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1. The global economy

The consequences of the COVID-19 pandemic transformed completely the conditions of **global economic growth**. The dramatic spread of the epidemic brought about a dual – both supply and demand-side – shock. The temporary stoppage of economic activity disrupted labor market conditions as well. The ensuing uncertainty about how long the virus crisis will be, what measures the governments are willing to implement, etc. puts pressure on both demand and supply. The impact of falling Chine production quickly became felt in other countries of the world, particularly in Europe and the US. It is not yet clear whether the recovery begins in the summer months or the economies begin to stabilize only during the fall. If the latter is the case, the global economy risks a slump so deep and social and economic losses so severe that the prospect of a timely recovery becomes quite distant. In such an environment, making quantified projections is near-impossible: negative growth in the first half of the year is certain but the developments during the second half are anybody's guess. The restrictions imposed during the past weeks are likely to be eased only very gradually, and it cannot be known whether a renewal of restrictions becomes necessary later. The epidemic is plateauing in the US while it slowly retreats in several countries in Europe, but this – along with the lull in China – may prove temporary.

International trade has probably collapsed as soon as the first quarter of 2020 when indispensable Chinese nodes of the global value chains stopped supplying European and US-based producers. Collapse deepened along with the health crisis, and according to some estimates – not even the most pessimistic ones – the degree of contraction of global trade flows may reach 20-30 percent.

The prices of industrial **commodities** have been on a freefall, due to the implosion of demand, oil markets are drowning in the oversupply of oil, which pushes oil prices downward. The market is extremely volatile.

The detrimental effect of the pandemic pushed the central banks toward continuing the line of **monetary easing** that started in 2019: besides keeping interest rates low, they pump surplus liquidity into the markets. The monetary policy tools are, however, clearly on their last legs, with few additional tools available, hence large-scale **fiscal measures** will be instrumental in dealing with the consequences of the fall in production. The fiscal emergency packages of various magnitude in each country may give a large boost to fiscal expenditures.

The main partners of the European Union face economic downturn everywhere. The **US** economy is expected to contract by 2.3 percent, with downward risks, while the GDP is expected to fall by 1.7 percent in Japan. **China**, on the other hand, is still expected to grow by 4.9 percent in 2020, although more pessimistic projections about a growth of approximately 2 percent are also in circulation.

The coronavirus impact is brutal in the **euro area** as well. At present we expect – in an optimistic scenario – an annual decline of 5.2 percent, provided that normalization starts not too far into the second half of the year. If the beginnings of normalization appear only toward the very end of the year, the annual GDP fall may reach 8 percent. **Central Eastern European** countries cannot decouple itself from the recession of core EU member states, hence in these countries, the economy is expected to contract by 3-5 percent in 2020.

2. Central European new member states

The region performed well in the last quarter of 2019, even though growth rates softened somewhat. The average growth rate was 3.2 percent in the region, still quite good compared to the past couple of years. Hungary led the way with 4.5 percent, followed by Romania (4.3 %) and Estonia (3.9 %) but Poland is also worth mentioning, due to its high weight within the region (3.5 %). Still, the EU-level deceleration made its mark on several Eastern European member states. Growth rates fell way below the regional average in Slovenia (1.7 %), Czechia (1.8 %) and Slovakia (2%). In all three cases, falling export was the main culprit behind the deceleration, but in Slovakia, investments stagnated as well. On the whole, annual average regional growth was 3.6 percent in 2019 in the new member states, a palpable, although not drastic, slowdown compared to the 4.3 percent in 2018.

Inflation was 2.6 percent in the last year in the region, mostly determined by the Polish (2.1%) and the Romanian (3.9%) rates. Core inflation was lower, 2.1 percent while food prices consistently pushed the price index higher and energy prices pulled it down. In any case, central banks have begun considering introducing liquidity-absorbing measures.

But the global pandemic fundamentally redrew the growth map of the region. No country remains unaffected from the negative impact since the shock is both endogenous and exogenous. Smaller, more open economies are hit the hardest by the external impact. Thus, the Czech Republic, Hungary and Slovakia are particularly affected by the stoppage of European automotive production, caused by not only the temporary closure of local production units but also by the disturbances in the value chains that heavily depend on nodes in China. Hungary is affected even more since the domestic electronics firms rely on Chinese supply chains for both their import and export. The external shock made significant output fall the baseline scenario in Slovenia as well: its metal, machinery and electronic industry is an organic part of the European value chain, but it is also concentrated to a couple of large firms, making this segment of the economy less diversified and more vulnerable.

With export on the retreat, import volume will also decrease, somewhat easing the downward pull on the economy. Still, productive capacities will remain unutilized, making the larger loss for the economy the larger is the value added usually produced by those capacities. Due to a generally higher level of high value-added activities in the Czech Republic, the loss in newly produced value added may double the loss in Hungary and triple the loss in Slovakia.

The countries that have larger domestic markets are somewhat less exposed to external shocks because their economy can be more effectively stimulated through private consumption. In Romania and Poland, the consumption ratio is much higher than in Hungary and in Czechia. Therefore, how governments respond to the crisis to elevate consumption expenditures can be crucial. The table below lists the planned fiscal measures in several Eastern European countries:

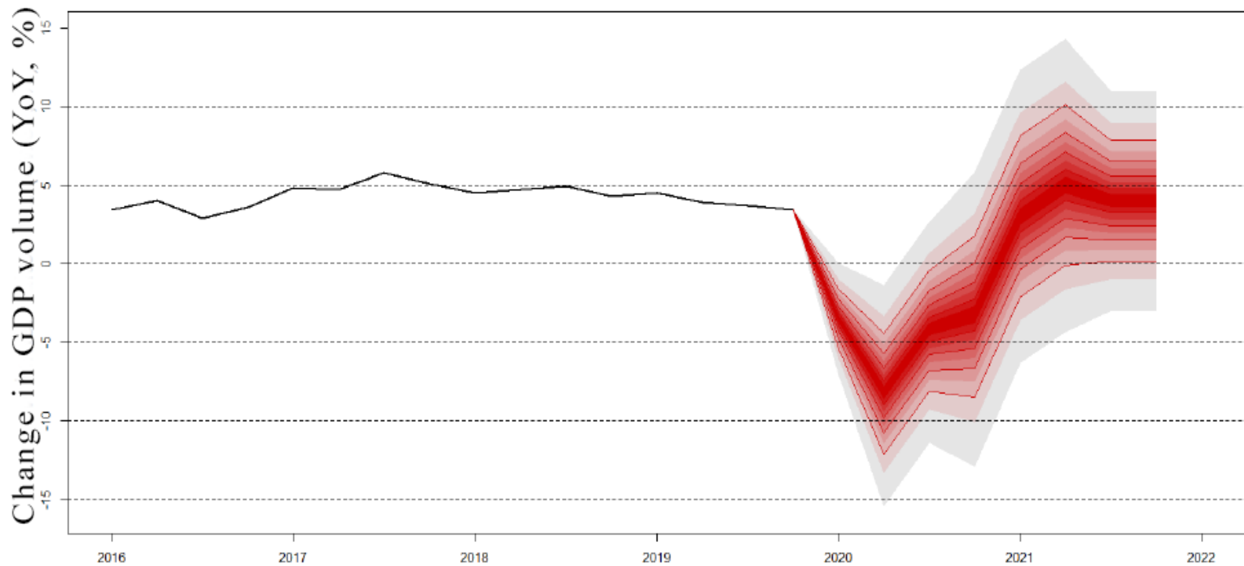
Most important fiscal measures due to the pandemic in the new EU member states (until 3 April 2020)

Member state	Magnitude of fiscal measure as a % of GDP	Main elements of the measure
Bulgaria	2%	Wage supplement for employees with jobs at risk, up to 60% of their wage
Cyprus	3%	Extra funding of the healthcare system up to EUR 100 million; income supplement for households, reduction of the VAT rate
Czech Republic	2%	Wage supplement up to 60% for quarantined employees and up to 80% for laid-off employees
Estonia	2%	Compensation of wage cuts; temporary suspension of the obligation to pay taxes; provision of liquidity credit for businesses
Croatia	ca. 1%	Temporary suspension of the obligation to pay taxes for firms operating in the affected economic areas, for at least 3 months; subsidized net wage up to the sum of the minimum wage for furloughed workers
Poland	2%	Wage supplement; business loans for SMEs; the loss run in this year can be written off in next year's tax declaration
Latvia	3%	Wage supplement of to 75% of the total wage (up to 700EUR), suspension of PIT payment obligation on income from this supplement
Lithuania	5%	Extra funding of EUR 500 million for healthcare; additional subsidies for affected employees (in the form of a rent)
Malta	12%	Tax allowances for employees; wage supplements (guaranteed minimum wage, and additional subsidy for employees with wages higher than the minimum wage, up to EUR 1200); raise of unemployment benefits
Romania	2%	Extra funding for healthcare; wage supplement for quarantined employees and employees with jobs at risk
Slovakia	unknown	Temporary suspension of tax-paying obligation for firms in the affected economic areas; wage subsidy for jobs that would be otherwise terminated, due to reduced economic activity, and for the self-employed
Slovenia	6%	Suspension of tax-paying obligation for firms in the affected economic areas for 2 years; wage supplement for troubled economic areas the for quarantined employees; reduction of the price of price regulated goods and services

Source: IMF, own collection

The fiscal policy is clearly aimed at stimulating private consumption, but the magnitude of the measures is not sufficient by far to avoid recession in the coming period. Households typically respond to a crisis with elevated saving activity, thus consumption would slightly contract even in the hypothetical case where households, due to fiscal subsidies, get 100 percent of their former income.

Estimated change in GDP between 2020-2021 in the new EU member states



Source: Kopint-Tárki

Central banks pumped extra liquidity in the financial systems in every country, to ensure the necessary level of financing, through buying government and corporate bonds, lowering reference rates and other, non-conventional means. This may result in an upward jump in inflation, which in turn adversely affects the efficiency of the fiscal measures that aim at consolidating the labor market situation. The protectionist measures, on the other hand, pose a downward risk for inflation, as many countries introduced export embargo for various, strategically important products. The epidemic affects agriculture as well since the harvesting season is coming, but foreign guest workers cannot cross the borders, which may lead to soaring food prices globally, compounding the recessionary effect of the epidemics and prompting further measures by the central banks.

Our growth estimates are based on a moderately optimistic scenario – we assume that the global economy will contract by 2-4 percent in 2020. Under such a scenario, the region may suffer a recession of 3-5 percent this year. If the emergency measures related to the epidemic are lifted well before the end of the year, economic activity may be able to restart in time to gather momentum and achieve a substantial growth of 3-5 percent in 2021.

Table 2/1.

Economic Growth in the EU Member States

(Percentage change of real GDP over the previous year)

	Weight	2014	2015	2016	2017	2018	2019	2020*	2021*
Germany	20.9	2.2	1.7	2.2	2.5	1.5	0.6	-4.5	1.2
France	14.7	1.0	1.1	1.1	2.3	1.7	1.3	-4.2	0.5
Italy	10.9	0.1	0.9	1.1	1.7	0.9	0.3	-7.0	0.4
Netherlands	4.9	1.4	2.0	2.2	2.9	2.6	1.7	-4.3	2.0
Belgium	2.9	1.3	1.7	1.5	1.7	1.4	1.4	-2.4	1.0
Luxembourg	0.4	4.3	3.9	2.4	1.5	2.6	2.3	-3.7	1.8
Ireland	2.1	8.6	25.2	3.7	8.1	8.2	5.5	-7.1	2.5
Greece	1.1	0.7	-0.4	-0.2	1.5	1.9	1.9	-3.9	0.5
Spain	7.6	1.4	3.8	3.0	2.9	2.4	2.0	-5.9	1.0
Portugal	1.3	0.9	1.8	1.9	2.8	2.1	2.2	-4.0	1.2
Austria	2.4	0.7	1.0	2.1	2.5	2.4	1.6	-2.5	1.2
Finland	1.5	-0.6	0.5	2.8	3.0	1.7	1.0	-5.8	1.3
Estonia	0.2	2.9	1.9	3.5	4.9	3.9	4.3	-4.5	3.6
Slovakia	0.6	2.8	4.2	3.1	3.2	4.1	2.3	-4.0	4.1
Slovenia	0.3	3.0	2.3	3.1	4.9	4.5	2.4	-4.7	4.3
Cyprus	0.1	-1.3	2.0	4.8	4.5	3.9	3.2	-2.7	3.0
Malta	0.1	8.2	10.8	5.6	6.8	6.7	4.4	-4.0	2.7
Latvia	0.2	1.9	3.0	2.1	4.6	4.8	2.2	-4.0	3.8
Lithuania	0.3	3.5	2.0	2.4	4.1	3.5	3.9	-4.0	3.7
Euro Area	**72.4**	**1.4**	**2.1**	**1.9**	**2.5**	**1.9**	**1.2**	**-5.2**	**1.1**
United Kingdom	15.3	2.9	2.3	1.8	1.8	1.4	1.4	-2.8	0.5
Denmark	1.9	1.6	2.3	2.4	2.3	1.5	2.2	-4.2	1.2
Sweden	2.9	2.7	4.4	2.4	2.4	2.3	1.2	0.2	0.5
Hungary	**0.9**	**4.2**	**3.5**	**2.3**	**4.1**	**4.9**	**4.9**	**-5.5**	**3.3**
Czech Republic	1.3	2.7	5.3	2.5	4.4	2.9	2.4	-4.4	4.4
Poland	3.2	3.3	3.8	3.1	4.8	5.1	4.1	-3.3	4.1
Romania	1.4	3.4	3.9	4.8	7	4.1	4.1	-3.5	3.8
Bulgaria	0.4	1.3	3.5	3.9	3.8	3.1	3.4	-4.0	3.8
Croatia	0.3	-0.1	2.4	3.5	2.9	2.6	2.9	-3.3	3.7
EU-15	**90.8**	**1.3**	**2.4**	**1.9**	**2.3**	**1.8**	**1.3**	**-4.6**	**0.9**
New EU-13	**9.2**	**2.7**	**3.8**	**3.2**	**4.8**	**4.3**	**3.6**	**-3.9**	**4.0**
EU-28	**100**	**1.8**	**2.3**	**2.0**	**2.6**	**2.0**	**1.5**	**-4.6**	**1.2**
BREXIT	**84.7**			**2.0**	**2.7**	**2.1**	**1.5**	**-4.9**	**1.3**
Memorandum items									
USA		1.8	2.5	2.9	1.6	2.2	2.3	-2.6	2.2
Japan		2.0	0.3	1.1	1.0	1.9	0.7	-1.7	0.6
China		7.7	7.3	7.0	6.7	6.8	6.1	4.9	6.4
Russia		1.3	0.7	-2.8	-0.2	2.2	1.3	-6.1	1.9
South-Eastern Europe									
Serbia		-1.8	1.7	3.3	2.1	4.3	3.2	-3.2	3.7
Turkey		5.2	6.1	3.2	7.4	2.5	-2.3	-2.7	2.9

* Kopint-Tárki forecast

EU-15 = Countries that joined the European Union before 2004 (“Old EU Member States”)

New EU-13 = Countries that joined the European Union in 2004, 2007 and 2013 (“New EU Member States”)

Source: Eurostat, national statistical offices, OECD

Table 2/2.

