REPORT ON THE BALANCE OF PAYMENTS

2020
OCTOBER

*‘We may not always be able to do what must be done,
but we must always do what can be done.’*

Letters 27
Gábor Bethlen

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In accordance with Act CXXXIX of 2013 on the Magyar Nemzeti Bank, the primary objective of the MNB is to achieve and maintain price stability and, without prejudice to its primary objective, the central bank is also responsible for maintaining the stability of the financial intermediary system. Developments in the external balance are key to financial stability, as processes relating to the balance of payments allow for conclusions to be drawn concerning the sustainability of economic growth and the relevant risks. Moreover, the analysis of the balance of payments allows for the earlier identification of economic problems, when they are developing, and thus steps can be taken to avoid such problems.

To this end, the Magyar Nemzeti Bank regularly performs comprehensive analyses of the trends relating to Hungary's external balance, examining a number of indicators to assess macroeconomic imbalances and identifying elements and processes which are of critical importance for Hungary's vulnerability.

Given the lessons from the financial crisis and the recent period, a country's balance of payments and the trends therein indicating potential dependence on external financing are particularly important in the economic media. Developments in the external balance position are also closely monitored by market participants and analysts. The primary goal of the Report on the Balance of Payments is to inform market participants about the developments in the balance of payments by way of this regular analysis, and thus provide deeper insight into the workings of the economy.

The analysis was prepared by the Directorate Monetary Policy and Financial Market Analysis. Contributors: Anna Boldizsár, Csaba Csávás, Balázs Kóczián, Péter Koroknai, Dániel Simon, Balázs Sisak, Daniella Tóth and Márton Varga. The Report was approved for publication by Barnabás Virág, Deputy Governor.

The Report is based on information pertaining to the period ending 21 September 2020.

Summary

The four-quarter value of **Hungary's net lending corresponded to 1.1 percent of GDP in 2020 Q2**, falling short of the figure from the previous quarter. With net lending remaining stable, Hungary's external balance position continues to be **favourable in the region**, while net borrowing is high in several countries.

In the second quarter, the moderation of external balance indicators that had been stabilising in previous quarters **is attributable to the decrease in the trade surplus, which has been significantly impacted by the coronavirus pandemic**. Net exports were reduced to a greater degree by the declining services balance, which was mainly due to the **downturn in tourism and transportation services**, but the **fall in goods exports** as a result of the collapse of external demand and factory closures also contributed to this, while imports decelerated owing to the downswing in consumption and investment. The decline in the trade surplus was partly offset by **the improvement in the income balance in view of foreign-owned companies' lower profits**. With the absorption of EU transfers remaining stable, **the transfer balance** continues to **contribute** significantly **to Hungary's net lending**.

As a result of the revision carried out simultaneously with the quarterly data release, **the current account deficit-to-GDP ratio declined by 0.6 percentage point to 0.3 percent in 2019**. The more favourable current account balance resulted from **the lower than previously estimated value of the income of foreign-owned companies** operating in Hungary. This impact was attenuated by the fact that – in connection with its annual GDP revision – the HCSO **reduced the figure for last year's trade surplus**. Due to the base effect, the revision also improved the 2020 H1 income balance, while 'Net errors and omissions' in the balance of payments declined considerably.

The four-quarter **external balance position** calculated **on the basis of financing data fell to close to zero in 2020 Q2**. Dividend disbursements notwithstanding, **net FDI inflows continued in 2020**, but **significant amounts of funds flowed out of the country through portfolio equities**, with non-residents' sales of shares and domestic players' purchases of foreign mutual fund shares also contributing to these developments. The net borrowing that evolved on a quarterly level, as well as generating the funds necessary for dividend disbursements and purchases of foreign shares, necessitated **inflows of debt liabilities**, which was partly offset by the decline in non-residents' holdings of government securities. **All three sectors contributed** to the increase in the external debt of the economy.

Accordingly, following the previous quarter's low, **external debt indicators rose slightly in Q2, but remain at very low levels**. The **net external debt-to-GDP ratio of 8.2 percent** was attributable to inflows of debt liabilities, changes in nominal GDP and revaluation effects. The latter were related to the decline in government securities yields, which is a favourable development in terms of sustainability. The **FX bond issuance** by the state did not affect the net external debt. The level of FX reserves continues to **significantly exceed the level expected and deemed safe by investors**.

Looking at the savings of sectors, **the decline in net lending is attributable to the general government deficit**, which rose sharply as a result of falling tax revenues and substantial healthcare procurements, while the net savings of the private sector increased. While **household savings increased** in line with a decline in consumption and the strengthening of precautionary motives, **corporate net borrowing decreased as a result of more subdued investment activity**. The shift towards longer maturities and the rise in **households' government securities holdings** continue to **reduce external vulnerability**.

As a special topic, we analysed **the income of foreign-owned corporations operating in Hungary**. According to incoming data, **foreign-owned companies' profits as a proportion of GDP continued to fall** in 2019. As the size of the dividends paid to owners even slightly exceeded the previous year's figure, the decline in income **was reflected in a drop in reinvestments** – although the size of the latter **remains large**: foreign-owned companies continued to invest more than half of their income in Hungary, which is **significant in a regional comparison as well**. The decline in the profits of foreign-owned companies was also **reflected in the decrease in the gap between GNI and GDP**.

