections.

A long-overdue change of attitude has taken place in the European Union, with the EU institutions, after a decade, no longer turning a blind eye to the violations of law and systemic corruption in some Member States – primarily in Hungary and Poland.⁶ The time has come not only for the European Parliament, but also for the European Commission and the decision-makers of key Member States to take a tougher stance against autocracies and hybrid regimes that flout and destroy EU norms. The clearest manifestation of this is the so-called rule of law mechanism, which was adopted at the December 2020 meeting of the European Council after two years of negotiations. As a result, the EU will eventually make cohesion funding conditional on respect for the rule of law: only those Member States that comply with the EU's rule of law standards will be eligible to receive these funds. However, the scope of this mechanism is relatively limited: following the ruling of the Court of Justice of the European Union, the conditionality regulation can only be applied to infringements resulting from corruption involving EU funds, i.e., the impact of the infringements on the EU budget must be demonstrated.⁷

After the decision in December 2020, various legal procedures and a lack of political will delayed the entry into force of the rule of law mechanism for more than a year, before it was activated against the Hungarian government in April 2022, for the first time in the history of the EU.

In addition to the rule of law mechanism, the war that broke out in February has also affected the government's performance on the rule of law and its willingness to address corruption risks. The war, in addition to its overall impact on the political and security situation in the region, including Hungary, also has an impact on the rule of law in Hungary. Indeed, the Orbán administration declared a state of emergency due to the war, just as the coronavirus epidemic - the previous reason for a state of emergency - has subsided, allowing the government to continue to approve measures by decree.⁸

The launching of the rule of law mechanism is an obvious consequence of the public power processes in Hungary since 2010. Fidesz and the administration intertwined with it could therefore only briefly rejoice in the fact that they have had an almost uninterrupted constitutional majority for 13 years, and they already have to face the fact that this time it will not be enough to fake the rule of law for the European Union.

For the time being, the violation of the rule of law has resulted in a minimal permanent loss of funds; and technically, it is not the result of the rule of law mechanism either, but the loss of EUR 1.7 billion from the recovery fund made necessary by the coronavirus crisis (because the European Commission

⁶ József Péter Martin: Csak szemfényvesztés? [An illusion?] *Magyar Narancs*, 12 October 2022 (available at <https://magyarnarancs.hu/publicisztika/csak-szemfenyvesztes-253045>)

⁷ See judgments of the Court of Justice of the European Union in cases C-156/21 and C-157/21.

⁸ See Government Decree 424/2022 (X. 28.).

did not adopt the Hungarian government's Recovery Plan in time), but this is only a fraction of the total available funds.

The vast majority of the EU funding is available in principle, but is conditional. As of January 2023, under the rule of law mechanism, Hungary will not have access to 55 percent of the funds from the three operational programs for the 2021-2027 budget cycle, i.e., EUR 6.3 billion (around HUF 2,500 billion, almost 30 percent of total cohesion funding), until it meets 17 conditions ("milestones") set by the European Commission. And EUR 5.8 billion (around HUF 2,300 billion) in direct grant from the Recovery and Resilience Fund (RRF) is conditional on meeting 27 so-called "super-conditions".

The latest information suggests that the Commission is gradually raising the stakes. A statement issued on 22 December indicates that, in addition to the requirements of the rule of law and the 27 "super-milestones", the implementation of the values set out in the Charter of Fundamental Rights of the European Union is also a prerequisite for obtaining the funds. So from now on, the fate of all cohesion funding available between 2021 and 2027 - nearly EUR 22 billion - will depend on the Hungarian government's willingness to guarantee the rights of asylum seekers and members of the LGBTQ+ community, and restore academic freedom, among other things.⁹

As of January 2023, the suspension, which amounts to at least HUF 4,800 billion, will remain in place until Hungary meets the conditions set by the EU institutions.

2.2. Hungarian government: the goal is money, not the rule of law

Since last summer, the government has made considerable efforts to convince the Commission of its commitment to fight corruption. It has agreed to take action in a total of 17 areas to increase the effectiveness of the fight against corruption and to protect EU funds. Of course, it was already clear in the first, early stages of this process, in 2022, that the government is not even capable of acting democratically to achieve the right and proper goals, such as reducing corruption and at least partially rebuilding the long-destroyed rule of law: laws, drafted and voted on almost by the dozens, have often been submitted to parliament without any input from anyone, such as professional or civil society organizations, or from opposition parties in parliament. Although not considered to be too important in terms of its subject, it deserves special mention that the government even passed the law, which stipulated that in the future ministries that prepare legislation without prior public debate should be fined up to HUF 100 million, without any consultation.¹⁰

By the time the European Council, following the Commission's proposal¹¹, decided¹² to suspend almost HUF 5 billion of funds otherwise available to Hungary in December, it was clear to everyone that the government's aim was not to restore the rule of law but to obtain EU funds. The commitments made to the Commission, although they have some points of progress in terms of reducing corruption, are not sufficient to rebuild democracy and restore the rule of law.

⁹ Press release of the Commission on 22 December 2022: EU Cohesion Policy 2021-2027: Investing in a fair climate and digital transition while strengthening Hungary's administrative capacity, transparency, and *prevention of corruption* (available at https://ec.europa.eu/commission/presscorner/detail/en/ip_22_7801)

¹⁰ See Act XXX of 2022 amending Act CXXXI of 2010 and Government Decree No 567/2022 (23.12.2022).

¹¹ European Commission's Proposal for a COUNCIL IMPLEMENTING DECISION on measures for the protection of the Union budget against breaches of the principles of the rule of law in Hungary, 18.09.2022 (COM(2022) 485 final). The Commission submitted this proposal to the Council on 30 November 2022 (see the Commission's press release at https://ec.europa.eu/commission/presscorner/detail/en/ip_22_7273).

¹² Council Implementing Decision (EU) 2022/2506 of 15 December 2022 on measures for the protection of the Union budget against breaches of the principles of the rule of law in Hungary

While the government tries to mimic the rule of law in Brussels, Hungary is still governed by decree. The spirit of some of the concrete measures it has undertaken on the suggestion of the Commission does not permeate the day-to-day running of the country either, as the government's controversial steps on transparency illustrate. The rule of law mechanism has made the transparency of public funds and public data a priority, and Hungary has introduced several important reforms in this area. Despite these reforms, however, authorities and other organizations using public money conceal information about their operations and use of public funds almost routinely. This is nothing new, of course, but it seems at the very least presumptuous that the government has refused to disclose data on the acquisition of Vodafone's Hungarian subsidiary, for example, originally planned at HUF 715 billion and almost entirely financed by the state, at the very time when it vowed in Brussels to significantly improve the transparency of public spending.¹³ From this point of view, the secrecy of the waste management concession contract with Mol Nyrt. for 35 years is equally problematic, as is the refusal of the state to hand over the details of the procedure for the extension of the operating licenses of casinos in Budapest, also for 35 years. In these cases, TI Hungary has filed lawsuits against the state for access to data of public interest.

2.3. Measures to reduce corruption

As already mentioned, the Court of Justice of the European Union has ruled that the Commission may use the rule of law mechanism primarily to protect the financial interests of the European Union. For this reason, all rule of law conditions imposed on Hungary are aimed at solutions designed in some way to guarantee and control the regularity of the use of EU funds. The conditions can be divided into two groups. On the one hand, the government has undertaken to implement reforms in a total of 17 areas as part of the rule of law mechanism. These 17 commitments included, in addition to improving transparency in public spending and reviewing the public procurement system, commitments resulting in well-known solutions such as the creation of the Integrity Authority, and breaking the Prosecution Service's monopoly on prosecuting corruption cases.

