Hungary's macroeconomic situation; bilateral economic relations with Greece

1) Economic situation in Hungary

In terms of macroeconomic developments, 2012 was a somewhat controversial year for Hungary. In certain areas the country achieved outstanding results, whereas in some other fields the performance was not yet satisfactory. Some of the major indicators are very promising and enviable in European comparison, whereas certain others must definitely be improved in 2013 and the following years.

		2010	2011	2012
Population	million	10.0	10.0	10.0
GDP at current price	billion EUR	98.0	100.0	97.7
real GDP growth	%	1.2	1.6	-1.7
GDP per capita (current price)	EUR/capita	9 800	10 000	9 770
Inflation (annual average)	%	4.9	3.9	5.7
Unemployment	%	11.2	10.9	10.9
Current account balance	% of GDP	1.1	0.9	1.6
Budget balance	% of GDP	-4.3	+4.3	-1.9
Government debt (end of year)	% of GDP	81.8	81.4	79.2

Positive results in 2012 – fiscal discipline was exemplary:

a. Government deficit was kept well within the Maastricht limit and it is 1.9% of GDP. This means that Hungary has fulfilled the relevant Maastricht criterion for the second year in a row. What's more, in its latest report the European Commission acknowledged that our 2013 budget also gave enough guarantee for the trend to continue. Although there's still some discussion regarding the 2014 budget (about which we cannot really know anything yet), but now we can reasonably expect that the EU will soon terminate the excessive deficit procedure (EDP) that has been in progress ever since Hungary joined the European Union. In late 2011 the Council decided upon the withholding of some of the structural funds earmarked for Hungary because of the excessive deficit. Then in spring 2012 the decision was reversed but the EDP is still pending. The Hungarian Government is committed to ensure that the excessive deficit procedure be finally terminated in 2013.
b. Hungary was one of the best performers in terms of decreasing government debt in 2012. Actually, in this regard, only Greece could achieve more significant reduction but Greece's result was due to the debt write-off and restructuring measures. Government debt has been on a decreasing path since 2010, at the end of 2012 it was 79.2% of GDP.
c. Trade and current account balances have continued to be steadily positive, following the trends of the preceding two years. Exports and imports have only grown very moderately, 0.1 and 0.5% respectively, giving a positive trade balance of EUR 6.8 bn. (Exports reached EUR 80.1 bn, imports were about EUR 73.3 bn.) Foreign direct investment inflow has gained momentum in 2012 with new investments worth about EUR 3 bn, and by year end the total stock of FDI was over EUR 75 billion. In the

Central European region this is the highest figure compared to the GDP, and second highest per capita.

d. Unemployment figures have stayed stagnant, although in international comparison they are still not bad: 10.8% at the end of 2012. The number of employed persons have increased somewhat, but this is to a large extent due to the Government's public work scheme for unemployed persons. There is a need to create more jobs in the private sector and the Government is taking measures in this direction (Job Protection Action Plan, state subsidies for job-creating investments in the SME sector, simplified taxation system for SMEs).

Figures to be improved:

e. Instead of the originally planned slight positive growth, GDP dropped by 1.7%. This is partly due to the austerity measures that had a negative effect on growth; partly due to adverse weather conditions that badly affected agricultural output (causing losses equal to almost 1% of the GDP); partly due to the unfavourable international conditions, slow growth in the world and slight decline in the EU.
f. The rate of investment has dropped to a level that can hardly make up for the depreciation (investment rate: 17.2%).
g. Lack of liquidity is a major problem in the Hungarian economy, too. Banks have drastically reduced the amount of new credits, and there has been a very significant capital transfer from the Hungarian banking system: in the 12-month period until end of September 2012 foreign parent banks withdrew some EUR 7.9 bn from their Hungarian subsidiaries. In order to boost liquidity, the National Bank of Hungary announced a preferential Funding for Growth Scheme and a foreign exchange swap facility in early April 2013. In the framework of the Funding for Growth Scheme the Bank will provide HUF 250 bn [EUR 862 million] to the commercial banks at 0% interest rate to boost their lending to SMEs at a maximum interest rate of 2.0% (plus max. 0.5% guarantee fee). Additional HUF 250 bn will be provided under the same conditions, to convert SMEs' FX loans into HUF debt. In the third pillar of the plan, the central bank offsets the liquidity boosting effect of these steps, by providing FX swaps from its surplus FX reserves for commercial banks. This substantial program provides for SME lending a total of almost 2% of GDP.
h. Inflation in 2012 was high at 5.7%; Hungarian forint was too volatile and rather weak at the beginning of 2013. However, inflation forecast for 2013 is optimistic, it might be at around the 3% maximum target set by the central bank, not the least due to the Government's measures that lower the households' power, heating and other utility costs.

