HUNGARY

INVESTMENT: A STRATEGY TO BOOST ECONOMIC GROWTH

In 2024, Hungary is expected to be among the region's worst performing economies, entering a technical recession in Q3. Real GDP growth is one of the government's priorities, with an official target of 3% to 6% next year. The budget for 2025 recently submitted to Parliament aims at both revitalising the economy and consolidating public accounts. However, medium-term potential growth, estimated at 3% by the IMF, has been revised upwards compared to its 2019 estimate. In particular, it is buoyed by favourable prospects for FDI, particularly from China, which would support investment.

FOCUS ON GROWTH IN 2025

Contrary to expectations, Hungary entered a technical recession in Q3 2024 with a decline in GDP of 0.7% q/q after -0.2% q/q in Q2. The details of the national accounts have not yet been published, but investment and external demand are expected to have contributed significantly to this economic contraction. Investment, which has been sluggish since September 2022, fell significantly in recent quarters (-13.3% y/y in Q2, -8.6% in Q1), and more sharply than in neighbouring countries. In addition, industrial activity is suffering from the weakening German economy. On the other hand, consumption, which has been recovering for the past two quarters, has held up well probably thanks to rapid growth in real wages (+10.2% y/y on average over the first eight months of the year), strong retail sales and improved surveys on purchasing intentions for durable goods. With a carry over of only 0.6% at the end of Q3, real GDP growth will be weak this year, after -0.8% in 2023.

For 2025, economic growth is clearly stated as a priority for the Orban government with a target of 3% to 6%. The support measures aimed at revitalising the economy, the details of which are not yet known, will focus on access to housing, the convergence of the minimum wage towards the average wage and support for SMEs. Moreover, households can now use their pension fund to finance real estate projects (buying a home, renovation). In any case, the high end of the growth target range seems difficult to achieve without a substantial budget. Apart from consumption, other sources of growth are limited. The moderate upturn in the German economy expected in 2025 suggests only a slight improvement in external demand. Similarly, the recovery in investment is likely to be postponed until 2026, taking into account the likely continuation of the blockage of part of the European funds used to finance public investment. The rise in electoral uncertainties in the second half of 2025 (general elections scheduled for April 2026) should lead to the postponement of private investment projects.

FORECASTS

	2021	2022	2023	2024e	2025e
Real GDP growth, %	7.1	4.3	-0.8	1.4	2.3
Inflation, CPI, year average, %	5.1	14.5	17.6	3.6	3.5
General gov. balance / GDP (%)	-7.2	-6.2	-6.7	-5.0	-4.7
General gov. debt / GDP (%)	76.2	73.8	73.4	74.8	75.3
Current account balance / GDP, %	-3.9	-8.5	0.8	2.1	1.4
External debt / GDP, %	86.5	91.9	85.9	88.4	90.2
Forex reserves, EUR bn	38.4	38.7	41.4	46.9	52.0
Forex reserves, in months of imports	3.8	3.0	3.4	4.1	4.4

TABLE 1 — e: ESTIMATES & FORECASTS — SOURCE: BNP PARIBAS ECONOMIC RESEARCH

CENTRAL EUROPE: INVESTMENT GROWTH IN VOLUME TERMS

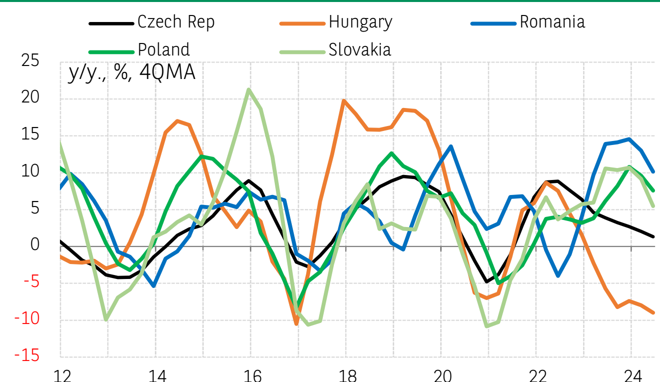

CHART 1 — SOURCE: EUROSTAT, BNP PARIBAS

UPWARD INFLATIONARY PRESSURES

Inflation has fallen significantly in recent months. It reached 3.2% y/y in October (the peak was 25.6% y/y in January 2023). It is now slightly above the Central Bank target of 3% but could rise again to 4% y/y by December 2024. Food prices have recently started to rise once again. Disinflation in the services sector is slowing. Wage pressures will remain sustained in the short term due to the expected increase in the minimum wage to 50% of the average wage by 2027. This increase would be in stages, probably at a rate of 10 to 15% per year. The fiscal measures on financial transactions, introduced in August, will only have a moderate impact on total inflation, in the order of +0.1 points this year and +0.2 to 0.3 points in 2025 according to Central Bank estimates. Inflation is not expected to return to its target before 2026.

A SHORT-TERM MONETARY PAUSE

Monetary easing, which began in October 2023, continued uninterrupted until July. A further drop of 25 basis points (bps) took place in September 2024, bringing the key rate to 6.5%. However, the rather aggressive pace of easing at the start of the cycle, at 50-75 bps at each meeting, has slowed since last June.

Last October, the Central Bank once again opted for a pause, which is expected to last longer this time. This new direction is due to core inflation remaining high (4.5% y/y in October) and higher than overall inflation. Downward pressures on the Hungarian forint were undoubtedly a factor in the Central Bank's decision.