The government undertook these 17 obligations within the framework of the rule of law mechanism to lift the freezing of the cohesion funds available to Hungary. However, this may only be enough to de-block roughly half of the frozen funds, around HUF 2 500 billion in cohesion funding. Hungary could access a further HUF 2300 billion from the Recovery and Resilience Fund. Although not subject to the rule of law mechanism, RRF funds are not automatically available either, but only if the Commission approves the plan prepared by Hungary to mobilize these funds. In the assessment of the plan, the Commission has applied the same criteria as those applied in the rule of law mechanism. Finally, in December 2022, the plan submitted by Hungary was the last of the Member States to be adopted.¹⁴ However, the Commission immediately suspended the disbursement of the funds until the measures set out in the RRF plan, the so-called milestones, were met. More specifically, the Council identified 27 "super-milestones" out of hundreds of milestones, the achievement of which is a precondition for payments.¹⁵ The 27 "super-milestones" are the 17 commitments identified in the rule

¹³ See the Government's announcement of 25 August 2022: *A magyar állam közreműködik a Vodafone Magyarország hazai tulajdonba vételében* [The Hungarian State participates in the purchase of Vodafone Hungary] (<https://kormany.hu/hirek/a-magyar-allam-kozremukodik-a-vodafone-magyarorszag-hazai-tulajdonba-veteleben>) and 4IG Nyrt.'s announcement of 9 January 2023: *Sikeresen zárul a magyar távközlés történetének egyik legjelentősebb tranzakciója* [One of the most significant transactions in the history of Hungarian telecommunications is successfully completed] (<https://www.4ig.hu/sikeresen-zarul-a-magyar-tavkozles-tortenetenek-egyik-legjelentosebb-tranzakcioja>).

¹⁴ Council Implementing Decision on the approval of the assessment of the recovery and resilience plan for Hungary (15447/22)

¹⁵ The 27 "super-milestones" are defined in footnote 9 of the Annex to the Proposal for a Council Implementing Decision on the approval of the assessment of recovery and resilience plan for Hungary (15447/22 ADD 1).

of law mechanism, supplemented by ten additional conditions, mainly concerning the independence of the judiciary.

The 27 milestones include, among others, a commitment to establish the Integrity Authority and an Anti-Corruption Task Force, reform of the rules on access to public data, a significant reduction in the proportion of single-bid sham tenders as part of the many requirements for public procurement, and a review of the regulation of public interest asset management foundations carrying out public duties (KEKVAs). The "super-milestones" also include several conditions to facilitate the functioning of the judiciary free from political interference, as well as the obligation to cooperate with the European Anti-Fraud Office, OLAF, and to strengthen the enforcement of conflict of interest rules in the use of EU funds.

TI Hungary, in cooperation with other civil society organizations, has been closely following the events of the last six months concerning the rule of law values. We first assessed the government's rule of law package in October 2022.¹⁶ Our findings were confirmed less than a month later.¹⁷ More recently, we submitted a shadow report to the Commission's Rule of Law Report, also as part of a coalition of civil society organizations.¹⁸

We conclude that the package, which was put in place under EU pressure to curb the misuse of EU funds, is the most serious anti-corruption package in a decade and a half. These measures, provided the EU institutions rigorously monitor the implementation of the legislation, could reduce the misuse of EU funds in the future. In the short term, however, they will not be able to end state capture or restore the rule of law.

Below we look at the most important of the 27 requirements.

2.3.1. The Integrity Authority

This authority, with its innovative powers and important tasks, could have done a lot to combat corruption, provided it had been set up a decade ago. But the Integrity Authority was launched in 2022, not 2012, and in practice, it is still being organized and won't start working for another six months or so. The learning curve might very well be steep as well. Moreover, the powers of the Integrity Authority are undersized, and it cannot exercise most of them independently. For example, it cannot launch investigations, it cannot be a party to legal proceedings, and in general, if it detects any kind of irregularity, it cannot act on its own, but is forced to refer them to the competent authority. It has somewhat stronger powers concerning public procurement, as it can suspend a specific procurement procedure for up to two months if it suspects an infringement. However, it cannot itself remedy the suspicious circumstance, i.e., it cannot oblige a municipality or state agency that has issued a public procurement notice that appears to be tailor-made to publish a new notice that ensures genuine competition. Although it can investigate such cases, it is not empowered to deal with the irregularities it detects and prevent their recurrence. The same is true in the area of asset declarations,

¹⁶ Hungarian Helsinki Committee - K-Monitor - Transparency International Hungary: *Half-hearted Promises, Disappointing Delivery - An Assessment of the Hungarian Government's New Measures to Protect the EU Budget and Related Recommendations*, 7 October 2022 (available at <https://transparency.hu/wp-content/uploads/2022/10/Assessment-of-measures-to-protect-EU-budget.pdf>)

¹⁷ Hungarian Helsinki Committee - K-Monitor - Transparency International Hungary: *The European Commission should be more intransigent to stop systemic corruption in Hungary - Civil society on Hungary's unfolding anticorruption package*, 17 November 2022 (available at https://transparency.hu/wp-content/uploads/2022/11/HU_17_measures_assessment_17112022.pdf)

¹⁸ *Contribution of Hungarian CSOs to the European Commission's Rule of Law Report*, January 2023 (available at https://transparency.hu/wp-content/uploads/2023/01/HUN_CS0_contribution_EC_RoL_Report_2023.pdf)

where it can also investigate, but has no power to sanction irregularities detected, nor to force other authorities to do their job.

The Integrity Authority is therefore likely to be (and will be) reliant on the willingness of other authorities to cooperate. Although its power is fairly limited, and more akin to those of an ombudsman, its creation is a significant development. Ombudsmen can be important participants of state authority and guarantors of effective legal protection. This depends mainly on their exercising their powers with the wise foresight of the Hungarian ombudsmen of the 1990s. Of course, the Integrity Authority will have a difficult game to play, since the partner authorities on whose willingness to cooperate its own success depends or fails are almost invariably part of the captured institutions of the state. The Public Procurement Authority, the State Audit Office, the Hungarian Competition Authority, the Prosecution Service, the tax authority, and the police, as well as many other state control organizations, have demonstrated over the past decade, to a far greater extent than is acceptable, that they are first and foremost standing in solidarity with the authorities, and only secondarily see their task as that of uncovering the truth and combating abuses. This is unlikely to change.

The effectiveness of the Integrity Authority will therefore be measured primarily by the extent to which it can or is willing to engage in conflict with the captured institutions of the state and the government itself to break systemic corruption and curb corrupt practices.¹⁹ Much will therefore depend on the commitment of the Authority's leadership and apparatus, and whether they are ready to distance themselves from the government in their role - taking advantage of the Authority's reporting obligation to the EU - or whether they operate as a de facto government body.

2.3.2. The Anti-Corruption Task Force

TI Hungary is directly involved in the Anti-Corruption Working Group of the Integrity Authority, as it applied for and was selected as a member together with several other independent organizations fighting corruption, such as K-Monitor and Atlatszo.hu. Our participation is subject to pre-defined conditions, the essence of which is that TI Hungary will remain a member of the Task Force only as long as there is a chance of meaningful work.²⁰ The main tasks include the overall assessment of existing solutions to fight corruption and making proposals to combat abuses more effectively. If the Task Force does its work well, and the Integrity Authority and the government accepts its findings and recommendations, it could be very useful in the fight against corruption. However, this depends on several factors. The work of the Task Force can be undermined by captured institutions of the state, and the operation of the Integrity Authority can be made impossible as well.

Given the nature of corruption in Hungary and the state's involvement in it, the Task Force cannot be expected to perform miracles. However, the creation of a forum for dialogue between governmental and non-governmental organizations in the fight against corruption is an important development. TI Hungary is aware of the risks of participation, but we believe that our anti-corruption efforts are also worth voicing in this forum.

