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External balance improvement under external pressure

According to the forecast of GKI Economic Research Co. prepared in co-operation with Erste Bank, the global economic crisis pushed the Hungarian economy onto a new development path. External imbalances are improving fast, but GDP will contract by 4-5 per cent. Real earnings will decrease by 2-3 per cent, purchased consumption by 5 per cent.

At present the fallout of general government revenues is projected to total about HUF400 bn-HUF450 bn compared to the plan included in the budgetary law. With low inflation–around 3.5 per cent even after the increase of VAT and the excise tax rates–and contracting demand corporate profits will decline substantially, therefore corporate tax revenues in the general government are likely to shrink as well. The less than expected volume of aggregate wages and purchased consumption (down by 5 per cent), too, diminish general government revenues. Value added and excise tax rates grow, but a certain part of additional revenues deriving from rate increases will be returned to taxpayers by the reduction of social security contributions and–to a lesser extent–personal income tax rates. General government expenditures are projected to be lower by HUF300 bn-HUF350 bn than those envisaged in the budgetary law. Freezing some expenditure items and cutting fiscal support account for a part of this sum. The general government deficit is anticipated to be about HUF100 billion higher than planned corresponding to 3 per cent of the smaller volume of nominal GDP. This is similar to the level of 2008 and it is acceptable in the given international environment.

The increase of government debt cannot be contained this year (similarly to many European countries!). If Hungary draws all or most part of the international stand-by loan, technically gross government debt may exceed even 80 per cent of GDP, although this depends also on the exchange rate of the forint to the euro at year end. If most of the loan rests with the National Bank of Hungary as deposit, then the increase of indebtedness is the temporary price paid for enhanced foreign exchange reserves to ensure safe financing of international obligations. With consolidation these loans become unnecessary or may substitute for other, more expensive sources of external financing. As far as the non-cyclical component of government debt is concerned, Hungary does not stand out of the row of other EU-member states at all in the course of the crisis. According to the IMF, the average G20 general government deficit relative to GDP is expected to amount to 9 per cent and government debt will surpass 90 per cent of GDP already in 2009.

The shortage of financial sources in financial markets forces the reduction of external deficits. The external financing requirement is decreasing to €2 billion or 2.2 per cent of GDP in 2009 from €7.8 billion 2008. Foreign trade surplus increases substantially as a result of waning imports, and profit repatriation also decreases as profits go down, although interest payments rise. Net EU transfers climb to about €2.5 billion from €1.1 billion. The €2 billion deficit needs to be financed by net capital inflows or by the IMF-EU stand-by loan.

Real wages are to decrease by 1-2 per cent in the business sector and by 6-7 per cent in the public sphere. Incomes in the grey economy are also likely to rise to some extent. Real income of households will decrease by 1.5-2 per cent. The consumers' propensity to save increases spectacularly. This is the consequence of rising instalments of credit re-payment, hard access to more expensive credits, and of rising interest rates on deposits and higher required own resources, the saving of which takes time. The savings ratio will increase to at least 5 per cent of GDP.

Forecast of GKI Economic Research Co. on Developments in the Hungarian Economy in 2009

	2006	2007	2008	January 2009	2009 (forecast)
1. Volume of GDP (per cent)	104,1	101,1	100,6	-	95,5
2. Industrial production (constant prices per cent)	110,1	108,1	98,9	77,1	86,0
3. Investment in the national economy (constant prices per cent)	93,8	101,5	97,0	-	95,0
4. Construction (constant prices per cent)	98,4	85,9	94,9	84,0	95,0
5. Retail trade (volume index)	104,4	97,0	98,2	97,2	96,0
6. Exports (current prices in euro per cent)	116,6	115,7	105,6	68,8	93,0
7. Imports (current prices in euro per cent)	113,9	111,9	105,6	70,9	90,0
8. Trade balance (billion euros)	-2,4	-0,1	-0,2	-0,2	2,0
9. Combined balance of the current and capital accounts (billion euros)	-6,2	-5,4	-7,8	-	-2,0
10. Average exchange rate of euro (forints)	264,3	251,3	251,2	294,2*	290
11. Deficit of the general government (cash flow basis, without local governments; billion forints)	2034	1291	907,1	256,6**	750
12. Index of average gross earnings	108,1	108,2	107,5	94,8	102,0
13. Consumer price index	103,9	108,0	106,1	103,1**	103,5
14. Consumer price index at the end of the period (corresponding month of the previous year=100)	106,5	107,4	103,5	103,0**	104,5
15. Rate of unemployment (at the end of the period, per cent)	7,5	7,7	8,0	9,1***	9,3

* first quarter 2009
** January-February 2009
*** December 2008 – February 2009
Sources of actual data: CSO, NBH, MoF