2) Measures by the Government regarding the 2012 budget

- The Government managed to implement a very tight budget in 2012 with downsized expenditures in several areas and increased tax revenues from certain business sectors (retail, energy supply and public utilities, telecommunication, banking and financial institutions).[1]

[1] Decreasing state subsidies on drugs, freezing of procurements in government sector. The bank tax was introduced in 2010, and was originally due to be halved in 2012 and abolished in 2013. In 2011, these targets

- Crisis tax on banks and financial institutions: approximately EUR 0.5 bn budget revenue per year (calculated on the basis of the assets in banks' balance sheets).

3) Measures in the 2013 budget to keep the deficit under 3.0%

The Government compiled three sets of measures in late 2012 in order to keep the fiscal targets in year 2013. These measures will ensure that the deficit steadily remains under the Maastricht limit.

Key figures of the 2013 budget:[2]

- deficit target: 2.7%
- expected GDP growth: 0.9%
- inflation: 5.2%
- average EUR/HUF exchange rate: 1 EUR = 283.4 HUF

Fiscal effects of the measures related to the 2013 budget, announced in October and November 2012 (billion HUF):

	2013
Increasing the EU co-financing rate of projects	55
Hiring freeze, ban on parallel payment of wages and pensions	30
Postponement of the implementation of the career path model for teachers to January 2014	73
Improved targeting of social benefits	8
Abandonment of the regressive rates for social security contributions	51
Expansion of financial transaction tax to cash withdrawal, raising the payment required from the Treasury	60
Whitening of the economy (extension of reverse charge VAT to the swine sector, electronic connection of cash registers to the tax authority) and changes in the regulation of small business taxation	120
Halving of the special tax on financial institutions abandoned	72
Rate increase of financial transaction tax	130
Broadening of the local business tax base	35
Introduction of the utility tax	30
Increase of the healthcare contribution on fringe benefits	40
Further whitening of the economy (restriction of cash transactions between businesses, introduction of invoice level VAT return, reinforcement of the tax authority, more severe sanctions)	60
Increasing the dividends of Szerencsejáték Zrt.	10
Increasing revenues from the tax on on-line gambling	10
Expansion of the utility tax	30
Increase of the income tax levied on energy providers	40
Total	854

In total the above adjustment measures in 2013 add up to HUF 854 bn [EUR 2.95 bn] which is approximately 2.9% of the GDP.[3]

were put back by a year, and in November 2012 the tax was made permanent. Bank tax rates are calculated on the basis of banks' balance sheet totals.

[2] The Convergence Programme of Hungary, submitted to the European Commission in April 2013, corrected the GDP growth forecast to 0.7% and the inflation forecast to 3.1%.

[3] For all HUF/EUR conversions in this document, an exchange rate of 1 EUR = 290 HUF is used.

Social measures effective from 1 January 2013:

- Minimum wage increase from HUF 93,000 to HUF 98,000 [EUR 338], and from HUF 108,000 to HUF 114,000 [EUR 393] for skilled labour. According to the calculations of trade unions, this will enhance purchasing power of families by 2.2%.
- 10% decrease in gas, district heating and electricity prices (the potential for further decreases is currently evaluated, and the Parliament plans to adopt laws for decreasing other utility costs, such as water and communal services, bottled gas etc.).

4) Negotiations with the IMF, international bonds, credit rating

On 6 November 2008 the Hungarian Government signed an agreement with the IMF and the EU on a standby loan arrangement that provided approximately EUR 18,7 billion for Hungary. The amount was jointly provided by the IMF and the EU as follows:

- IMF undertook to provide SDR 10,5 billion (equals roughly EUR 12,2 billion; SDR is the IMF's special accounting unit);
- EU undertook to provide EUR 6,5 billion.

Of this amount, by September 2009 the Hungarian Government drew SDR 7,6 billion (appr. EUR 8,8 billion) from the IMF and EUR 5,5 billion from the EU. In 2010 the new Hungarian Government discontinued the loan agreement, so the rest of the credit line has not been drawn. As of the end of January 2013 Hungary has to repay appr. EUR 4.1 bn in 2013 and EUR 0.8 bn in 2014 to the IMF, and EUR 2.0 bn in 2014 and EUR 1.5 bn in 2016 to the EU.