¹⁹ *Integritás Hatóság és Korrupcióellenes Munkacsoport: valódi küzdelem a korrupció ellen vagy személyvesztés az uniós pénzekért?* [Integrity Authority and Anti-Corruption Task Force: a real fight against corruption or a waste of EU money?] Transparency International Hungary blog, 26 September 2022 (<https://korrupcio.hvgblog.hu/2022/09/26/integritas-hatosag-antikorrupcio-elemzes/>)

²⁰ Transparency International Hungary's resolution on participation in the Anti-Corruption Task Force (See <https://transparency.hu/hirek/a-transparency-international-magyarorszag-allasfoglalasa-a-korrupcioellenes-munkacsoportban-valo-reszvetelrol/>, the full text of the resolution available at https://transparency.hu/wp-content/uploads/2022/10/TI_allasfoglalas_2022_1004.pdf)

2.3.3. Private prosecution - the end of the Prosecution Service's monopoly on corruption prosecutions?

In the prosecution of corruption, the Prosecution Service is very often criticized for delays and, in many cases, for failing to prosecute at all. The inaction of the prosecuting authority is a serious problem, even though in recent years three - now only former - members of parliament from the governing party have found themselves on trial for corruption involving the misappropriation of EU funds, as well as bribery. At the moment, it seems that the NER has abandoned Pál Völner, who formerly served as Secretary of State for Justice, as well as György Simonka and István Boldog. As things stand, Flórián Farkas, who has also lost his parliamentary seat in the meantime, has fared better than his former colleagues. He has not even been questioned by the authorities, even though he was the head of the National Roma Self-Government responsible for the implementation of the Bridge to the World of Work project, which involved a repayment obligation of more than HUF 1.5 billion.²¹

From this year onward, as part of the anti-corruption package pledged to the EU, anyone can go directly to court in such cases, except state and municipal authorities.²² The question is whether this will genuinely remove the Prosecution Service's monopoly on prosecution, which it has guarded very closely so far. In theory, certainly. But the practice is different. Investigating high-profile cases, especially corruption cases, is an extremely resource-intensive task, and the necessary capacities are typically not available either to private citizens or to civil society or economic operators. The rules of the new procedure are also rather complex. In essence, if the law enforcement authorities fail to act, a complaint - known in the law as a motion for reconsideration - can be submitted to the court, which can then order the proceedings to be initiated or continued. If the authorities terminate the procedure in the second round as well, a new complaint may be lodged and, with the court's permission, the complainant may also bring charges. However, the law allows only one month to prepare a complaint and later an indictment, and access to the case file is also very limited. It would be quite a feat to be able to bring an indictment in a month based on incomplete documents in a case where the prosecution has failed to do so for years.

The legislation was changed several times along the way, and under the law that was finally passed, the Integrity Authority can file a motion for reconsideration, but will not be entitled to press charges. In other words, by making full use of the procedural possibilities, the Integrity Authority can provide the infrastructure for an individual or civil society organization with the right to bring charges if the prosecution fails to do so. The question is of course whether the Integrity Authority will be willing to do so.

This new type of private prosecution will only apply to complaints filed on or after 1 January 2023. This means that it will not be possible to act as a private prosecutor in previous corruption cases, such as the Bridge to the World of Work project, which was closed last November, or the Elios case, which

²¹ See the NAV [National Tax and Customs Administration]'s decision No. 60100-51-955/2015 to terminate proceedings (in the possession of TI-Hungary). Ágnes Vadai addressed question No. K/2387 to the Prosecutor General on the matter (<https://www.parlament.hu/irom42/02387/02387.pdf>), in response to this question, Prosecutor General Péter Polt, in his reply KSB.883/2015/106, called the investigating authority's procedure adequate (<https://www.parlament.hu/irom42/02387/02387-0001.pdf>).

²² The new Chapter CV of the Criminal Code was established by Act XLIV of 2022.

was closed five years ago. In other words, what the authorities have already done away with is likely to remain so.²³

2.3.4. Freedom of information reform - a substitute action or deliberate misdirection?

Since 2010, the government has deliberately dismantled the legal and institutional framework for freedom of information, abolishing the office of the ombudsman and creating more and more legal barriers to accessing data of public interest. The coronavirus pandemic has also been used as a pretext for secrecy, as the government, in a decree adopted in early 2020 in response to the state of emergency, raised the deadline for responding to data requests from 15 days, as required by the law, to 45 days. Following the rule of law mechanism launched by the European Commission, the government has finally not only stopped the deliberate destruction but has withdrawn some restrictions as well. As of 1 January this year, 45-day extensions are no longer possible, and the new rules have also significantly reduced the amount of money that can be charged for the release of public interest data.²⁴

The government has also introduced new provisions to strengthen publicity. For example, public authorities will be obliged to publish certain details of their contracts involving public funds on a dedicated central website. Of course, this obligation is nothing new, as contractual information has been required to be disclosed since 2012. However, as there has been no monitoring of compliance and no sanctions for non-compliance, not much has been achieved. However, from 1 March this year, the National Authority for Data Protection and Freedom of Information (NAIH) can impose fines of up to HUF 50 million on those who fail to disclose the required data.²⁵ In addition, from 1 January, courts will be obliged to hear cases for access to data of public interest within very tight deadlines.²⁶

At first glance, the government's measures seem like a rather impressive freedom of information package, but as always, the devil is in the detail. The provision banning the extension of the deadline for complying with a data request to 45 days is perhaps the only substantive improvement. While the removal of the uncapped costs is important, it was more of an annoyance than a real barrier. Data controllers have rarely used this option, so the practical benefits of the new legislation will be minimal.

The situation is similar with the new transparency website. The fact that data that was already subject to publication should now (also) be made available elsewhere does not change anything. The fine that the NAIH can impose is not as heavy as it seems. Although HUF 50 million is not a small amount, it is easy to see that the incentive to disclose is modest, since even the details of a multi-billion dollar contract can be kept secret in exchange for such a sum. The government has not gone so far as to follow the example of Slovakia in requiring the mandatory disclosure of contracts involving public funds, failing which no payment can be made.

Of all the changes, however, the acceleration of litigation is the most controversial. Although faster litigation in principle leads to a faster access to information, short deadlines are more challenging for

²³Miklós Ligeti: *Kormányzati mosolyoffenzíva Brüsszel lebéngelésére?* [Governmental charm offensive to impress Brussels?] Transparency International Hungary blog, 22 July 2022 (<https://korrupcio.hvgblog.hu/2022/07/20/kormanyzati-mosolyoffenziva-brusszel-lebengerlesere/>).

²⁴ See Section 21 of Act CXXX of 2021 and § 5 of Government Decree 425/2022 (X. 28.).

²⁵ See Section 33/A of Act CXII of 2011, established by Act LVI of 2022.

²⁶ See Section 21/A of Act CXII of 2011, established by Act XL of 2022.

data applicants, who typically have limited resources, than for public authorities or publicly funded companies, who in many cases have inexhaustible resources.²⁷

2.3.5. Declaration of assets in Hungary: an absurdist tragicomedy

The government is constantly fiddling the asset declaration system. First, earlier this summer, the system of asset declarations, which is otherwise inadequate for auditing the wealth of public officials, was replaced by the solution used in the European Parliament. Unfortunately, this provided even less insight into the source of assets than previous declarations in Hungary and hardly allowed for the tracking of wealth accumulation. Under this regime, there was virtually no need to declare assets at all, only income, and that too only in income bands. Then, in response to the Commission's criticism, the government partially reinstated the previous domestic declaration system.²⁸ After this back and forth, a solution was found that resulted in less transparency than the initial situation. Previously, declarations of assets had to indicate the various types of income of the declarant by stating the specific amount. In contrast, the reform now requires only income bands to be given, and the declarant does not have to declare the residential property he/she uses.

In this case, the government's intention was clearly not to effectively solve the problem, which is also shown by the fact that the introduction of minimum requirements for asset declarations, which TI Hungary has been advocating for almost ten years, has not even been considered.²⁹

2.3.6. Public interest asset management foundations carrying out public duties: extended to Brussels

The pseudo-reform, which can be described in essence as „changing while preserving”, could not escape the NER's perhaps least legally comprehensible formation, the public interest asset management foundations carrying out public duties, commonly known as KEKVAs. It is well known that except for six institutions³⁰, the government has organized the entire public higher education sector, as well as several other formerly public assets, into foundations.³¹ In total, 35 KEKVAs manage assets worth thousands of billions of forints thanks to stakes in Mol and Richter, university and other real estates, and generous Treasury funds.³² All this is under the direction of the life-appointed Board of Trustees chosen from the favorites of the government. Crony trustees have very broad powers, they can not only decide on their own successors but also have full authority to manage the estate. To sit on the Board of Trustees of the KEKVAs is not only an honor but also very lucrative, with the top decision-makers receiving between HUF 1 and 1.5 million per month on average. The huge amounts of free money are a magnet for members of the government and other

²⁷ On this, see Transparency International Hungary's resolution *Közérdekeű adatigénylések: a szabályozás változik, az áttörés elmarad*. [Requests for Data of Public Interest: regulation changes, no breakthroughs made.] 20 October 2022 (<https://transparency.hu/hirek/kozerdeku-adatigenylesek-a-szabalyozas-valtozik-az-attores-elmarad/>).

²⁸ The amendments were introduced by Act XVIII of 2022, passed on 19 July 2022, and partially revoked by Act XXXI of 2022, passed on 24 October 2022.

