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Hungary Economic News Letter

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Embassy activities

Company visit to the Hungaro Casing Kft - member of the Teeuwissen group, specialised in food casings, an example of a Dutch investment in Hungary on May 20th. Many thanks to William Janssen, and Roelof ter Maat who received Bert van der Lingen and Éva Szabó.

On May 28th, a lunch was organised for the Dutch companies sponsoring King's Day at the residence with 3 HITA guests. The new structure of HITA and its services to investors/companies were presented by the president, János Berényi. He remarked that companies often turn to HITA when already encountering problems instead of asking for free advice in advance. The services offered range from site selection through supplier search. HITA organises trainings for Hungarian companies willing to export, but also for cities/settlements in order to make them more investor-friendly.

EU relations

EU funding management to be audited

Hungary's body for auditing European funds is drafting a report for the European Commission on the new system for managing the country's European Union funding by the end of May, the Prime Minister's Office told MTI. The Directorate General for Audit of European Funds (EUTAF) is reviewing changes to the way EU funding is managed and controlled according to a methodology agreed with the EC. The EUTAF is an independent body funded by the central budget established in 2010 to "*carry out audit authority tasks regarding EU and other international funds determined by the government*", according to the government's website.

In April, Brussels voiced concern over a restructuring of the system for managing EU funding and requested further information, especially regarding the implementation capacities of the newly established minirsterial organisations.

As to the on-going implementation of the previous financial framework, the European Court of Auditors has found recently serious problems with the transfer and management of R&D projects. Spot checks by auditors found that consultants' fees and personnel expenditures made up a large proportion of the funds earmarked for innovation, a website 444 reported. Moreover, the EC had raised questions about Hungary's transport development programme and about the ratio of refundable support in the economic development operative programme too. The Hungarian government is hoping to get the matter closed as soon as possible and is ready to accept some penalties, deputy state secretary Nandor Csepreghy admitted.

Business environment / Legislation

Hungary's competitiveness slightly up

Hungary's competitiveness has slightly improved after continuous deterioration over the past few years, IMD's World Competitiveness Ranking showed. The step Hungary made forward is attributable primarily to its improving economic performance and better infrastructure, whereas the country's government efficiency did not improve and business efficiency even worsened.

This year, Hungary ranks 48th in overall competitiveness, up from 50th last year when Hungary slipped 5 places. It should be noted that Hungary ranked ahead of fellow east and central European countries Romania and Slovakia (which placed 76th and 78th respectively), while Hungary still trailed fellow regional countries Poland and the Czech Republic (which placed 42nd and 46th, respectively, on the latest GCI).

As to the sub-indicators, one of the most substantial improvements in Hungary was documented in terms of economic performance since its 44th position was followed by 32nd in 2014. This was mainly due to the surplus in international trade, ameliorating FDI trends, and the dampening costs of living. As for the government efficiency score: it has slipped one place to 53rd in the 2014 issue. As a consequence, it has remained relatively stable because of the fiscal prudency (i.e. fiscal indicators have gone through an amelioration in numerical terms).

However, the companies' executives expressed their concerns over the sustainability of the achievements via one-off measures like crisis taxes. As far as the business efficiency deterioration is concerned, it was caused by the worsening productivity and investment activity as well as the brain drain. Additionally, the opinion survey confirmed that many enterprises and individuals are concerned about the critical approach of the government regarding globalisation.

On-line shopping on raise again

After February's eight-year record, March retail sales in Hungary again posted a record, showing that the strengthening of domestic consumption is both "sustained and continuous," the Economy Ministry commented the release of retail data which the statistical office had revised upwards.

A total of 69% of 586 online shops participating in a Webshop-Experts survey reported rising revenue in 2013. A total 91% of the shops said that they conduct sales only in Hungary. Average spending per online purchase was 22,000 forints, up 3,000 forints from 2012.

The increase in consumer confidence was also reflected in the monthly GKI-Erste confidence survey too. Consumers said they were worse off financially than earlier, but more expected to be able to make savings in the coming twelve months, and more saw a chance to make big purchases.