Inflation in the EU Member States

(Harmonized consumer price indices, percentage change over the previous year)

	Weight	**2014**	**2015**	**2016**	**2017**	**2018**	**2019**	**2020***	**2021***
Germany	19.8	0.8	0.1	0.4	1.7	1.9	1.4	1.2	1.4
France	14.2	0.6	0.1	0.3	1.2	2.1	1.3	1.1	1.4
Italy	12.1	0.2	0.1	-0.1	1.3	1.2	0.6	0.8	1.1
Netherlands	4.0	0.3	0.2	0.1	1.3	1.6	2.7	1.5	1.8
Belgium	2.7	0.5	0.6	1.8	2.2	2.3	1.2	1.5	1.5
Luxembourg	0.2	0.7	0.1	0.0	2.1	2.0	1.6	1.8	2.0
Ireland	1.2	0.3	0.0	-0.2	0.3	0.7	0.9	1.1	1.4
Greece	1.4	-1.4	-1.1	0.0	1.1	0.8	0.5	0.6	1.0
Spain	8.0	-0.2	-0.6	-0.3	2.0	1.7	0.8	1.1	1.4
Portugal	1.5	-0.2	0.5	0.6	1.6	1.5	0.3	1.1	1.5
Austria	2.2	1.5	0.8	1.0	2.2	2.1	1.5	1.3	1.5
Finland	1.4	1.2	-0.2	0.4	0.8	1.2	1.1	1.7	1.8
Estonia	0.2	0.4	0.1	0.8	3.7	3.4	2.3	2.9	2.5
Slovakia	0.6	-0.1	-0.3	-0.5	1.3	2.5	2.8	2.9	2.7
Slovenia	0.3	0.4	-0.8	-0.2	1.6	1.9	1.7	3.0	2.7
Cyprus	0.2	-0.2	-1.6	-1.2	1.0	0.8	0.5	2.6	1.9
Malta	0.1	0.7	1.2	0.9	1.3	1.7	1.5	2.7	1.5
Latvia	0.2	0.7	0.2	0.1	2.9	2.6	2.7	3.4	2.0
Lithuania	0.3	0.3	-0.7	0.7	3.8	2.5	2.2	3.6	2.5
Euro Area	**70.4**	**0.4**	**0.0**	**0.2**	**1.5**	**1.8**	**1.2**	**1.2**	**1.5**
United Kingdom	18.0	1.5	0.0	0.7	2.7	2.5	1.8	1.7	2.2
Denmark	1.6	0.4	0.2	0.0	1.1	0.7	0.7	1.2	1.9
Sweden	2.3	0.2	0.7	1.1	1.9	2.0	1.7	1.2	1.7
Hungary	**0.8**	**0.0**	**0.1**	**0.4**	**2.4**	**2.9**	**3.4**	**3.2**	**3.5**
Czech Republic	1.2	0.5	0.2	0.7	2.3	2.0	2.6	3.5	3.0
Poland	3.4	0.1	-0.7	-0.2	1.6	1.2	2.1	2.8	2.8
Romania	1.6	1.4	-0.4	-1.1	1.0	4.1	3.9	5.4	3.3
Bulgaria	0.4	-1.6	-1.1	-1.3	1.0	2.6	2.5	3.3	2.5
Croatia	0.3	0.3	-0.3	-0.6	1.3	1.6	0.8	2.6	1.9
EU-15	**90.6**	**0.6**	**0.1**	**0.4**	**1.7**	**1.9**	**1.4**	**1.3**	**1.6**
New EU-13	**9.4**	**0.3**	**-0.4**	**-0.2**	**1.7**	**2.2**	**2.6**	**3.5**	**2.8**
EU-28	**100.0**	**0.5**	**0.0**	**0.3**	**1.7**	**1.9**	**1.5**	**1.5**	**1.7**
BREXIT	**82.0**			**0.2**	**1.6**	**1.8**	**1.4**	**1.4**	**1.6**
Memorandum items[a]									
USA		2.1	1.5	1.6	0.1	1.3	1.8	1.9	2.1
Japan		0.0	0.4	2.7	0.8	0.5	0.8	1.1	0.9
China		2.6	2.6	2.0	1.4	2.0	2.2	3.2	3.0
Russia[b]		6.8	7.8	15.5	7.0	2.9	4.5	4.0	4.3
Délkelet-Európa									
Serbia		1.5	2.3	1.1	3.1	2.0	2.5	3.5	3.0
Turkey		7.8	8.9	7.7	11.0	16.7	13.3	11.0	7.0

a Non-harmonized consumer price indices

b December/December

* Kopint-Tárki forecast

EU-15 = Countries that joined the European Union before 2004 (“Old EU Member States”)

New EU-13 = Countries that joined the European Union in 2004, 2007 and 2013 (“New EU Member States”)

Source: Eurostat, national statistical offices, OECD

Table 2/3.

Harmonized Unemployment rates in the EU Member States

(Unemployed as a percentage of the labor force aged 15-74, ILO-Eurostat)

	Weight	2014	2015	2016	2017	2018	2019	2020*	2021*
Germany	17.5	5.0	4.6	4.1	3.8	3.4	3.2	5.8	4.9
France	12.2	10.3	10.4	10.1	9.4	9.1	8.5	8.3	6.8
Italy	10.5	12.7	11.9	11.7	11.2	10.6	10.4	14.8	13.2
Netherlands	3.7	7.4	6.9	6.0	4.9	3.8	3.4	3.8	4.2
Belgium	2.1	8.5	8.5	7.8	7.1	5.9	5.6	6.3	6.5
Luxembourg	0.1	6.0	6.5	6.3	5.6	5.3	5.3	5.3	5.2
Ireland	1.0	11.9	10	8.4	6.7	5.8	5.1	12.1	8.3
Greece	1.9	26.5	24.9	23.6	21.5	19.3	17.8	16.4	15.0
Spain	9.4	24.5	22.1	19.6	17.2	15.3	14.0	13.9	12.9
Portugal	2.1	14.1	12.6	11.2	9.0	7.0	6.4	6.7	6.0
Austria	1.8	5.6	5.7	6.0	5.5	4.9	4.7	6.5	6.0
Finland	1.1	8.7	9.4	8.8	8.6	7.4	6.8	8.8	8.7
Estonia	0.3	7.4	6.2	6.8	5.8	5.7	5.5	6.6	5.4
Slovakia	1.1	13.2	11.5	9.7	8.1	6.9	5.8	6.7	5.3
Slovenia	0.4	9.7	9	8.0	6.6	5.6	4.2	6.0	4.9
Cyprus	0.2	16.1	15	13	11.1	8.2	6.5	7.0	6.5
Malta	0.1	5.8	5.4	4.7	4.0	3.9	3.5	4.1	3.6
Latvia	0.4	10.8	9.9	9.6	8.7	7.3	6.5	6.9	6.4
Lithuania	0.6	10.7	9.1	7.9	7.1	6.5	6.1	6.6	6.0
Euro Area	**66.4**	**11.6**	**10.9**	**10**	**9.1**	**8.2**	***7.6***	**9.3**	**8.2**
United Kingdom	13.5	6.1	5.3	4.8	4.4	4.0	3.8	6.8	6
Denmark	1.2	6.6	6.2	6.2	5.7	5.0	4.9	5.1	5.2
Sweden	2.2	7.9	7.4	6.9	6.7	6.3	6.8	7.0	6.7
Hungary	**1.9**	**7.7**	**6.8**	**5.1**	**4.2**	**3.7**	**3.4**	**7.5**	**5.5**
Czech Republic	2.2	6.1	5.1	4.0	2.9	2.4	2.3	4.0	3.1
Poland	7.0	9.0	7.5	6.2	4.9	3.3	3.8	4.4	3.7
Romania	3.6	6.8	6.8	5.9	4.9	4.3	4.2	5.0	4.2
Bulgaria	1.3	11.4	9.2	7.6	6.2	6.0	4.0	5.1	4.0
Croatia	0.7	17.2	16.1	13.4	11.1	9.1	6.0	8.0	6.0
EU-15	**80.2**	**10.5**	**9.9**	**9.2**	**8.4**	**7.5**	***7.1***	**8.8**	**7.9**
New EU-13	**19.8**	**10.4**	**7.9**	**6.6**	**5.5**	**4.5**	***4.1***	**5.3**	**4.3**
EU-28	**100.0**	**10.2**	**9.4**	**8.6**	**7.6**	**6.8**	***6.4***	**8.1**	**7.1**
BREXIT	**86.5**			**9.2**	**8.2**	**7.3**	**6.7**	**8.3**	**7.3**
Memorandum items [a]									
USA		7.4	6.2	5.3	4.9	4.3	3.7	6.9	9.1
Japan		4.0	3.6	3.4	3.1	2.8	2.4	4.4	3.8
China[b]		4.6	4.7	4.1	4.0	4.0	3.8	5.5	5.5
Russia[c]		5.5	5.1	5.6	5.7	5.4	5.2	7.3	7.5
South-Eastern Europe									
Serbia[d]		22.1	19.2	15.3	13.5	12.7	11.0	15.0	12.5
Turkey		9.0	9.9	10.9	10.9	11.0	14.0	16.0	13.6

a Non-harmonized unemployment rates
b Urban unemployment
c OECD statistics, unemployment rates for the age group 15-64
d National statistics, unemployment rates for the age group 15-64
* Kopint-Tárki forecast

EU-15 = Countries that joined the European Union before 2004 (“Old EU Member States”)
New EU-13 = Countries that joined the European Union in 2004, 2007 and 2013 (“New EU Member States”)

Source: Eurostat, national statistical offices, OECD

3. The Hungarian economy

The coronavirus epidemic caused unprecedented uncertainty, making economic forecasts almost impossible. As opposed to the typical crises, this one is not initiated by economic factors, hence there are no well-tested ways to model and calculate its effects. It is hard to tell the duration and depth of the trigger of the crisis – the pandemic – hence it is doubly hard to make meaningful predictions about the crisis itself. The epidemic brought about a double whammy – supply and demand shock at the same time. Due to the restrictions on mobility, the operation of plants and service providers is hindered, supply chains are disrupted, and the resulting loss of jobs and income will lead to a severe drop in household consumption, resulting in a demand shock. A significant part of the service sector was forced to suspend operation.

Under such conditions, it is especially vital to lay down explicitly the assumptions on which the forecast rests. These assumptions about the time scale of the epidemic cannot be seen as predictions – such predictions are outside of the domain of economic forecasters – but only as conditions under which the economic forecast is plausible.

The economic forecast of the Kopint-Tárki rests on the assumption that by the end of the summer all the restrictions will be lifted, as the epidemic fizzles out, there will be no second and third wave of the epidemic, hence the last third of this year will be characterized by the progress of economic consolidation. This admittedly is an optimistic scenario.

Based on this scenario, we expect **the GDP to drop by 5-6 percent in 2020**. The economy may have grown by roughly 1 percent in the first quarter, due to the reasonably good pace in January and February, even though both industrial output and construction output certainly fell in March. Only the value added of services is expected to achieve modest positive growth in the first quarter as a whole. On the expenditure side, the retail trade turnover grew even more dynamically in the first quarter than in 2019, since in March the level of spending was kept high by panic buying, but the consumption of services plunged in March. Overall private consumption may have grown by roughly 4 percent in the first quarter.

The second quarter, on the other hand, will be marked by plummeting economic activity almost across the board – GDP will probably drop by more than 10 percent. Unemployment has been rising precipitously during the past month and a half, a sizeable part of households (first of all: the precariat and individual entrepreneurs) has lost its livelihood. Due to this, and also due to the decreased availability of services and retail outlets, private consumption may fall 10 percent or more in the second quarter, along with a similar drop in fixed investments. The net export position is bound to deteriorate: while the net export of goods may remain stable, or may even improve – if merchandise import decreases at a steeper pace than export – the net export of services will collapse, along with inbound tourism, the largest item within the external trade of services.

The second half of the year is even more hard to predict. Assuming that by the end of summer some inroads will be made in consolidating the level of economic activity, GDP may "only" decrease by 8-9 percent in the third quarter, and by 2-3 percent in the fourth. In 2020 as a whole, household consumption may drop by 4-5 percent and fixed capital formation by 5-7 percent.

This is a relatively pessimistic growth estimate, with ample negative risks attached. If the epidemic lasts further, or returns toward the end of the year, the economy may fall by as much as 10 percent.

The numbers above represent the “baseline” prediction of the Kopint-Tárki that assumes that no serious measures are taken to save the jobs and to keep the fall of household incomes under check.

The epidemic triggered a wave of emergency packages, financed from fiscal resources, among the countries of the world, to provide temporary help to the economy. Such measures are supported by the European Union as well since the Commission called for an easing of fiscal policies and for using all the available funds to combat the virus crisis. Governments seek to give a lifebelt to firms that got into difficulties to keep them above the water during the months of the epidemic and to help them keep much of their workforce. The overview of the emergency measures in 193 countries, provided by the IMF (https://www.imf.org/en/Topics/imf-and-covid19/Policy-Responses-to-COVID-19#P), shows a wide palette of actions. But the most important common feature in these packages is the efforts to prevent catastrophic job losses. These efforts simultaneously serve to ensure the survival of firms, the maintenance of the fabric of the economy and to provide income for households, thus preventing consumption levels from plummeting. Besides, a wide variety of other measures can be found in various countries, from tax holidays or the prolongation of tax deadlines, provision of preferential credit, credit guarantees, or even helicopter money, that is, the distribution of one-off money transfer among the population (see, for example, the USA).

In comparison, the Hungarian emergency package came after a delay of almost one month. The first package included only debt service moratorium, tax holidays for a number of tax types, a moratorium on rent hikes, and certain benefits for the tourism sector. All this, however, only constituted a few tenths of a percent of GDP. The debt service moratorium simply transferred the burden on the banking sector that would, therefore, face a severe liquidity crisis, had the NBH not intervened with measures of its own that entailed the provision of unlimited and cheap credit for the banks. By the reduction of the tax burden on small businesses, the government only renounced revenues that would have been lost anyway, since it is the self-employed working in the liberal professions, small industry entrepreneurs, professional service providers, artists, etc. who typically opt for the Small Business Tax, and they are exactly those who completely lost their income with the onset of the virus crisis.

This is why there was so much hope before the announcement of the second package on April 7, followed by bitter disappointment after the announcement.

1. To start with the positive, the package contains the awaited wage subsidy scheme for those employees who are now put on a short-time working arrangement, up to 70 percent of the otherwise lost part of the wages for a maximum of three months. The firms that are most severely affected by the crisis (with a fall of more than 75 percent in economic activity), or the firms relatively mildly affected (a fall of less than 15 percent) are excluded, thus limiting the access to this scheme. There is also a (not very generous) upper limit for the sum paid after individual employees.

In any case, the delayed introduction of the package caused serious harm to the business sector. The crisis not just destroys but also redistributes relative positions among the

companies. International market power positions may change significantly. The firms in countries that reacted to the crisis faster and more efficiently may gain market positions over firms based in countries with a lagging response and therefore with a more severely tattered business sector.

In addition, a number of other measures are included in the package that, although not really relevant on a macro scale, do help to alleviate the problems of certain social groups – these include the deferment of certain tax return or tax payment deadlines, the prolongation of the provision of student loans or the provision of support for those caring for children with special needs.

2. The package was in part disappointing because it has parts that are to be activated only in 2021 – the raise of pensions, for example – thus do nothing to alleviate the difficulties of firms or families now.

On the other hand, it is also clear that part of the measures is not even linked – directly or indirectly – to the virus crisis. Instead, they are included in the package to intervene in the direction of economic development, providing investment subsidies and buttress certain economic areas selected by the government as a way to create jobs. But the task here and now is to keep the economy functioning, to save jobs by helping the firms to stay alive, so that they are able to continue their operation after the crisis in the largest number possible. Before the crisis, the Hungarian economy functioned reasonably well, even if not perfect by far, and even developed. The second emergency package, however, focuses not on saving the functioning businesses but on pushing through forceful state intervention, at a magnitude of several thousands of billions of forints, while only a couple hundred billion forints are used to direct crisis management.

The statements about the post-crisis "restarting" of the economy suggest a misunderstanding about the role of economic policies on the part of the government. In the case of a timely and effective rescue package – that is, if the state helps the firms through the crisis with the use of fiscal means – there is no need for "restarting" the economy because the economy will restart on its own.

It is also very doubtful whether the government is the best arbiter of which economic areas are to be developed – the historical experience is less than encouraging in this regard. Still, it would be understandable if the government – responding to the experience of this health crisis – wanted to buttress the health industry and the pharmaceutical industry. Healthcare is in great part is the responsibility of the state to start with. To select some other, market-based industries and to support them with preferential loans or even by giving them state capital, whatever those areas be – construction, logistics, film industry, and especially tourism – will lead to market distortions even if we assume that the allocation of subsidies is free of political considerations or consideration of "friendly links". The Hungarian tourism sector is already very well developed: Large hotels and smaller high-end pensions and tourism attractions have been mushrooming during the past decades. Economic policies should focus on preserving those, instead of making up subsidized credit schemes for the tourism sector at a magnitude of many hundred billion forints. Especially considering that even the utilization of the existing tourism capacities will take considerable time since tourism is expected to be among the areas that will be the slowest to recover.