²⁹ Transparency International Hungary: *Vagyonyilatkozási minimum [Minimum requirements of asset declarations]* (available at https://transparency.hu/wp-content/uploads/2016/07/policy_paper3_FIN.pdf)

³⁰ These are the Eötvös Lóránd University, the Liszt Ferenc Academy of Music, the Budapest University of Technology and Economics, the Hungarian University of Fine Arts, the University of Public Service, and the Eötvös József College in Baja.

³¹ As elections approach, public assets are transferred to foundations. See Civitas Institute - Transparency International Hungary Foundation. *Black Book II Corruption and State Capture in Hungary*, Budapest, 2021., p. 57-59.

³² The normative basis for the KEKVAs was created by the 9th Amendment to the Fundamental Law and Act IX of 2021, the annex to which contains a list of the KEKVAs.

public leaders. Eight of the dozen or so ministers serve as Trustees of a total of eleven KEKVA Boards. In addition to them, 17 other state leaders (government commissioners, state secretaries, the prime minister's political director, etc.), three Fidesz MPs, and six municipal leaders from the governing party are also serving as trustees.³³

KEKVAs implement everything that is unacceptable to citizens who fight corruption and are concerned about the rule of law. The politically motivated distribution of substantial unearned incomes is a textbook example of rent-seeking. The takeover of the foundations by political and business elites has led to a previously unimaginable increase in conflict of interest and the revolving door phenomenon. The latter is perhaps most recently exemplified by former Minister for Technology and Industry László Palkovics, who, almost as soon as he left government, took over as Chair of the Board of the foundation that runs the University of Győr.³⁴ János Lázár's deputy, Nándor Csepreghy, has been employed as Executive Director of the Blue Planet Foundation, which is linked to János Áder, following the end of his post as deputy minister in the Hungarian Prime Minister's Office. When he became deputy minister again in 2022, he had to give up his position at the foundation due to a conflict of interest but was allowed to sit on the Board of Trustees of the foundation, which had been upgraded to KEKVA status. Since then, he has been pulling in HUF 3 million a month as a trustee.³⁵

Of course, Brussels was also aware of this, and the Commission included the restructuring of the KEKVAs as a condition of the rule of law mechanism. One of the requirements was that the KEKVAs should be obliged to call for tenders as contracting authorities when using the public funds entrusted to them. The Commission also called for a tightening of the conflict of interest rules, i.e., for government members to resign from foundations boards.

The government has so far only complied with the requirement for public procurement by the KEKVAs,³⁶ but has only prohibited minor forms of conflict of interest, requiring only that trustees should not participate in decisions that would benefit them personally.³⁷ At the end of January 2023, political appointees were still trustees of the foundations' Boards.³⁸ However, the EU pressure is

³³ See the analysis of Transparency International Hungary: „A KEKVA-k is az uniós pénzek útjában állnak” [KEKVAs are also obstacles to EU funds] 17 January 2022 (<https://transparency.hu/hirek/a-kekva-k-is-az-unios-penzek-utjaban-allnak/>). Revisited by Máté Pálos: „A fél kormánynak távoznia kell a vagyonkezelő alapítványokból, ha nem lesz kibúvó” [Half the government must leave the trusts if there is no way out] 23 January 2022 (<https://g7.hu/kozelet/20230123/a-fel-kormany-nak-tavoznia-kell-a-vagyonkezelelo-alapitvanyokbol-ha-nem-lesz-kibuvo/>).

³⁴ „Magasabb dimenzióban a tudomány, innováció és vállalkozás az egyetemet fenntartó alapítványnál” [Higher dimensions of science, innovation, and entrepreneurship at the university foundation] University of Győr, 8 December 2022 (<https://www.uni.sze.hu/post/magasabb-dimenzi%C3%B3ban-a-tudom%C3%A1ny-innov%C3%A1ci%C3%B3-%C3%A9s-v%C3%A1llalkoz%C3%A1s-az-egyetemet-fenntart%C3%B3-alap%C3%ADtv%C3%A1ny%C3%A1l>)

³⁵ Dániel Kozák: „Nettó kétfélmillió forintot keres Áder alapítványánál Lázár helyettese” [Lázár's deputy earns a net salary of HUF two million at Áder's foundation] 15 September 2022. (<https://24.hu/belfold/2022/09/15/kek-bolygo-alapitvany-csepreghy-nandor-ader-janos-fizetes/>)

³⁶ The provision of the Public Procurement Act, as amended by Article 13 of Act XXIX of 2022, includes KEKVAs and legal entities established or maintained by KEKVAs among contracting entities.

³⁷ See § 95 (1a) and § 182 (3a) of Act CXXV of 2018 and § 15 (3) of Act IX of 2021.

³⁸ The conflict of interest rules for senior political leaders are governed by Article 182 of Act CXXV of 2018. Paragraph (3a) exempted the KEKVAs from the conflict of interest. Act XXIX of 2022 abolished this exemption with effect from 13 October 2022, and Act XXXI of 2022 reintroduced the exemption with effect from 1 November 2022.

working: according to a press release of 25 January, the Hungarian government is "ready to change the law to eliminate conflicts of interest in the Boards of Trustees of public foundations".³⁹

We don't know whether the Hungarian government will give in, but if it does, it will be because in mid-January it became clear to the public that the European Council, following a proposal by the Commission, has excluded universities maintained by foundations from future EU funding under Erasmus+ and Horizon 2020. The government has admitted, after some of its usual spin, that it was already aware of the unmet expectation.⁴⁰

2.3.7. Judicial reform

At first, it seemed surprising that the Commission did not put the independence of the Hungarian courts on the agenda as part of the rule of law mechanism. In the end - perhaps partly as a result of conclusions drawn from reports by civil society organizations fighting for the rule of law, such as TI Hungary - the judicial package of 10 conditions was included among the "super-milestones" for access to RRF funds. The government put the draft law up for public debate on 20 January, allowing two weeks for comments.⁴¹

TI Hungary was not able to complete its evaluation of the draft law until the manuscript of this report was finalized. What can be seen, however, is that the government is willing to make major concessions on several points. Among other things, the possibility for public authorities to submit a complaint to the Constitutional Court would be abolished. The National Judicial Council (OBT), a monitoring body elected by the judges from among themselves, would also have its powers considerably expanded. However, it remains to be seen whether the next election of the OBT in 2024 will bring back committed judges who will want to use their enhanced powers.

TI Hungary continues to believe that the courts are the last line of defense of the rule of law and democracy in Hungary. However, the cracks are already showing, so the European Union must use all means to ensure the independence of the Hungarian courts.

³⁹ Eurologus: *Navracsics: A kormány kész kivonulni az egyetemi kuratóriumokból.* [Navracsics: government ready to withdraw from university Boards of Trustees.] 25 January 2023

(https://hvg.hu/eurologus/20230125_Navracsics_a_kormany_kesz_kivonulni_az_egyetemi_kuratoriumokbol)

⁴⁰ The statements made by Gergely Gulyás, Head of the Prime Minister's Office, at a press conference on 12 January 2023 are also confirmed by the Government's notice. „Ha nem vezetnek eredményre az Erasmus-ösztöndíjjal kapcsolatos tárgyalások az Európai Unióval, akkor a kormány kifizeti az ösztöndíjak költségét - közölte a Miniszterelnökséget vezető miniszter csütörtökön Budapesten, a Kormányinfón.” [If the Erasmus scholarship negotiations with the European Union do not lead to a result, the government will pay the cost of the scholarships – stated the Head of the Prime Minister's Office at a press conference in Budapest on Thursday.] (<https://kormany.hu/hirek/a-kormany-kifizeti-a-2024-es-erasmus-osztondijakat-ha-nincs-megallapodas>)

⁴¹ Draft bill amending certain laws on justice, 18 January 2023 (The full draft legislation is available on the government website: https://kormany.hu/dokumentumtar/egyeb-igazsagugyi-targyu-torvenyek-modositasarol-szolo-torvenyjavaslat?fbclid=IwAR2cbNvhhPhoWV82lCB6ctGZYVvW_qVY5ufYrbOCyXsAZiUkN-kT9GQIDS0).