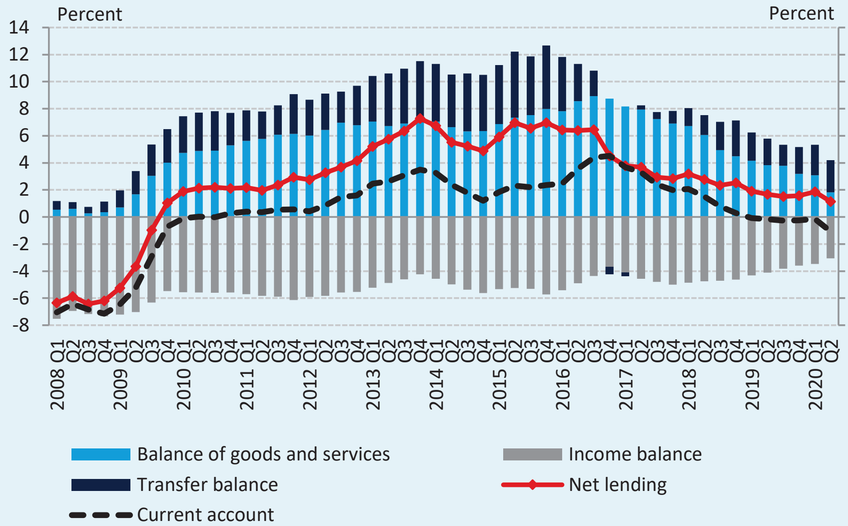
Contents

1 Real economy approach

According to the real economy approach, Hungary's four-quarter net lending declined to 1.1 percent of GDP in 2020 Q2, while the current account deficit amounted to 1.1 percent of GDP. The developments underlying the external balance indicators were determined by the impacts of the coronavirus pandemic. The decline in net lending is primarily attributable to the lower trade surplus (related to both services and the goods balance), which was partly offset by an improvement in the income balance. Net exports decelerated growth significantly, while the significant decline in export and import volumes was mitigated by favourable developments in the terms of trade. Despite the above developments, in part due to the continued existence of the large transfer balance surplus, the Hungarian economy's net lending position remains among the highest in a regional comparison.

In 2020 Q2, Hungary's four quarter net lending according to the real economy approach declined to 1.1 percent of GDP, while the current account deficit corresponded to 1.1 percent of GDP, following the previous quarters' figures, which were close to zero (Chart 1). The decline in four-quarter net lending was primarily due to the decrease in the goods and services surplus, the impact of which could not be offset by the improvements in the transfer balance and the income balance. According to *unadjusted quarterly data*, the external net borrowing in Q2 was EUR 190 million, resulting from a current account deficit of EUR 847 million and a capital account balance of EUR 657 million. Although the latter increased compared to the previous quarter, it was unable to offset the current account deficit. As a result, net lending turned into a net borrowing in Q2.

Chart 1: Developments in the components of net lending* (four-quarter values as a percentage of GDP)

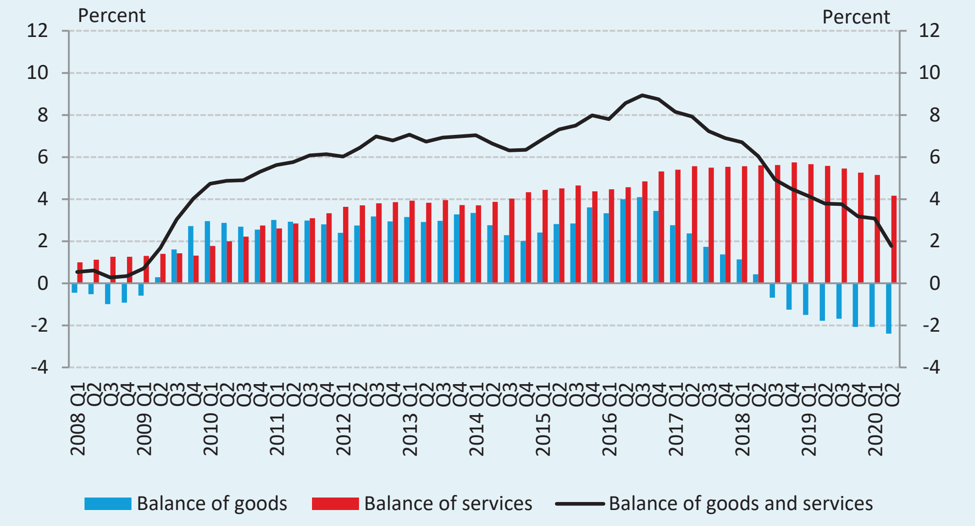


** Income balance: earned income, income on equity and income on debt. Transfer balance: sum of the capital account and other primary and secondary income.*
Unless otherwise indicated, the source of the charts is the MNB.

1.1 Trade balance

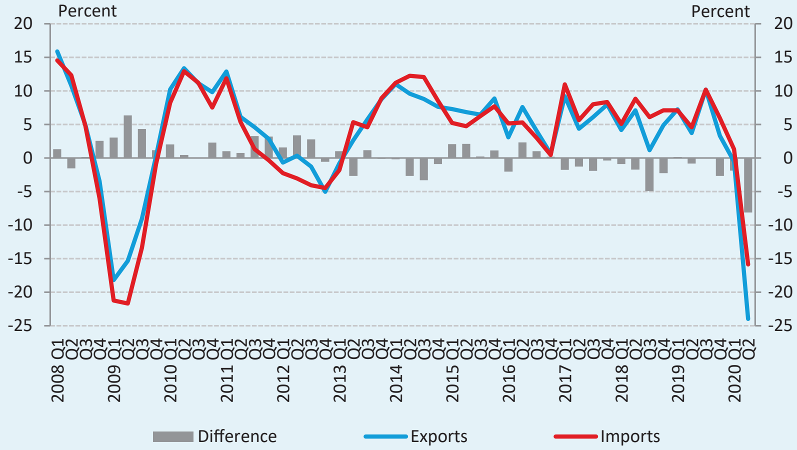
In 2020 Q2, the four-quarter trade surplus continued to contract as a result of the pandemic, with a contribution from both the decrease in the goods balance and the decline in the surplus of the services balance, which fell more sharply than in the previous quarter (Chart 2). The downward trend in the trade balance observed from early 2017 had appeared to come to an end in 2019, but then resumed again from late 2019, with the decline accelerating in 2020 Q2. Although the *services balance* continues to be a major contributor to the trade surplus, the surplus of the former fell from the level of nearly 6 percent observed in previous quarters to 4 percent by 2020 Q2. Tourism and transportation services, which represent a major weight within the services balance, already declined in March, but in Q2 the balance of these services subsectors dropped even more significantly, resulting in a sharp fall in the surplus on the overall services balance. In addition, the *goods balance* as a proportion of GDP also reduced the trade balance more strongly than in the previous quarters.

