GKI Economic Research Co.
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The forecast of GKI Economic Research Co. for 2021-2022

(Summary of 2021/3 detailed forecast for the press, 29 September 2021)

In recent months, both the growth of Hungarian GDP and the rise in price levels have been faster than previously thought. The strained relationship with the EU is now causing economic losses due to delayed access to reconstruction funds and other EU resources. The confrontational EU policy of the government, its loose fiscal and income policy and the tightening of the central bank, which is mainly verbally strong, but actually manifests itself in the interest rate hikes, all point to a policy that is not sufficiently consistent, subordinated to short-term electoral goals and pushing balance of payments considerations into the background This is unlikely to change before the elections. However, the possible more serious consequences of the fourth wave of the pandemic, which has already begun, could entail a slowdown in the rate of growth and price increases now assumed.

GKI forecast for 2021-2022

	2018	2019	2020	2021	2022
		(fact)		forecast	
GDP	105.4	104.6	95.0	**107**	**105**
• Agriculture (1)	104.1	100.4	93.2	**102**	**100**
• Industry (2)	103.3	104.1	95.1	**113**	**107**
• Construction (3)	115.1	113.0	90.6	**109**	**106**
• Trade (4)	110.8	110.8	101.2	**106**	**105**
• Commercial lodgings and catering (5)	104.7	106.5	67.8	**103**	**115**
• Transport and storage (6)	106.5	105.2	83.7	**105**	**104**
• Information, communications (7)	110.4	108.8	106.1	**109**	**106**
• Financial services (8)	104.9	108.1	103.4	**103.5**	**103**
• Real estate services (9)	104.5	98.9	94.8	**102**	**102**
• Professional, scientific, technical activities (10)	109.6	106.5	92.8	**107**	**102**
• Public administration, education, healthcare (11)	100.9	100.3	96.5	**105**	**103**
• Arts, entertainment (12)	107.6	106.5	90.6	**103**	**105**
• Core growth	106.8	106.2	94.8	**108**	**105**
GDP domestic demand	107.1	106.6	97.3	**105**	**103.5**
• Private consumption	104.1	104.6	97.4	**103.5**	**104.5**
• Gross fixed capital formation	116.4	112.8	92.7	**106**	**105**
Exports (goods and services)	105.0	105.8	93.3	**112.5**	**110**
Imports (goods and services)	107.0	108.2	96.1	**110.5**	**109**
Consumer price index (preceding year = 100)	102.8	103.4	103.3	**104.7**	**104**
Unemployment rate (annual average)	3.7	3.4	4.3	**4.1**	**4**
General government balance in per cent of GDP (ESA)	-2.3	-2.1	-8.1	**-7.5**	**-6**
Balance of the current and capital accounts					
• EUR billion	3.4	1.7	0.6	**-0.5**	**3**
• In per cent of GDP	2.5	1.2	0.4	**-0.3**	**1.8**

Source: HCSO, GKI

World economy: The IMF's global economic forecast, published in July this year, projects global GDP to expand by 6 per cent in 2021 and 4.9 per cent in 2022, after a 3.2 per cent fall last year. Compared to spring, the summer forecast is unchanged for 2021, but 0.5 percentage points higher for 2022.

Economic expectations: Although the EU's economic sentiment index fell slightly in August compared to July, it still reflects strong optimism. After its big jump in April, GKI's economic sentiment index was only slowly rising in the summer months, and the September data actually indicates stagnation. GKI's economic sentiment and business confidence indices already exceed the pre-crisis level of early spring 2020.

Economic policy: The government is prepared for a protracted dispute with the EU, as demonstrated by the issuance of foreign currency bonds, while it **intends to continue** its election-driven economic policy of stimulating demand, favouring loyal ownership groups and inevitably increasing inflation. Despite its sharp rhetoric, however, the central bank also takes the government's interests very much into account. This is reflected in the surprise reduction in the rate of interest rate hikes in September, the continuation of its corporate bond-buying programme and the launch of a new "green" lending programme. Economic policy change can be expected only after the elections.