Mostly because of the uncertainties of the international economic situation, the Hungarian Government approached the IMF again in November 2011, and negotiations started in the middle of July 2012. What Hungary wants this time is a kind of "safety net" in the magnitude of about EUR 15 bn. This would be different from the previous standby loan agreement, since it would not directly provide loan to Hungary, it would only secure the opportunity to obtain quick financial assistance in case of serious market disturbances. The aim is to sign a precautionary credit agreement (so-called flexible credit line). In late 2012 the Prime Minister of Hungary stated that the Government had cleared all obstacles that stood in the way of IMF talks. The Government still retains its aim of concluding a precautionary credit agreement with the international organizations but not at any price. At the moment the two sides in the negotiation disagree in a few major points (incl. the 2014 budget deficit and whether Hungary's growth is struggling because of turmoil in the European economy or because of taxes on banks). A deal is unlikely unless these views converge. The current market conditions make it possible to draw the resources from the markets without any external assistance, and in early February 2013 Hungary successfully issued international bonds worth USD 3.25 billion (with 5.4% interest on the the ten-year bonds).

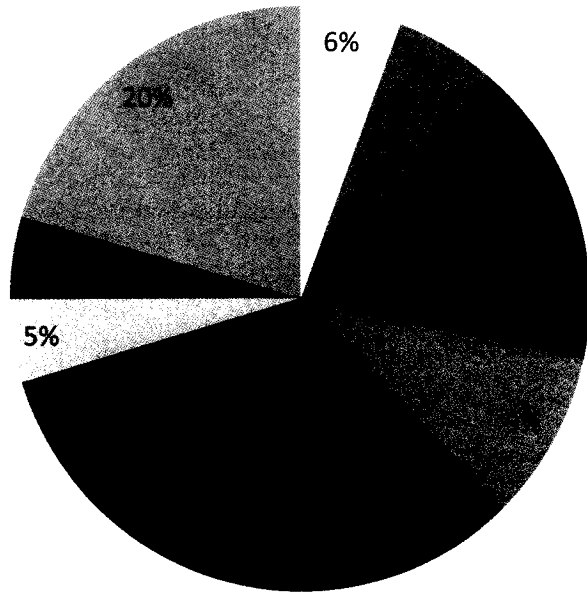
The successful bond issuance in February proves that Hungary is capable of securing capital from the international markets, despite the ratings by the three major rating agencies that put the country in the "not recommended" category:

- Moody's: Ba1 (negative outlook)
- S&P: BB (negative outlook)
- Fitch: BB+ (stable outlook)

5) Hungary-Greece bilateral trade and investment

Hungary's trade with Greece

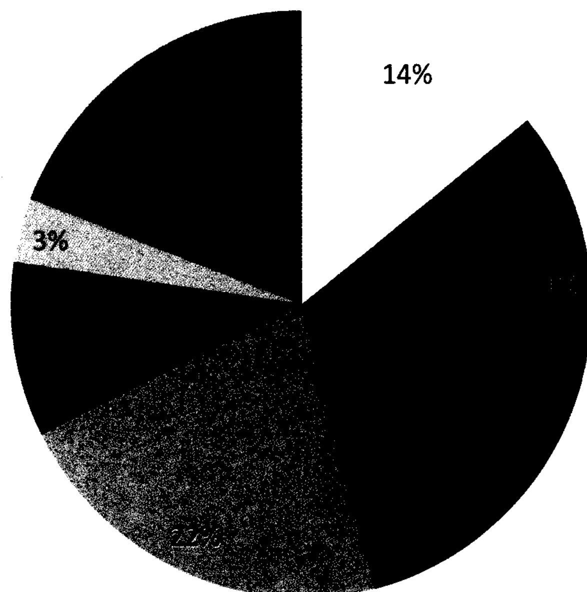
Composition of Hungary's exports to Greece (2012)



Total exports in 2012: EUR 262.9 million

- live animals and animal products (14,7)
- cereals (14,5)
- crude maize oil (9,6)
- pet food & food industry by-products (14,0)
- pharmaceutical products (21,7)
- plastics, rubber and their products (24,5)
- iron, steel and their products (8,9)
- electrical products (77,0)
- cars and car parts (12,0)
- refrigerators and office machines (12,0)
- other products (53,9)