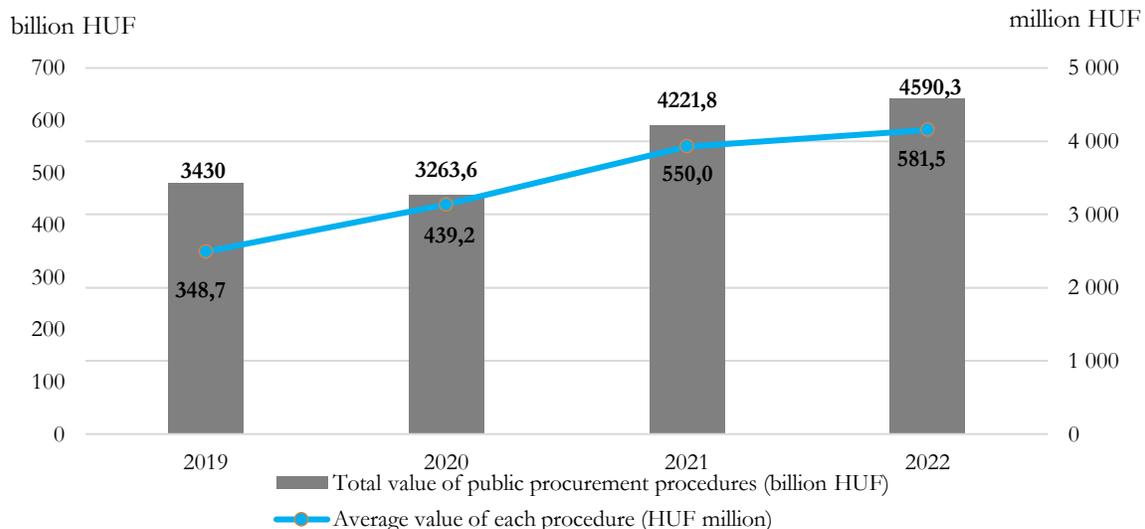
3. Public procurement and EU funding

3.1. How the public procurement system works

Public procurement plays a major role in the economy, and its weight in 2022, a year of elections, war, and record inflation is proving even greater than in previous years. The total value of public procurement procedures in 2022 exceeded HUF 4590 billion, an increase of 9 percent compared to the previous year's HUF 4222 billion,⁴² and well above the results of the years before the coronavirus epidemic. Meanwhile, the number of procedures increased by only 3 percent compared to 2021 and decreased by 20 percent compared to 2019. Growth in the value of public procurement took off strongly in the six months before the elections, in the third quarter of 2021, but the pace of expansion slowed in the second half of 2022.

The data of the Public Procurement Authority (PPA) show a remarkable dynamic: while in the first three quarters of 2022 there was a 48 percent increase in prices compared to the same period of the previous year, by the end of the year procurement had been cut back to such an extent that for the whole year, there was only a 6 percent increase in the average price for individual procedures. However, compared to the pre-pandemic period (2019), the average amount received under public procurement procedures increased by 67 percent, which, in addition to inflation, certainly reflects the increased overpricing of public procurement.

Figure 3: Total value of public procurement procedures (HUF billion) and average amount per procedure (HUF million), 2019-2022



Source: TI Hungary's calculation based on the Public Procurement Authority's 2022 flash report

Identifying and mitigating the risks associated with public procurement is a central element of the negotiations between the European Union and the Hungarian government to obtain EU funds, as the

⁴² See the Public Procurement Authority's flash report: *A magyar közbeszerzések számokban, 2022* [Hungarian public procurement in numbers, 2022] (available at: <https://kozbeszerzes.hu/media/documents/gyorsjelentes-2022-pdf.pdf>)

exposure of the public procurement system to corruption is quite significant in Hungary as well.⁴³ The European Commission has made several findings on irregularities in public procurement in Hungary, highlighting the typically low level of competition and high concentration in public procurement, referring among other things to a survey by the Corruption Research Center Budapest. According to the findings of this study, 42 companies owned by 12 individuals close to the government won more than a fifth of EU-funded public contracts between 2010 and 2021.⁴⁴ The Commission also raised concerns about problems with the application of framework agreements, the detection, prevention, and correction of conflicts of interest, and the use of EU funds by public trust funds.

The Commission has, for the umpteenth time, highlighted the high proportion of single-bid tenders, which has a major impact on the intensity of competition in the public procurement market and is also linked to its exposure to corruption. According to the European Commission, 39 out of 100 public procurement procedures above the EU threshold (i.e., higher) received only one bid in 2021, a figure that fell to just under 35 percent in 2022, according to the PPA.⁴⁵ For lower-value domestic procedures, the share of single bids accounted for a fifth of contracts last year. A report by the Prime Minister's Office also shows that in 2021, the share of single-bid procurement was higher for domestic procedures, which are funded by the taxpayers (36 percent), while it was much lower for EU-funded procurement (16 percent).⁴⁶ In 2021, single-bid tenders were particularly high in supply contracts, their share being 70 percent for domestic tenders and 77 percent for tenders above the EU threshold (see Figure 4).

In 2022, the government also recognized the need to reduce the proportion of single-bid procedures. The commitments in Hungary's Recovery and Resilience Plan⁴⁷ include a reduction of the contested rate from 39 percent to 15 percent for high-value contracts under EU procedures (which are not the same as EU-funded procedures). The analysis and evaluation of procurement risks will also be an important task of the Integrity Authority, newly established by the government. To analyze risks, it is essential to have public procurement data of sufficient quality and in a well-analyzable format. In 2022, the PPA has also made available the data from result notices detailing final decisions on public procurement procedures as a downloadable data package. However, the aggregated disclosure also highlighted shortcomings in the quality of public procurement data.⁴⁸

⁴³ Council Implementing Decision (EU) 2022/485 on measures for the protection of the Union budget against breaches of the principles of the rule of law in Hungary (18 September 2022)

⁴⁴ CRCB: *Corruption risk and the crony system in Hungary, A brief analysis of EU funded contracts in Hungarian public procurement 2005-2021*; 7 March 2022 (available at https://www.crcb.eu/wp-content/uploads/2022/03/2022_research_notes_03_220307_02.pdf)

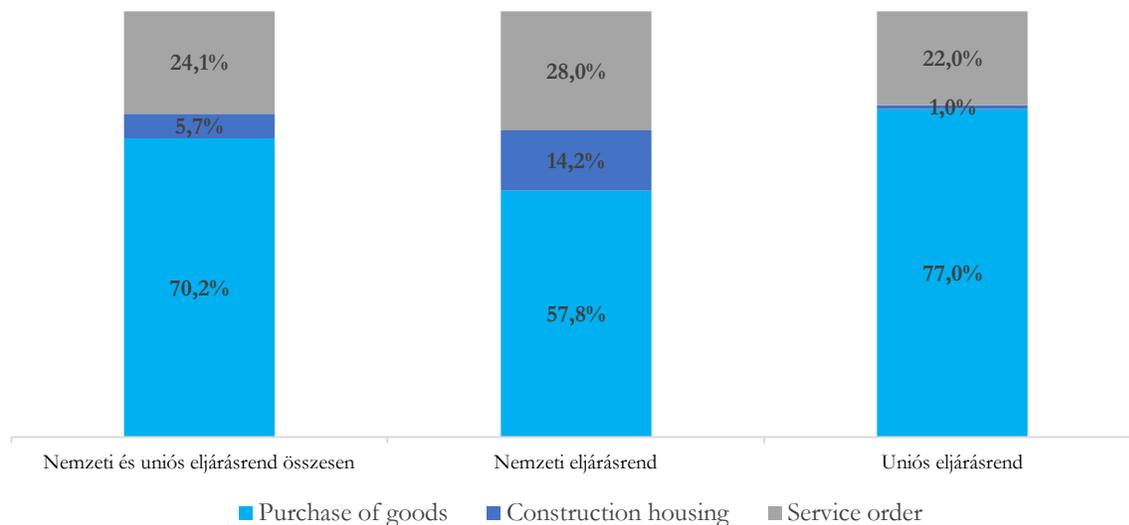
⁴⁵ See Single Market Scoreboard indicator 1 on public procurement (https://single-market-scoreboard.ec.europa.eu/policy_areas/public-procurement_en)

⁴⁶ Prime Minister's Office, State Secretariat for Public Procurement Supervision: *Elemzés az egyajánlatos közbeszerzések alakulásáról, 2019-2021 [Analysis of the development of single-bid public procurement, 2019-2021]*; (available at <https://www.palyazat.gov.hu/elemzs-az-egyajánlatos-kzbeszerzsek-alakulstl>)

⁴⁷ See Council Implementing Decision on the approval of the assessment of the recovery and resilience Plan for Hungary, 30 November 2022; (https://ec.europa.eu/info/sites/default/files/com_2022_686_1_hu.pdf)

⁴⁸ Transparency International Hungary has analyzed and shared the errors detected in the published data with the Public Procurement Authority in a letter. In its reply, the Authority has indicated to TI Hungary that it does not intend to correct the errors detected. See Judit Zeisler, *Közbeszerzési adatok nyilvánossága: csontvázak a szekrényből [Disclosure of public procurement data: skeletons in the closet]*, Transparency International Hungary blog, 28 November 2022 (<https://korrupcio.hvgblog.hu/2022/11/28/kozbeszerzesi-adatok-nyilvanossaga-csontvazak-a-szekrenybol/>).