Economic growth: GKI continues to expect economic growth of **around 7 per cent** in 2021. The faster than expected second quarter growth is offset by the fourth wave of the pandemic. The significant rise of the export surplus played an important role in GDP growth in the first half of the year, with a stronger expected contribution of consumption and investments in the second half. In 2022, as in 2021 the Hungarian economy is already performing above the level of 2019, growth **will slow down to around 5 per cent**. The election budget foresees faster-than-expected consumption growth, financing and market problems imply slower investment dynamics, and the export/import gap may close. In 2022, with the exception of tourism, which is expected to grow strongly, growth in almost all sectors will be more modest, especially in industry and construction. At the same time, this slowdown is expected to be characteristic of the EU as a whole, while Hungarian growth rates may be at the forefront of the region.

Consumption: The level of household consumption this year will reach its level of 2019. **In 2022, as an election year, a noticeable acceleration in minimum wage, real income and consumption is expected**, while GDP growth is slowing down. The expiry of the moratorium on credit repayments and the inflationary impact of rapidly rising purchasing power will further amplify the impact of rising income differentials. Consumption is expected to expand by 3.5 per cent this year and 4.5 per cent next year.

Investments: The level of fixed capital formation will only exceed its 2019 level **in 2022**. The investment rate remains high at around 27-27.5 per cent. In particular, however, there are few investments aimed at modernising the economy and society in real terms, partly as a result of adaptation to the financing state and not to the market.

Employment: The number of employees will increase by 1 per cent this year and by 0.5 per cent next year, after a decrease of 1.2 per cent on average last year. Unemployment increased from 3.4 per cent in 2019 to 4.3 per cent in 2020, with an average of 4.1 per cent and 4 per cent expected in 2021 and 2022. Some professions are again facing labour shortages.

Financial sector: Banks are planning to increase their corporate and retail lending in the second half of 2021, and this is expected to continue in 2022. At the same time, the rise in interest rates and the expiry of the moratorium in the middle of next year foresee a **deterioration of the existing loan portfolio** and more cautious borrowing, with a high degree of differentiation.

General government: The high general government deficit in 2021 and 2022 is a consequence of **election budgets**. This year's deficit of 7.5 per cent of GDP will be followed by a deficit of around 6 per cent next year. The huge foreign currency bond issue in September will allow the financing of election targets despite the delay in EU transfers, but **makes the mandatory reduction of government debt required by the debt rule this year uncertain**. After last year's 80.4 per cent, a government debt-to-

GDP ratio of around 80 per cent is expected, but it is likely that this will also require creative accounting methods. The government debt ratio could fall to around 77 per cent in 2022.

Inflation, interest rates and exchange rates: Although the central bank's cycle of interest rate hikes stopped the dangerous weakening of the forint, the forint is unlikely to remain stronger than last year's annual average, partly because of the slowdown in the pace of base rate hikes. After last year's HUF351, 1 euro may be worth **HUF355** this year, and a little more next year, **HUF357**. **Inflation averages 4.7 per cent this year**, will be at least 5 per cent at the end of the year and in the first months of 2022, and could **average 4 per cent in 2022**. Loose fiscal and income policies will prevent a sharper slowdown in price increases. With further monthly increases of 15 basis points, the year-end **base rate** will be **2.1 per cent by the end of 2021**, rising to or even above 3 per cent by the end of 2022, depending on international trends.

External equilibria: The current account deficit could be around EUR2bn per year in 2021 and 2022. Although **financing capacity could be negative this year**, it could reach EUR3bn next year, from the EU's economic reconstruction fund and European budgetary resources for 2014–2020 and 2021–2027. Foreign currency bonds issued in September, totalling around EUR4.5bn, represent around 3 per cent of GDP. At the end of June 2021, the **net debt** of the national economy was EUR17.2bn, of which the increase in September amounted to about a quarter. In September, Moody's **upgraded** Hungary's credit rating to the same level as other major international rating agencies. However, Hungary is still one of the **lowest ranked** countries in the region.

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