31 JULY 2017

BUDGETARY ADVANCE PAYMENT OF EU TRANSFERS INCREASED SHARPLY

In Hungary, the faster than expected GDP growth in the first quarter of 2017 was followed by a slight slowdown in April and a pick-up in May. GDP growth is expected to accelerate to around 3.5 per cent in 2017 from 2 per cent in 2016, primarily as a result of investments rising this year, whereas they declined last year. Although external and internal equilibria will deteriorate slightly in 2017, and inflation will accelerate, these trends are acceptable in the short term.

Gross fixed capital formation fell by more than 15 per cent in 2016 due to a decline in EU transfers. In 2017, as a result of the resumption of the EU investment cycle 12 per cent growth is expected. The investment rate was 17.8 per cent in 2016, which is rather low for a moderately developed country such as Hungary In 2017 increase can be expected with a 19 per cent rate. Although the government advertised the calls for tenders of the new EU budget period started in 2014, decision-making typically requires 6-9 or more months instead of the promised one month. Project targets of new calls for tenders are fragmented and unclear; the main objective is to spend money fast (before the parliamentary elections of 2018). This can be seen from the fact that the government wishes to announce all calls for tenders until the end of 2017. However, there is no substantial acceleration compared to the previous period. Of the more than HUF5,000bn available for applicants in the 2014–2020 cycle only about half of it has been spent until now. In addition, as major projects were handled first in order to benefit as much and as fast as possible, a significant portion of disbursements are advance payments, thus no substantive activities have started in these areas yet (they are often only financial allocations for projects set up later by local governments). The actual investment process will be postponed to the next few years (up to 2023).

The general government deficit was exceptionally high in June (HUF700bn), whereas the combined deficit in the first five months was hardly more than HUF200bn. The main reason for this is that budgetary advance payments of EU transfers to the beneficiaries have increased sharply. The magnitude of revenues from EU transfers received in the budget has so far fallen far behind that of payments. For reasons of statistical settlement, this does not jeopardize the government's deficit target of less than 3 per cent of GDP. However, its persistence would limit the options for reducing the government debt-to-GDP ratio.

Developments in recent months have not justified the fears that after the British referendum on leaving the EU and then the American presidential elections a breakthrough of populist and Eurosceptic political forces could be expected. The strengthening of the Franco-German tandem improves the possibilities of concerted EU actions against the protectionist trade policies of the US. However, it narrows the scope of action for EU member states expecting the further inflow of EU transfers but refusing solidarity with the European Union in a number of cases. Enlargement of the euro area and the move towards any form of fiscal union makes it probable that the remaining EU member states will be drifting towards the periphery of the EU.

The forecast of GKI for 2017

	Description	2014	2015	2016	2017	
					01-05	forecast
1	GDP (%)	104.0	103.1	102.0	4.2**	103.5
2	Industrial production (%)	107.7	107.5	100.9	105.7	105.5
3	Investments (%)	119.3	103.8	80.0	128.4**	112
4	Construction services (%)	113.4	103.0	81.2	126.9	122
5	Retail trade turnover (%)	105.2	105.8	104.5	103.5	104
6	Exports (current prices in euro, %)	104.0	107.0	102.9	110.9	110
7	Imports (current prices in euro, %)	104.7	104.6	101.5	112.3	112
8	Foreign trade balance (EUR billion)	6.3	8.6	9.9	4.3	9
9	Balance of the current and capital account (EUR billion)	6.1	8.7	6.1	1.4	7.5
10	Average exchange rate of euro (in HUF)	308.7	309.9	311.5	309.5***	313
11	General government deficit* (HUF billion)	825.7	1218.6	848.3	911.2***	1300
12	Index of average gross earnings	103.0	104.2	106.1	112.1	112
13	Consumer price index	99.8	99.9	100.4	102.3***	102.5
14	Consumer price index at the end of the period (Corresponding month of the previous year=100)	99.3	100.9	101.8	101.9***	102.5
15	Rate of unemployment (at the end of the period, %)	7.1	6.2	4.4	4.3****	4.3

* *Cash flow basis, without local governments*
** *First quarter of 2017*
*** *First half of 2017*
**** *Apr-Jun 2017*
Sources of actual data: CSO, NBH, NGM

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