Dutch presence in Hungary

Hungaro Casing Ltd-the food processing company

Hungaro Casing is Hungary's leading domestic manufacturer and distributor of raw materials, like natural and artificial casings, spices & blends, functional ingredients for the food industry. The products are sold to food production companies in order to create high-quality, marketable products for their customers. After having obtained a majority interest in Hungaro Casing Ltd in March 2011, the Dutch Teeuwissen Group acquired 100% of the shares in 2012. The transaction is seen as a next step in rolling out the Group's growth strategy into Eastern Europe and an important step towards broadening the group's product portfolio.

The Hungarian company is located in Budapest, has a modern facility of 13.000 m2 and 120 employees. The company has its own in-house laboratory, experimental factory, product-development team and a printing house.

R & D & I / Creative Industries

Hungary to become innovation hub?

Hungary is a production centre and will become an innovation hub, Economy Minister Mihály Varga told the annual general meeting of the Hungarian Innovation Association. The government's aim is to have twenty cutting-edge innovation centres in Hungary by 2018 and lifting the number to 30 by 2020, he added. Tax breaks for companies introduced over the past few years will be maintained. And "*if there is room for manoeuvre in the budget*", burdens will be further reduced, he said. He said the government's industrial strategy will reduce the economy's exposure to the vehicle industry and several areas will be chosen to focus on such as the electronics industry, logistics, the health industry and tourism, as well as the defence and food industries.

The government will allocate 10% of all funds earmarked for Hungary during the 2014-2020 EU budgetary period for R+D+I, he underlined. The amount available under the current EU budgetary framework is HUF 800bn (EUR 2.62bn), twice the amount earmarked in 2007-2013, state secretary Zoltán Cséfalvay added.

Hungary joins INTERS PUTNIK

Hungary became a full-fledged member of Intersputnik International Organisation of Space Communications. The organisation has 26 member states, among them Poland, the Czech Republic, Romania, Germany and Ukraine. As the Hungarian government places special emphasis on high value-added industries, including the space industry, Hungary's membership is highly important, said Balázs Solymár, Deputy State Secretary for Info-communications. Hungary also aims to achieving full membership in the European Space Agency (ESA) by the end of 2014.

Transport / Logistics

Transport remains a priority for EU finds

Hungary expects HUF 1,034bn (EUR 3.4bn) in funding to become available for transport projects in the 2014-2020 European Union budget period, deputy state secretary Nándor Csepreghy told *Magyar Hírlap*. Actually the Hungarian government had finalised eight of ten operative programmes for EU funding in the 2014-2020 financial framework.

The amount available in Hungary's proposed Integrated Transport Development Programme (IKOP) is less than the HUF 2,000bn (EUR 6.7bn) in the 2007-2013 budget period, but the current period promises to be more flexible, and important areas will get priority, Csepreghy told the paper. He added that a further HUF 373bn (EUR 1.2bn) is available for railway projects from the Connecting Europe Facility until 2016.

Siemens wins EUR 60mn contract

Siemens has won a EUR 60mn contract from state infrastructure developer NIF to supply train protection systems (ETCS) on three routes covering 200 km of track, the company announced. The project will be completed by 2015. The EU has required railway companies to put automatic train control systems in place.

EU okays e-toll fee system

The electronic toll system for trucks introduced last summer is compatible with EU norms, Development Ministry deputy state secretary Pál Völner said after consultations in Brussels on the topic have ended. EU officials had earlier raised objections to the size of the fee and mode of calculation. The ministry said it set the fees in accordance with the relevant Eurovignette directive. The European Commission acknowledged the government's argument that its usage-based fees take into account the state of the roads and lack of reconstruction works in previous years. The government has agreed to review the fees every two years, Völner added.