Composition of Hungary's imports from Greece (2012)



Total imports in 2012: EUR 67.0 million

- fruits, vegetables (9,5)
- rice (2,6)
- processed food products & drinks (7,4)
- pharmaceutical products (6,6)
- plastics, rubber and their products (4,7)
- aluminum and products thereof (14,5)
- iron, steel & their products (2,0)
- electrical products (4,5)
- other machines (2,4)
- other products (12,4)

Bilateral trade volumes million EUR

	2004	2005	2006	2007	2008	2009	2010	2011	2012
HU export	260.0	343.4	317.9	565.6	449.3	325.0	305.2	288.9	262.9
HU import	66.9	59.5	61.7	73.1	72.3	56.3	80.1	91.6	67.0
Balance	193.1	283.9	256.2	492.5	377.0	268.7	225.1	197.3	195.9

- HU imports from Greece: EUR 60-80 million for many years except for 2011 (EUR 91.6 million)
- HU exports to Greece – great jump in 2007 (mostly in telecom items and cars, but also in wheat and maize) then fast drop back to pre-2007 levels and still slowly decreasing

Major Greek investments in Hungary

million EUR

	2010		2011		2012	
	annual flow	total stock	annual flow	total stock	annual flow	total stock
Greek investments in Hungary	2.4	0.4	-0.9	-1.2	1,2	0,1
HU investments in Greece	0.0	0.1	4.3	4.4	-3,6	0,9

(Source: National Bank of Hungary, April 2013)

Available official statistics do not show any significant investment but it is due to the fact that most of the Greek investments arrived at Hungary via intermediary third countries.

Coca-Cola Hungary is registered with appr. EUR 29 million, and has invested more than HUF 110 billion [EUR 379 million] over the years. One of its latest investments is a new aluminium canning line which started operation in early 2012 and doubled the exports of the company from HUF 7 billion to about HUF 15 billion [EUR 51.7 million]. Coca-Cola Hungary is the first one among those multinational companies (now well over a dozen) with whom the Hungarian Government signed cooperation agreements. In the spirit of this agreement Coca-Cola has already raised its purchases of raw materials from Hungarian suppliers, thereby substituting imports.

The Zeritis Group still owns two paper mills, although the most important one (Piszke Paper Factory Co. Ltd.) went bankrupt and was sold at the end of 2011.

Investments that are known to be related to Greek investors:

Name of company	**Registered capital**
Chipita Holding Ltd. (asset management)	USD 177.6 million
Coca-Cola HBC Hungary Ltd. (soft drinks)	HUF 8397 million
M.J. Maillis Hungary Packing Systems Co. Ltd. (trade in packaging materials)	HUF 292 million
Marathon-Foods Trading Co. Ltd. (food processing and trade; CY?)	HUF 359 million
Budafok Recycling Paper Factory Co. Ltd. (paper mill)	HUF 203 million
Szentendre Paper Factory Co. Ltd. (paper mill)	HUF 225 million
FORNAX Technical and Business Consultancy Private Ltd. (IT services and management consultancy)	HUF 100 million
Chipita Hungary Trading Ltd. (food wholesale trade)	HUF 3 million
Alapis Hungary Trading and Servicing Co. Ltd. (trade in veterinary drugs)	HUF 3 million

Hungarian investments

The outbound FDI invested by Hungarian companies abroad is close to EUR 24 billion, putting Hungary among the top major investors in the Central European region. The major targets of outbound FDI are Slovakia, Bulgaria, Romania, Serbia, and the most important target sectors are business services, banking, oil exploitation and refinery, retail trade.

There is no significant and known Hungarian investment in Greece. This is mostly due to the fact that Greece has never been in the focus of investor attention from Hungary, and the outbreak of the crisis naturally prevented any change in this regard. Hungarians also prefer predictable and stable macroeconomic and political environment, business-friendly legal background. After the worst two years of the crisis, Greece is on the right track to lay down or enforce these fundamentals for investment. As the general international interest will slowly return, potential Hungarian investors might also reconsider their restraints towards Greece.

6) Promising sectors for increasing Hungarian exports to Greece

- milling wheat and other cereals, maize
- food products, especially meat preparations, frozen or canned fruits and vegetables
- maize oil and other intermediary products of plant or animal origin
- waste treatment and water cleaning equipment and technology
- military equipment
- medical devices and accessories
- pharmaceutical products
- machinery and precision tools
- IT solutions, especially IT security