HUNGARY

CAUTIOUS OPTIMISM

After an expected recession in 2023, better growth prospects lie ahead in 2024. Economic activity is expected to be driven by both an improvement in domestic demand and a slight rebound in growth in the Eurozone. The monetary easing cycle initiated at the end of 2023 should continue, albeit cautiously, due to the persistence of strong wage pressure. External accounts remain strong, with foreign exchange reserves having increased for several years. Hungary is expected to post a current account surplus in 2023, after a deficit of -8.2% of GDP in 2022. As to public accounts, the budget deficit has continued to deteriorate, and is expected to exceed 5% of GDP in 2023. Like many European countries, Hungary may face an excessive deficit procedure in 2024.

RECESSION IN 2023 FOLLOWED BY MILD RECOVERY IN 2024

Hungary is one of the worst performing economies in the region, with negative growth expected for 2023. Over the first three quarters of 2023, real GDP fell by 1.2% y/y, primarily due to weak domestic demand (-6.0% y/y over the same period). The higher cost of credit and high inflation weighed in heavily. Net exports of goods and services, by contrast, contributed positively to growth and only partially offset the contraction in domestic demand.

In Q4 2023, economic activity was a mixed bag judging by economic indicators. On the one hand, industrial production fell below its pre-Covid-19 level in November and fell across all sectors. New car registrations, on the decline since last April, have continued their downward trend (-3.5% in 2023). On the other hand, household purchase intentions for durable goods in the coming months and the household confidence index have improved. The increase in real wages in the manufacturing sector, which has turned positive since last August (+1.3% y/y in August, +2.8% in September and +5.6% in October), argues in favour of a rebound in consumption.

Economic growth prospects are expected to improve in 2024, but should remain modest. Consumption will be buoyed by lower inflation, the upward revision of pensions (+6% in 2024 and payment of a premium in February), of the minimum wage (+15% in December 2023) and of wages for certain categories of civil servants (+32.2% for teachers in January 2024, +20% for nurses in March). Similarly, the expected easing of lending conditions, brought by recent central bank policy rate cuts and new support measures for first-time buyers (interest payment subsidies through the CSOK Plus programme), will revitalise the property sector and the credit market. Nevertheless, some caution remains necessary. The expected increase in public investment remains conditional on the release of European funds this year. Similarly, the outlook for private investment remains uncertain as the extension of windfall taxes in certain sectors (introduced in 2022) up to the end of 2024 could discourage the implementation of new projects. The expected recovery in Hungarian exports could be disappointing in the event of weaker growth prospects in the euro area.

MONETARY EASING

In 2023, Hungary recorded the highest inflation rate amongst European Union countries, at 17.5% on average. By way of comparison, inflation stood at 5.5% in the euro area over the same period. Inflation reached 11% in Poland, 9.8% in Romania, 12% in the Czech Republic and 8.7% in Bulgaria. A positive point is that inflation has fallen significantly from the peak of 26.2% seen in January 2023 and in particular, since September, so that Hungary is now posting a lower figure than Central European countries.

FORECASTS

	2021	2022	2023e	2024e	2025e
Real GDP growth, %	7.2	4.6	-0.5	3.3	3.2
Inflation, CPI, year average, %	5.2	15.3	17.5	4.8	3.6
General gov. balance / GDP (%)	-7.2	-6.2	-5.9	-3.8	-3.2
General gov. debt / GDP (%)	74.5	70.6	67.1	65.0	64.3
Current account balance / GDP, %	-4.1	-8.2	0.5	0.5	0.6
External debt / GDP, %	87.3	91.0	81.0	79.6	83.3
Forex reserves, EUR bn	38.4	38.7	41.4	43.0	46.0
Forex reserves, in months of imports	3.8	3.0	3.5	3.6	3.7

TABLE 1

e: ESTIMATES & FORECASTS
SOURCE: BNP PARIBAS ECONOMIC RESEARCH

INFLATION IN CENTRAL EUROPE

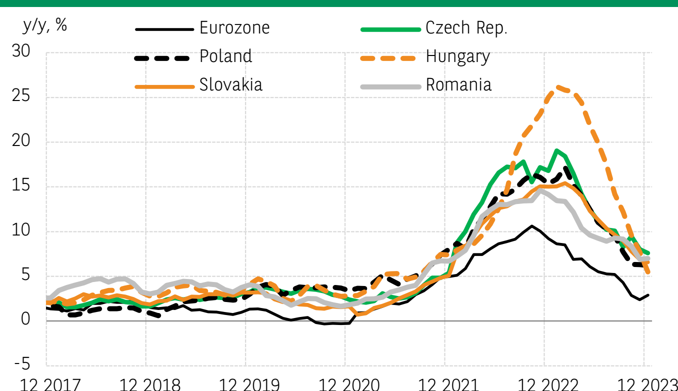

CHART 1

SOURCE: EUROSTAT, BNP PARIBAS

Last December, inflation stood at 5.5% y/y compared to 7.6% y/y in the Czech Republic, 6.6% in Poland and 7.0% in Romania. The rapid fall in inflation is attributed to a lower contribution from 'food' items to 1.3 percentage points in December, compared to 11.1 points in January 2023 and a negative contribution from the 'energy' item (-0.9 point).