HUF 8bn (EUR 26mn) more for M0 project

The government has increased its funding for the ongoing work on the Budapest ring road M0 to HUF 105bn (EUR 340mn) from HUF 97.5bn (EUR 316mn), it was reported in the official gazette Magyar Közlöny. The M0 is to be widened to a three-lane motorway between the M1 and M5 highways. The Development Minister will talk to the European Commission about modifying EU subsidies for the project.

Hungary to buy LNG from Qatar

Hungary could soon be buying liquefied natural gas exported by Qatar, President János Áder said after talks with the Emir of Qatar. After the talks, which focused on investment opportunities, Áder said that Qatar had the third largest natural gas stock in the world, and had built a huge capacity to export its gas in liquefied form. Hungary could soon have some of those billions of cubic metres of gas exported, Áder said, but added that a few kilometres of pipeline and

two interconnectors were still to be completed so that supplies could be provided to Hungary and the whole region, "*if we agree on financial conditions*". "*Standing on several legs*" is important for Hungary to make the country independent of Russian gas supplies, Áder said. He argued that the gas could be an alternative for Visegrad countries, while those countries, using over 40 bcm of gas annually, could become an important market for the exporter.

Budapest gas prices second lowest in the EU

Budapest offers the second lowest natural gas prices among European capitals, a report published by the Hungarian Energy and Utilities Regulatory Office said. The price of electricity is the third cheapest in the Hungarian capital, it said. In July 2013 Budapest had ranked second worst in a European comparison, but after the government put a utility price-cut scheme in place in April Budapest fares much better: prices are higher in Bratislava, Bucharest, Prague, Warsaw and Lisbon, Zsolt Scherer, a spokesman for the Energy and Utilties Regulator said. The utility bill cuts began in January 2013 with cuts of 10% to gas, electricity and district heating prices. In November a further cut was administered in gas, electricity and district heating, amounting to 11.1%. As of April 1, just before the general elections prices were cut by another 6.5%.

It should be also added that the gas and electricity consumption in Hungary has declined for several years, primarily due to the economic crisis. The data from the Hungarian Energetics and Public Utilities Regulatory Office (MEKH) shows that gas consumption fell to about 8.5 billion cubic metres last year from 9.3 billion in 2012, 10.3 billion in 2011 and 11.3 billion in in 2010, according to MEKH's data. Households that bought their gas on the regulated market consumed 3.1 billion cubic metres last year, down from 3.6 billion in 2010.

Orbán meets Gazprom chief Miller

Prime Minister Viktor Orbán and Gazprom President Aleksei Miller talked about speeding up the construction of the South Stream gas pipeline at a meeting. Gazprom said in a statement that the two discussed ways of reworking the proposed route of the pipeline after Austria decided in April to join the USD 16bn project. he Hungarian section would run along 229km between Hercegszántó on the Serbian border and Tornyiszentmiklós near the Slovenian border. Gazprom and state energy company MVM would share the estimated USD 600mn cost in a joint venture. Gazprom said the reworking of the route will not affect the planned deadline of 2017.

Orbán and Miller agreed that the Ukrainian crisis has proven that South Stream has become pivotal for the security of Europe's gas supply.

Government works to lower energy bills for industry

The government will form non-profit utility companies after a bill on public services is passed, with a view to lowering energy costs for industry, former Development Minister Zsuzsanna Németh said. "*We need to offer low energy prices in order to maintain Hungary's competitiveness*", she told a conference hosted by state energy company MVM, adding "*our goal is have the lowest electricity prices in Europe for house-holds and industry*". The expansion of the Paks nuclear power plant is closely linked to the country's energy independence, she remarked.

MVM is now the 20th largest company in the region, as its revenues have grown from HUF 550bn (EUR 1.8bn) in 2010 to an expected HUF 1.2trn (EUR 3.8bn) this year, said CEO Csaba Baji.

Audi building geothermal power plant

Audi Hungaria Motor is building a geothermal power plant, which will cover 60% of the energy needs of the car factory in Győr, the company announced. The 22.5MW plant will be opened by the end of 2015 after a 2km well is drilled between Győr and the nearby town of Pér.