3. **The emergency package does not include any measures to directly help those who completely lost their livelihoods due to the crisis**. There is no support for families, although the epidemic brought a spread of severe poverty, malnutrition of children and homelessness. Casual workers do not get help either. Employees can hope that they remain at least on a part-time basis – possibly receive support under the aegis of the shortened work time scheme – or if everything else fails, they can get unemployment benefits for three months. But the wide segment of self-employed cannot count any kind of help. As a result, the existence of hundreds of thousands, maybe even a million, is under threat. This is a problem that should be treated with the means of social policy, rather than as a law enforcement problem.

The Hungarian economy may suffer from the virus crisis more heavily than its neighbors mostly because here the number of those among the threatened who are completely excluded from the rescue package is larger, hence the consumption level of wide segments of the population will hit rock bottom. The majority of the vulnerable families do not have savings with which they could temporarily substitute the inflow of current incomes.

4. As for the newly introduced special banking and retail taxes and the stripping of local governments from their income sources: **out of the 193 countries surveyed by the IMF, not a single one, save Hungary, introduced new taxes or confiscated revenues. This is, indeed, a "true Hungarian specialty"**. The banking sector – that already paid a special tax to the magnitude of HUF 65 billion per year – is hit by the credit service moratorium as well, even if many debtors will opt for the continuation of debt service, that is, if they can afford it. On the other hand, those who make use of the moratorium – most likely the debtors who lost their income source – will find themselves in an impossible situation when the moratorium ends and they will have pay both the current and the accumulated obligations, while they were never got any compensation for the incomes foregone during the crisis. In other countries, the governments seek to strengthen the banking sector, thereby seeking to keep up the flow of credit to the business sector, instead of burdening the banks with more taxes. The Hungarian situation is greatly alleviated by the preferential loan program of the NBH. The latter helped the forint as well: the euro/forint exchange rate dipped below 360 after the program's announcement on 7 April.

As is well known, the **new retail tax** is not the first attempt to weaken the multinational retail chains. The new tax will probably accelerate the already steep rise of food prices, pushing the inflationary pressure upward.

The rationale of the measure to deprive the **local governments** of revenues amounting to HUF 34 billion cannot really be captured in terms of fiscal or macroeconomic needs – it is rather a result of political considerations.

5. The new scheme Funding for Growth "Go!", announced on 7 April, offers business loans with a maturity of up to 20 years at an interest rate not higher than 2.5 percent to enterprises through the banking system. An important advantage of this scheme that it allows any type of credit (investment loan, current asset financing, loan for payment of wages, or loan replacement). The effectiveness of the program is limited, however, by the fact that the assessment of creditworthiness remains in the hands of the banks, due to which probably many firms that have been brought to their knees by the crisis will be

unable to obtain the loan. The involvement of the state guarantee fund may alleviate this problem, but many firms may be excluded from the scope of this fund as well.

6. The question of to what degree the fiscal deficit can be let grow unchecked under the conditions of the coronavirus crisis is a subject of debate in every country. It is a question of to what degree the burden should be passed on the coming years in the form of enlarged fiscal debt. Most countries concluded that to address this – presumably temporary – crisis, it is warranted to go very far in letting the deficit balloon. The rationale is that in the case of a "prudent" fiscal stance the economy will suffer more from mass bankruptcies and scattered supply chains than from an elevated fiscal debt in the case of a more accommodating fiscal stance. Moreover, the automatic stabilizer will raise the deficit even without specific measures since the fall of incomes and consumption will drastically reduce tax revenues. on the other hand, if the state gives fiscal support to enterprises to help them survive than a part of the subsidies may be later reimbursed during the recovery, in the form of surplus tax revenues.

Even though Hungary's fiscal position is much more favorable this time than it was at the onset of the 2008 crisis, the fiscal wiggle room still falls below that in most of the other EU member states. During recent years, many countries achieved major fiscal consolidations, utilizing the opportunity given by the worldwide economic upturn. As a result, in 2019 almost half of the member states posted a fiscal surplus. By contrast, the Hungarian deficit remained near 2 percent of GDP, which means that the Hungarian fiscal policy was less countercyclical than in other countries. As a result, the upper limit of a fiscal stimulus still deemed acceptable by investors and international organizations may be lower in Hungary than elsewhere. It may help, however, that there is an unusually large reserve separated in the 2020 budget. This reserve will be badly needed.

The 5.5 percent recession will in itself worsen the fiscal balance by 4.4 percentage points, primarily due to the loss of revenues – first of all, personal income tax and social security contribution revenues – but also due to rising expenditures on unemployment benefits. The automatic stabilizer is still operative, even though the short duration of unemployment benefits and the flat tax rate stunts its effect somewhat. Still, additional fiscal demand stimulation would be needed, but the already known measures are not very promising on that front.

The government communicates an enormous fiscal package amounting to 18-22 percent of GDP. But – apart from the vagueness about the details, only a small fraction is aimed at directly helping firms and households to weather the crisis. Moreover, much of the package does not come from new spending but the reallocation of existing funds, extra taxes and funds taken away from local governments. The most effective way of short-term demand stimulation is raising new resources through (additional) deficit financing, not reallocating existing funds. The pension hike, starting in 2021 and completed three years later, obviously does not help in short-term demand stimulus, either. It should be noted that the timing notwithstanding, it would more effective – in terms of stimulating demand – to concentrate the pension hike to lower pensions, instead of supporting the social group whose income – in general – is the least jeopardized by the present crisis. The actual demand stimulus not even reaches 1 percent of GDP, unlike in other countries. While some measures – like the suspension of the obligation to pay the Small Business Tax – are positive, the subsidized shortened working time scheme only bears a surface similarity to the German Kurzarbeit program, because while in Germany a

substantial part of the total wage is paid by the state, in Hungary the state only assumes the payment of 70 percent of the part of the former wage that is now lost by the employee, due to the shorter working hours.

As things stand at present, the fiscal deficit will rise to 5.1 percent despite the fact that the positive effect of fiscal stimulus will be quite limited. With a larger stimulus, the recession could be kept less drastic, which would eventually benefit the state budget as well, thereby reducing the cost of the fiscal intervention. In any case, the debt-to-GDP rate will certainly rise back above 70 percent, to which will the weakening of the forint will contribute as well. The impact of the forint weakening is moderated by the fact that the share of FX-denominated debt within the overall state debt has considerably decreased over the ten years.

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Several prominent economists have drawn attention to the fact that the addressing of the consequences of the coronavirus entails an increase of fiscal spending of such proportions that is impossible – but also undesirable – to finance through the usual method of deficit financing, that is, by issuing bonds. Financing the rescue package through the reallocation of spending is self-defeating since it decreases the demand of certain sectors and thus cannot achieve the goal of offsetting the decrease of private demand with state demand. Therefore, it is worth considering the possibility of moving beyond the usual framework of fiscal rules and taboos that prohibit the direct financing of fiscal deficit by the central bank. Temporarily allowing such a way of deficit financing would significantly help cushioning the economic crisis.

The NBH announced in 7 April that it would embark on purchasing government securities from the secondary markets. Previously such a practice was deemed taboo too. Still, the direct deficit financing by the central bank would be a technically easy solution worth considering. The central bank places the necessary sum on the current account of the state (provides credit) – this sum will simultaneously appear on the resource side of the balance sheet of the central bank as an addition to the monetary base (cash and bank deposits). The cash part of the monetary base is a liability of the consolidated general government (that includes the central bank) but it is not a debt since it has no maturity and no interest. Such a financing method should only be applied under extraordinary circumstances, but the present situation is extraordinary enough.

Macroeconomic indicators for Hungary and Kopint-Tárki forecast

(year-on-year change, percentage)

	Data			Forecast	
			2020	2020	
	2018	2019	Q1	2019 Dec.	2020 Apr.
GDP aggregates, real growth					
GDP total	5.1	4.9		3.2	**-5.5**
Domestic Demand	7.3	5.6		3.4	**-4.3**
Private Consumption	4.0	4.4		3.7	**-4.6**
Public Consumption	2.0	2.0		0.0	**0.9**
Gross Fixed Capital Formation	17.1	15.3		5.0	**-5.6**
Gross Capital Formation	18.3	9.5		5.0	**-5.6**
Export	4.3	6.0		5.0	**-8.9**
Import	6.8	6.9		5.1	**-7.6**
Industrial production	3.6	5.4	*0.1*	4.3	**-10.0**
Consumer Price Index	2.8	3.4	*4.4*	3.4	**3.2**
Employment, earnings					
Number of Employed, growth [a]	1.1	1.0	*-0.2*	0.5	**-8.0**
Employment rate [a]	60.4	60.8	*60.6*	61.1	**56.0**
Unemployment Rate [b]	3.7	3.4	*3.5*	3.3	**7.5**
Unit Labor Costs, in EUR[c]	4.9	-11.6		4.8	**-2.2**
Gross Nominal Wages	11.3	11.4	*9.2* [f]	8.5	**6.0**
Net Real Wages	8.3	7.7	*4.3* [f]	4.9	**2.7**
Savings Rate, % of GDP [d]	6.2	5.0		4.0	**5.0**
Current and Capital Accounts Balance, % of GDP	2.2	1.0		1.0	**0.8**
General government					
Fiscal Balance, ESA-2010, % of GDP	-2.1	-2.0		-1.0	**-5.1**
Gross Government Debt % of GDP	70.2	66.3		66.5	**73.9**
Short-term Government Yields (3M), eop	0.00	-0.01	*0.77*	0.2	**1.0**
Long-term Government Yields (10Y), eop	3.01	2.01	*2.65*	2.5	**3.0**
External assumptions					
Internat. Trade in Goods and Services [d]	4.0	4.0		3.2	**-3.9**
Brent Oil Price ($/bbl, p. avg.)	71.3	64.4	*50.4*	63.0	**45.0**
GDP Real Growth, Eurozone	1.9	1.2		1.2	**-5.2**
GDP Real Growth, New EU Members	4.3	3.6		3.0	**-3.9**
EUR-HUF, period average	319	325	*339*	330	**360**
EUR-USD, period average	1.18	1.12	*1.10*	1.11	**1.10**

a ILO methodology, period averages, aged 15-74, including public workers
b ILO methodology, period averages, aged 15-74, excluding public workers
c Manufacturing, based on gross value added and the monthly average compensation of employees in euro, cumulated from the beginning of the year
d Net lending of households according to the financial accounts statistics, as a percentage of GDP
e Trade of goods and services, data based on IMF World Economic Outlook
f January-February

Manufacturing confidence survey results at the end of March

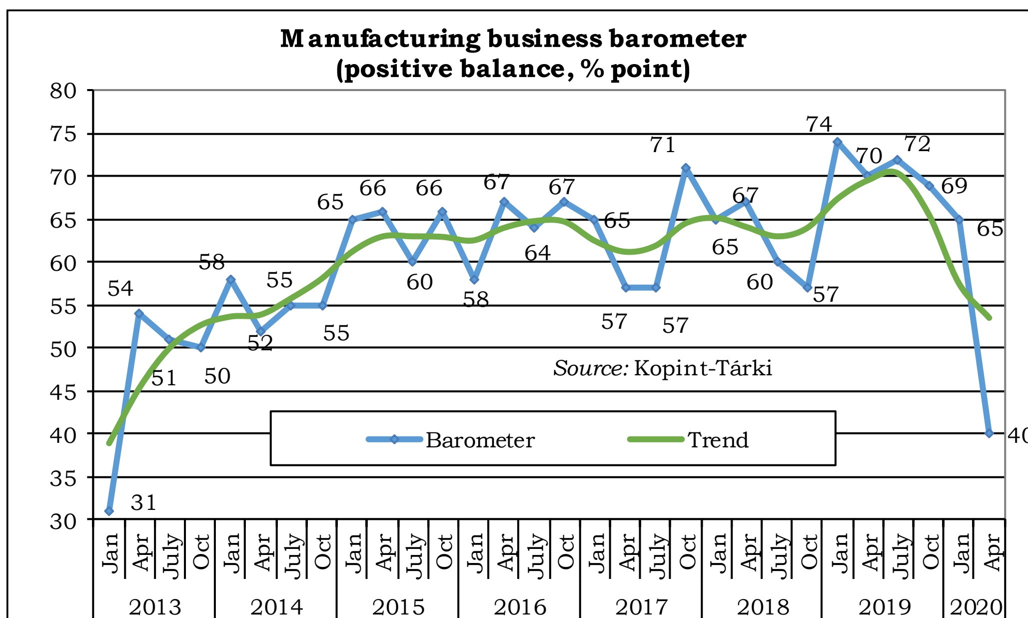
In the first quarter of 2020, business prospects deteriorated drastically for manufacturing firms. The survey, conducted in the second half of March, dropped to its lowest level within the last 132 months. The business barometer (a combined assessment of the present situation and future prospects by the firms themselves) fell to 40 points from the 65 points in January. The barometer score has almost never not been lower: the two exceptions are the acute crisis in 2008-2009 on the one hand, and the return of recession in 2011-2012 on the other.

The confidence index, a combined index of more objective indicators (output stock, stock of orders, production forecast) plunged from 57 points in January to 43 points in late March. This, too, is quite close to the historical negative record registered during the winter of 2008. Beside the global crisis, only during the low point of the "transformational crisis" in 1992 was the sentiment of manufacturing firms nearly as dim.

The respondents unequivocally deem the prospects of the Hungarian economy unfavorable, with the score falling from 50 points (that is, stagnation) in January to 22 points in late March.

The assessment of the near future is gloomy among the firms across the board, in all size categories. The subjective assessment of the future – 29 points – is an absolute record, worse than even the assessment professed in late 2008. The number of firms whole previously good prospects soured dramatically is very high. As a result, the production outlook fell to 34 points. Among the hindering factors, insufficient demand and economic uncertainty suddenly became more prominent, at 29 and 34 percent of respondents, respectively. True, these ratios are still below the typical levels during most of the past decades, but the ratios are bound to climb further during the second quarter. In contrast with the past 7 years, the firms' employment projections are clearly negative, at 41 points.

59 percent of the respondents reported a decline in production volume and 14 percent reported complete halt of production activity. 82 percent of the firms have only liquidity

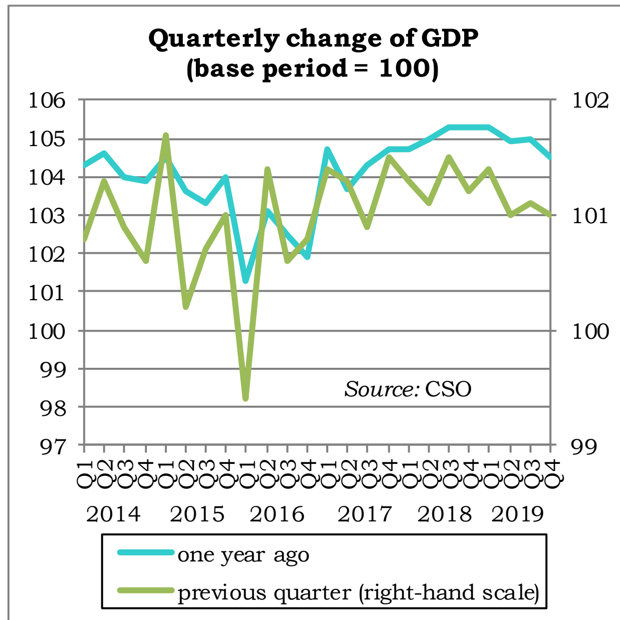


reserves up to three months at most. 28 percent is forced to implement severe restructuring (layoffs, credit rescheduling), and only 43 percent was able to restart production immediately if the virus-related restrictions had been lifted in a short period of time. The rest, however, faced a collapse of their markets, hence it would take at least 3 months for them to restart production. Under such circumstances, more than half of the respondents expect deterioration in their financial standing in 2020, and only 10 percent expects some improvement compared to 2019.