Figure 4: Distribution of the number of single-bid tenders by type of supply contracts in each procurement system, 2021



Source: Prime Minister's Office

Competition to win public contracts is not helped by the fact that the government regularly exempts the most important procurements from traditional tendering, citing, for example, the coronavirus epidemic, or national security. This was no different last year, when concession procedures that had been launched in previous years in violation of EU law were closed, usually with pro-government winners.⁴⁹ Crony oligarchs won the right to operate and maintain the freeways for 35 years, the details of this business were made public by the National Bureau of Concessions following a data request lawsuit filed by TI Hungary.⁵⁰ The consortium led by Themis, a private equity fund linked to László Szíjj, who is the yachting partner of Foreign Minister Péter Szijjártó, and other private equity funds linked to Lőrinc Mészáros will together pocket almost HUF 5500 billion, far exceeding the total annual public procurement budget, over the three and a half decades of the contract. Mol Nyrt. has been awarded the municipal waste management contract for the same period, so as things stand, this is the only company in Hungary that will be able to collect and handle municipal solid waste and carry out the related investments in the decades ahead. Although the public procurement regulations do not apply to the gambling industry, it is worth mentioning a third concession, also expiring in 2056, which granted the right to manage the casinos in Budapest to oligarchs István Garancsi and Kristóf Szalay-Bobrovniczky, who has since been appointed Minister of Defense, for a further 35 years. Later, the company of the minister's business partner, Árpád Habony, took over Kristóf Szalay-Bobrovniczky's share.⁵¹

⁴⁹ Gabriella Nagy: *Koncessziókkal jogászokodik a kormány* [The government's legal maneuvering around concessions], Transparency International Hungary blog, 28 September 2021 (<https://korrupcio.hvgblog.hu/2021/09/28/koncessziokkal-jogaszkodik-a-kormany/>)

⁵⁰ See Transparency International Hungary's data request and relevant background calculations: *Közvetésszük a 35 éves sztrádaconcesszió háttérszámításait* [Background calculations for the 35-year freeway concession published], 15 December 2022 (<https://transparency.hu/hirek/kozvetesszuk-a-35-eves-sztradakoncesszio-hatterszamitasait/>)

⁵¹ András Bódis: *Ez a jóslatunk is bevált: részben Habonyhoz kerültek a fővárosi kaszinók* [Another one of our predictions came true: casinos in Budapest went in part to Habony], 9 January 2023 (<https://www.valaszonline.hu/2023/01/09/habony-arpad-fovarosi-kaszinok-garancsi-istvan-las-vegas-casino-csoport-2056-ig/>)

3.2. Hungary's share of EU funds and how they are being used

A new funding period for the use of EU funds started in 2021 but, as mentioned in previous chapters, money is being withheld by the EU due to rule of law issues, mainly corruption involving EU funds. In practice, this means that not a single euro has been received from the Cohesion Fund and the recovery funds for the new programming period.

However, the allocation of the funds has already started in 2021, as they are subject to a strict spending schedule.⁵² According to the official application portal, 193 applications have been awarded direct grants worth some HUF 528 billion from the recovery fund announced in the meantime by the end of 2022 or roughly 20 percent of the total available resources.⁵³ Most of the money has already been paid out to the applicants. For the time being, all this is financed by the Hungarian budget, i.e., the taxpayers. Almost all the winners are state, municipal, or church-owned organizations. The only "market" winner known so far is OPUS TITÁSZ Zrt., one of the energy companies owned by Lőrinc Mészáros. The company has already received nearly HUF 8 billion of the more than HUF 13 billion in grants awarded.⁵⁴ However, other companies close to the government have also been among the beneficiaries of the funds distributed through public procurement, such as 4iG Nyrt., which was involved in the acquisition of Vodafone.⁵⁵

The Commission decided to partially suspend the funding for the three above-mentioned operational programs because the priority projects involving larger grants appeared in these, attracting many pro-government actors through the related public procurement. Despite the suspension, the value of the funds requested under the program for spatial development for the period 2021-2027, with an allocated budget of HUF 1962.5 billion, has already reached HUF 1170 billion. The amount of grants awarded is close to HUF 550 billion, and HUF 410 billion has already been paid out from the central budget for the winning applications.⁵⁶

The use of EU funds in Hungary has long been characterized by the fact that fast spending overrides all other criteria, including regional distribution and competitive return, putting public administration under pressure to absorb them.⁵⁷ The justification of objectives, project design, and monitoring have become secondary. Indicating the inefficient use of funds, the European Anti-Fraud Office (OLAF) requested the Hungarian authorities to investigate 18 cases of misuse of EU funds between 2017 and 2021.⁵⁸ The organization has proposed one of the most severe financial sanctions for Hungary: repayment of 0.7 percent of domestic funds was initiated, compared to the EU average of 0.3 percent.

⁵² Gabriella Horn: *Már 373 milliárd forintot kifizetett a kormány a meg sem kapott uniós helyreállítási pénzekből* [The government has already paid out HUF 373 billion of the EU recovery funds not even received yet], 11 October 2022 (<https://www.szabadeuropa.hu/a/mar-373-milliard-forintot-kifizetett-a-kormany-a-meg-sem-kapott-unios-helyreallitasi-penzekbol/32052517.html>)

⁵³ See the relevant details on the government tendering portal (available at https://www.palyazat.gov.hu/tamogatott_projektkereso)

⁵⁴ Gabriella Horn: *Mészáros Lőrinc érdekeltségének már 13 milliárd jutott a még meg sem kapott uniós helyreállítási pénzekből* [Lőrinc Mészáros's interests have already received HUF 13 billion from EU recovery funds not even received yet], 18 July 2022 (<https://atlatzo.hu/kozpenz/2022/07/18/meszaros-lorinc-erdekeltsegenek-mar-13-milliard-jutott-a-meg-meg-sem-kapott-unios-helyreallitasi-penzekbol/>)

⁵⁵ See 4iG Nyrt.'s special notice on high-value contracts (available at https://www.4ig.hu/4ig-nyrt_-rendkivuli-tajekoztatasa---2022_-junius-01_-2)

⁵⁶ Gergely K. Kiss: *Kiderült, mit lép a kormány az EU-s pénzek felfüggesztésére* [The government's action plan in response to the suspension of EU funds revealed], 13 December 2022 (<https://24.hu/fn/gazdasag/2022/12/13/eu-unios-forras-felfuggesztes-jogallamisagi-mechanizmus-europai-bizottsag-penzmegvonas-unios-palyazat-navracsics-tibor/>)

⁵⁷ Gergő Medve-Bálint - Péter József Martin - Gabriella Nagy: *Céllentétes következmények? Az uniós források hasznosulása Magyarországon, Társadalmi Ríport*, 2022 [Counterproductive Consequences? Use of EU Funds in Hungary, *Social Report*, 2022]; (https://taki.hu/sites/default/files/2022-12/033_052TRIP2022_MedveMartinNagy.pdf)

⁵⁸ See OLAF report 2021 (available at https://anti-fraud.ec.europa.eu/system/files/2022-09/olaf-report-2021_en.pdf)

However, the Hungarian authorities failed to act in 67 percent of the cases detected; a total of 6 cases were investigated, of which 2 were closed with no charges pressed, and only 4 were pursued on OLAF's recommendations. OLAF cannot carry out investigative measures in the Member States, nor can it press charges. The European Public Prosecutor's Office, of which Hungary is not a member, would have the power to do so.

