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How the EU provides lifebelts for autocratic regimes

The European Commission could cripple Hungary's semi-authoritarian regime — but it won't

The European Commission's suggestion to suspend one-third of Hungary's EU budget allocation and the European Parliament declaring the country a 'non-democracy', suggests a new elevation to the EU institutions' fight against authoritarian Member States. However, even this time, the conflict might not end with a breakthrough but with some soft compromises. While the desire to keep EU unity and avoid plunging Hungarian state finances into ruin is politically understandable, this clearly shows, once again, how the EU provides lifebelts for autocratic regimes in its ranks to survive for the simple reason that it lacks a strategy to engage and re-democratise them.

Hungarian cooperation

September 2022 has witnessed two crucial developments in the European Union's more than decade long struggle to address the authoritarian developments in Hungary. On 15 September a European Parliament resolution, passed with a comfortable majority of 433 in favour, 123 against and 28 abstaining, declared that since 2010 Hungary has evolved to a 'hybrid regime of electoral autocracy', hence it cannot be considered a democracy any longer. Although, among leading democracy measuring indices — like V-Dem or Freedom House — there was a consensus on Hungary's authoritarianism for many years, it was the first time that a representative political body made such an astonishing judgment about the ruling Orbán-regime.

As shocking as the conclusion of the European Union appears to be, it is still accommodating non-democracies, as the immediate political implications of the EP resolution might be rather limited. This is definitely not the case, however, with the seemingly bold move of the European Commission's proposition to suspend EUR 7.5 bn — close to one-third of Hungary's national allocations under the EU Multiannual Financial Framework (MFF) 2021-2027 — due to breaches of the rule of law. This might have far-reaching consequences for the Hungarian state finances.

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Over the past two years the European Commission significantly improved its toolkit designed to enhance rule of law and impose sanctions over Member States disregarding fundamental EU values. The suspension of the European Recovery and Resilience Facility resources (ERRF; colloquially: the Corona Recovery Package) and the triggering of the Conditionality Regulation against Hungary's government left the impression that the Commission drew its lessons from its decade long failure.

As a matter of fact, the suspension of the EUR 5.8 bn Corona Recovery Fund and the prospect of further EUR 7.5 bn financial penalties under the Conditionality Regulation started shaping Hungary's governmental behaviour as early as June. In contrast to Poland, which refused any further concessions with regard to rule of law in order to de-block the country's ERRF appropriation, the Hungarian government became increasingly cooperative. For good reasons.

A fragile success

While the Russian war of aggression against Ukraine benefited the government of Prime Minister Orbán in the short term and helped him achieve a victory at the April general elections, in the long term the war's economic impact will heavily hit and destabilise his government. Due to the economic implications of the Covid-19 pandemic as well as the pre-election expenditure hike, Hungarian state finances became imbalanced and in certain respect are in worse shape than in 2009-2010, immediately after the 2008 economic crisis. While the inflation induced surge of VAT-revenues may stabilise the budget deficit in the short term, most likely remaining below the deficit level of 7 to 8 per cent expected at the beginning of the year, Hungary is facing one of the worst inflation rates within the EU. Which is predicted to peak close to 20 per cent at the end of the year. This, together with the deep-diving currency exchange rates, makes the financing of the country's external debt difficult, while the debt-per-GDP ratio has risen above 80 per cent and is on eye-level with the debt values from 2008-2009.

Against this background, gaining access to external funding is essential for the Hungarian government to avoid a downgrading of its credit ratings and a potential mid-term default. As the country has no other strategic option for external funding but the European Union, the Hungarian government started addressing the corruption, rule of law and public tendering related complaints of the European Commission in a seemingly constructive way, promising closer cooperation with the EU Anti-Fraud Office (OLAF), decreasing the share of single-bidder tenders, establishing a new Integrity Authority to combat corruption, and increasing the quality of legislation through regular public consultations in the legislative process.

In the words of budget commissioner Johannes Hahn, who praised the Hungarian government's constructive approach while he announced the EUR 7.5 bn budget cut proposal on 18 September, the European Commission appreciates the efforts of the Hungarian government and appears to be ready to close the conflict with a compromise if the Orbán regime provides enough guarantees that may safeguard EU financial interests in Hungary from rampant political corruption.

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This approach of the European Commission is understandable if one considers short-term realist arguments. First, the Hungarian regime has already demonstrated that it is ready to block strategic European decisions with regard to Russia, hence the European Commission may be reluctant to push Orbán into a political war.

Second, with no prospect to EU external funding, financial markets may become nervous, prompting a further collapse of the Hungarian state finances. The European Commission is definitely not interested in a Member State defaulting; thus, it has to keep the Hungarian economy afloat, which is severely limiting its policy options as well as the credibility of its threats vis-á-vis Budapest.

Third, even if the Commission would be committed to playing hardball with Orbán and propose the suspension of EUR 7.5 bn to the Council - the EU decision making body acting with qualified majority according to the Conditionality Regulation - it is uncertain whether Member States will let the Commission proposal fly or fail. Following the outcomes of this weekend's Italian elections, the resurrection of the Polish-Hungarian anti-EU alliance, and the continuous existence of Central European solidarity, the chances of imposing financial sanctions on Hungary appear to be rather weak in the Council. Timing, once again, works for Orbán in this game.

Recognising undemocratic bias

What could the European Commission do to avoid the accusations that it once again makes a foul compromise, giving-up real leverage over the Hungarian government for smoke and mirrors? Hungary is not democratic with systemic deficiencies when it comes to rule of law, and the institutional guarantees offered by the Hungarian regime should be evaluated through this lens. Whatever is promised by Budapest with regard to the independence of the new Integrity Authority, at the end of the day, the institution will operate in a politically deeply biased constitutional framework which will fundamentally determine its leeway.

Acceptable institutional guarantees can only be found outside of the Hungarian legal and constitutional system, at the level of the European Union. Even if access to EU-funds cannot be legally conditioned to joining the European Public Prosecutor's Office (EPPO), the Commission should insist that — given the rule of law situation in Hungary — the only acceptable guarantee in exchange of the termination of the Conditionality Regulation procedure is actually Hungary joining the EPPO. That could be a significant achievement on the Commission's end and perhaps a real game changer regarding Hungary's authoritarian track. Whether the Hungarian government is desperate enough to make this concession, is to be seen. But without exploiting the opportunity and pushing Budapest hard, the Commission is just heading once again to a bad compromise that will keep the EU's non-democrats on a badly needed external lifeline.

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