Disinflation is expected to continue throughout 2024 without, however, reaching the Central Bank's inflation target of 3%. However, while prices on the international commodity markets may ease further, new taxes on fuel, toll and retail that came into force on 1st January 2024 will maintain upward pressure. Similarly, wages continued to grow steadily (+15.2% y/y in October 2023; +15.4% on average from July to September). The rise in the minimum wage of 15% for unskilled workers and 10% for skilled workers in December 2023, along with the expected impact on wage pressure in other professions, should keep core inflation at high levels. A return to the inflation target zone is not expected before 2025.

The slowdown in inflation has enabled an easing of monetary policy since the end of 2023. The monetary authorities cut their key rate by 300 basis points cumulatively to 10.00% in January 2024. Recent comments from the Central Bank suggest that monetary easing should continue in the coming months, but room for manoeuvre remains limited due to wage pressure.

HEADING FOR AN EXCESSIVE DEFICIT PROCEDURE IN 2024

With inflation, the public debt-to-GDP ratio is expected to improve further in 2023 and fall below the 70% mark, even though economic growth has weakened. That said, the budget deficit has remained elevated since 2020 (-7.6% of GDP, -7.2% in 2021 and -6.2% in 2022) due to the multiple shocks faced by the economy, which have in turn led to an increase in government spending.

The budget deficit would have been more pronounced without the fiscal consolidation efforts since summer 2022, which included the introduction of a tax on exceptional profits and the removal of price caps on fuel in 2022 and on foodstuffs in 2023. In 2023, the deficit is expected to reach 5.9% of GDP, compared to the 3.5% forecast pencilled in the budget. Government interest payments, estimated at 4.3% of GDP (2.8% in 2022), have increased significantly and are now among the highest in the EU. This surge is primarily attributable to interest paid on inflation-linked bonds. In addition, the extension of energy subsidies, pension hikes (+15% in 2023), plus the supplement paid to pensioners, have weighed on expenditure. The participation in certain companies has resulted in exceptional disbursements. And lastly, the authorities have funded some projects that were supposed to be financed by European funds, suspended by Brussels. For 2024, the authorities are predicting a less pronounced deficit than last year but higher than 3% of GDP. Interest costs will still be higher than 4% of GDP. To bring the budget deficit back below 3% of GDP, a large primary surplus will be necessary, and this is unlikely this year. Since 2020, the country has recorded a primary deficit (-5.2% in 2020, -4.9% in 2021 and -3.4% in 2022), and this will probably still be the case in 2024, even if a significant reduction is expected.

As a result of an expected deficit exceeding 3% of GDP in 2024, Hungary, like many EU countries, will have difficulty avoiding an excessive deficit procedure. In fact, the escape clause concerning the Stability and Growth Pact, temporarily introduced during the Covid-19 pandemic, came to an end on 31st December 2023.

HUNGARY: GOVERNMENT'S INTEREST PAYMENTS

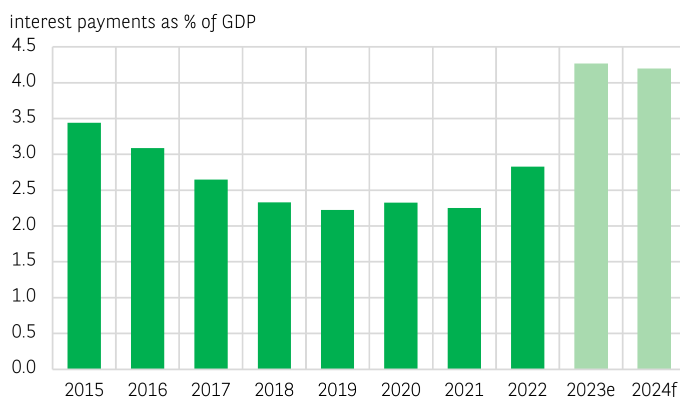

CHART 2

SOURCE: CENTRAL STATISTICAL OFFICE, BNPPARIBAS

Nevertheless, public debt remains sustainable. The temporary suspension of the issuance of inflation-linked bonds (13% of public debt) and lower inflation should ease the burden of interest payments. Moreover, fiscal consolidation efforts and the gradual withdrawal of support measures related to the energy shock suggest that Hungary should return to a primary surplus by 2025/2026. In addition, the debt profile has improved since 2011. The share of government debt denominated in foreign currency (mainly in euros) fell sharply (26.9% of the total in 2023 according to the Hungarian debt management agency (AKK) compared to 50% in 2011). The share of fixed-rate debt is in the order of 68.6% of the total. However, financing needs remain high and are unlikely to improve significantly in the medium term. Gross government bond issuances are estimated at HUF 10,273 billion in 2024 (around 12% of GDP), including HUF 2,515 billion to cover the financing needs of the government budget.

SOME IMPROVEMENTS

External accounts have improved. After a deficit of 8.2% of GDP in 2022, the current account is expected to once again generate a surplus in 2023 (EUR 0.5 billion over the first nine months cumulatively) owing to a reduction in the energy bill. Similarly, net capital flows were resilient over the first three quarters overall, at EUR 3.5 billion. Foreign exchange reserves increased to EUR 41.4 billion in 2023, with an import cover ratio of 3.5 months.

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