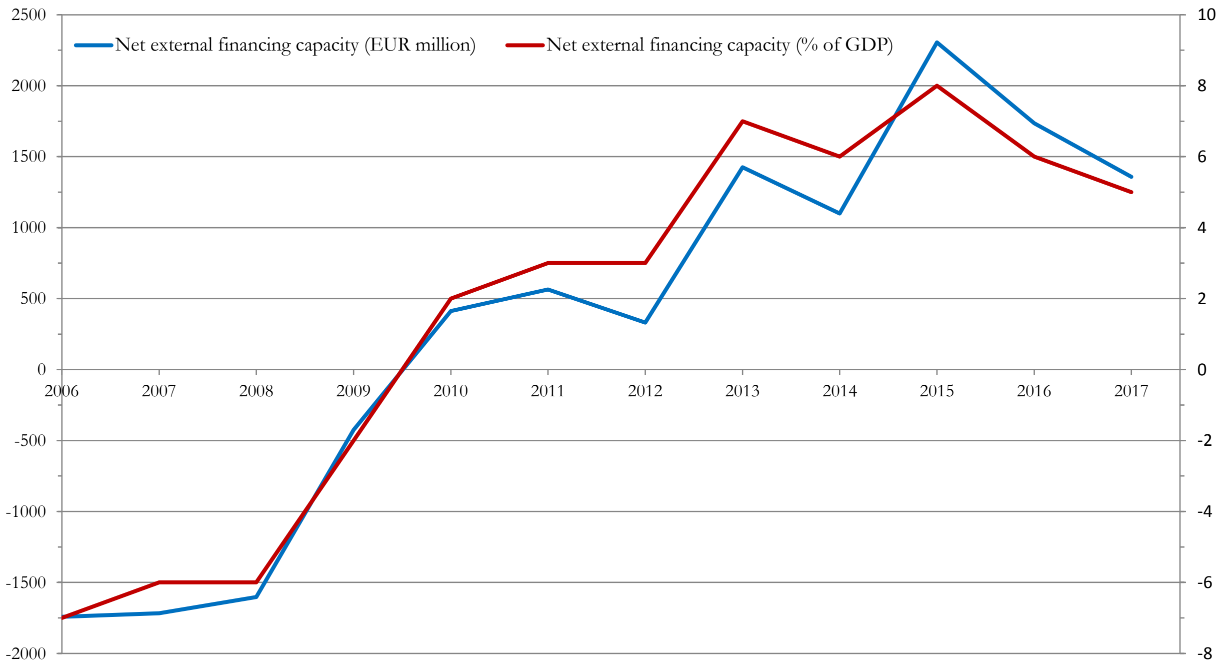
MINISTRY
FOR NATIONAL ECONOMY

Hungary's net external financing capacity exceeds 5 percent of GDP

In the first quarter of 2017, Hungary's net external financing capacity was EUR 1352 million (HUF 420bn), data adjusted for seasonal effects show, which corresponds to 5 percent of GDP as of Q1 2017 – according to a recent press release of the National Bank of Hungary (MNB).

Net external financing capacity is an indicator that shows the combined surplus of current account and capital balances. In case this sum is positive, it is called financing capacity, in case it is negative, it is called financing needs. In Hungary, this indicator had turned positive in 2009 and reached 1 percent of GDP by the end of that year (Fig. 1.). After that, according to annual data compiled by the MNB and the Hungarian Central Statistical Office (KSH), it continued to steadily improve up to 2012, only to exceed 7 percent on the back of two substantial leaps in 2013 and 2015. In light of the latest MNB report, unadjusted and calendar-effect adjusted data currently show EUR 1358 million and EUR 1352 million, respectively, which corresponds to more than 5 percent of Hungary's first quarter GDP in 2017.