Long-term expectations had been also revised downward during the global financial crisis, but that was mostly because of the worsening financing conditions. Now, on the other hand, financing conditions remained quite favorable while production slowed down or even halted worldwide, sometimes due to direct government orders. While the restrictions of economic activity are very slowly eased in early May, a possibility of a severe second wave of the epidemic keeps the outlook depressed. The supply of parts and materials is quite precarious, especially since the supplier developing economies are to be hit by the virus crisis much more severely than the developed countries.

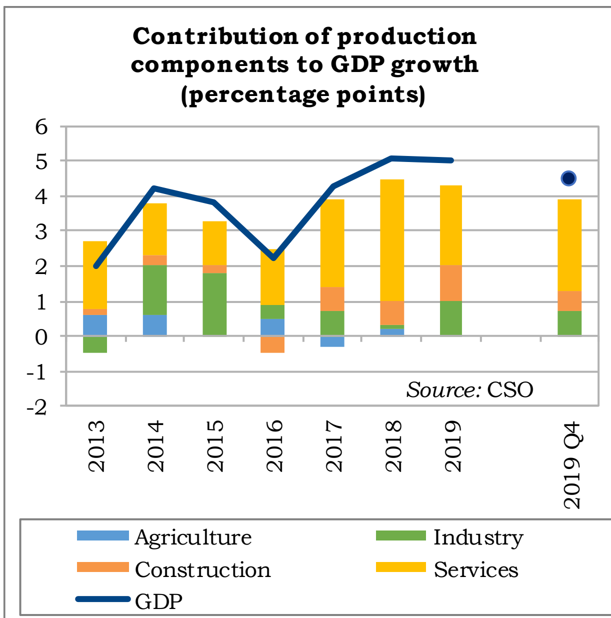
GDP and its components

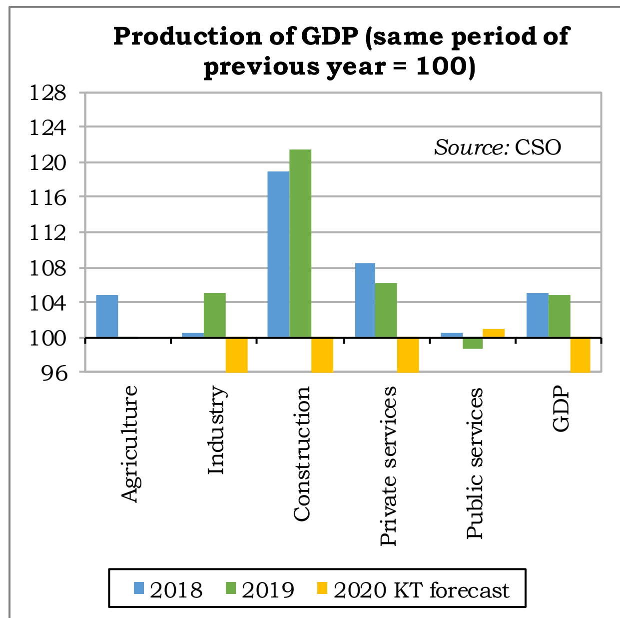
In the fourth quarter of 2019, GDP growth was still going strong, with a rate of 4.5 percent. As a result, **average annual growth** was 4,9 percent in the last year, the second highest within the EU.



As for the structure of growth, on the ***production side*** the acceleration of market services growth, driven by domestic demand, was the main supporting factor behind the high growth rate. At the same time, *industry* and *construction* decelerated more steeply than previously expected.

On the ***expenditure side***, consumption growth gained further momentum while *fixed capital formation* decelerated steeply, primarily due to the negative turn in manufacturing investments at the end of the year. Still, ***final domestic use*** grew by an impressive 6.6 percent in the fourth quarter. On the other hand, merchandise export growth almost halted in the last quarter, resulting in a marked deterioration of net export position.





The ***whole year of 2019*** was characterized by the strong expansion of domestic use whole net export held back economic growth to a degree, due to the negative growth contribution of net merchandise export. On the production side, construction value added grew at a dramatic pace above 20 percent – despite the slowdown in the last quarter – while industry and market services expanded at a solid pace.

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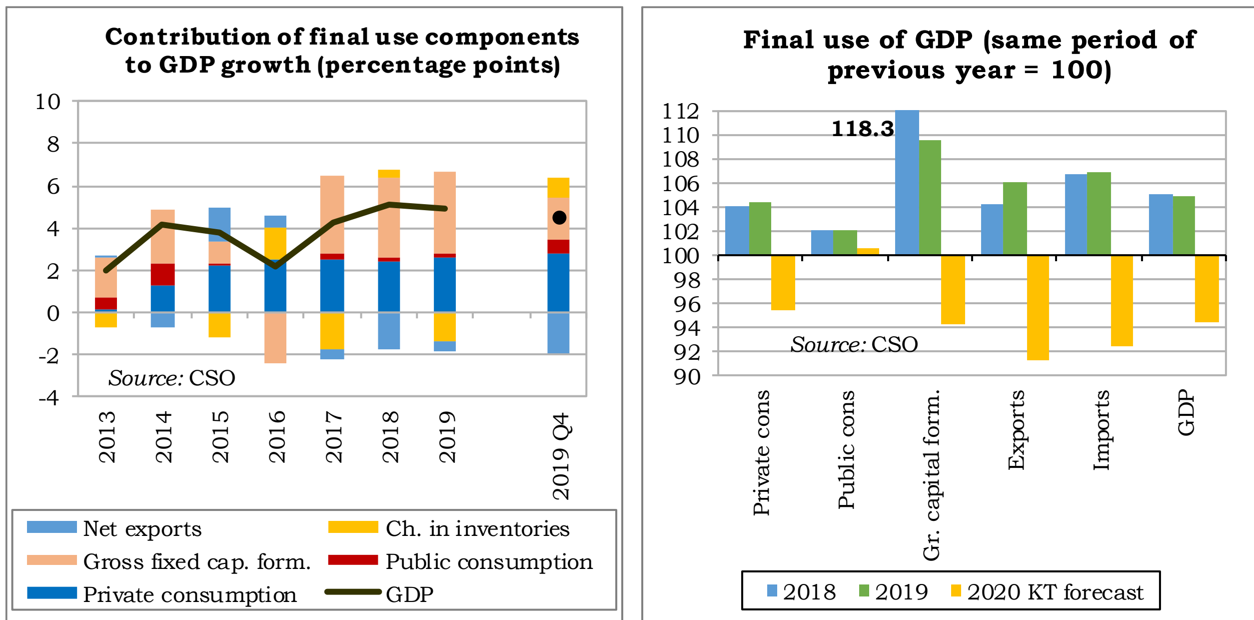


While the economy kept growing in the first two months of 2020, March saw an implosion of economic activity, due to the virus crisis and the accompanying restrictive measures. While a substantial part of the population does not leave its home, some segments of their market demand automatically ceased to exist, at least temporarily. There is virtually no tourism, the restaurant, catering and personal service sector is almost completely inactive. Food retail turnover jumped in March, but this was temporary. Automotive plants were closed until late April, due to both demand and supply shocks, and other industrial firms were also forced to halt or drastically reduce production. Without sales revenues, the firms' financial standing is deteriorating, the wave of layoffs and bankruptcies is underway.

The operation of certain economic branches – agriculture, food industry, freight transport, energy supply – must be maintained even amid the pandemics, but even these areas are not spared from disruptions. Vital international transport routes within the EU became congested due to the activation of national borders, and transport firms are hit by the reduced solvency of their customers.

While the overall demand for *food products* will not necessarily decline, a marked shift in its structure will take place during the epidemic. In *construction*, the arrival of new orders has slowed down, and many smaller firms suspended their activity as early as in March.

On the whole, while GDP is expected to expand by about 1 percent in the first quarter, it will drop drastically – probably at a double-digit rate – in the second quarter. The question is, what will happen after that.

At the moment, ***we optimistically assume that the epidemic peters out by the end of the summer, and there will be no second wave***. Therefore, it is assumed that the pace of the recovery from the autumn mostly depends on economic, and not health, factors, such as: how shaken the whole private firm sector will be by that time, to what degree the households' financial standing and willingness to spend will deteriorate, and in how bad shape the world economy will be at that point.

Due to the widespread layoffs and the growing uncertainties about the income prospects, households are to put a massive break on ***consumption***. Since unemployment benefits

are not expanded and only a limited pool of employees will get financial support from the government (in the form of the subsidized shortened work time scheme), the perception of existential risk on the part of the household will remain acute. This – in addition to the drop of spending capacity of many households, the growing number of households sliding into poverty and destitution – will pull down private consumption, and this is also true in the case of household investments.

As for the ***business sector***, the main question is how widespread bankruptcies will become and how far the erosion of existing productive capacities wil get by the end of the epidemic. The main thrust of the government and the central bank is apparently to provide very ample liquidity in the forms of cheap loans. But even so, we expect a severe wave of bankruptcies, primarily among smaller firms, with a considerable loss of capacities, especially in services. A support scheme with a stronger focus on non-refundable subsidies for the SME sector may have been able to raise the survival rates among SMEs and make a somewhat faster recovery possible.

In any case, the rupture in the financial standing and prospects of firms causes a drop in the willingness of private firms to start ***investment projects***. The government says that it will initiate a public investment program at a magnitude of about 1 percent of GDP to stimulate the economy and cushion the fall of investments. In the second half of the year, this initiative may stimulate the recovery, even though a part of the funds earmarked will not be utilized before the start of the next year.

As both consumption and investments will fall, ***final domestic use*** is also expected to decrease by more than 4 percent in 2020. At the same time, both export and import flows will drop – the net balance is expected to be negative, due to loss of tourism income, the main factor behind the usually very sizeable surplus in the external trade of services.

To sum up, a very steep fall of GDP is expected from March to the end of summer. The subsequent recovery will be hindered by the high unemployment and the decimation of the sme-sector – both the rebuilding of the workforce and the enterprise sector will take time. The elevated level of unemployment will pull down wage growth even after the end of recession. This, and the high number of households with brittle income prospects, will hinder the recovery of private consumption.

This also raises the question whether the sudden halt in the formerly dynamic trend wage growth will cause a prolongation of the previous growth model – that is, the growth model based on cheap labor supply – that just began losing its viability, after several years of fast wage growth. If this is the case, then the difficult switch to a different, more perspectivical growth model will be delayed.

We expect the GDP to fall by about 5.5 percent in 2020, with a moderate upturn in the next year. It should be noted, however, that the chance of such an upturn will be greatly threatened if the "whatever-it-takes" spending policy of 2020 gives way to a harsh corrective fiscal stance on the part of the EU, as it happened after the 2008-2009 crisis.

3.1. The production of GDP

3.1.1. Industry

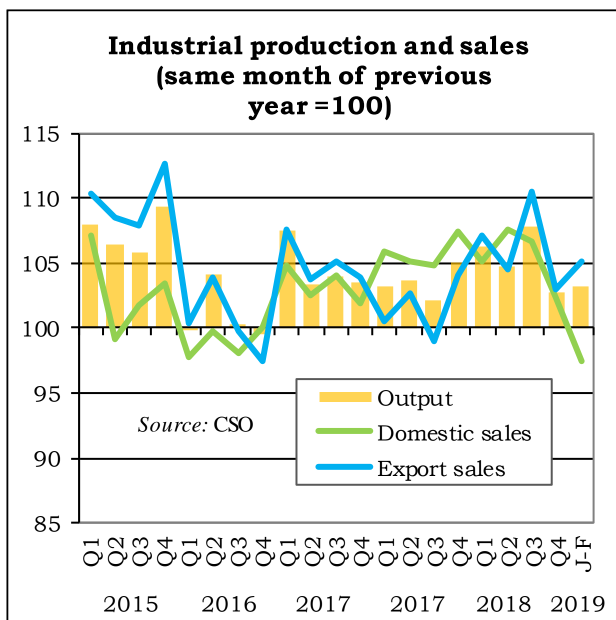
In 2019, industrial production expanded at a relatively good pace of 5.4 percent, but with a marked slowdown in the last quarter. In *January-February*, industrial growth was only 3.2 percent (only 2.2 percent without the extra day in February, due to the leap year). In contrast with 2019, domestic sales pulled the overall growth rate down considerably in January-February. From March, of course, the epidemic upset all the previous trends as the large automotive firms halted production, followed suit by most of their major suppliers.

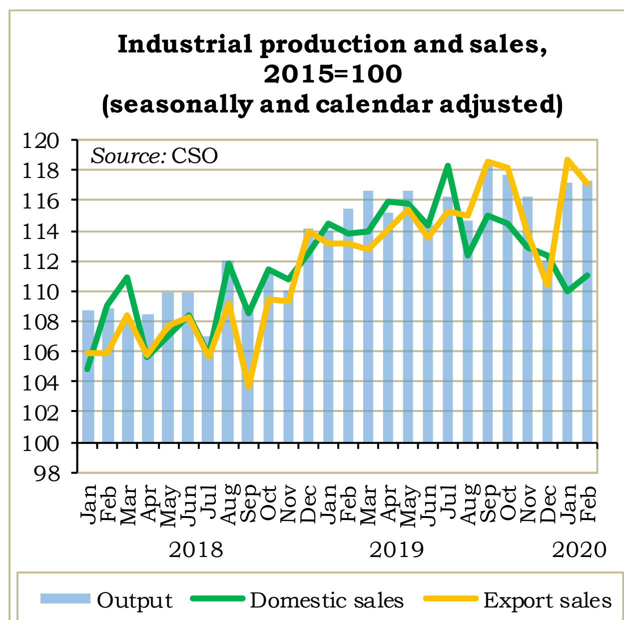
But stoppages have occurred in other industrial branches as well. According to the latest manufacturing survey by Kopint-Tárki, more than one-tenth of industrial firms halted, and another 20-25 percent of firms severely reduced their production activity. Industrial output may drop by 15-20 percent in second quarter of this year – even though the major automotive firms have already begun to restart production at an extremely reduced level – and only a slight improvement can be expected in the third quarter, as the epidemic is unlikely to fizzle out before late summer.

The recovery of industrial production afterwards will depend on how fast the spending ability and willingness of households in and outside Hungary will be rebuilt, particularly with regard to consumer durables. On the supply side, recovery depends on how many industrial firms can weather the virus crisis relatively undented.

It is to be seen whether the present crisis prompts a lasting change in industrial firms' behavior – they may seek to enhance resilience by altering their present stock management practices or rearrange their supply chains. But enhancing resilience this way would probably cause additional costs and possibly somewhat lower profits

On an annual average, **we expect industrial production contract drastically, by about 10 percent, in 2020**.





3.1.2. Construction

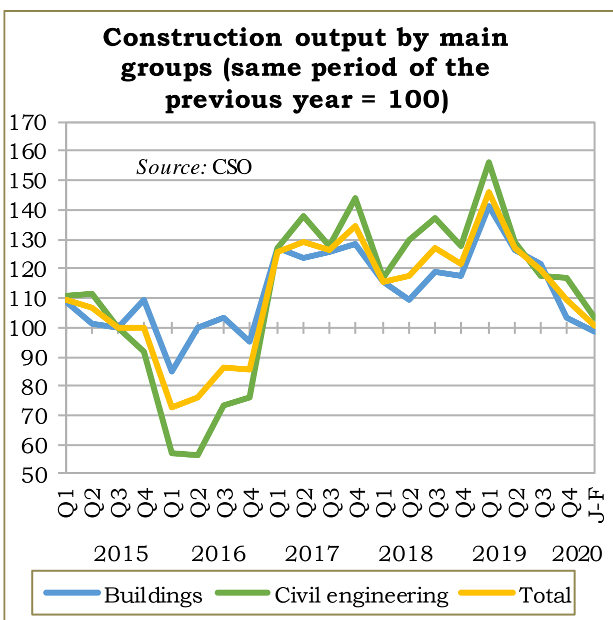
In 2019 construction output was up 21.7 percent, basically the same as in the previous year. The last two months, on the other hand, saw a drastic slowdown, due to the sudden year-end dip in the construction of buildings. While the output in this main group rebounded in January, the year-on-year growth rate remained negative, due to the statistical base effect. In civil construction, on the other hand, year-on-year growth remained vigorous in the last months of 2019 but decelerated in January-February. It is worth noting that in much of 2019 – save the jump at the start of the year – neither main group showed a rising trend.