Audi signed a 17-year co-operation contract with the constructor, which may be extended by 15 years. Although the company building the plant was not named, there is a good chance that it is PannErgy, as the two companies signed an annual 370,000 GJ heat delivery contract last December, website Portfolio speculates.

Environment / Water Management

Utility cut reaches water sector

The Hungarian government is planning to establish a system of uniform water service fees. The bill regulating the universal water service will soon be involved in the Hungarian Parliament's agenda. The government has aimed to continue reducing utility fees, introduce a uniform water service fee, coordinate maintenance work and ensure access to EU funding necessary for developments. Initially water utilities act was adopted in 2011 in order to establish grounds for the consolidation of the water utilities segment. As an advancement of this process the unification of tariff system can be the next step to reduce fees. As a result, the number of water supply companies have been reduced from 400 to 40 and more reductions are expected to take place.

Hungary wants to cooperate with Saudi Arabia in water and energy

Hungary's foreign trade chief Péter Szijjártó discussed opportunities for cooperation in energy and water management with Mohammed Al-Saud, Saudi Arabia's deputy minister of water and electricity, in Budapest. Saudi Arabia is Hungary's second largest trading partner in the Arab world, and the two areas offer the most opportunities for further cooperation. Budapest Waterworks has the qualifications required to work in Saudi Arabia, and negotiations concerning urban service management and sewage treatment projects are under way, a statement said. Hungarian energy company MVM is in cooperation with a Saudi company to jointly bid for projects aimed at renewing the electricity networks of Arab countries, the document added.

Budapest to buy back sewage works

Talks on the city of Budapest repurchasing the 25% plus one share stake of a foreign consortium in the sewage works Budapest FCSM have reached a final stage, Népszabadság reports. The company was privatised in 1997 for 25 years, guaranteeing a fixed annual 18% return until 2000 and an inflation-adjusted 18% afterwards.

Economic indicators

GDP growth accelerates

Hungary's first-quarter GDP growth accelerated to 3.5% year-on-year, up from 2.7% in Q4 2013, the Central Statistics Office (KSH) reported. The rate was the highest registered since a 3.7% increase in Q4 2006. London analysts had put the year-on-year rate well over 2%, with some saying it could match Q4 growth. National Economy Minister Mihály Varga stated on public television that Hungary's economy could grow 2.5% this year.

However, the London-based EBRD (European Bank for Reconstruction and Development) said the Russia-Ukraine crisis was having a serious impact on the economies of Central and Eastern Europe. In its new prognosis, the EBRD acknowledged "surprisingly brisk" GDP growth of 2.7% in the fourth quarter of last year in Hungary, but it said the increase was mainly driven by domestic demand which was supported by one-off factors, such as government-mandated utilities price cuts and the disbursement of EU funding at the end of the 2007-2013 budget period.

Investment activity up 22% in Q1

Investments in Hungary rose by an annual 22.6% in volume terms in the first quarter, lifted by capital expenditures in the manufacturing, transport and farm sectors, the Central

Statistical Office (KSH) said. In absolute terms, investments came to HUF 824.1bn (EUR 2.7bn). Investment in manufacturing rose by 27.6%, in the transport and logistics sector climbed 64.6% to reach HUF 122.4bn (EUR 0.4bn). Farm investments increased by 18.5% and were at HUF 51.3bn. András Balatoni of ING Bank said investments had started to grow in the private sector as well as the public sector. He also noted the base effect on the big increase in Q1. It should be also noted that banks have extended HUF 138.6bn (EUR 0.45bn) in loans in the second phase of the central bank's Funding for Lending scheme, of which the vast majority has been new loans taken out to finance investments.

