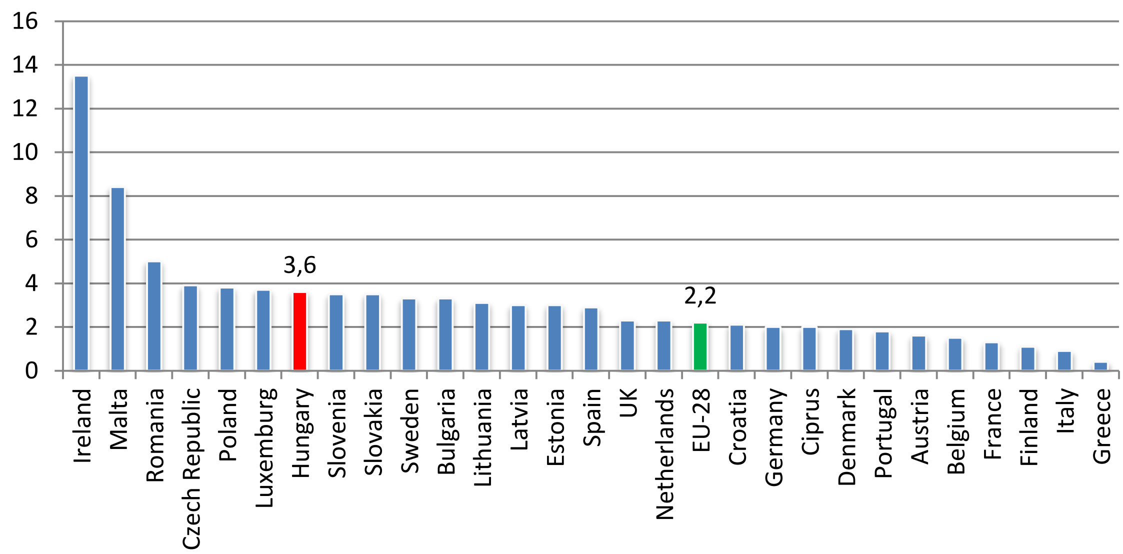
Hungary's economic outlook to remain bright in coming years

The Government of Hungary has recently published the country's Convergence Programme with an outlook for 2018-2022 and the European Commission has also released a spring forecast for 2018-2019. Both studies predict robust economic growth above the EU average for this year in Hungary.

The Hungarian economy has been capable of posting an economic growth rate which exceeded the average of the EU28 (2.2 percent) in the past four years. In the period 2014-2017, the 3.6 percent average annual growth rate has even been above that of the majority of CEE countries. The only countries where average growth in this period was slightly higher were Romania (with 5 percent, from a much lower base), the Czech Republic (3.9 percent) and Poland (3.8 percent). From this aspect, 2017 was a year of success, as GDP growth has hit 4 percent, and this placed Hungary as ninth on the GDP growth ranking of the EU28.

Average annual GDP growth in 2014-2017 (%)



Source: NCP, 2018

The Government of Hungary is expecting steady economic growth, slightly above 4 percent in coming years, up to 2022. Studies show that this trend is going to be underpinned by favourable global economic conditions that are predicted to drive demand for Hungarian goods and services higher which in turn will boost Hungarian exports.

