The forecast of GKI Economic Research Co. for 2022

(Summary of the forecast of GKI Economic Research Co. as of December 21, 2021)

The trajectory of the Hungarian economy in 2021 was more favourable in terms of GDP growth than expected in the budget for 2021 amended at the beginning of summer. At the same time, equilibrium conditions turned out to be much worse than planned, with inflation and the general government cash deficit soaring, the forint weakening and the external balance turning into a significant deficit. A considerable part of the divergence can be attributed to the excessive use of demand stimulus policies, which can be linked to the elections. At the same time, the escalating conflict with the EU, which led to the withholding of transfers, as well as unfavourable developments in the global economy, such as the energy price hike and the related deterioration in the terms of trade, and global supply disruptions (e.g., chip shortages), also played an important role.

The recovery from the crises caused by the pandemic was achieved in 2021 in the sense that the GDP production of the Hungarian economy exceeded its pre-pandemic level. This in itself predicts a slowdown in growth. After an increase of 6.7 per cent in 2021, a GDP growth rate of around 4.7 per cent is expected in 2022. This is also supported by the fact that improving the equilibrium situation necessarily requires a reduction in demand stimulation, including investments that have less impact on households. The government has already taken some small steps to this direction (such as postponing some investments), and the tightening of monetary policy is starting to be more pronounced in terms of more aggressive interest rate hikes and the announced end of government and corporate bond purchases. If meaningful corrective action is taken, growth could be slower than the current GKI forecast and a more favourable equilibrium situation could emerge, which would be desirable for a sustainable equilibrium. The change in social and economic policy is also justified by the need to resolve the strained relationship with the EU, which is threatening to result in significant financial losses, and for this the Hungarian position needs to be reviewed. The Hungarian economic policy of the past decade has become unsustainable, but substantial changes can only be expected after the elections.

Despite the economic and social problems caused by the fourth wave of the pandemic, the European economic outlook remains favourable, with the **EU's economic sentiment index falling within the statistical margin of error in November** and fluctuating in a narrow but high band since August. **GKI's economic sentiment index** fell back to its summer level in December. The confidence index for all sectors declined, whereas that for consumers improved after a sharp fall in November. Companies' willingness to hire is strong but declining, their efforts to raise prices are strengthening, and they are pessimistic about the future of the Hungarian economy. However, households are more optimistic about these issues than they were in November.

GDP increased by 7.1 per cent in the first three quarters compared to the same period in 2020. The **role of industry and foreign trade declined sharply** in the third quarter, and this is expected to continue in the final quarter of this year. GKI expects economic growth to be between 4.5 per cent and 5 per cent in the fourth quarter, and thus **around 6.7 per cent for 2021 as a whole**, broadly in line with the forecast of the Ministry of Finance. **An increase of 4.7 per cent is likely in 2022.** Hungary's GDP growth is expected to be among the CEE region's best in 2021, but only weak to medium in 2022, due to the need to address equilibrium problems.

In 2021, average real earnings are projected to rise by 3.5 per cent, real pensions (due to the high pension premium and the payment of the first week of the 13th month pension, despite some disputes about its lagging slightly behind the inflation rate) by 4 per cent, **real income is expected to increase by 4 per cent, and household consumption by 3.5 per cent** (but within this, purchased consumption is growing faster). In 2022, **gross earnings** will rise by an average of less than the minimum wage, by around 14 per cent, resulting in an increase in real earnings of 8-9 per cent. The real value of **pensions** grew by 6 per cent. **Real incomes will mount by about 7 per cent and consumption by 4.5 per cent. Investments** may rise by 8 per cent in 2021 and by 4 per cent in 2022. A radical tightening of economic policy could lead to a **lower rate**.

The info-communications, financial and trade sectors did not fall even in 2020, and by 2022 all sectors will **reach their pre-crisis GDP levels**, with the exception of tourism, the entertainment industry and agriculture, which has been declining for the third year running. One of the big questions for 2022 is **how far Hungarian industrial exports will find their way**, which will depend to a large extent on the state of global production chains. **Employment** is expected to rise by 0.5 per cent in 2021 and 2022, whereas the **unemployment rate** is expected to be around 4 per cent.

