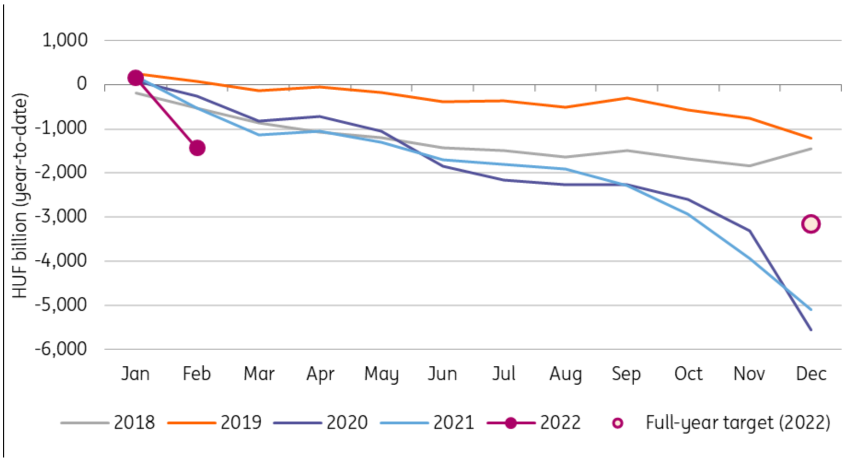
Hungarian budget deficit balloons

With all the extraordinary government transfers in February the writing was clearly on the wall, but the war has made the situation really complicated

People in Budapest

The Hungarian budget posted a HUF1,585bn deficit in the month of February, the second biggest monthly deficit ever. With the small surplus in January, the year-to-date deficit accumulation is at HUF1,434bn. This equals to 45.5% of the full-year cash-flow based shortfall target.

Cash-flow based year-to-date central budget balance



Source: Ministry of Finance, ING

For those who do not follow Hungarian economic policy closely, this budgetary performance may be quite surprising. However, we have already highlighted in our budget assessment in February, that a huge deficit figure is looming. The Finance Ministry's statement reveals the main drivers. The families raising children in February received their personal income tax paid in 2021, pensioners received a 13-month pension, and those employed by the armed forces and law enforcement agencies got a six-month bonus payment. All in February. In addition to these one-offs, the government has also decided on significant tax cuts in January. As a result, people under the age of 25 are receiving a full PIT exemption, while the payroll tax has been reduced by 4ppt to 13%. But this is impacting the budget during the whole year.

This front-loaded deficit accumulation was a well-planned action based on the strong economic activity last year and the expected good performance this year. In a vacuum, this is not a data that would concern us. What makes the situation delicate is the war in Ukraine, which could have significant implications on the 2022 fiscal targets.

The government planned the 4.9% of GDP deficit target with an expected 5.9% GDP growth, but the war and the sanctions are reducing the viability of that growth projection. On the contrary, inflation is flying much higher than planned, probably ending up somewhere around 8%. This gives extra inflow on the revenue side even if we take into consideration the expected slowdown in the real GDP growth. Plainly speaking, nominal GDP growth could be even higher (but due to the wrong reason).

Thus, the real issue regarding the budget is not necessarily related to the macroeconomic performance. What could cause headaches are:

- increasing interest payments due to the higher bond yields;
- deteriorating central bank earnings due to higher interest rate environment and a weaker forint (budget bears the loss of the central bank, though it is rather an issue in 2023);
- soaring energy costs are making the anti-inflationary shields more expensive, especially the utility cost cuts. State-owned utility providers need to be recapitalized.

These three things are possible to generate a HUF1,000-1,500bn extra budgetary spending if the situation won't improve soon. Compared to the planned HUF3,153bn cash-flow based deficit target, this is a significant impact.

Too early to choose between austerity or recalibration

In this volatile and fragile situation, we don't expect the government to rush into any decision, whether it is an austerity measure or a recalibration of the deficit and debt targets –especially not with the general election looming (3 April). In this respect, we see the government and the debt management agency operating in a "business as usual as possible" mode and will explore their possibilities in the second half of the year.

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