4. Corruption and economic performance

According to a substantial body of scientific research and policy analysis, corruption and economic performance are linked.⁵⁹ Corruption, as a major cause and consequence of "bad governance", tends to "grind" the gears of the economy. The systemic nature of abuses goes hand in hand with the destruction of the rule of law. When a biased state institutional system, which secures the power of the ruling elite, does not prosecute but tolerates or encourages corruption, it often leads to economic loss and increased inequalities. In this case, the oligarchs, top politicians, cronies and loyal economic actors and citizens in general will have more power and wealth, while another significant part of society - unable or unwilling to take such 'loyalty oaths' - will not benefit from the prosperity, or will benefit only to a limited extent. If access to resources is dependent on the favor of the state, this leads to the marginalization of fair competition and meritocracy, and to the spread of rent-seeking mentality that seeks to curry favor with the powers that be. A worsening business climate could lead to a decrease in investment, which could undermine sustainable growth. An apt thesis is that resource allocation systematically skewed towards the ruling elite causes more macro-level damage than the stolen wealth itself, apparently because it makes corruption the norm, and often legalizes it.⁶⁰

However, this link between corruption and economic development is not universal, and often not immediate, but delayed over time. In many countries, particularly in Asia, high levels of corruption are consistently associated with impressive economic performance, with China being the most obvious example.⁶¹ But in other countries, even those with a Western(ish) economic culture, corruption can also have a temporary "oiling" effect, seemingly boosting economic performance.⁶² For example, the overpricing of public spending and public procurement for corruption purposes can distort investment and growth statistics. Abuse and rent-seeking can also reduce, for a time, market transaction costs, thereby improving the reported economic performance.

4.1. High corruption, low economic performance: Hungary is in the bottom group of the EU

In the European Union in 2022, as in previous years, a strong correlation remains between economic performance, measured by Gross Domestic Product (GDP) per capita, and scores on Transparency International's Corruption Perceptions Index (see Figure 5). In the EU, the correlation between corruption and economic performance is therefore well established, although the regression coefficient of 0.81, which indicates the strength of the relationship, is now slightly lower than in 2020 and 2021 (0.83 in the previous two years).

Figure 5 shows the regional position of EU countries, including Hungary. The 2022 CPI shows Hungary as the most corrupt Member State in the EU. In terms of GDP per capita, Hungary performs better than only three EU countries (Bulgaria, Romania, Croatia), and is essentially on a par with Poland. At the periphery of the EU, the performance of the Eastern and Southern European group of countries is becoming "mixed": Greece's anti-corruption performance is worse than that of the

⁵⁹ Organization for Economic Cooperation and Development (2012) *Issues Paper on Corruption and Economic Growth*. Working Paper. pp. 1-43. (<https://bit.ly/31HDCih>); Acemoglu, Daron & Robinson, James, A. (2013) *Why do nations fail?* HVG Publishers.

⁶⁰ Rothstein, Bo (2011) *The Quality of Government: Corruption, Social Trust and Inequality in International Perspective*, Chicago: Chicago University Press.

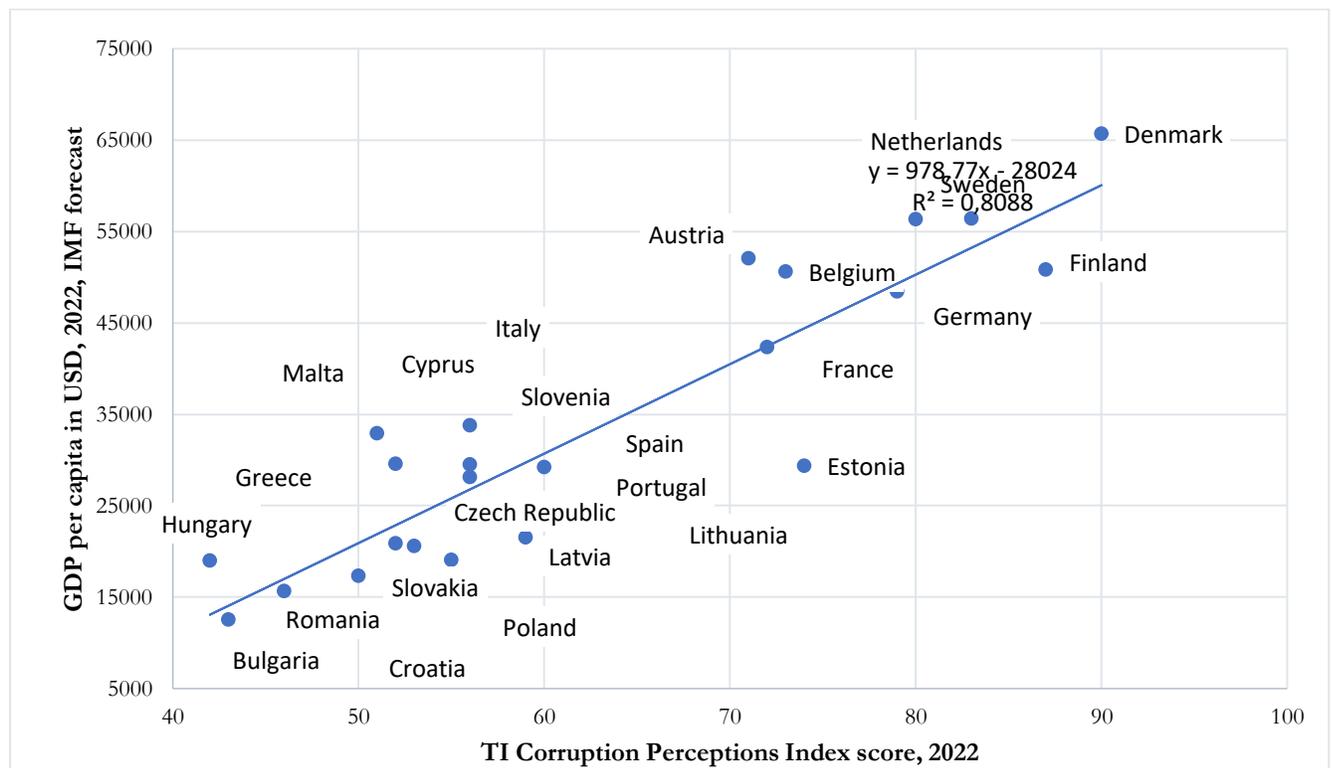
⁶¹ See the OECD study cited in footnote 59.

⁶² Heo, Yuna, et al. (2021) Does corruption grease or sand the wheels of investment or innovation? Different effects in advanced and emerging economies. *Applied Economics*, 53:1, pp. 35-60.

Visegrad Group and Slovenia - except for Hungary - not to mention the Baltic States. Furthermore, Greece also lags behind Slovenia, Czechia, and all three Baltic States in terms of GDP per capita. In addition, the CPI and GDP indicators of Cyprus, and even Italy, Spain, and Portugal, are increasingly similar to those of the more developed Central and Eastern European countries. The EU's eastern and southern periphery are practically forming a block against Western Europe, with Estonia being the only exception to the periphery in terms of corruption exposure, approaching the Western bloc.

Hungary is stuck in the EU's bottom group of corruption-ridden Member States with low national incomes by EU standards, despite having experienced strong economic growth, averaging over 4 percent in the seven years preceding the coronavirus outbreak. According to data from the International Monetary Fund (IMF), GDP per capita grew from USD 13 666 in 2013 to USD 18 983 in 2022, an overall increase of no less than 39 percent.⁶³ Despite the relatively high growth rate, the total economic growth rate of the last decade is - contrary to government propaganda of success - only sufficient to reach the bottom of the regional middle range.

Figure 5: Correlation between corruption and national income in EU countries, 2022



Source: TI Hungary calculations based on the Corruption Perceptions Index and IMF 2022 data.⁶⁴

⁶³ See the International Monetary Fund (IMF) World Economic Outlook Database (available at: <https://www.imf.org/en/Publications/WEO/weo-database/2022/October/select-country-group>)

⁶⁴ The higher the Corruption Perceptions Index score, the lower the exposure to corruption. Among the European Union Member States, Luxembourg (GDP per capita of USD 128 000) and Ireland (GDP per capita of USD 102 000) have been excluded for technical reasons due to their different accounting of national accounts compared to other Member States. The R² value in the figure shows the strength of the correlation between GDP per capita and the Corruption Perceptions Index score, which is 0.81, meaning that the correlation between the two variables is strong.