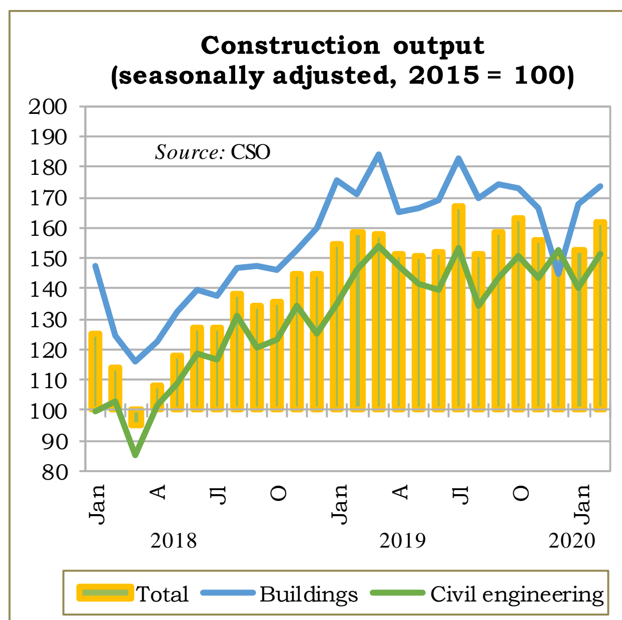
After the arrival of the coronavirus, however, the question is, to what degree the output will fall in 2020. In civil engineering the public sector is the main customer, and this – with the continuing inflow of EU funds – can be a stabilizing factor. But local governments, suddenly cash-starved, will be forced to postpone at least a part of their construction projects, which will pose a challenge for civil engineering firms.

As for the construction of buildings, here the role of private sector customers is larger, hence this main group may be hit more drastically amid the melting of demand of private firms and households. This already was visible during March-April: according to ibuild.info, while the value of new projects in building construction started was growing up until 15 March – mostly due to non-housing building projects – from mid-March, new starts suddenly turned into a sharp fall (on a year-on-year basis).

On top of this, the epidemic disrupts supply chains – primarily in the construction of buildings – while the drastic weakening of the forint pushed upward the prices of certain inputs.

As a result, we expect **construction output to decline** in 2020, but so far we assume that this decline will remain moderate, approximately 5 percent.



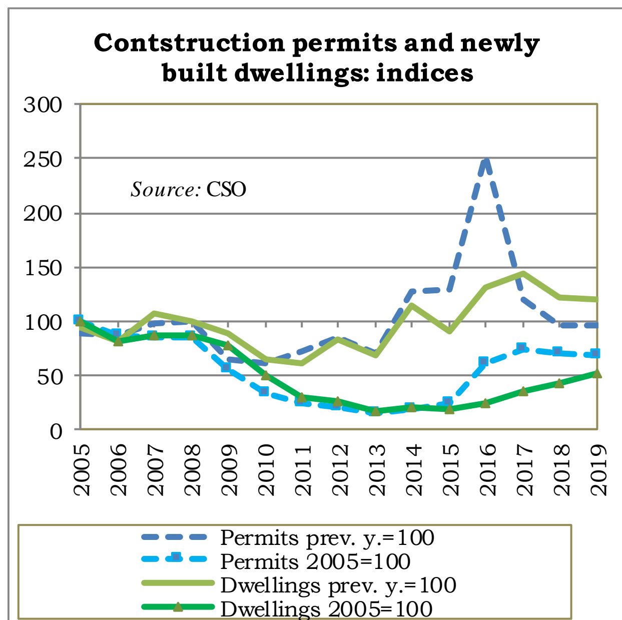


3.1.3. Housing construction, housing market

Due to an extraordinary year-end upturn (a 45 percent growth in the last quarter), the *number of dwellings built* grew by an impressive 19.5 percent in 2019. Apparently, many housing projects, after long delays, were at last completed in late 2019. On the other hand, the number of building permits and notifications was lower by 4.3 percent in 2019 than in 2018, and the newly started housing construction projects significantly fell in value terms – on a year-on-year basis – in the fourth quarter. This implies that the housing construction outlook was less than bright even before the COVID epidemic, and now a major fall seems inevitable.

The epidemic lowered demand – as a reaction, the number of home sale advertisements also fell steeply, and the remaining ads often use lower guide prices than before. Apart from falling demand, supply chain disruptions may slow down construction works as well.

As job and income security vanishes among wide segments of the population, housing demand is bound to fall further. Housing construction was expected to stagnate or decrease even before the crisis, but now a significant decline seems inevitable. At present, we expect the number of dwellings built to fall by roughly 10 percent in 2020, and no sharp rebound in the subsequent years seems likely.



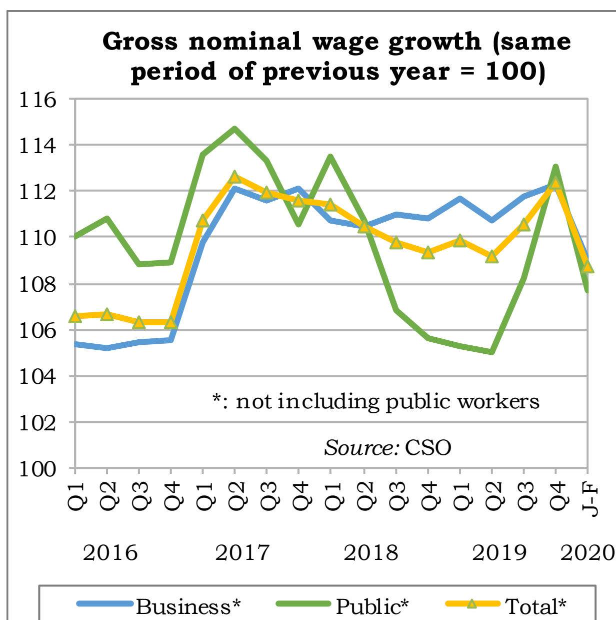
3.2. Final use of GDP

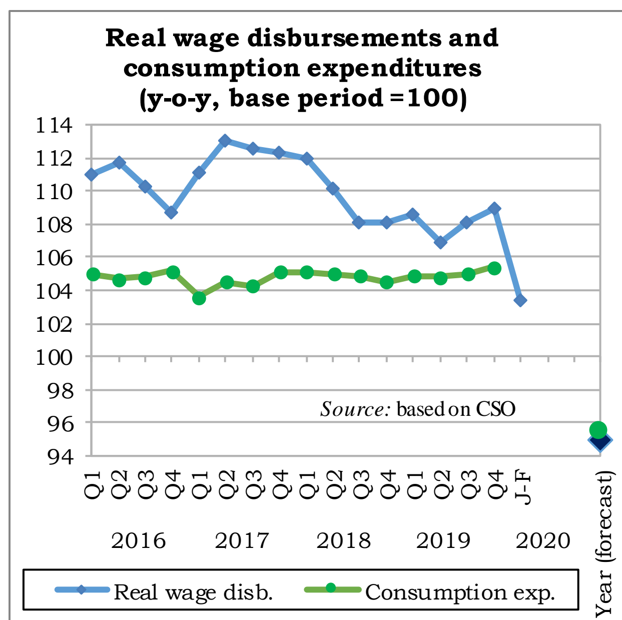
3.2.1. Household income, consumption and savings

In 2019, nominal wages rose by 10.6 percent (public workers not included), which means that nominal wage growth slightly surpassed the growth rate in 2018. A year-end jump in public administration wages notwithstanding, business sector wages grew at a much higher pace than public sector wages. If public workers are included, nominal wages were up 11.4 percent in the last year, resulting in a 7.8 percent growth in **net real wages** and a 8.3 percent growth in ***net real wage disbursements***.

In the **first two months of 2020**, wages continued to grow at a good pace, by 9 percent, but real wage growth decelerated to 4.3 percent, due to higher inflation. Furthermore, the number of employees decreased not just because of the downsizing of the public works program but also due to the private sector, too. This means that the labor market situation took a negative turn even before the epidemic. But nominal wage growth itself did not seem to be at risk – after all, a number of firms announced double-digit raises for this year.

From March, however, the financial prospects of firms have changed dramatically, along with their ability to raise (and, indeed, even to pay) wages. On the other hand, the jump in unemployment shifted the relative bargaining power between firms and workers. Many employees have been put on non-paid leave. In the coming months a couple of hundred thousand employees may take part in the subsidized shortened working time program, which may save their job but also lowers their actual wage. The wage agreements reached after the onset of the crisis are bound to be different from what could have been previously expected, but also many of the already signed agreements will be revised in the course of the year. At the moment, the steep deceleration of nominal wage growth can be taken for granted, but the actual degree of this deceleration is hard to surmise. At the moment we expect a **nominal wage growth of roughly 6 percent** in 2019, but this forecast is subject to a substantial downward risk. As a result, while average real wages still may grow somewhat, real wage disbursement will decline, probably





substantially, due to the reduction of workforce.

At the start of the year, ***household consumption expenditures*** are determined by the strong growth in January-February (according to the retail trade data) and the panic buying in much of March. On the other hand, the consumption of goods and services other than everyday goods, medical supplies and some info-communication devices certainly took a drastic hit from March on, auto sales being an obvious example. Demand will remain very subdued in the second quarter.

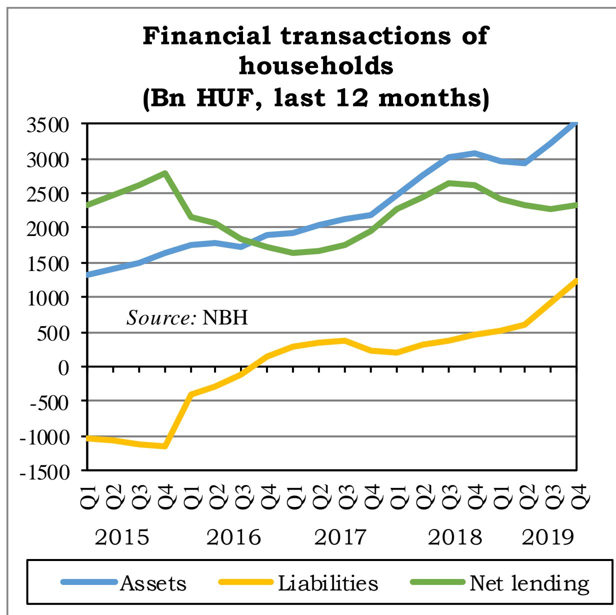
Food consumption, on the other hand, is not likely to contract substantially since even households in financial straits try not to get under a certain standard of food consumption level. A structural shift toward the lower cost goods is likely to occur. But the overall level of household consumption is bound to decrease along with growing job insecurity and the absolute or relative deterioration of wage prospects. Even the consumption of those with no change in their financial conditions will probably decrease since – in the environment of reduced mobility – the scope of their consumption opportunities decreases. The government measures do not help those who lose their jobs – there is no improvement in unemployment benefits, and the financial resources of the local governments that may offer some help to those in dire need are being severely tapped by the central government. This will compound the effect of the crisis on private consumption.

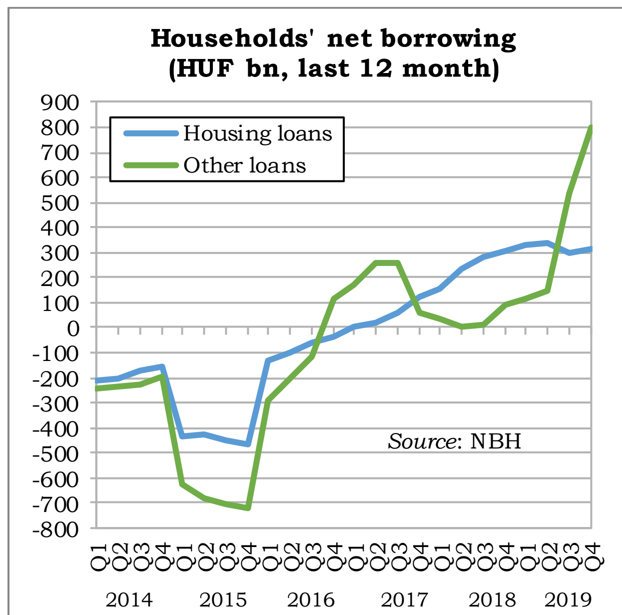
On the whole, we expect ***household consumption to fall by 4-5 percent in 2019***.

The households' ***net financing capacity*** decreased in 2019, due to a very strong growth of net borrowing. The latter is a result of a jump in net *consumption borrowing*. The annual savings rate (% of GDP) fell to 5 percent from 6.2 percent in 2018. We expect a halt in the downward trend: while many households will be forced to use their savings, others will try to stabilize their position with increased savings. Both housing and consumption borrowing will decrease even as the troubled families may increasingly rely on overdraft loans – until they can.

3.2.2. Investments

Investments grew by 13.9 percent in 2019, still a good pace, and without a drastic slowdown in the fourth quarter the annual growth rate could have remained near 20 percent.



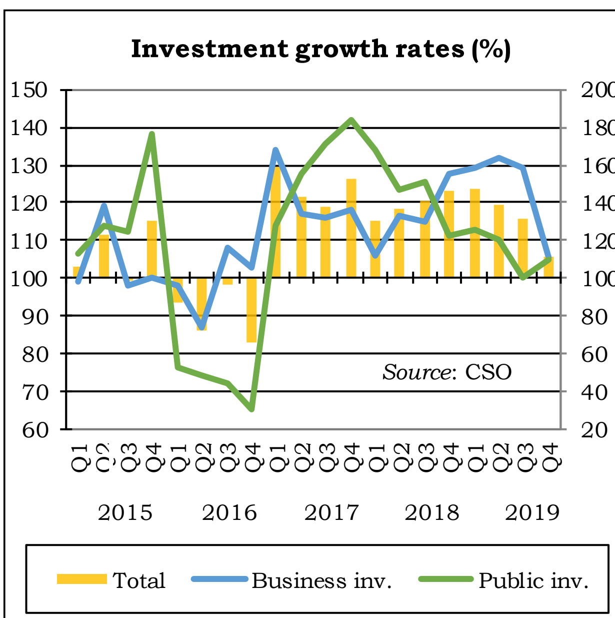


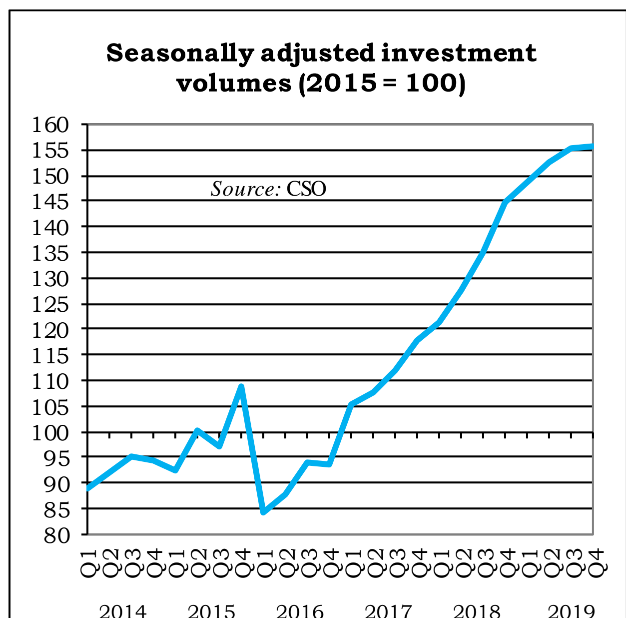
The said slowdown appeared in the majority of economic areas, yet the suddenly negative growth of *manufacturing* investments – following three quarters of roughly 30 percent expansion – was the primary factor. Manufacturing investments, in turn, declined mostly because of the fall in automotive investments. As a result, business investment decelerated sharply while public investments gathered some speed. According to the NBH, it was actually the state-connected segment of firms, the so-called quasi-fiscal sector, that continued to increase its investment activity, while the investments of private firms declined on average, due to the downward pull of automotive investments.