WEAK BUDGETARY CONSOLIDATION

Consolidation efforts since 2022 have failed to significantly reduce the budget deficit over the past two years. Along with six other European Union countries, Hungary has been placed under the excessive deficit procedure for failure to comply with the budgetary rules that came back into force this year, after a short period of suspension. In 2024, even if the budget deficit is expected to ease slightly, it will still be well over 3% of GDP due to the still high burden of debt interest payments (4.7% of GDP in 2023). The cost of financing on the bond market is the highest in the region, with a yield differential of 444 bps between 5-year Hungarian and German government bonds. However, the Hungarian government has made use of international markets to finance itself at lower interest rates. It raised funds on the Japanese market twice in 2024.

For 2025, large-scale fiscal consolidation is unlikely due to concerns about growth and the electoral calendar (general election scheduled for 2026). The budget for 2025 is banking on a deficit of 3.7% of GDP, but economic growth projections of 3.4% are optimistic. Public debt, at 73.4% of GDP in 2023, is the highest in Central Europe. It is expected to increase over the next two years, then gradually fall to below 70% (but far from the 60% threshold) by 2029/2030, thanks in particular to a primary surplus expected from 2027/2028 onwards.

THE WINDFALL OF CHINESE FDI

According to the latest UNCTAD figures, Hungary received the equivalent of USD 119 billion in cumulative foreign direct investment (FDI) at the end of 2023. In the region, Poland led the way with FDI stock worth USD 335 billion, ahead of the Czech Republic with USD 216.6 billion. However, Hungary ranks second ahead of Poland when FDI is considered as a share of GDP.

In 2021 and 2022, net FDI inflows reached record levels at 5.6% and 8.3% of GDP, respectively. In 2023, they returned to pre-Covid levels, but a rebound in these flows is expected in the coming years. Overall, these FDI inflows have mainly benefited the automotive and services sectors. In addition, there is a change in the geographical composition of the FDI stock, with a significant increase in the share of Asian countries, particularly South Korea and China, to the detriment of the American continent and, to a lesser extent, Europe. Over the recent period, China has positioned itself as a significant investor. According to Rhodium Group, Hungary receives a significant proportion of Chinese FDI for Central Europe. In Hungary, the total stock amounts to USD 6.7 billion, out of a total of USD 414.7 billion in Europe.

These observations are in line with the Hungarian government's strategy in the electric mobility sector. Hungary aims to become a major player in the field of batteries for electric vehicles.

HUNGARY: CUMULATIVE VALUE BY INDUSTRY

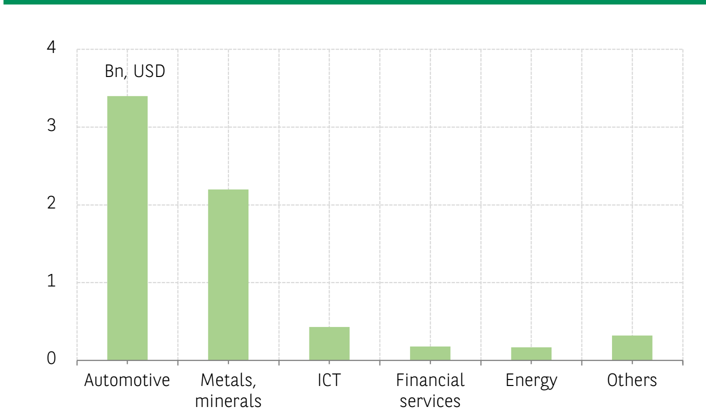

CHART 2 SOURCE: RHODIUM GROUP, BNP PARIBAS

On the European level, Hungary is expected to become the second largest supplier by 2030, after Poland. Moreover, the country is relying on local production of electric vehicles with the production site of the Chinese company BYD, which is expected to be operational in two years. This strategy goes with incentives, including tax benefits, aimed at increasing the attractiveness of Hungary. The country is in fact offering one of the lowest corporate tax rates in Europe at 9%, compared to 19% in Poland and the Czech Republic, and 29.9% in Germany.

The prospects for FDI remain strong in the short term, given greenfield investment projects announced over the last three years (2021: USD 6.3 billion, 2022: USD 12.5 billion, 2023: USD 9.2 billion). Chinese FDI is likely to increase in 2025 and 2026 as protectionist measures on Chinese electric vehicles, which already exist in Europe, are expected to intensify in the US after Donald Trump's recent presidential election victory. Hungary is an attractive production and export base for the EU, enabling Chinese producers to bypass tariff measures. In the long run, the domestic market could also be affected, although for the time being new car registrations in Hungary still show a clear preference for European (54%) and Japanese makers (33% in 2023). Nevertheless, two factors could mitigate the prospects for FDI, including weakening activity in the automotive sector and a possible extension of the timeframe for the transition to electric vehicles in the US or Europe.

In the medium term, the outlook for Asian FDI in Hungary, particularly Chinese FDI, should revitalise investment and support potential growth. The IMF estimate of Hungary's potential growth is now 3%, an increase of 1 point compared to its previous 2019 estimate. In the short term, however, caution remains necessary. The revitalisation of investment will struggle to fully materialise if a proportion of European funds remains blocked (around EUR 20 billion). As a matter of fact, in 2022, total investment in volume remained low, despite the record year recorded for FDI.

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