Budget deficit at 96% of the annual figure

Hungary posted a cash-flow budget deficit of HUF 951.1bn (EUR 3.13bn) in January-April, or 96.6%of the full-year target, the economy ministry announced. The four-month shortfall rose by HUF 363.4bn from a year earlier. The rise reflected one-off factors, which did not affect the full-year cash-flow deficit and will not endanger the full-year target, the ministry said. In April alone, the cash-flow deficit was HUF 235.4bn, nearly triple of the deficit one year earlier. Lower-than-planned inflation will reduce budget revenue, but higher than forecast growth will have the opposite effect, Economy Ministry deputy state secretary Péter Benő Banai said. One-off effects lifted the cashflow deficit in January-April, Banai said, noting that they expect a considerable surplus in May. Every one percent drop in the inflation rate cuts budget revenues by about 0.1% as a direct effect, Banai said, adding that part of this effect could be offset by the higher volume of purchased goods, namely higher consumption.

As to Hungary's public debt, it came to 84.6% of gross domestic product in the first quarter, amounting to HUF 24,904bn (EUR 81.5bn) at the end of March, the National Bank of Hungary said. It rose from 79.2% at the end of 2013 and from 82.8% at the end of the first quarter last year. The public debt peaked in the second quarter of 2010.

Economic and Monetary Policy

Rate cutting cycle continues

This month the National Bank of Hungary's (MNB) rate-setters cut the base rate by 10 basis points to 2.4%, in line with expectations. They continued an easing cycle started in August 2012.

In a statement, the rate-setting Monetary Council suggested the policy easing could continue, depending on the outlook for the economy, risk perceptions and scenarios in the central bank's next quarterly inflation report due out in June. "*The Monetary Council will decide on the need and possibility of reducing the base rate further after a comprehensive assessment of the macroeconomic outlook and developments in perceptions of the risks about the economy and in view of the baseline projection and alternative scenarios in the June issue of the Quarterly Report on Inflation,"* the statement said. Justifying its decision, the MC cited the negative output gap and said inflationary pressure was "*likely to remain moderate for an extended period*".

Indeed, the inflation headline figure is impressive: Hungarian consumer prices eased 0.1% in the twelve months to April, the Central Statistical Office (KSH) announced. It is worth adding that the twelve-month consumer price index (CPI) fell below zero for the first time since 1968. Part of the drop reflected the latest of a series of regulated price cuts that reduced the base fee for gas in April, but it was foods that weighed on prices more heavily, while prices for fuel, clothing and durable goods also continued to fall in annual terms. Given the annual inflation is 0% in the first quarter, the rise in net wages is significant, analysts observed.

MNB will create "bad bank" to revive lending activity

The MNB is contemplating the possibility of forming a "bad bank" to take over bad loans as it considers regulatory measures to help banks clean up their books governor György Matolcsy announced in London. Similarly, the MNB's Financial Stability Report concludes that the most effective way of solving the problem of non-performing loans is to create "bad banks", where commercial lenders would transfer such bad assets. Burdens on banks stemming from the high ratio of bad loans are hindering their ability to lend. The report states that Hungary's banking system remains strong in terms of stability and liquidity, but also refers to structural problems that are stifling economic growth. The report also alluded to the need to curb the risks to banks from retail lending by introducing stricter conditions. The MNB would introduce a loan-to-value and a payment-to-income cap for new mortgage loans to avoid unhealthy and overly exuberant growth, as was seen before the financial crisis.

Events

June 25th, 2014

Business Meeting with the local Economic and Agricultural Officers of the Embassy

Venue: Hotel New Babylon Bezuidenhoutseweg 53, 2594 AC Den Haag

More information: http://www.rvo.nl/actueel/evenementen/loop-binnen-het-buitenland

June 22-24th : Visit of **Rijksmuseum director Wim Pijbes in Budapest**

Wim Pijbes, co-chair of the jury of the international architecture tender related to the planned museum quarter in City Park (Liget Budapest Project) together with Museum of Fine Arts director László Baán, is in Budapest in preparation of the project.

June 26th, **Maarten Hendrix in Budapest**

In connection with the World Industrial Design Day, Dutch designer and architect Maarten Hendrix is to hold a presentation at the Design Terminal, entitled “Co-creation and co-ownership”