Capacity utilization fell by 9 percentage points from January to April in manufacturing, according to the Eurostat, obviously due to the epidemic. This may decrease the drive to implement labor-substituting investments. On the other hand, the virus highlights the vulnerability of human workforce and may reinforce the intention of robotization among firms, provided that they are not too busy trying to remain avoid bankruptcy and they still have resources for investment, despite the dearth of current sales revenue. But a great part of firms will postpone or even call off their investment plans, although investments into digital communication, online payment systems, home delivery capacities in retail trade are likely to grow.

The government seeks to rev up public investments – at least those implemented by the central governments – as reflected by the establishment of a new investment facility. But the crisis and the government together pull the rug from under the feet of local governments, thus many of even the more affluent local governments will be forced to postpone some of their investment projects originally planned for 2020.

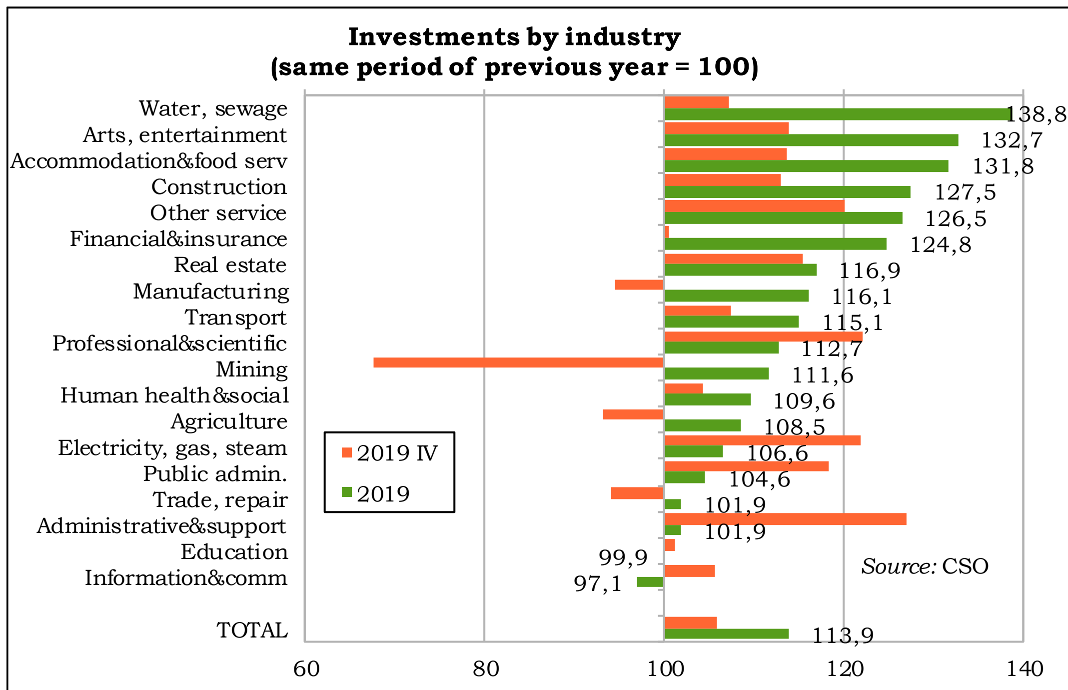
To keep up the pace of the EU-funded development projects, the government apparently tries to speed up the transferring of the funds to the beneficiaries. But that will not help too much in the case of firms that are currently struggling to stay alive – those firms will have to delay the projects undertaken. The government made this possible by deferring the deadlines by three months. Also, the government temporarily suspended the conditions posed by the government (and not by the EU) regarding the cost levels, or the expected rise in sales revenues, responding to the changes in demand conditions and rising costs due to the devaluation of the forint. But even so, the coming delays in the





materialization of the EU-related investment projects will have a negative effect on the overall investment performance.

On the whole, we expect **investments to fall by 5-6 percent in 2020**.



3.2.3. External trade

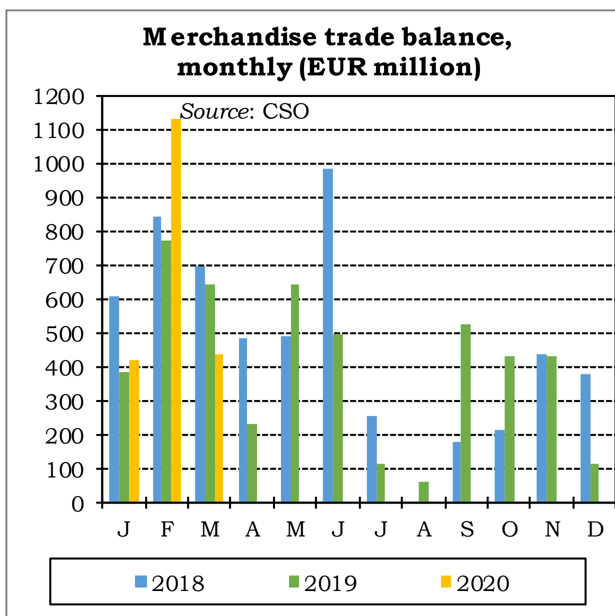
In the last quarter of 2019, export growth slowed down substantially while import growth slowed down moderately. The export slowdown was mostly due to machinery and transport vehicle export – in accordance with the industrial data that showed an end-year decrease in automotive export sales. As a result, the previous downward trend of **trade surplus** returned at the end of the year, and the annual surplus – **4.9 billion euro** – was about 12 percent lower nominally than in 2018.

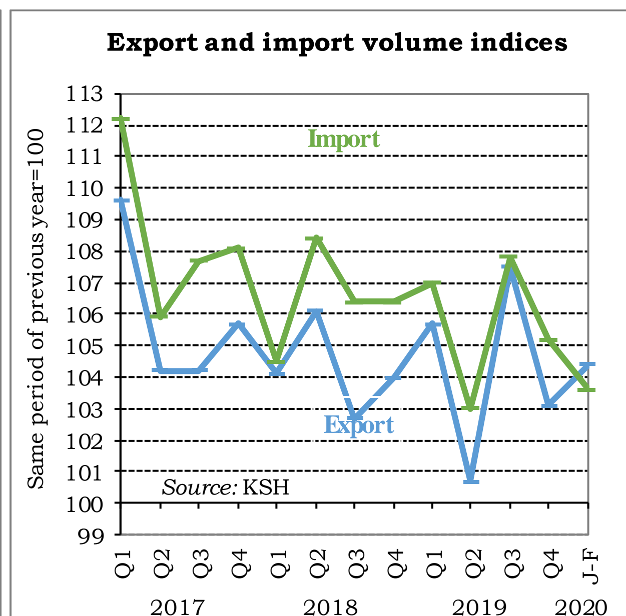
In the first two months of **2020**, the external trade surplus grew by 34 percent year-on-year in euro terms, although this was helped by improving terms of trade. But all the most important product groups – machinery and transport vehicles, manufactured products, food products – saw an acceleration of export growth. By the end of March, the cumulative growth of the surplus diminished to 10 percent as export took a hit from the coronavirus crisis.

In the coming months both export and import will suffer from the pandemic. Probably the trade flows related to the automotive industry will drop the most, even though a very gradual restart of production has already begun. This is bad news since the Hungarian economy and export is highly dependent on the auto industry.

If the ongoing wave of bankruptcies will not be extremely widespread, manufacturing export may recover relatively fast in the last quarter of the year. In the case of food export this might be more difficult since – if external trade channels remain congested – the food products may end up on the domestic markets, and a part of them may be already gone by the time the international channels normalize.

In any case, amid a simultaneous fall in both export and import, a significant part of the trade surplus may melt away, even amid improving terms of trade.





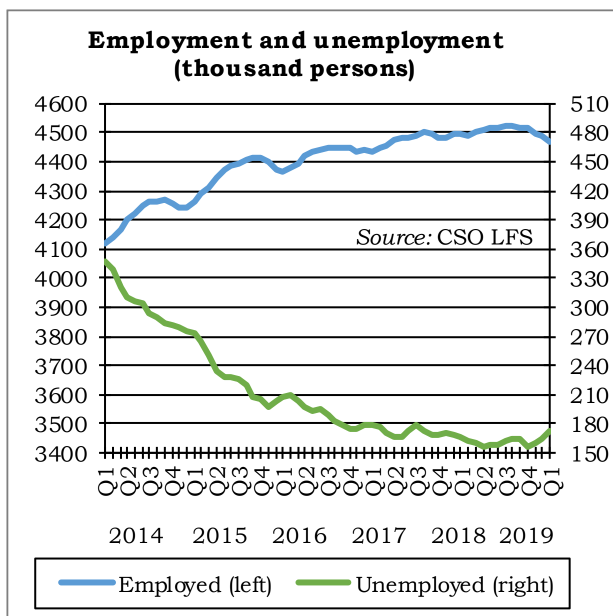
3.3. Employment, unemployment

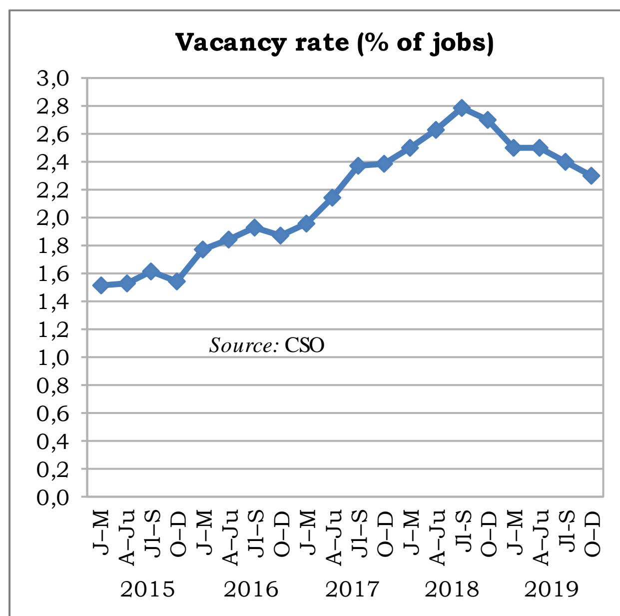
The *number of employed* grew by 1 percent in 2019, according to the LFS statistics. The *unemployment rate* was 3.4 percent in the last year, a slight improvement compared to the 3.7 percent in 2018.

By February, the rising trend in employment mostly lost momentum, but from March the near-stagnation gave way to a marked deterioration, due to the virus crisis. As a result, the number of employees decreased by 0.7 percent on a year-on-year basis. But compared to February, the number of employees dropped by 1.3 percent in March, and a much more drastic decrease is expected in April. The unemployment rate rose to 3.7 percent, a not so drastic change, which is due to the fact that only a fraction of those who lost their jobs became labelled as unemployed – the rest became inactive, according to the statistical office.

While large-scale downsizings already began in March without much fanfare, the number of officially announced mass layoff jumped only during April. As the epidemic pulled the rug out from under whole economic areas, and many firms were forced to halt or drastically reduce their operation, agency workers, informally employed workers and fixed-term employees were let go first, but the scope of layoffs broadened later. In early April, about 4 thousand employees lost their jobs every day. In the second half of April, the government announced a version of the subsidized shortened working time scheme that – also still less generous than the German Kurzarbeit – provides more than symbolic support to a set of troubled firms and their employees at risk. For the firms outside that set, only liquidity is offered – in enormous quantities, it should be noted. Whether the firms will be willing to keep their employees for months while financing their wages by loans is doubtful.

At this point, only very rough estimates can be made about the extent and duration of the ongoing labor market calamity. We expect the number of employees to drop by 7-8 percent while the unemployment rate may rise to 8-9 percent in 2020, *unless* the March pattern continues and most new jobless will be never labelled as unemployed.





3.4. Fiscal, monetary and financial developments

3.4.1. Fiscal trends and outlook

The 2020 budget

The spread of the coronavirus and the measures to tackle the epidemic created a new situation in the economy and also in the fiscal outlook. Below we will show how the 5.5 percent fall of GDP would affect the fiscal balance in the absence of government measures, assess the impact of the already announced stimulus measures and sum up the combined effect of these two factors.

In the recent years the fiscal deficit stabilized around 2 percent of GDP, marking a period of relatively disciplined fiscal policy that managed to slowly, gradually bring down the government debt ratio. It is also true that the economic upturn in the second half of 2010s could be utilized better, by reducing the deficit and debt ratios more aggressively, to have more fiscal reserves by the time of the new crisis. In most of the EU member states and the regional rivals, fiscal policy was more clearly anticyclical, and the deficit was lower than in Hungary – in half of the member states the fiscal balance was even positive. As a result, although the state budget is in a better shape than at the time of the global financial crisis, the fiscal room for maneuver is still smaller than in other countries. This may limit the scope of the measures that aim at cushioning the present crisis.

While preparing the budget for the year 2020, the government expected a GDP growth of 4 percent, as opposed to the 5.5 percent drop that seems likely now. This in itself enlarges the annual deficit/GDP ratio by 4.4 percent. More than half of the revenue loss comes from the non-materialization of personal income tax and social security contribution inflows, as the level of employment will fall short from previous expectations by far. The other half is a result of lower receipts from corporate taxes and taxes on consumption, in addition to the higher cost of unemployment benefits, also related to the worsening of labor market conditions. It should be noted here that two crucial factors of the automatic stabilizer are – could be – the progressive income tax and the generous unemployment support that is lacking in Hungary, due to the strictly linear tax rate and the very short duration (three months) of the unemployment benefit. This can be partially offset by the inflation-linked indexation of pensions that ensures that the purchasing power of pensions does not decrease, as opposed to real wages.

As for the stimulus measures, it is important to point out that – as far as short-term stimulus goes – a mere restructuring of expenditures within the budget has only limited impact, hence there is not much to hope from them, even if it was more transparent where the funds will be transferred from toward crisis management purposes. From a perspective of macroeconomic stimulus, only additional spending has a real impact – that is, tax cuts or additional expenditures that result in a larger deficit. This is why we assume here that the announced stimulus measures will in great part financed by fiscal deficit, thereby providing new resources to the Hungarian economy.

The announced stimulus measures so far account to 1 percent of GDP, which is only a fraction of what was mobilized by most of the other member states. The most important measure is the shortened working time scheme in which the government covers 70 percent of net wages that are not received by the employees because they were put into

part-time work, due to the crisis. This kind of benefit can be paid for a maximum of three months. Other major measures are the exemption from social security contributions, for up to four months, in the most crisis-hit economic areas, and the one-off large-scale direct income support given to health-care employees. The rest of the measures (exemption from the small business tax (KATA), exemption from tourism development contribution and tourism tax), while certainly alleviates the situation in certain economic branches or professions, it has no significant impact on a macro scale. The effectiveness of the stimulus package is weakened by the fact that it is in part financed by newly introduced special taxes (banking and retail tax), hence the overall **fiscal effect of the package only amounts to about 0.9 percent of the GDP.**

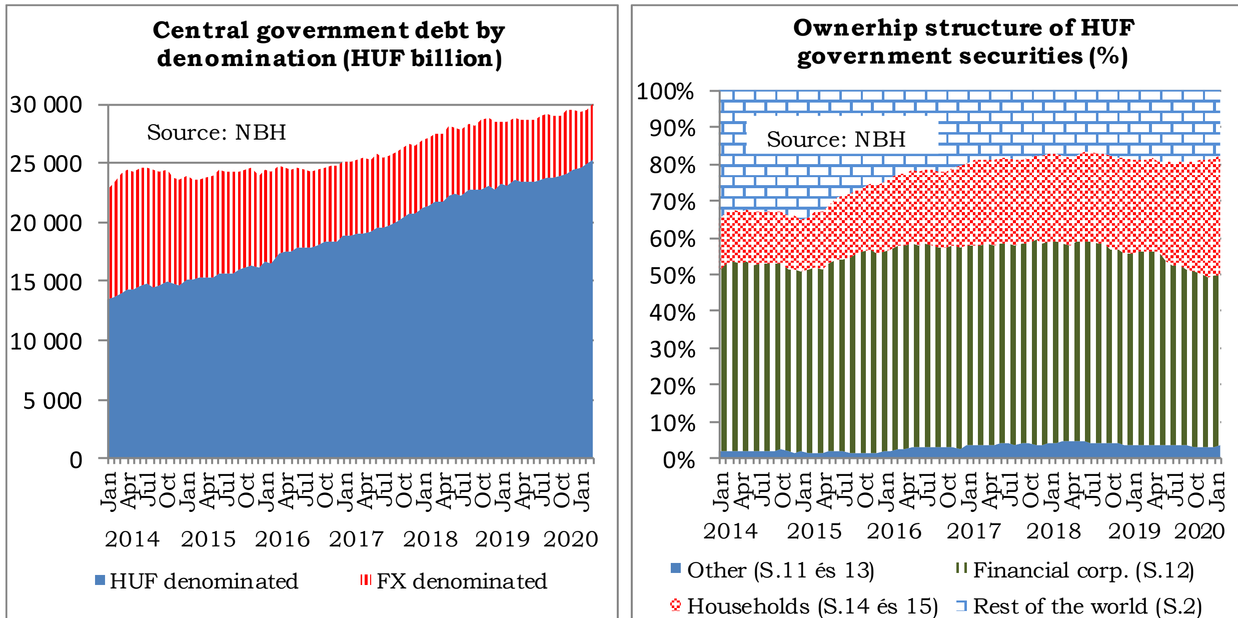
While making our fiscal forecast, we used our previous forecast in last December – a deficit amounting to 1.2 of GDP – as a starting point. We revised this number by considering the adverse effect of the economic downturn on the one hand – a deterioration of fiscal balance by 4.4 percentage point – and the effect of the stimulus package that amounts to 1.9 percent of GDP on the other. In addition, we considered the liquidity support coming from the EU – 0.6 percent of GDP – and the fact that in the original budget an unusually large fiscal reserve – amounting to 1 percent of GDP – was separated. According to our expectations, about half of this reserve will be used up to offset the fact that the original budget was too optimistic – even before the epidemic – about the revenue inflows, a flaw that we pointed out in our December report. The other half of the reserve, however, can be used now to finance crisis-related spending or to cushion some of the virus-related revenue loss.