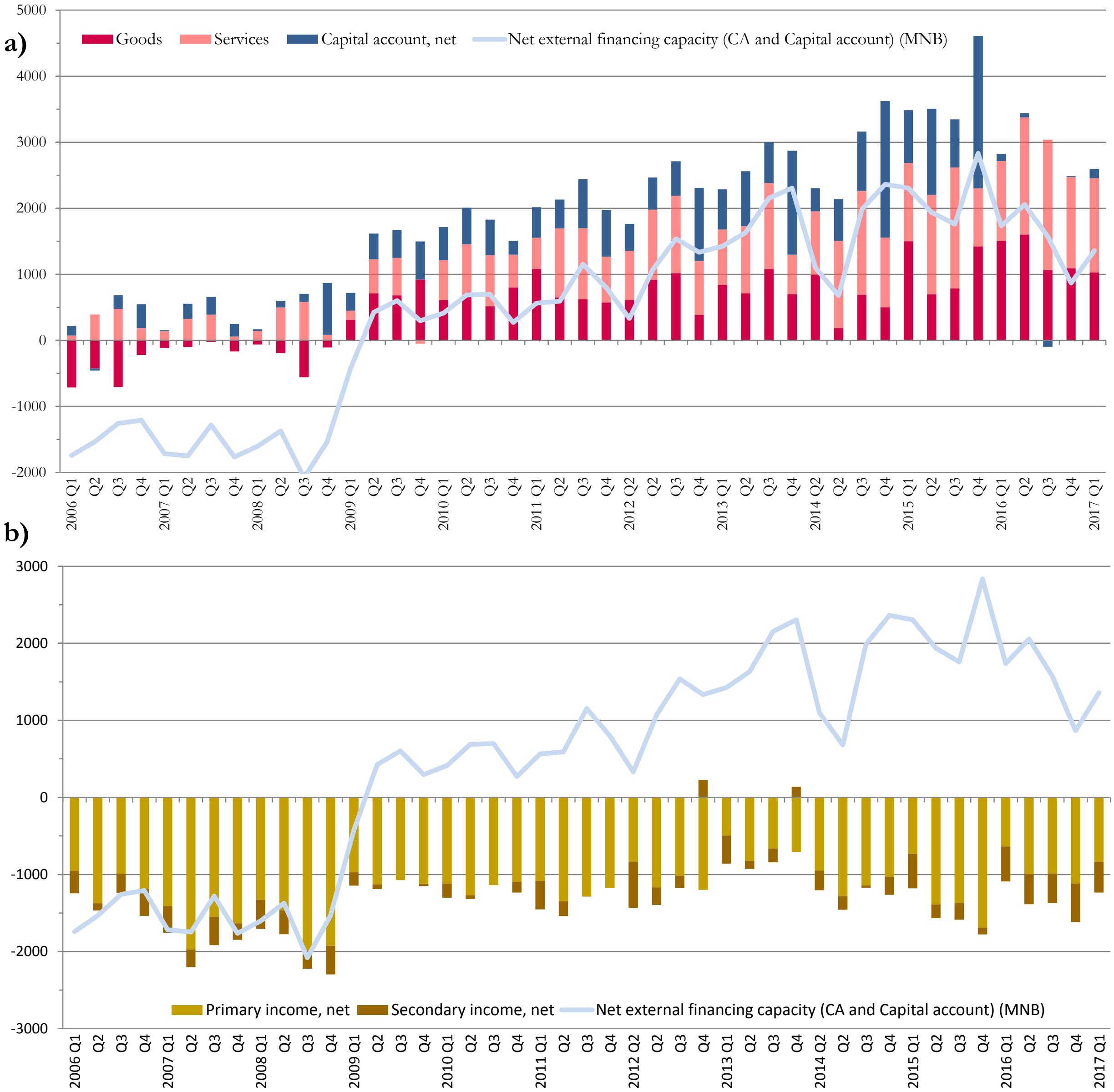
Figure 1: Hungary's net external financing capacity (left hand side axis: EUR million, right hand side axis: % of GDP)



Source: MNB

Analysing **components of net financing capacity** reveals that the balance of goods and services has – albeit fluctuations occurred -- improved since 2006, as the MNB's quarterly data show (Fig. 2a). The balance of the trade of goods has been persistently in the green since the end of 2008, and after a major pullback in 2014 it reached EUR 1500 million in the first quarter of 2015, while since the end of 2015 it has remained above the threshold of EUR 1000 million. Until the end of 2009, the services balance had seen wide swings, while it stabilized after 2010 and since 2014 it has been above EUR 1000 million. In the first quarter of 2017, the balance of the trade of goods was EUR 1028 million, while that of services was EUR 1427 million.

Figure 2: Hungary's net external financing capacity by indicator components, seasonally adjusted data, excluding special-purpose enterprises (EUR million)
a) balance of goods and services as well as capital accounts
b) primary and secondary income balances in comparison to net external financing capacity



Source: MNB Statistical Directorate (press release, 2017)

Hungary's capital balance surplus ranged between EUR 300-700 million in the period 2009-2015, while it soared to some EUR 2310 by the end of 2015. At the end of the three years prior to 2017, the indicator had hit similarly high figures, whereas after 2016 the surplus declined markedly and reached only EUR 137.5 million in the first quarter of 2017.

According to the MNB press release, the **peak observed in 2015** stemmed from the payments related to EU transfers of the 2007-2013 programming period. The downward trend of recent years has been caused on the one hand by the sudden slump in EU fund inflows and the decrease of foreign trade balance surplus on the other, the latter factor driven primarily by the deterioration of the balance of goods. On the other hand, the drop in net exports has been partly offset by industrial export growth, and thus the foreign trade surplus has remained steadily close to 10 percent of GDP. The income balance has also stabilized: the compensation of employees and net interest paid on foreign loans have both declined. This factor and the slight fall in the transfer balance caused the decrease that followed the peak of 2015, while FDI inflow has continued at an even pace.

Hungary's net external debt decreased by some EUR 0.7bn, thanks mainly to the ongoing downward trend concerning the Hungarian government securities holdings of non-residents and to the concurrent high demand for these assets by resident investors. The declining state debt trend prevalent in recent years resulted in a gross government debt-to-GDP ratio of 69 percent, and in a figure of 18 percent in terms of net debt. The stock of foreign currency reserves, at EUR 24.4bn, is above the levels considered adequate by investors. Experts predict GDP growth of 1.7 percent and 1.8 percent in the EU for 2017 and 2018, respectively.

It has been a general trend in recent years observed in EU member states that growth in terms of external financing capacity as of percentage of GDP has stalled. In the press release, the MNB concludes that this has been the consequence of rapidly deteriorating transfer balances. Hungary's 5.5 percent of GDP net financing capacity is well above the regional averages even though this figure is already below the best levels seen in recent years.

Data from the past ten years show that the Hungarian economy has been stable; it has been growing dynamically and has a massive savings surplus. The country's position is also favourable from a regional aspect, and the exposure to external risks has been improving. The main factors behind this phenomenon are household savings and tight caps on the expenditure side of the state budget. Although Hungary's current account surplus has decreased last year, it is at the level – still high compared to regional averages - last seen at the end of 2015.