Chart 2: Developments in the balance of trade and its components (four-quarter values as a percentage of GDP)



In 2020 Q2, both exports and imports declined considerably year on year as a result of the economic developments and restrictions related to the coronavirus, although imports fell less than exports (Chart 3). Annual real growth in exports was already slightly negative in the previous quarter as well, but the fall in Q2 was close to 25 percent: such a negative value was not seen even during the 2008–2009 financial crisis. Hungary's largest trading partner is the European Union, and thus the 14-percent drop in European GDP in Q2 also had a very unfavourable effect on Hungary's export sector. Not only lower external demand, but factory stoppages around the spring peak of the pandemic also contributed to the downturn. The deceleration in exports was reflected in the drop in imports as well (through, *inter alia*, the slowdown in highly import-intensive export products and investment), with imports also reduced by more subdued household consumption. At the same time, the decline in imports was moderated by the government's high-value purchases of healthcare equipment.

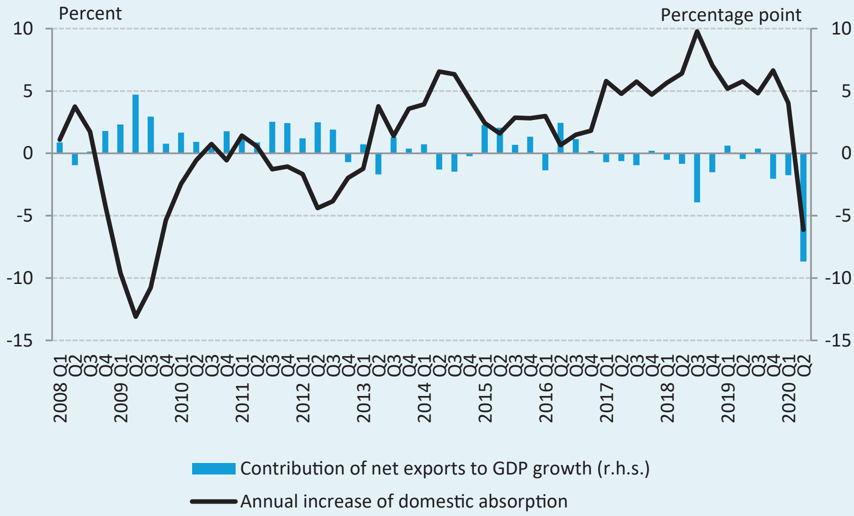
Chart 3: Annual real growth in exports and imports



Source: HCSO

The annual growth rate of domestic absorption decelerated in Q1 already and shifted to a decline in Q2, while the downturn in net exports also restrained growth significantly (Chart 4). Within the domestic absorption items, in addition to the decline in household consumption, the fall in investment in view of the domestic and international effects of the coronavirus pandemic also resulted in slower growth. Investment by companies producing for external markets – and within that, development projects in manufacturing, which have a high weight – fell by more than 10 percent year on year, and the downturn was even larger in the sector producing for the domestic market and in the services sector. In addition to the annual decline in domestic absorption items, the contribution of net exports to growth in 2020 Q2 restrained economic growth to a much greater degree than in the previous quarter.

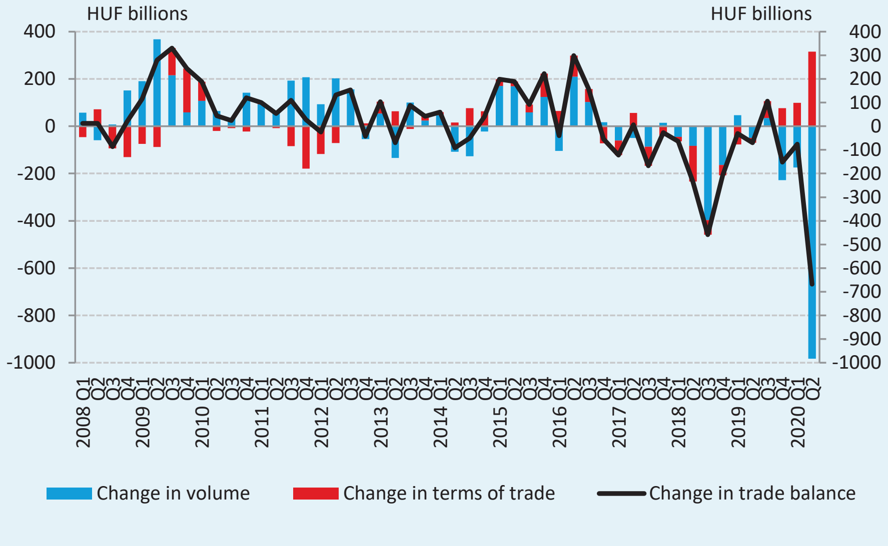
Chart 4: Annual growth rate of domestic absorption and contribution of net exports to GDP growth



Source: HCSO

The decline in the trade balance in 2020 Q2 was attributable to the change in volume, which was partly offset by a considerable improvement in the terms of trade. In Q2, the widening gap between the annual volumes of exports and imports as well as the fall in export volume, which was much larger than during the 2008 financial crisis, resulted in a major decline in the trade balance related to quantities. The sharp fall in oil prices that started at the end of Q1 continued in Q2 as well. As a result, the oil price, which on average remained close to its historical low during the quarter, mitigated the negative impact originating from the change in volume via the price effects stemming from the improvement in the terms of trade. (Chart 5).

