GKI Economic Research Co.
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The change started

According to the forecast of GKI Economic Research Co., the successful accomplishment of negotiations with the IMF and the EU will be enough only for mitigating the contraction of GDP. The recovery of confidence of portfolio and particularly foreign direct investors may bring results only in 2013 the earliest.

By the beginning of 2012 the Hungarian economy and the government got into an unsustainable position, close to a solvency crisis. The series of legal acts and economic policy measures provoked the critics of almost all political and financial centres of the world and they caused deep mistrust among investors. The exchange rate of the forint to the euro wakened above HUF320 temporarily, auctions of government securities proved to be unsuccessful, the yields of long-term government bonds reached 11 per cent, the CDS premium 750 bps. All credit rating agencies downgraded the Hungarian government securities to junk status. Hungary's reputation is the worst in the region. With growing fear from government default, domestic savings have tended to flow out of Hungary.

The more conciliatory rhetoric of the government and the retreat in important issues (such as the independence of the National Bank of Hungary, the access to the EU's financial pact) improved Hungary's reputation spectacularly, the exchange rate of the forint to the euro dropped below HUF300. However, the improvement of financial indicators compared to the lows of 2011 may easily prove to be temporary, playing for time by the government may easily lead to a new crisis spiral of financial indicators. It would be a serious failure to qualify the negations with the IMF and the EU as budgetary in nature since the present financial and solvency crisis is primarily of political nature and a confidence issue and it is partly related to economic policy and the budget. It seems to be unavoidable that the government should be willing to introduce such essential institutional and legal changes that restore at least the rule of law as accepted in the European market economies.

According to the latest forecast of the IMF a slight recession is likely in the eurozone in 2012. Although with the completion of investments in car manufacturing, Hungarian exports will grow dynamically, the possibilities of the other export industries will narrow further. The fall of domestic demand will exert a very negative impact on companies selling their goods and services in the domestic market. Due to the contraction of real earnings by 3.5 per cent and in spite of the easing in burdens of FX debtors, the consumption of households is likely to decreases by 2.5 per cent. Because of the shortage of resources and sales market as well as legal uncertainty, investments are expected to decline by another 4 per cent.

The willingness and the ability of lending by banks hit bottom. They lost HUF174 billion on the repayment of FX loans by debtors under preferential conditions. The losses may double by the end of February. According to the agreement between the banks and the government, banks will be allowed to write down 30 per cent of losses from their taxes of 2011. In spite of this, they need huge capital injections. Due to the deterioration of their capital endowment and the catastrophic economic prospects, banks stop providing new credits; in several cases even the stock of loans will be reduced.

The general government deficit on cash flow basis in 2011 was two and a half times higher than originally planned. The structural deficit excluding one-off items may equal to 5-6 per cent of GDP, its reduction explains the austerity measures envisaged for 2012. The planned general government deficit of 2.5 per cent of GDP in 2012 is unlikely to be achieved. The government is under great pressure to keep the deficit below 3 per cent of GDP even in the case of a recession held improbable by the government. Therefore, the general government deficit will probably be around 2.9 per cent of GDP in 2012. In areas included in the negotiations with the IMF, significant mid-year adjustments will be necessary.

The forecast of GKI Economic Research Co. on the Hungarian economy in 2012

		2009	2010	Jan. - Nov. 2011	2011 forecast	2012 forecast
1.	Volume of GDP (previous year=100)	93.2	101.3	101.8*	101.5	98,5
2.	Industrial production (constant prices, previous year=100)	82.3	110.5	105.6	105	105
3.	Investments in the national economy (constant prices, previous year=100)	93.5	94.4	95.5*	98	96
4.	Construction (constant prices, previous year=100)	95.7	89.9	91.2	90	95
5.	Retail trade (volume index, previous year=100)	94.8	97.7	100.1	100	97.5
6.	Exports (current prices in euro, previous year=100)	80.6	121.4	112.8	112	111
7.	Imports (current prices in euro, previous year=100)	75.2	119.4	111.4	110.5	109
8.	Trade balance (EUR billion)	3.7	5.5	6.6	7.2	10
9.	Balance of the current and capital account (EUR billion)	1.4	2.8	2.7*	3.7	4.5
10.	Average exchange rate of euro (in HUF)	280.6	275.4	279.2**	279.2**	300
11.	Deficit of the general government (cash flow basis, without local governments; HUF billion)	918.6	870	1734.4**	1734.4**	750
12.	Index of average gross earnings	100.5	101.4	104.7	104.5	103.2
13.	Consumer price index	104.2	104.9	103.9**	103.9	105
14.	Consumer price index at the end of the period (corresponding month of the previous year=100)	105.6	104.7	104.1**	104.1**	104.5
15.	Rate of unemployment (at the end of the period, previous year=100)	10.5	10.8	10.6***	10.7	10.8

* I-III quarters of 2011
** Actual figure, year
***September-November 2011
Sources of actual data: CSO, NBH, NGM