On the whole, we expect the fiscal deficit to reach 5.1 percent of GDP in 2020. This is much higher than the deficit expected by the government in early April – 2.7 percent – and still much higher than the new deficit target of 3.8 percent, contained in the new convergence program, as of early May. Should some new fiscal measures be introduced, or should the economic outcome be significantly different from what we expect, the fiscal outcome may diverge from our projection as well, in either direction.

Fiscal debt

The consolidated gross debt of the general government stood at 66.3 percent at the end of 2019, according to the Maastricht methodology. Net fiscal debt, on the other hand, amounted to 54.8 percent.

Within the forint-denominated debt the share of households has risen further and reached 32.1 percent by the end of February 2020. At the same time, the share of foreign owners of forint-denominated securities dipped below 18 percent by February. (Foreign owners are still dominant regarding FX-denominated government debt securities.) In the case of households, the rise can be attributed to long-term securities – the share of the latter reached 28.6 percent by the end of February. The weight of households is much higher in the case of short-term securities (63 percent in February), but it has remained relatively stable during the recent months.



Although the overall share of FX loan within the central budget was only 15.4 percent in February, it rose to 15.9 percent in March, and will probably rise further in April – along with the overall debt-to-GDP ratio – due to the epidemic-related depreciation of the forint. The 7-9 percent depreciation of the forint during March in itself pushes the debt ratio upward by 0.8-0.9 percent. This, together with the projected 5.5 percent fall of GDP and the projected 5.4 percent fiscal deficit, is expected to push the debt ratio up to 73.9 percent by the end of 2020.

Fiscal outcome in 2019

In 2019, fiscal debt amounted to 2 percent of GDP, according to the preliminary data, slighly exceeding the 1.8 percent envisaged in the budget law. While in the first half of the last year it seemed reasonable to expect a yearly deficit below the target, the trend changed direction in the second half. This is partly due to a couple of measures taken during the course of the year (like the adoption of the family protection law in last April), and partly because of the revved-up spending by the budgetary units. Only five EU member states – and only one new member state, Romania – had a higher deficit ratio in 2019, while the EU average was around 1 percent.

While the details of the implementation of the 2019 budget will only by known in the autumn, it can be seen from the preliminary numbers that both the revenue and the expenditure targets were overachieved. On the revenue side most of all the receipts from taxes on consumption – primarily VAT revenues – surpassed the target (in the case of VAT, by 0.5 percent of GDP), due to the buoyant consumption growth and also to the whitening of the economy. But the inflow from the personal income tax, from the incomes on state assets, and interest revenues also surpassed expectations.

Still, expenditures exceeded the targets even more. This was primarily a result of the spending of government units, and to a smaller degree to elevated spending on healthcare and paid interest.

As a result, total revenues grew by 8.4 percent in 2014, including a 10.2 percent rise in income taxes, a 9.6 percent rise in VAT revenues, and a 6.2 percent rise in social security contributions. Total expenditures grew at a similar rate, 8.2 percent, but with a more polarized distribution of growth in the specific items. Investment expenditures soared by 12.2 percent, labor costs by 5.6 percent, monetary transfers (pensions, family allowance, unemployment benefit) by merely 4.7 percent.

3.4.2. Inflation

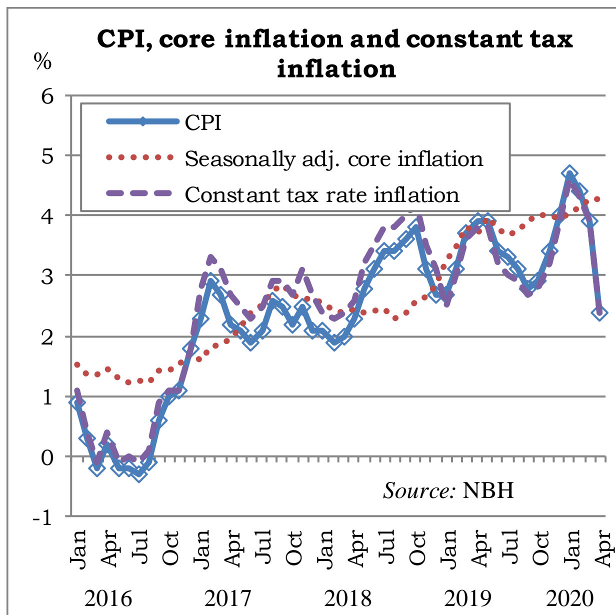
We revise our inflation forecast for 2020 to 3.2 percent from the 3.4 percent offered in our previous report. Price trends pointed toward a somewhat lower yearly inflation rate even before the arrival of the epidemic. Still, due to the statistical base effect, year-on-year inflation rates were unusually high in January-February, and only in March the rate dipped below 4 percent.

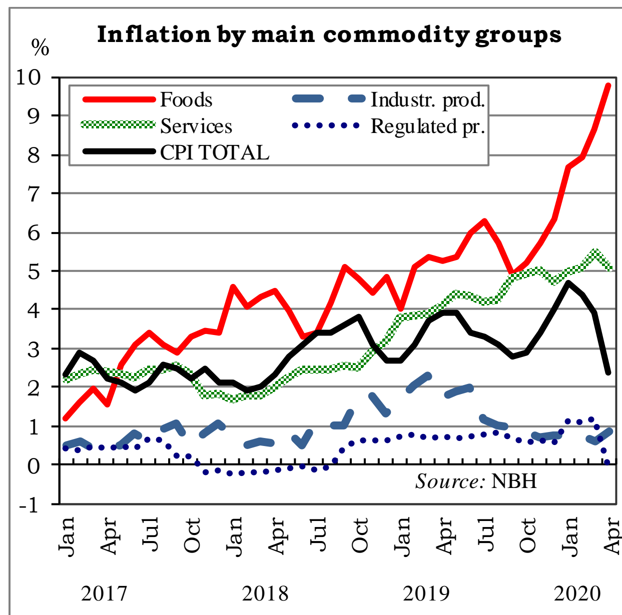
Food prices were the primary movers of inflation at the beginning of the year. While we expected food prices rise at an above-average rate in 2020, the 8.5 percent rise in the first four months (according to the NBH methodology) surpassed even our pessimistic expectations. Now we expect food price inflation exceed 8 percent in 2020. While agricultural production may remain favorable in this year, the disruptions in food import (due to either export restrictions or transport bottlenecks) will push vegetable and fruit prices upward during early summer. Also, while demand for most of the other product categories will significantly decrease, demand for food in general is expected to remain relatively stable.

At the same time, global oil prices dropped to record low, which in turn exerts a downward effect on inflation, not just through fuel and chemical prices but – less directly – through a wide array of products, by lowering transport costs. In April, this downward effect became dominant, pulling the monthly inflation rate down to 2.4 percent, a level unprecedented for nearly two year. The weak state of the world economy does not support any lasting rise of oil prices, unless the producers decide very drastic cuts in their output.

While the upward effect of soaring food prices and the downward effects of low oil price will to a degree offset each other, now we expect the oil price effect proving the stronger.

The prices of the other product categories are also moved into different directions. The drastic weakening of the forint should in principle give a push to the prices of goods with high import content (clothes, consumer durables). But the demand for these product categories are expected to be very sluggish during the rest of the year, even if the recovery of household incomes becomes visible toward the end of the year. Therefore, we predict the stagnation of clothing prices and a rise of about 0.5 percent





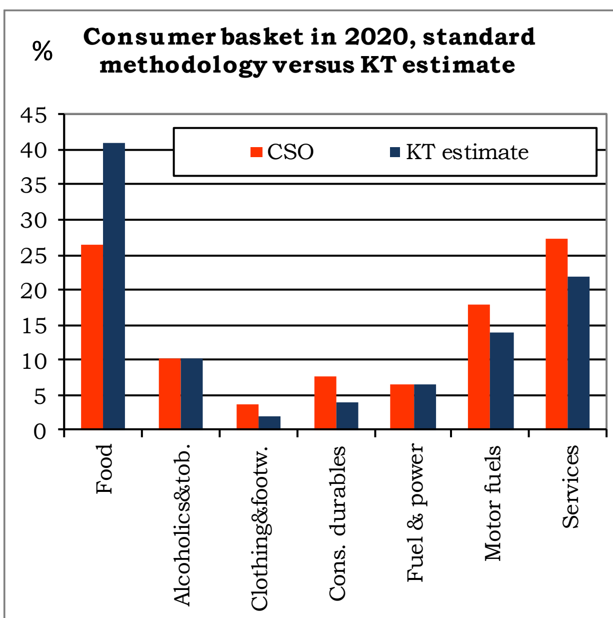
in consumer durable prices. The price increase will remain moderate in the case of services as well. In the first quarter services prices climbed 3.8 percent, but a much lower pace is likely, due to weak demand, for the rest of the year.

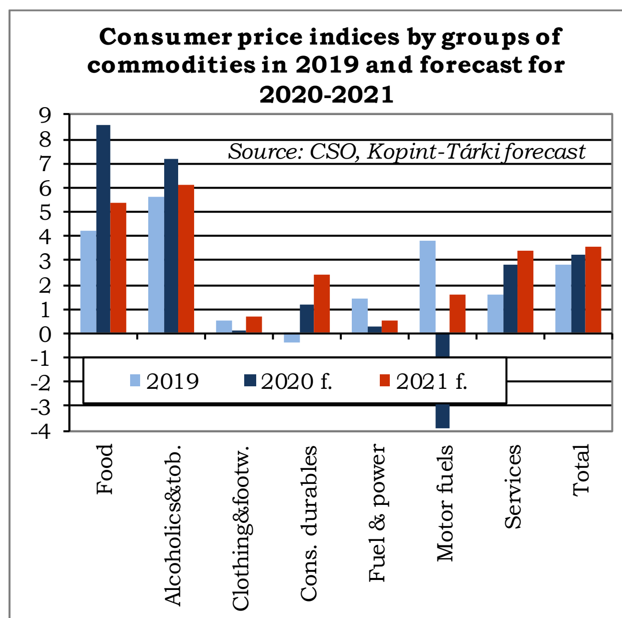
There is an important caveat, however. Our 3.2 percent prediction for 2020 is based on the internationally accepted methodology, that is, the calculation is based on the basket of goods in 2018. Usually, the use of the consumer basket of a year from the recent past does not causes any problems, because the composition of the basket usually changes slow. This year, however, will see a sudden and drastic change in the composition of goods and services purchased by the population, due to the plummet in households' income and also because the reduced mobility of the households and the movement restrictions rearranged the structure of everyday needs. Due to decreasing real incomes, a bigger part of incomes will be spent on food, while many other categories of goods and services will lose prominence. Moreover, many types of services become simply unavailable for a period of time, which obviously reduces their weight in household consumption.

If we attempt to make an estimate for this sudden change in the composition of consumption (shown on the left-hand chart) the overall inflation rate may reach about 3.9 percent in 2020. The higher inflation rate reflects the fact that the food products – the price index of which will be very high in 2020 – will be unusually prominent in this year's private consumption.

It needs to be emphasized that the estimated price index above is not a replacement for the officially accepted price index that is based on standard methodology, but only a complementary indicator that reflects on the extent to which the households will need to spend more, on average, due to elevated prices of their transformed shopping basket.

It is also to be noted that at this point, predicting inflation is marred by uncertainties just as much as predicting any other macroeconomic indicator. Both the upward and downward risks are unusually high. On the one hand, if the epidemic and the related restrictions on movement and transport are not over by the end of summer, and even everyday supply difficulties become a real possibility, than the price index may be





higher than projected. The reintroduction of the special tax on retail chains poses another upward risk since raising prices is the only way for the retail firms to obtain the necessary additional revenue. On the other hand, a larger-than-expected fall in consumer demand may slow down the price index of the non-food products and services even more than expected. Neither of the influencing factors can be reliably quantified at the moment, since the trajectory of the epidemic itself is unknown.

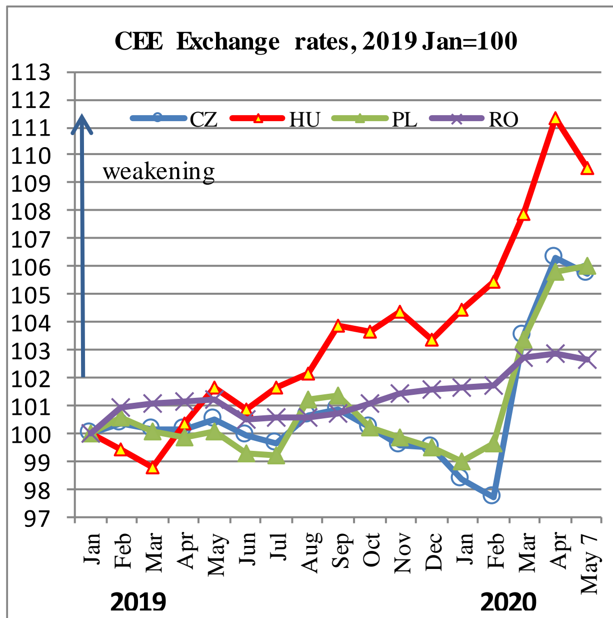
3.4.3. Financial and capital markets

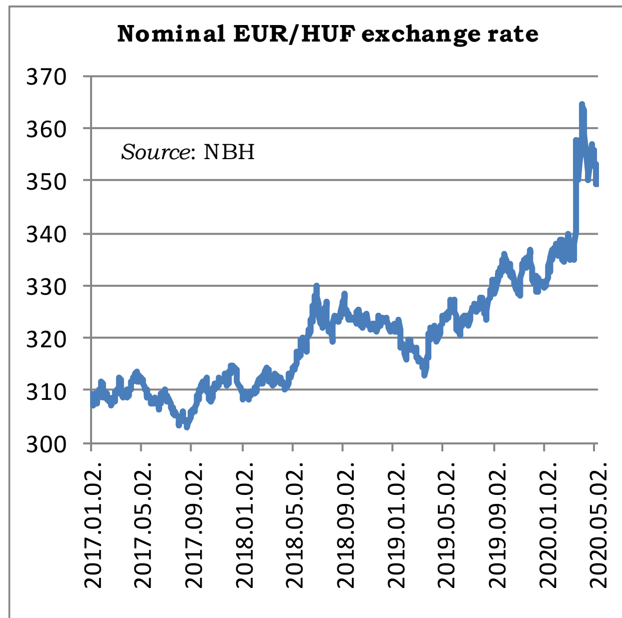
Exchange rate

After hovering around 310 vis-á-vis the euro for years and then within the 320-330 band between the spring of 2018 and the autumn of 2019, the forint began to weaken gradually, which turned into an unmitigated plunge in late March, after the arrival of the coronavirus epidemic and the worldwide restrictive countermeasures. In a period of two weeks the forint lost 6 percent of its value, and the euro exchange rate stood at almost 367 by early April. Since then, the euro/forint exchange rate seems to stabilize around 350-360 but the possibility of a further weakening spell cannot be excluded.