Chart 5: Developments in the balance of trade factors according to GDP (year-on-year)

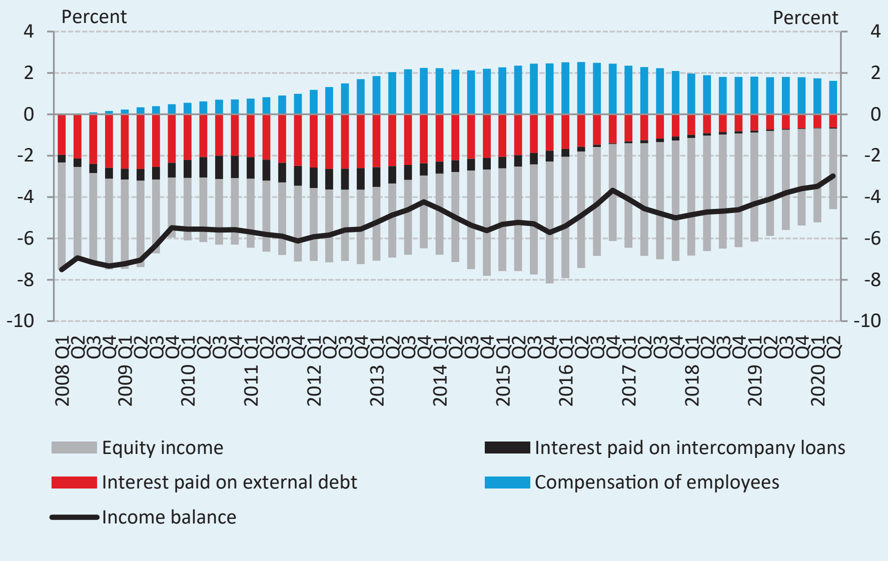


Source: HCSO.

1.2 Income balance

The deficit on the income balance declined further in 2020 Q2, primarily due to the falling profits of foreign-owned companies (Chart 6). The four-quarter deficit on the income balance fell to 3 percent of GDP in Q2, which was attributable to the decrease – due to the downward trend since 2018 and the effects of the pandemic – in the income related to equity of foreign-owned companies,[1] representing the highest weight within the income balance. Net interest expenditure related to foreign loans and intercompany loans stabilised at a very low level (below 0.7 percent of GDP). Employees' income from abroad dropped slightly compared to the previous quarter, presumably as a result of the factory closures and stoppages implemented abroad as well.

Chart 6: Developments in income balance items* (four-quarter values as a percentage of GDP)



** Income balance: earned income, income on equity and income on debt.*

1 We only have limited quarterly data concerning the profits of foreign-owned companies. Therefore, the information on profit outflows is based on estimates. For more details, see the publication 'Methodological notes to the balance of payments and international investment position'.

Box 1: Revision of the balance of payments

As a result of the revisions, the balance of payments data changed retrospectively, with a fundamentally positive impact on the balance (Chart 7). With the release of the Q2 balance of payments data, the MNB also published the revisions of the previous years' data. As part of this revision, with the receipt of the corporate questionnaires we were able to learn about the annual figures for the 2019 corporate income data in the September data release (for more details see the special topic). Nevertheless, these changes had no major impact on our assessment of external balance developments in past years. The most important changes concerning 2019 are the following:

- The largest change (EUR 1,409 million) relates to the decline in the income balance, which is attributable to various factors. Firstly, the data estimated previously for the 2019 profits of foreign-owned companies operating in Hungary were replaced by actual data based on the corporate questionnaires, as a result of which the slightly lower corporate income compared to previous indications lowered the income account deficit. Secondly, the income of those working abroad for less than one year also rose slightly.

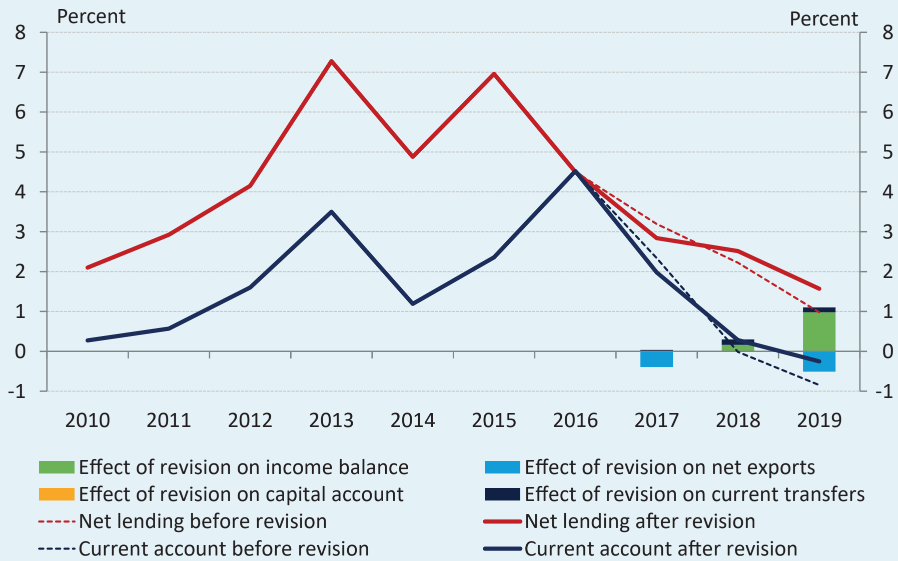
- Compared to previous indications, net exports declined by EUR 730 million, which was related to the revision of foreign trade data carried out by the HCSO and part of this change initially appeared in the balance of payments statistics.

- The balance of secondary incomes (previously unrequited current transfers) rose by EUR 175 million.

Accordingly, on the whole, in 2019 the current account balance exceeded the previously published value by EUR 853 million, and thus the deficit amounted to 0.3 percent of GDP (0.6 percentage point lower compared to the previously released figure), while net lending amounted to 1.6 percent.

In 2020 Q1, both net lending calculated from the real economy side and the current account balance improved by EUR 0.3 billion as a result of the revision, primarily due to the lower profits of foreign-owned companies.

Chart 7: Impact of the revisions on net lending (as a percentage of GDP)



As a result of the revision of the balance of payments, the financing side also changed, but – on the whole – there was a considerable decline in 'Net errors and omissions' in 2019. Some of the changes affecting the current account entail a change of the same size on the financing side as well. In addition to the aforementioned lower profits of foreign-owned companies, some companies amended – by retroactively increasing – the figures for last year's adopted dividends as well. Accordingly, in 2019 both factors pointed to lower reinvestment and thus to lower foreign direct investment. In addition to that, however, the changes affecting the current account also have a component that does not affect the financing side. For example, the trade balance, which was lower compared to the figure previously released by the HCSO, ultimately brought net lending calculated according to the two – real economy and financing – approaches closer to one another. As a result of the revisions, 'Net errors and omissions' in the balance of payments statistics dropped significantly, by EUR 0.6 billion in 2019.

