Hungary to outperform in 2020 despite a slowing economy

Hungary's economic activity is set to slow somewhat in 2020, but it will still outperform its EU peers. Don't expect the central bank to change its monetary policy despite above-target inflation. The most excitement could come from fiscal policy and the retail bond market


Hungarian Prime Minister Viktor Orban

3.8% GDP growth (YoY)

Yearly average

Hungary will probably end up with a GDP growth rate of 4.9% in 2019, which would indicate marginally lower productivity than the year before. 2020 will also bring lower economic activity, but this time a sharper deceleration is expected. Here's why:

- The labour market reached full employment, so additional improvements will be only incremental, meaning less impact on the increase in consumption
- Investment activity is expected to fade on the back of the closure of EU projects

- Industry is facing a significant drop in order levels, and external uncertainties won't help either, translating into lower export activity

3.5% Headline inflation (YoY)

Yearly average

Inflation expected to remain elevated on the back of the positive output gap, meaning that Hungary has been performing better than its potential output, strengthening demand-driven inflation. Continued wage pressure will put extra strain on corporates' profitability and a weaker, currency compared to last year, will also increase their cost level. Against this backdrop, we see inflation accelerating in 2020 as a whole. But it is not just about core elements. Energy prices will have a significant impact throughout the year due to base effects. Another additional force is the excise duty change affecting tobacco products, which will also have a significant impact on inflation. These are the main reasons (tax changes and non-core volatility), why the National Bank of Hungary will stick to the core CPI ex-tax measure as the main linchpin through 2020.

-0.9% General government balance

% of GDP

After an expected below 2% deficit-to-GDP ratio in 2019, this year we see further improvement. The main reason behind is the still strong labour market, rising consumption and rising inflation. Last but not least, the government carried out a lot of measures, which will be continued in 2020, aiming to diminish the shadow economy, widen the tax base and improve tax collection. Government financed investment activity will also reduce.

397 Net government debt issuance

in billion HUF

A planned HUF 397 billion of net government issuance is a third of the originally planned net issuance of HUF 1,260 billion in 2019. This significant drop is related to the decreasing cash-flow based deficit, which is supported by the transfers related to EU projects carried out using 100% finance from the budget (so-called pre-financing). FX debt issuance is expected to remain limited, pushing the share of foreign currency debt towards the 10-15% range. The Debt Management Agency will announce new, longer-dated retail bonds in the first half of the year to further support the retail market.

0.9% Central bank base rate

Year-end

The central bank didn't surprise in 2019 and we expect this trend will continue in 2020. Local and global developments are still supporting the NBH's wait-and-see approach. Although the risks surrounding the inflation outlook have become symmetric again, we hardly see the central bank changing its monetary stance as a base case scenario. As long as the Fed and especially the ECB don't alter monetary policy, the NBH will be fine with its current stance.

335 EUR/HUF

Year-end

With the very negative real rate and a too loose monetary policy stance for the changed current account dynamics (a shift from a meaningful C/A surplus in 2016 into C/A deficit in 2019-2021), we expect HUF to re-start its depreciation trend in the first half of this year. A nominal forint depreciation will also be needed to prevent real HUF from strengthening (or at least achieve real EUR/HUF stability) due to the high inflation differential when compared with the eurozone. As we face numerous global uncertainties, which can easily translate into an emerging market sell-off, we can't rule out a new record high EUR/HUF level in 2020.

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