Year-end spending frenzy in Hungary

The monthly deficit in October breaks a record, showing the strong push to increase aggregate demand, as the general election approaches

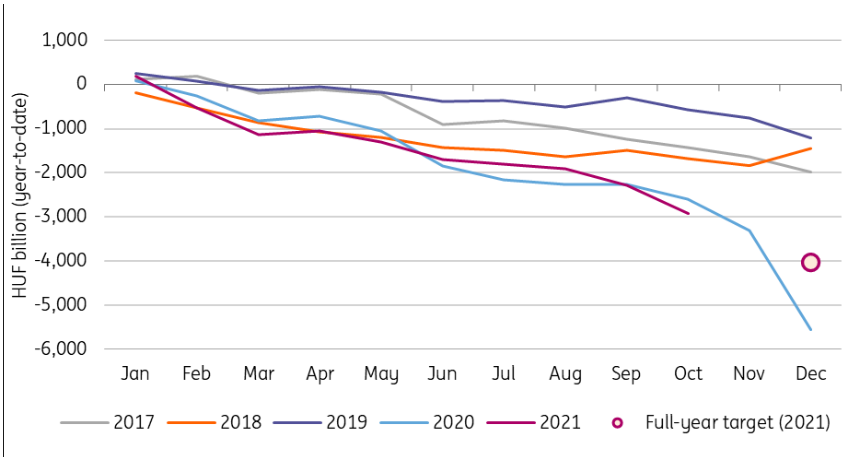
Shoppers in Budapest

The Hungarian budget posted a HUF 630b cash-flow based deficit in October 2021, which is the highest monthly deficit on record in October, roughly doubling the previous record from 2020. This monthly deficit adds to the already high year-to-date shortfall, which now sits at HUF 2.922t by the end of the tenth month.

However, as this equals only 73% of the amended full-year deficit plan, there is still room for more spending in the last two months of 2021. The government aimed a HUF 4t cash-flow based deficit, thus there is HUF 1.1t of room still available in the budget without jeopardising the goal.

With this monthly deficit in October, the deterioration of the budget situation has already been faster than in 2020 when the Covid crisis was in full swing. As such, it's clear that the government meant what it said about 2021 being the year of restarting the economy, with the Ministry of Finance really supporting activity in every area.

The year-to-date budget balance of the government



Source: Ministry of Finance, ING

According to the Ministry's press statement, the revenue side looks good thanks to strong economic activity and the stronger-than-expected labour market, with higher wage growth and a lower unemployment rate. Revenues from corporate tax, sales tax and personal income tax were higher during the first 10 months of 2021 than a year ago. As the government cut the social contribution tax (payroll tax) by 2ppt in July 2020, revenues from this are lagging compared to last year.

So the high deficit expected during 4Q21 is not coming from negative developments on the revenue side, rather it stems from a series of discretional spending decisions on the expenditure side. The statement underscores spending on programmes supporting road and railroad developments, rural developments, targeted support in transport, tourism, and agricultural sectors as well as programmes to improve the country's competitiveness.

The government is using all of its room to manoeuvre given the better-than-expected nominal GDP growth. Despite its extraordinary deficit-enhancing measures, the government is still able to meet the 7.9% deficit-to-GDP target as both real GDP growth and inflation will be much higher than the underlying assumption behind the amended budget plan.

This spending is boosting aggregate demand, helping to alleviate some of the downside risks stemming from the constrained export sector. Against this backdrop, we maintain our 7.7% GDP growth forecast for 2021, and see next year's performance at 5.2%. Such a performance will put the governing parties in the driving seat when it comes to economic performance ahead of the general election in April 2022. However, with this extra pressure on aggregate demand, the inflation problems created by shortages will deepen. From now on, all eyes will be on the National Bank of Hungary to react to this policy divergence.

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