Table 1: Impact of the revisions* on components of net lending (EUR billion)

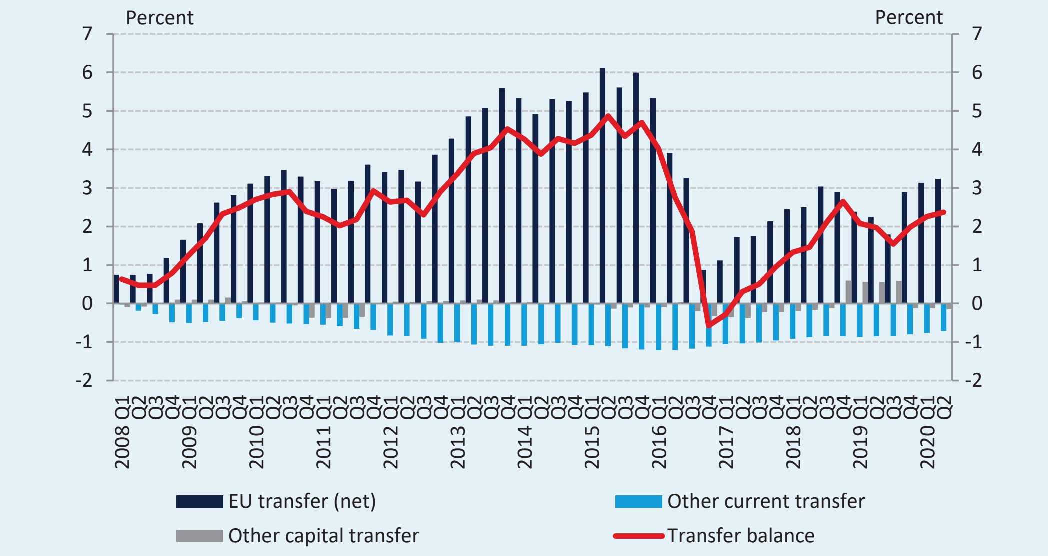
	2017	2018	2019	2020. I. n.év
I. Change in net lending from real economy side (1+2+3)	**-0.4**	**0.4**	**0.8**	**0.3**
1. Balance of goods and services	-0.5	0.0	-0.7	0.0
2. Income balance	0.0	0.2	1.4	0.3
3. Transfer balance	0.0	0.2	0.2	0.0
Current account	***-0.4***	***0.4***	***0.9***	***0.3***
II. Change in net lending from financing side (5+…+8)	**0.0**	**0.0**	**1.5**	**0.5**
5. Foreign direct investment	0.0	0.0	1.7	0.7
6. Portoflio equity	0.0	0.0	0.0	0.0
7. Financial derivatives	0.0	0.0	0.0	-0.8
8. Net debt	0.0	0.0	-0.2	0.6
Net errors and omissions (I.-II.)	***-0.4***	***0.4***	***-0.6***	***-0.2***

** Positive values in the Table denote an improvement in the external balance indicator compared to its previous value denote an improvement in the real economy side's indicator, while on the financing side smaller inflow of external funds, compared to its previous value.*

1.3 Transfer balance

The four-quarter surplus of the transfer balance as a proportion of GDP expanded slightly in Q2. In 2020 Q2, the transfer balance surplus rose to 2.4 percent of GDP, contributing significantly to maintaining Hungary's favourable external balance position (Chart 8). According to four-quarter data, inflows of EU funds in 2020 Q2 corresponded to 3.2 percent of GDP, while other current transfers had a less negative impact on the transfer balance than before. The income of those employed abroad for a short time declined due to the pandemic, and thus the amount of taxes and contributions paid abroad also fell slightly within the other current transfers item, which also contributed to the improvement in the transfer balance to a small degree.

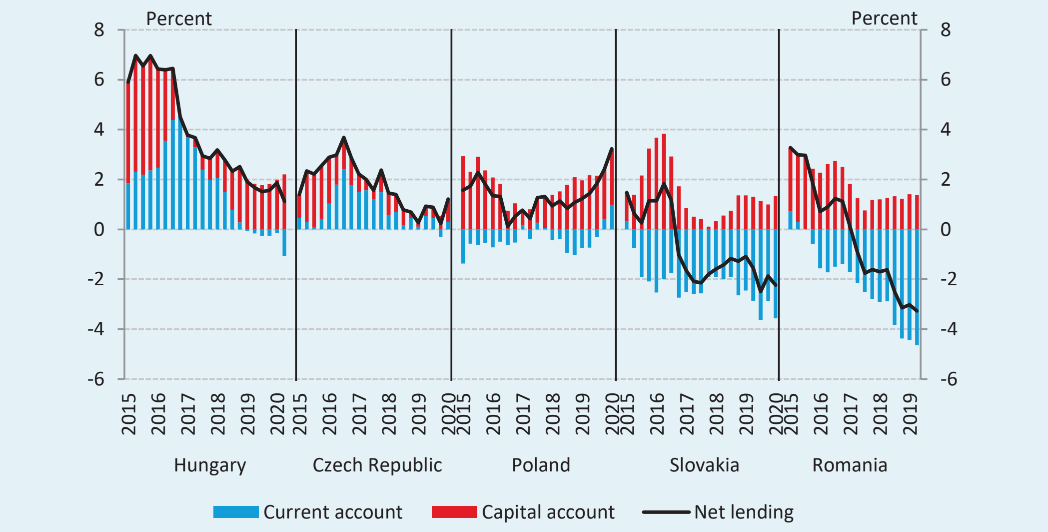
Chart 8: Four-quarter developments in the items of the transfer balance (four-quarter values as a percentage of GDP)



1.4 Regional comparison

As a result of developments related to the coronavirus, the net lending position of the Hungarian economy worsened in Q2, but remains favourable in a regional comparison (Chart 9). The external balance position is still supported by the surplus on the capital account, which is significant compared to the other countries of the region. At the same time, although Hungary's current account balance falls slightly short of the Czech or Polish levels, it significantly exceeds the figures for Slovakia or Romania. Comparability with the countries of the region is limited by the fact that in the case of the neighbouring countries only 2020 Q1 data are available, and thus the impact of the spring upswing in the pandemic on the economy is not yet reflected in the regional data. External balance indicators have typically declined in the countries of the region since 2016, which is attributable to the decrease in capital account balances between two EU budget cycles as well as to declines – related to economic growth – in the countries' current account balances. The level of Hungary's net lending is among the highest across the countries of the region. Developments in the external balance in Poland are worth highlighting, as an improvement has been observed there for several quarters in both the current account and net lending, with the latter amounting to more than 3 percent of GDP.

