

**LAPSE OF
TIME**

SM/21/91
Correction 1

June 17, 2021

To: Members of the Executive Board

From: The Secretary

Subject: **Hungary—Selected Issues**

Board Action: The attached corrections to SM/21/91 (6/4/21) have been provided by the staff:

Evident Ambiguity

Page 11

Factual Errors Not Affecting the Presentation of Staff's Analysis or Views

Pages 3 and 4 (para. 6)

Typographical Errors

Page 4 (para. 7)

Questions:

Mr. Dauphin, EUR (ext. 39705)
Ms. Vtyurina, EUR (ext. 38940)

compared to 1990 ~~while~~, under the Effort Sharing Regulation [Decision](#) (ESRD).⁷ Additionally, Hungary has, along with a few other EU countries, committed to reaching climate neutrality by 2050, entailing sustained emissions reductions and improving sink and other CO₂ removal capacities in the next three decades.

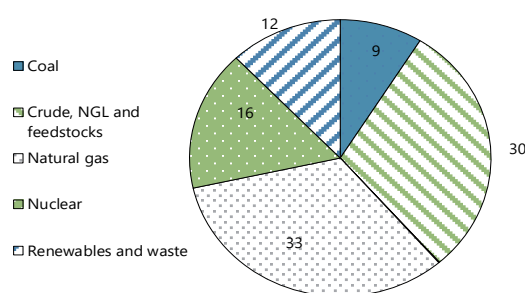
3. Tackling climate issues can help strengthen the post-COVID-19 recovery and build a more resilient and durable economy. The recovery provides an opportunity to shape consensus on actions to support the transition to a more sustainable economy, including carbon pricing, prioritizing public investment and incentivizing private investment in green infrastructure and innovation, reducing subsidies and tax exemptions for emissions-intensive activities, and promoting green finance (IMF, 2020b). Indeed, prior to COVID, the government considered its climate policy as “not (only) a green issue, but a new economic development model (green growth)” (Ministry for Innovation and Technology, 2019). In designing and scaling up national mitigation strategies, it is helpful for governments to have transparent, quantitative frameworks for projecting the emissions commitments, and for assessing the environmental, fiscal, and economic impacts of their mitigation policy options. Hungary is finalizing its long-term low emission development strategy (LTS), which is taking into account the effects of the COVID-19 pandemic as well.

4. This note aims to briefly overview Hungary’s mitigation goals, progress, and challenges. It specifically zooms in on areas where changes could be made *unilaterally* in sectors responsible for a large share of carbon emission (e.g., housing, transportation) and suggests options to further incentivize mitigation.³ It focuses on carbon pricing and other fiscal mitigation instruments that could effectively support green investment. Sector-specific policies and objectives are not discussed in detail in this note as they require large scale adjustments, including through EU agreements, notably carbon-border adjustment to reduce carbon leakage outside the EU.

B. Climate Objectives and Costs

5. The main sources of Hungary’s GHG are residential solid fuel combustion, and transport and industrial emissions. Hungary has limited fossil-fuel resources of its own, and its domestic production is declining. More than two-third of its total primary energy supply comes from fossil fuel (Figure 2). The country imports around 90 percent of its oil and natural gas and 30 percent of its electricity supply. Domestic electricity is mostly produced from

Figure 2. Total Primary Energy Supply, 2018^{1/}
(In percent of total energy supply)



^{1/} 2018 is provisional data; excluding net electricity import.
Sources: IEA, and IMF staff calculations.

³ More on Hungary’s efforts on this can be found in its [National Energy and Climate Plan](#).

nuclear power and coal⁴, with natural gas contributing to about a fifth of the total electricity generated in Hungary. The highest emitters among the domestic sectors are industry, transport, residential housing, and agriculture (Figure 3), although Hungary's agriculture is the least methane and NO emitter among European countries (Figure 4).⁵ Health costs stemming just from coal-fired power plants are estimated around 0.3-0.5 percent of GDP in 2013 (Schaible et al, 2016).

6. Recognizing the costs and risks of ~~air pollution~~ GHG emissions, over the years Hungary joined several international accords on climate issues and has made progress in meeting its commitments.⁶ Hungary reduced its GHG emission by 32 percent between 1990 and 2019, mostly due to the use of new technologies. By 2020, emissions not covered by the EU Emissions Trading System (non-ETS) had decreased by an estimate 9 percent from 2005 levels, while they were allowed to increase by 10 percent under the Effort Sharing Decision (Figure 5).^{7,8} Hungary has committed to reducing emissions by 7 percent under the ESR but this target might be subject to revision based on the new, at least 55 percent target.⁹ Proposals in that respect are expected in June 2021. Hungary's renewable energy objective is 13 percent of total energy supply. Already, solar generation capacities more than tripled (to 1,825 MW) between 2016 and 2020Q3 (Figure 6). However, progress on energy efficiency target has been less than intended, as in many other EU member states, as both primary and final energy consumption increased over 2014–19 (EC, 2019, 2020). For Hungary, a large increase in final energy consumption was observed in industry. Energy efficiency in the residential sector also remains weak. Thus, Hungary might miss its 2020 energy saving target, largely because household energy consumption per capita remains 12 percent higher than the EU average, even though income levels are considerably lower (Figure 7).

7. At the country level, Hungary has reaffirmed its commitment to combating climate change by adopting a number of action plans and through legislative action. The final National Energy and Climate Plan (NECP) was adopted in January 2020, while the Climate Protection Act (Act XLIV of 2020 on Climate Protection, CPA) and the Climate and Environmental Protection Action Plan (CEPAP) took effect in mid-2020. Additionally, the first Climate Change Action Plan (CCAP) was elaborated, and adopted in 2020, including adaptation, mitigation, and awareness-raising measures.

⁴ The coal industry has been relying on heavy direct (now discontinued at the central level) and indirect subsidies in Hungary, which exceed the value added reported by the industry by a vast margin (IMFa, 2019).

⁵ Efforts to reduce GHG from agriculture need abatement policies that are multi-pronged and well-calibrated at EU level, but fiscal policies at a national level can also be targeted to improve mitigation.

⁶ These include: United Nation Framework Convention on Climate Change, Montreal Protocol; Kyoto Agreement (UN); EU obligations including the Effort Sharing for 2013-20 and 2021-2030; 2015 Paris Agreement (UN); and, 2020 EU Green Deal.

⁷ OECD (2019).

⁸ The Effort Sharing legislation establishes binding annual GHG emission targets for Member States for the periods 2013–20 and 2021–30. The national targets will collectively deliver a reduction of around 10 percent in total EU emissions from the sectors covered by 2020 and of 30 percent by 2030, compared with 2005 levels.

⁹ 2020 targets are not under the ESR but governed by the previous Effort Sharing Decision.

remain limited. In 2015, the gap varied considerably across countries with Switzerland at 27 percent, and Russia at 100. It stood at 66 for Hungary. In particular, the housing sector in Hungary has one of the highest carbon pricing gaps. Figure 12 illustrates how low the effective price on residential emissions is in Hungary. The transport sector, however, is priced at above €60 per ton of CO₂ (cumulative) in Hungary, as in almost half of the sampled countries (Figure 13).