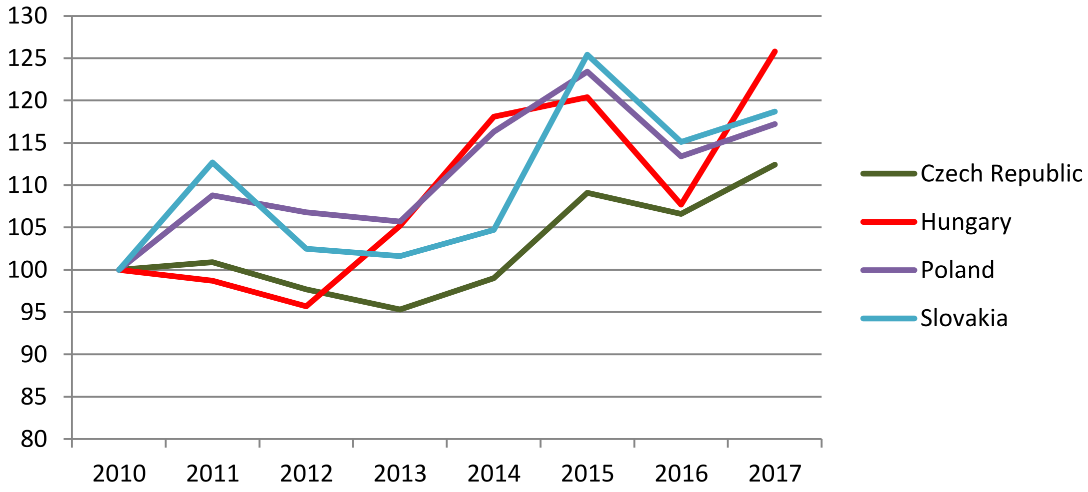
In addition, domestic demand is also expected to grow persistently in coming years. This will be partly driven by the six-year wage and tax agreement brokered earlier by the Government's Standing Consultation Forum, which aims to offset the impact of rising wages through the reduction of payroll taxes. As the rate of wage growth has recently exceeded that of consumption growth, the latter is expected to pick up in coming years. Besides adding to wage growth momentum, the Government has also been using fiscal tools, such as the Family Housing Subsidy Programme, lower VAT on newly built dwellings and the accelerated implementation of EU-funded projects, to improve the future economic outlook.

Although the Spring Forecast of the EU for Hungary outlines a growth path similar to the prediction of the Government, they are more conservative regarding growth estimates (2018: 4.0 percent, 2019: 3.2 percent). The analysts of the EU see domestic demand growth as the potential main driver of future expansion. Corporate investment is also predicted to grow markedly this year and next but increasingly insufficient capacities, especially in human resources, are seen to put a damper on growth. Household consumption is also expected to remain strong albeit the effect of wage hikes is set to peter out within the next one or two years. Experts still believe that international economic conditions will remain supportive but investment growth will cause the rate of import growth to exceed that of exports and this is set to slightly reduce Hungary's existing trade surplus in coming years.

Investment growth was robust already in 2017: the volume of investment totalled HUF 8200bn (EUR 26.5bn), up by 17 percent year-on-year. Thus, Hungary's investment rate has reached 21.5 percent of GDP, which is above the 20.3 percent average rate of our regional peers, members of the Visegrad Four. Gross fixed capital formation data show a very similar trend: in 2017, the rate of growth was the highest in Hungary compared to the level of 2010.

Gross fixed capital formation in V4 countries

(chain-linked volumes, 2010=100%)



Source: Eurostat

Given the fact that investment growth was observed in almost each sector of the national economy, growth is predicted to remain balanced also in the medium term, as new capacities created as a result of current investment projects will have a favourable impact on economic trends after production will have been started.

Fiscal processes have also remained sound in recent years: the budget deficit has been below 3 percent of GDP since 2012, and often it was mostly even below the formerly predicted target. In 2017, the deficit of the government budget was 2 percent, although both the Government and EU analysts are expecting this rate to edge up somewhat (to 2.4 percent in 2018), from 2019 on it is to decrease again. The EU's estimate is 2.1 percent for 2019, while the Government expects 1.8 percent and further decline to 0.5 percent by 2020.

Concurrently, the general government debt-to-GDP ratio has also been declining over the past couple of years, and the downward trend is seen to continue in coming years. The pace of decrease is seen to be faster than the trajectory regarded as optimal by the EU. Relatively rapid economic growth and modest fiscal deficits will both facilitate and accelerate the fall of the debt ratio. In the period 2010-2017, it has declined from 80.5 percent to 73.6 percent, and it is planned to be reduced to below 60 percent of GDP by 2022. Although the rate of decrease will be modest this year (73.2 percent), as of 2019 the indicator is seen to fall by several percentage points each year. This prediction is roughly in line with that of the EU, which prognosticates a debt ratio of 73.3 percent for 2018 and 71.0 percent for 2019.

It appears that Hungarian and international economic forecasts published in recent weeks have come to the conclusion that Hungary is well prepared to expand in a dynamic and balanced manner, posting a growth rate that exceeds the EU average, in coming years. The external environment, domestic economic trends and Government measures (among them a prudent fiscal policy) are all enhancing the country's growth potential.