Chart 9: Four-quarter net lending of the countries of the region (as a percentage of GDP)



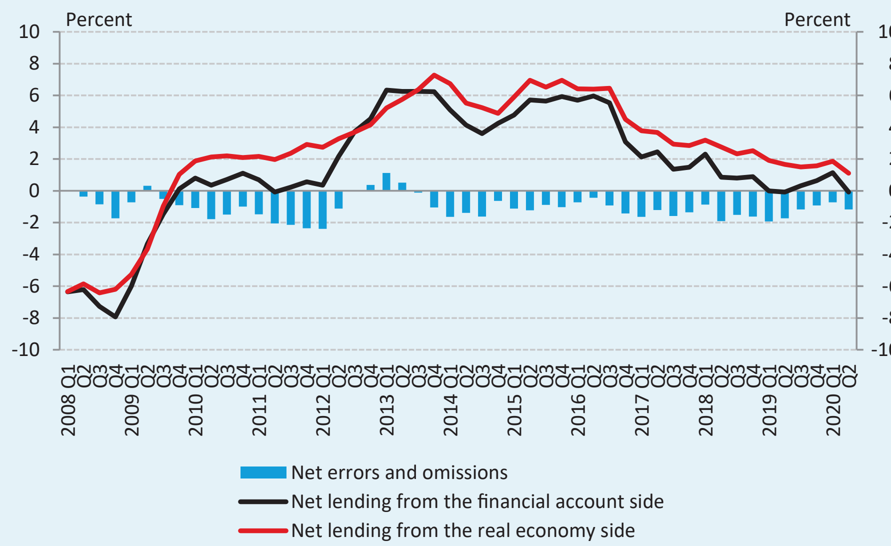
Source: MNB and Eurostat.

2 Financing approach

The external balance position calculated on the basis of the four-quarter data of the financial account also declined in Q2. Looking at transactions in Q2, net FDI inflows continued in spite of dividend disbursements. Nevertheless, as a result of a decline in portfolio equity funds, outflows of non-debt liabilities were observed, accompanied by a rise in debt liabilities. All three domestic sectors contributed to the rise in the economy's external debt, but it was mainly the external debt of banks and corporations that increased.

According to financing data, the four-quarter external balance position of the Hungarian economy was around zero in 2020 Q2 (Chart 10). Similarly to the real economy approach, four-quarter net lending calculated on the basis of the financing side also declined. The difference between the four-quarter rolling values of the two external balance indicators increased slightly, but the revision of the 2019 data significantly reduced the level of the difference between the two approaches retroactively as well.[2] Accordingly, net errors and omissions were close to 1 percent of GDP in Q2, which means that the error of the balance of payments is slightly below the level of the historical average.

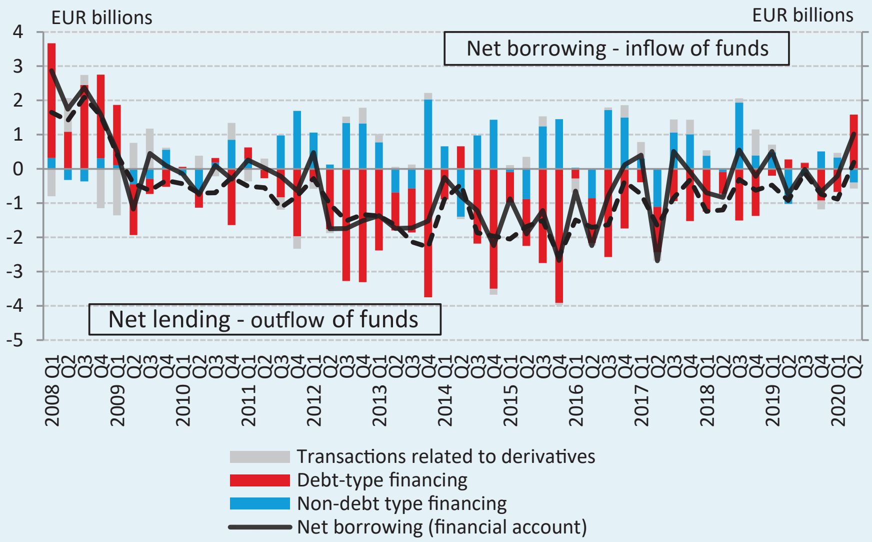
Chart 10: The two types of net lending (four-quarter data as a percentage of GDP)



Looking at the quarterly data, the increase in net borrowing based on the financial account continued in Q2 (Chart 11). Inflows of net debt liabilities rose to nearly EUR 1.6 billion, whereas in relation to the dividend disbursements typical in the second quarters and the decline in portfolio equity investments, outflows of non-debt liabilities amounted to nearly EUR 400 million. As a result of the above, net borrowing calculated on the basis of the financial account corresponded to more than EUR 1 billion in Q2.

2 Developments in the balance of payments can also be described in terms of the financing of real economy transactions. Namely, the financial account shows what kinds of transactions affecting net financial worth were used by resident economic agents to finance real economy transactions. While data derived from the real economy approach and the financing approach should be identical in theory, differences are likely to arise in practice due to non-integrated data sources, incomplete observation and the different treatment of the exchange rates, as indicated by the category 'Net errors and omissions'.