Banks plan to increase their corporate and retail **lending** in 2021 and 2022. At the same time, the rise in interest rates and the full expiry of the moratorium on repayments in the middle of next year foresee a deterioration in the existing loan portfolio and a more prudent demand for credit, with a high degree of differentiation.

However, the general government **cash-flow deficit** was already HUF3931bn at the end of November, **almost the amount planned for the whole year**, partly due to delays in EU transfers. In December, the government decided to postpone investments worth HUF350bn, and removed from the agenda the plan to buy Budapest Airport in 2021, which was not included in the budget. It is also possible that the **end-of-year spending** will be lower than previously thought. The accrual-based government deficit-to-GDP ratio is expected to be around the projected 7.5 per cent, the second highest in the CEE region after Romania. Taking into account the impact of higher revenue outflows and higher inflation, the traditional income redistribution before the forthcoming 2022 elections **would lift the 2022 general government deficit by around HUF1,000-1,100bn**. For this reason, the government has also **started some tightening** for 2022, with a 0.2 percentage point increase in the special retail tax (which is also unfavourable from an inflationary point of view). It is also possible that other sectoral tax increases could be considered. **Cutting back on domestic advances of EU transfers and cancelling some investments could be the main tools for further deficit reduction.** This should also help to meet the deficit target of 5.9 per cent of GDP in 2022, which would already be the highest in the CEE region.

Inflation will be around 5 per cent in both 2021 and 2022, the euro **exchange rate** could be around HUF358 in 2021 and HUF360 in 2022 after HUF351 in 2020, while the **key interest rate** could reach 4.5 per cent by autumn 2022, the expected value of inflation at the end of the year in the favourable case.

Although the **current account balance** is deteriorating at an accelerating pace, the external financing capacity could return to a surplus in 2022 after a deficit in 2021, subject to the settlement of the ongoing disputes with the EU and the disbursement of transfers.

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	2018	2019	2020	2021	2022	
	(fact)			(est.)	September	December
GDP	105.4	104.6	95.0	**106.7**	105	**104.7**
• Agriculture (1)	105.2	98.0	91.3	**99.0**	100	**100**
• Industry (2)	102.6	103.0	93.0	**111**	107	**107**
• Construction (3)	115.2	113.1	89.1	**111**	106	**104**
• Trade (4)	110.6	105.8	100.9	**107**	105	**107**
• Commercial lodgings and catering (5)	107.5	104.8	57.5	**101**	115	**115**
• Transport and storage (6)	107.0	105.2	89.5	**105**	104	**104**
• Information, communications (7)	110.5	110.3	105.0	**111**	106	**106**
• Financial services (8)	105.2	113.7	104.1	**104**	103	**103**
• Real estate services (9)	104.5	102.9	100.9	**102**	102	**102**
• Professional, scientific, technical activities (10)	109.1	106.3	95.1	**107**	102	**102**
• Public administration, education, healthcare (11)	100.9	100.6	96.7	**104**	103	**103**
• Arts, entertainment (12)	107.3	108.8	86.0	**103**	105	**105**
• Core growth	107.1	106.8	97.3	**107.7**	105	**104**
GDP domestic demand	107.1	106.6	97.3	**105.5**	103.5	**104**
• Private consumption	104.2	104.5	98.0	**103.5**	104.5	**104.5**
• Gross fixed capital formation	116.3	112.8	93.1	**108**	105	**104**
Exports (goods and services)	105.0	105.4	94.1	**110.5**	110	**110**
Imports (goods and services)	107.0	108.2	96.5	**109**	109	**109**
Consumer price index (preceding year = 100)	102.8	103.4	103.3	**105**	104	**105**
Unemployment rate (annual average)	3.7	3.4	4.3	**4.1**	4	**3.9**
General government balance in per cent of GDP (ESA)	-2.1	-2.1	-8.0	**-7.5**	-6	**-6**
Balance of the current and capital accounts						
• EUR billion	3.4	1.7	0.6	**-2**	3	**0.5**
• In per cent of GDP	2.5	1.2	0.4	**-1.3**	1.8	**0.3**

Source: HCSO, GKI

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