The performance of the Hungarian economy was ambivalent in the period from 2013 until the coronavirus crisis.⁶⁵ Short-term macro indicators (growth, inflation, unemployment, financial balance) were pleasing, while seven years of economic boom were not enough to remedy the economy's structural and efficiency problems. Both the productivity⁶⁶ and competitiveness of the economy remained below the performance of the Visegrad Group and the regional average.⁶⁷ The main reason for the latter is the poor performance of the public institutional system. In addition, human infrastructure is also underperforming: in education, PISA surveys show a worsening trend,⁶⁸ while health care has been persistently underfunded.⁶⁹

TI Hungary's analyses and other studies have already pointed out that the destruction of the rule of law and the closely related centralization, as well as systemic corruption, may have been the main reasons why, despite unprecedented EU funding averaging around 4 percent of GDP annually over the past decade, the Hungarian economy has failed to get on an inclusive growth path i.e., one that uplifts broad sections of society.⁷⁰ Longer-term trends in the utilization of EU funds show that, despite being one of the largest beneficiaries of the EU budget, the inflow of money has not contributed to increased efficiency or economic prosperity measured by the growing number of businesses, and inequalities have not decreased, while corruption has increased.⁷¹

Over the past two years, most of the short-term macro indicators have "deteriorated" towards the already poor efficiency and structural indicators that are supposed to ensure longer-term prosperity. Inflation hit an EU record at the end of 2022, the fiscal balance is long gone, with both budget and current account deficits reaching dangerous levels, and a recession in 2023, following the one in 2020, may not be avoidable.⁷² The worsening trends are partly due to external factors (the crises caused by the coronavirus and Russian aggression against Ukraine). Serious recent economic policy mistakes also play an important role. These include, but are not limited to, unprecedented spending before the elections on the fiscal side and delayed interest rate hikes on the monetary side. Only the unemployment rate, which is still below 4 percent,⁷³ and the surprisingly high level of investment

⁶⁵ József Péter Martin (2020) Resource Reallocation and Ambiguous Economic Performance in a Captured State - The Case of Hungary. In: *Systems, Institutions, and Values in East and West: Engaging with János Kornai's Scholarship*. CEU Press, 2020 (Eds. D. Piroška and M. Rosta) pp. 173-201.

⁶⁶ See on this the Eurostat database on economic productivity (available at: <https://ec.europa.eu/eurostat/databrowser/view/tipsna70/default/table?lang=en>)

⁶⁷ Comprehensive competitiveness surveys, both the World Economic Forum's (WEF) World Competitiveness Report and the World Bank's Doing Business report, have been on hiatus since the pandemic. Hungary ranked 47th (<https://www.weforum.org/reports/the-global-competitiveness-report-2020/>) in the WEF's latest comprehensive ranking and 52nd (<https://archive.doingbusiness.org/en/data/exploreconomies/hungary>) in the Doing Business list, lagging behind its Central European competitors.

⁶⁸ See the OECD 2018 Programme for International Student Assessment (PISA) results (available at https://www.oecd.org/pisa/publications/PISA2018_CN_HUN.pdf)

⁶⁹ For more information, see OECD State of Health in the EU, Country Health Profile 2019 (available at <https://www.oecd.org/hungary/Hungary-Country-Health-Profiles-2019-Launch-presentation.pdf>)

⁷⁰ See footnote 31; and Dóra Györfly (2021): Felzárkózási pályák Kelet-Közép-Európában két válság között. [Trajectories of catching up in Central and Eastern Europe between two crises.] *Közgazdasági Szemle*. January, p. 47-75.

⁷¹ See footnote 57.

⁷² See European Commission's economic forecast for Hungary (https://economy-finance.ec.europa.eu/economic-surveillance-eu-economies/hungary/economic-forecast-hungary_en)

⁷³ Nőtt a munkanélküliség Magyarországon, megindultak külföldre az emberek. [Unemployment has increased in Hungary, and people are moving abroad.] *Portfolio*. 27 January 2023 (<https://www.portfolio.hu/gazdasag/20230127/nott-a-munkanelkuliseg-magyarorszagon-megindultak-kulfoldre-az-emberek-593124>)

activity, despite the crises and the destruction of the rule of law, mitigates an otherwise rather depressing situation.

4.2. Investment paradox

Despite corruption and a poor institutional environment, the investment situation is complex. The investment rate, i.e., the volume of investment as a share of GDP, was falling almost hand in hand with the erosion of the rule of law before 2016. In other words, the thesis that the erosion of the rule of law, together with the deterioration of the business environment, has also reduced investment activity has been confirmed.⁷⁴

Later, however, this correlation did not hold: the investment rate was very high after 2016, exceeding 27 percent in the last three years, and the Hungarian rate was the second highest in the European Union after Estonia, according to the latest data for 2021.⁷⁵ In a crony state capitalist regime like Orbán's, this could of course be the result of a surge in public investment alone, which is largely funded by EU money. But the data show that the ratio of business investment to GDP is also relatively high by EU standards, with private investment at 16 percent in 2020 and 17 percent in 2021, putting Hungary in fifth place in the EU after Ireland, Estonia, Austria, and Czechia.⁷⁶ The intensive investment activity despite the destruction of the rule of law - the investment paradox of the Hungarian economy - is explained by several interrelated factors.⁷⁷ Firstly, the concentrated public procurement market, as well as the generous state support for crony companies and oligarchs trickled down later as private investments through the various reinvestments by these government-loyal actors. Second, inflation has consistently exceeded the base rate of the central bank after 2016, and the abundance of resources (lower than inflation borrowing rates) created by "cheap(er) money" has helped investment. Third, the systemic overpricing of public procurement and EU resource allocation improves investment and growth statistics, thus "oils" economic performance. Fourth, since the second half of the last decade, a significant number of economic actors have accommodated the disruption of the rule of law and systemic corruption, accepting it as a kind of "new normal".

Despite all this, it is a warning sign that the inflow of foreign direct investment (FDI) within private investments decreased significantly from 2020 to 2021. From an all-time high of USD 171 billion two years ago, annual FDI inflows reached only USD 30 billion in 2021.⁷⁸ While the final figure for 2022 is not yet available, the deterioration in the business environment outlined above may suggest that FDI inflows may be on a downward trend, and/or that their dynamics may be driven by often low value-added Eastern (e.g., Korean) rather than Western investment. Contrary to the loud rhetoric of

⁷⁴ József Péter Martin (2020): Olajozza vagy csikorgatja a fogaskerekeket? A NER korrupciós és gazdasági teljesítménye nemzetközi összehasonlításban [Oiling or grinding the gears? The corruption and economic performance of the NER in international comparison.] *Social Report*. p. 83 (Available at https://www.tarki.hu/sites/default/files/2020-10/060_089_Martin_web.pdf)

⁷⁵ According to data from Eurostat, the Estonian investment rate was 28.9 percent, while the Hungarian rate was 27.2 percent in 2021. (For more information on Eurostat's investment data, see https://ec.europa.eu/eurostat/databrowser/view/sdg_08_11/default/table?lang=en)

⁷⁶ See footnote 75.

⁷⁷ Martin, József Péter: *From Dual Economy to Parallel Universes: Attitudes and Coping Strategies of Hungarian Businesses vis-à-vis Crony State Capitalism - the Case of Hungary*. Center for International Private Enterprise Research. Washington, DC. 6 May 2022 (available at <https://www.cipe.org/resources/from-dual-economy-to-parallel-universes-attitudes-and-coping-strategies-of-businesses-vis-a-vis-crony-state-capitalism-the-case-of-hungary/>).

⁷⁸ See World Bank data on FDI (<https://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD?end=2021&locations=HU&start=1982>)

"Eastern Opening", Western businesses are still by far the largest investors at present. In 2019, Chinese and Russian FDI together accounted for less than 5 percent of total domestic FDI.⁷⁹

⁷⁹ The latest available data is for 2019 and does not include recently announced Chinese investments, including the battery plant in Debrecen planned by CATL (<https://statisztika.mnb.hu/timeseries/data-5637>)