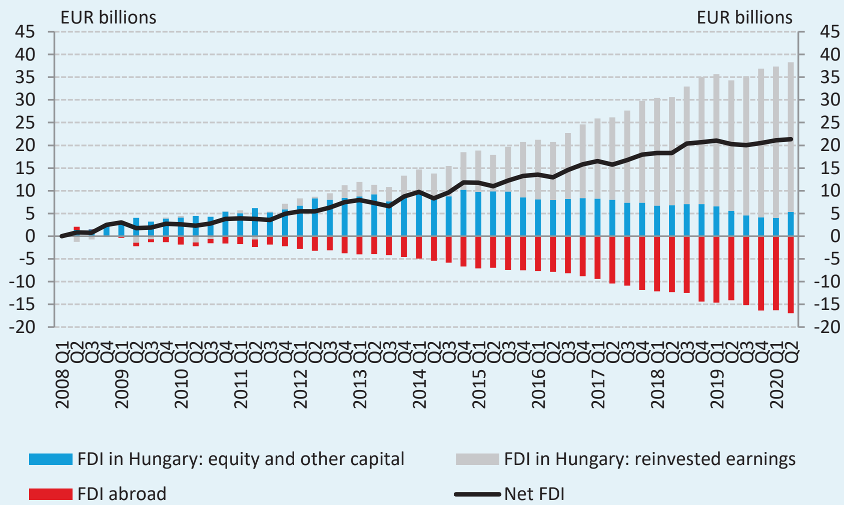
Chart 11: Structure of net lending (unadjusted transactions)



2.1 Non-debt liabilities

Net FDI increased further in Q2, despite liabilities being significantly reduced by the usual dividend payments and Hungarian companies' investment abroad (Chart 12). Based on data excluding capital-in-transit transactions and asset portfolio restructuring, net FDI inflows amounted to EUR 0.3 billion in Q2. As a result of the dividend disbursements typical in this part of the year, the equity-type liabilities of foreign-owned companies operating in Hungary and reinvested earnings declined. By contrast, the rise in net liabilities of intercompany loans originating from transactions supported the increase in FDI. These developments, however, were partly attributable to the expansion in adopted but not yet paid dividends. Net FDI inflows were reduced significantly (by nearly EUR 0.5 billion), as a result of Hungarian companies' investments abroad.

Chart 12: Developments in FDI excluding capital-in-transit transactions (cumulative transactions)

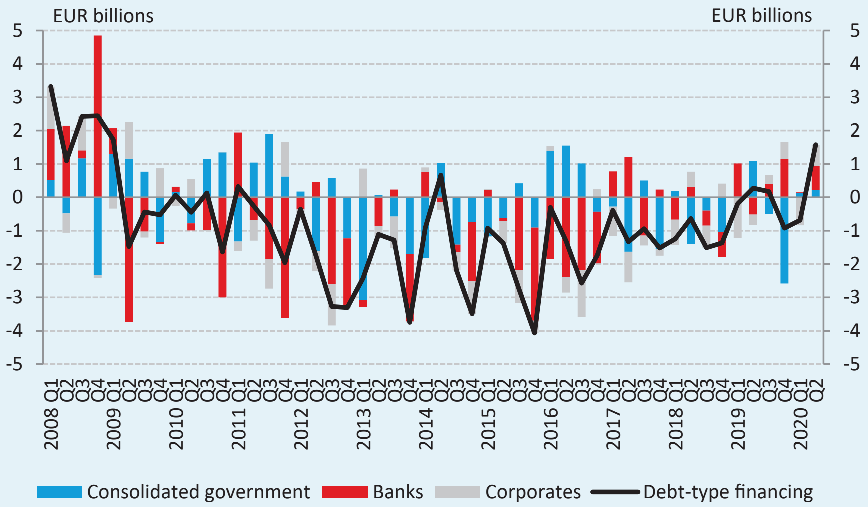


Net portfolio equity investments fell by EUR 670 million in Q2, attributable to a decline in domestic equity investments as well as a rise in portfolio investments abroad. In spite of the net FDI inflows, an outflow of non-debt liabilities took place, stemming from a decline in portfolio equity investments. Hungarian actors' portfolio equity investments abroad expanded by EUR 320 million, mostly relating to an increase in foreign mutual fund shares and to a lesser degree to an expansion in equities. One underlying reason for the asset purchases may have been that the drop in international stock market prices in the spring may have been a favourable point of departure for domestic investors – primarily through mutual fund shares. Accordingly, equity and mixed funds grew to the greatest degree, but – to a lesser degree – the expansion affected derivative funds as well. Meanwhile, non-residents' equity investments in Hungary declined by EUR 350 million, which may also have been attributable to reactions to the mounting effects of the pandemic (e.g. restructuring of investment portfolios based on international stock market developments).

2.2 Debt liabilities

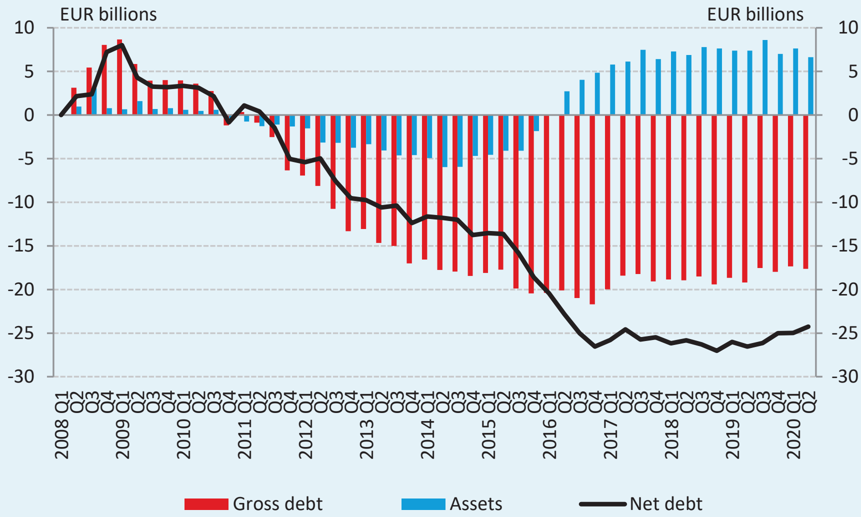
Inflows of debt liabilities were significant in Q2, with contributions by all three domestic sectors (Chart 13). In Q2, the net external debt of banks as a result of transactions increased by nearly EUR 650 million, while that of companies expanded by more than EUR 700 million, and the net external debt of the general government also rose slightly. Both the foreign currency needed for the aforementioned portfolio equity purchases abroad and corporate dividend disbursements may have entailed a decline in foreign assets, which – together with the foreign currency demand related to the state's healthcare equipment purchases – may have contributed to the stronger increase in debt liabilities.