Since early 2019, the position of the forint has changed relative to the other regional currencies too, since the weakening of the forint was unparalleled. This is due to the fact that Hungary has the lowest real interest rates among the emerging economies, and investors did not expect any substantial change in that respect.

It is also true that no country within the region could avoid the weakening of its currency during the recent months. While the longer-term weakening of the forint surpassed that of any other regional currencies, the recent coronavirus-related weakening was more drastic in the case of the Czech koruna or the Polish zloty. This may be related to the fact that the euro exchange rate of the forint (and the Romanian leu) already stood at record lows before the epidemic, while the zloty and the koruna remained stable during the previous years.





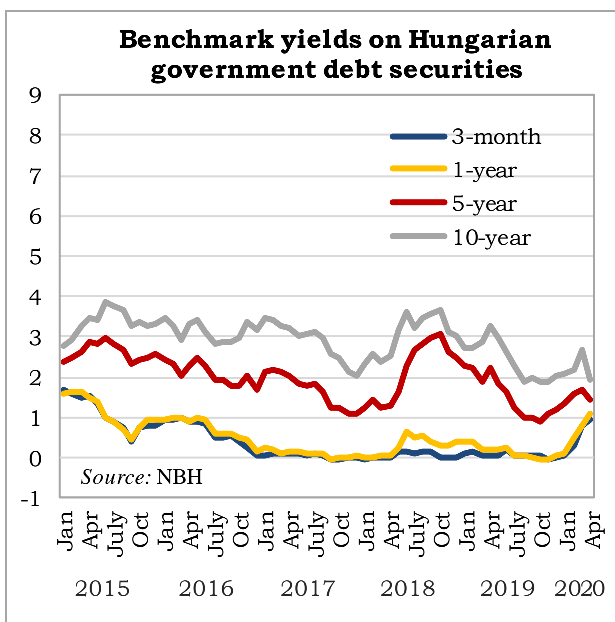
Government yields

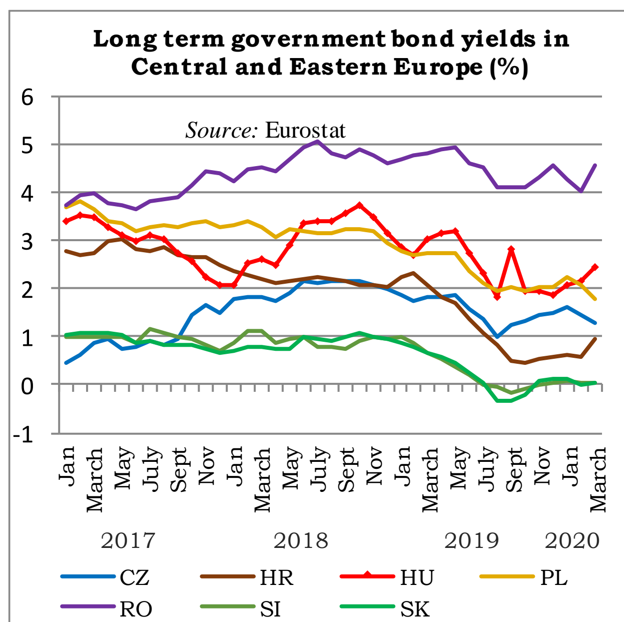
In late 2019 the formerly downward – or stagnating – trend was reversed, and a rise began that – unlike in the previous half decade – strongly affected not only long but also short-term yields. Before that, during much of 2018-2019, long-term yields first rose considerably than eased back, to eventually dipping below the previous low point. By October 2019 5-year yields were below 1 percent and 10-year yields below 2 percent, only to begin tto rise again between December and March. By the end of March, 10-

year yield stood at 2.65 percent while 5-year yields were at 1.69 percent, but even short yields were on the rise: the 3-month yield was at 0.77 percent, a level not seen since 2016.

This rising trend began before the epidemic – actually, April saw a moderation in the long yields. Also, it was not really a reflection of a wider regional trend: there was no such upward movement in the other Visegrad countries at the same time, although a rise took place in Slovakia and Czechia somewhat earlier.

In any case, the basic regional setup did not change in the past months: Romanian long yields are by far the highest, due to the country's overly expansive fiscal policy, and Hungary and Poland have higher yields than the Czech Republic. The 10-year yield of the euro area member state Slovakia has been fluctuated around zero for nearly a year.





3.4.4. Corporate and retail lending and interest rates

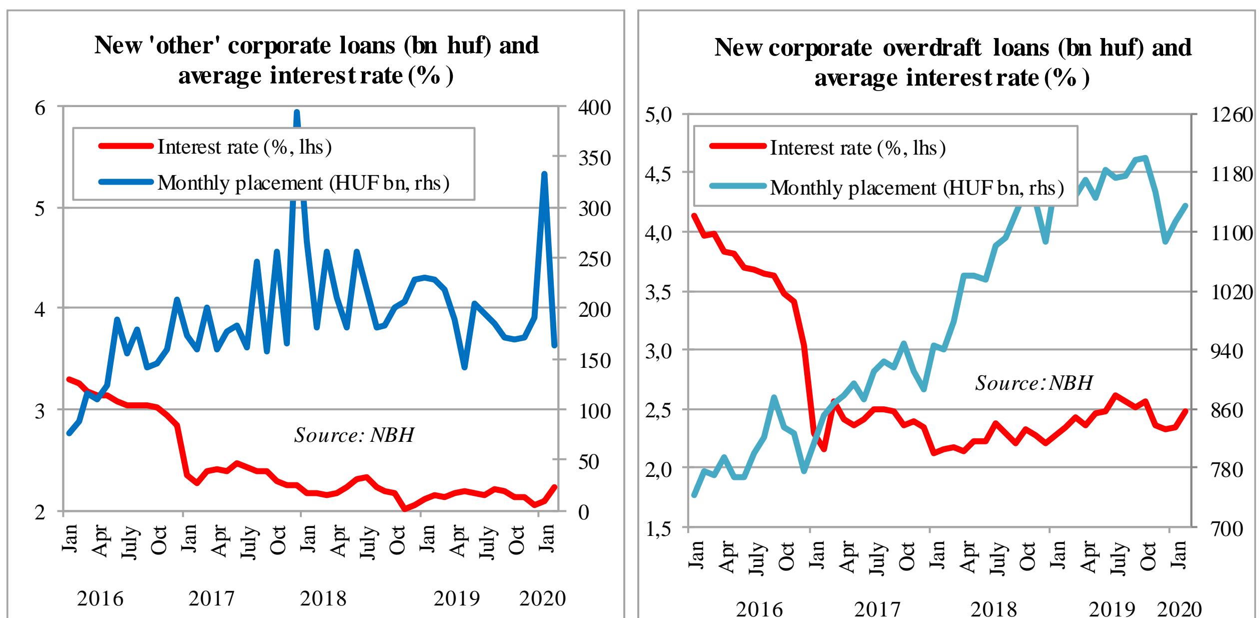
Corporate lending

While corporate overdraft borrowing was rising relentlessly since 2015, this trend was interrupted in the last quarter of 2019 with a sharp fall, although this fall was followed by a moderate upward in January-February. As for the other loans (primarily investment loans), their monthly sums are on a slowly descending trend (with wide fluctuations), even though this trend was temporarily interrupted by an upward shot in January.

The growth rate of the *stock* of corporate debt decelerated in the last quarter of the past year to 1.4 percent, from the 3-4 percent seen previously, mostly due to the large-scale debt repayment in December. There was no substantial slowdown, however, in the debt of SMEs – the year-on-year growth of SME debt was 14.4 percent in the fourth quarter.

Corporate debt growth was buttressed by the Funding for Growth Fix program, launched by the NBH in January 2019. Under the aegis of this program, HUF 495 billion was disbursed until the end of April 2020 in the form of either investment loans or leasing contracts. In value terms, investment loans made up 57 percent of the agreed-upon loans (with an average maturity of 8.6 years, while leasing contracts made up the rest, with an average maturity of 4.9 year. As for the sectoral breakdown, agricultural and manufacturing firms have the largest share with receiving 20 and 15 percent of the disbursed sum, respectively.

The *interest rate* of *corporate overdraft loans* decreased somewhat shortly toward the turn of the year, but after an upward correction it stood at nearly 2.5 percent again by the end of February. About the same happened in the case of the average interest rate of *other loans* – the latter was 2.23 in February.



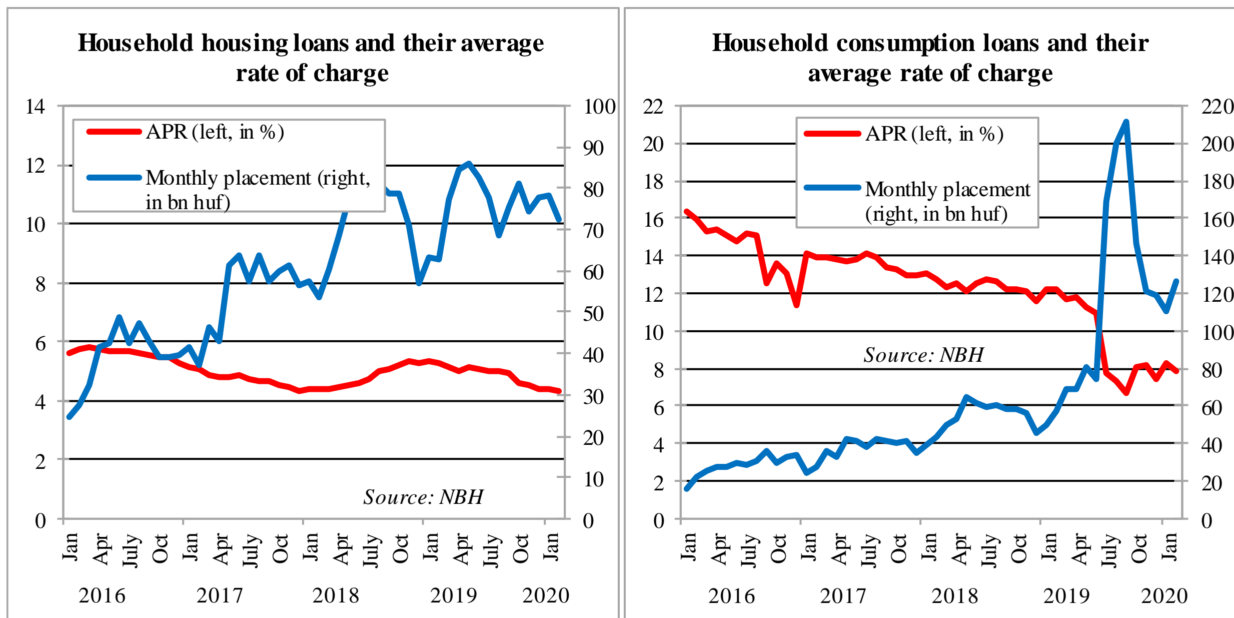
Retail lending

Since November the monthly sum of new forint-denominated *housing loans* has been fluctuating around HUF 75 billion, which means that there was no substantial change compared to the past couple of year. But the structure of housing loans is changing: the share of loans for purchasing existing dwellings has decreased by nearly 10 percentage points, to 65 percent, while the share of loans for purchasing new dwellings rose above 10 percent. On the other hand, the average sum of loans for second-hand dwellings only grew by 17.4 percent while the average sum of new loans for new dwellings only rose at a less steep pace of 15.8 percent.

In the case of *consumption loans*, a stabilization has taken place since October, following a rupture caused by the launching of the new “baby loan” in July that sent the monthly sum of new consumer loans through the ceiling. Between November and February, the monthly sums fluctuated between HUF 110-130 billion, a level higher than before last July but much lower than the readings in the July-September period. On the whole, the first six months from the launching a sum HUF 463 billion forint was disbursed under the “baby loan” scheme.

The total stock of household loans grew by 16.7 percent in the last quarter of 2019, which means that the growth rate nearly doubled compared to the start of the same year. While the baby loan rearranged the relative weights of different types of lending, even the stock of loans rose by 9 percent, which suggests that the baby loan scheme mostly generated new borrowing, not just crowded out other types of loans.

After a rise and a descent during 2018-2019, the *APR* of housing loans stabilized slightly below 4.4 percent by the end of the last year. As for consumption loans, the swift drop of APR due to the baby loans came to a halt and gave way to a fluctuation near 8 percent. Withing consumption loans, the APR of *loans for purchase of goods and other excluding over 5 years initial rate fixation* decreased from 5 percent in October to 4.4 percent in February.



Economic Indicators 2009-2016 Forecast 2017-2018 (percentage change)

	2012	2013	2014	2015	2016	2017	2018	2019	2020*
GDP AGGREGATES, ANNUAL REAL GROWTH									
GDP total	-1.5	2.0	4.2	3.8	2.2	4.3	5.1	4.9	-5.5
Domestic Demand	-3.0	2.0	5.3	2.4	1.7	5.2	7.3	5.6	-4.3
Private Consumption	-2.5	0.1	2.1	3.7	4.2	4.2	4.0	4.4	-4.6
Public Consumption	0.0	6.0	9.8	1.1	0.3	3.2	2.0	2.0	0.9
Gross Capital Formation	-6.0	6.1	12.8	-0.2	-4.1	9.0	18.3	9.5	-5.6
of which: Fixed Capital Formation	-3.0	9.8	12.3	4.8	-10.6	18.7	17.1	15.3	-5.6
Export	-1.7	4.1	9.2	7.4	3.8	6.9	4.3	6.0	-8.9
Import	-3.5	4.3	11.0	6.0	3.4	8.2	6.8	6.9	-7.6
PRODUCTION INDICES									
Agricultural Production (gross)	-10.0	12.5	11.4	-2.4	9.3	-4.1	2.7	-0.3	0.0
Industrial Production	-1.8	1.1	7.7	7.4	0.9	4.6	3.5	5.4	-10.0
Retail Trade Volume	-2.2	1.8	5.2	5.8	4.8	5.6	6.7	6.1	-3.7
EMPLOYMENT, EARNINGS									
Number of Employed	1.8	1.7	5.3	2.7	3.4	1.6	1.1	1.0	-8.0
Unemployment Rate	11.0	10.2	7.7	6.8	5.1	4.2	3.7	3.4	7.5
Gross Nominal Wages	4.6	3.4	3.0	4.3	6.1	12.8	11.3	10.8	6.0
Net Real Wages[a]	-3.4	3.1	3.2	4.4	7.4	10.3	8.3	7.7	2.7
PRICES, EXCHANGE RATES									
Consumer Price Index	5.7	1.7	-0.2	-0.1	0.4	2.4	2.8	3.4	3.2
EUR/HUF Exchange Rate (annual average)	289	297	309	310	311	309	319	325	360
EUR/ USD Exchange Rate (annual average)	1.28	1.33	1.33	1.11	1.11	1.13	1.18	1.12	1.10
Short-term Interest Rates (3M), eop	5.33	2.86	1.43	0.80	0.06	-0.01	0.00	-0.01	1.0
Long-term Interest Rates (10Y), eop	6.11	5.61	3.60	3.33	3.16	2.02	3.01	2.01	3.0
BALANCE OF PAYMENTS									
Current and Capital Accounts, % of GDP	4.1	7.3	4.9	7.0	4.5	3.2	2.0	1.0	0.8
GOVERNMENT BUDGET									
General Government Balance, ESA-95, % of GDP	-2.3	-2.6	-2.7	-2.0	-1.8	-2.5	-2.1	-2.0	-5.1
Gross Government Debt, % of GDP[b]	78.5	77.3	76.8	76.1	75.5	72.9	70.2	66.3	73.9

a The numbers do not take into account the effect of the family tax benefits.
b Including the balance sheet of Eximbank
* Kopint-Tárki forecast
Source: CSO, NBH

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