Chart 13: Developments in net debt-type financing by sector



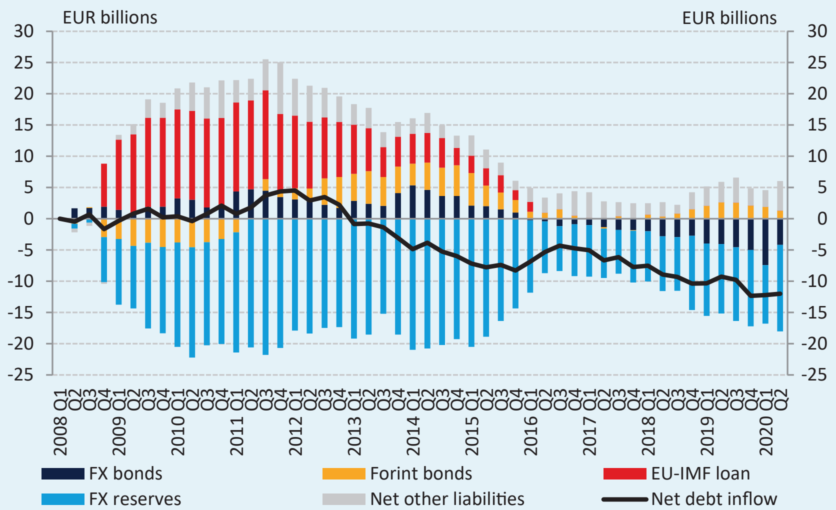
The foreign liabilities and assets of the banking sector declined to smaller and greater degrees, respectively, and thus the net external debt of the sector increased on the whole (Chart 14). Banks' debt inflows took place in a way that the decline in short-term funds was offset by an expansion in long-term liabilities. In Q2, the effect of a bank's FX bond issue was also reflected in the rise in the banking sector's long-term liabilities.

Chart 14: Developments in the banking sector's external debt and receivable (cumulative transactions)



The external debt liabilities of the consolidated general government including the MNB increased modestly during the quarter (Chart 15). FX reserves and gross liabilities both rose considerably – and thus net external debt was not affected – as a result of the FX bond issues during the quarter. At the same time, FX reserves rose to a lesser degree than gross liabilities as the decline in forint liquidity-providing FX swaps and the state's higher FX expenditures due to containment measures contributed to the decline in FX reserves and thus to a rise in net external debt. At the same time, non-residents' HUF-denominated government securities holdings fell considerably, by some EUR 600 million, which decelerated the increase in the net indicator and the gross liabilities of the state.

Chart 15: Breakdown of the change in the net external debt of the consolidated general government including the MNB (cumulative transactions)



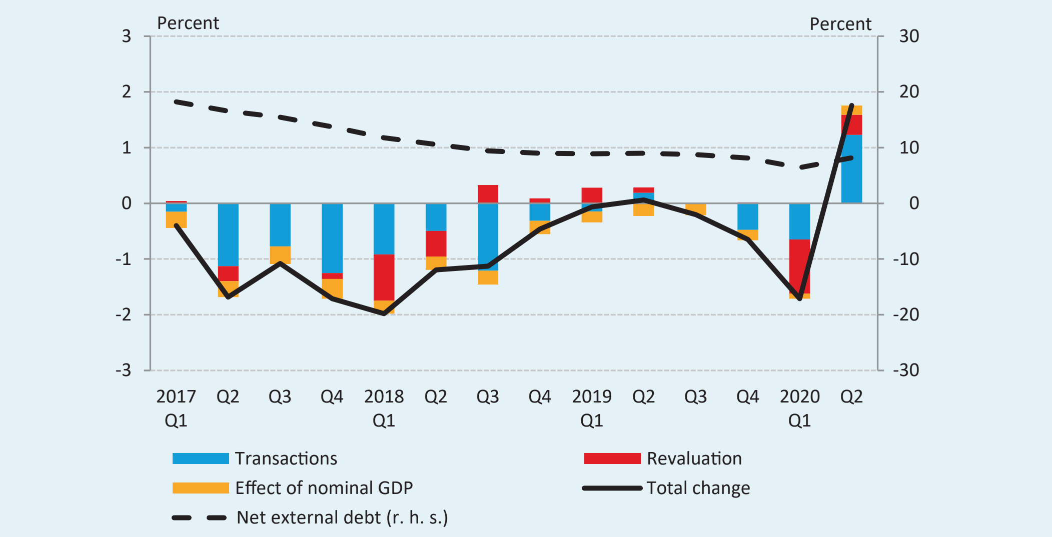
3 Developments in debt ratios

Following the previous quarter's low, external debt indicators rose in Q2: at end-June, net external debt and gross external debt corresponded to 8.2 percent and 55.1 percent of GDP, respectively. The increase in net external debt was primarily attributable to the inflows of debt liabilities seen in Q2, but revaluation effects and developments in nominal GDP also contributed to the rise in the indicator. The net external debt of both the government and the private sector expanded during the quarter. The gross external debt ratio increased to a greater degree than the net indicator, due mainly to the state's FX bond issue. At the same time, the expansion in FX reserves during the quarter exceeded the rise in short-term external debt, resulting in a further improvement in reserve adequacy. The foreign exchange reserves thus continue to significantly exceed the level expected and deemed safe by investors.

3.1 Developments in debt indicators

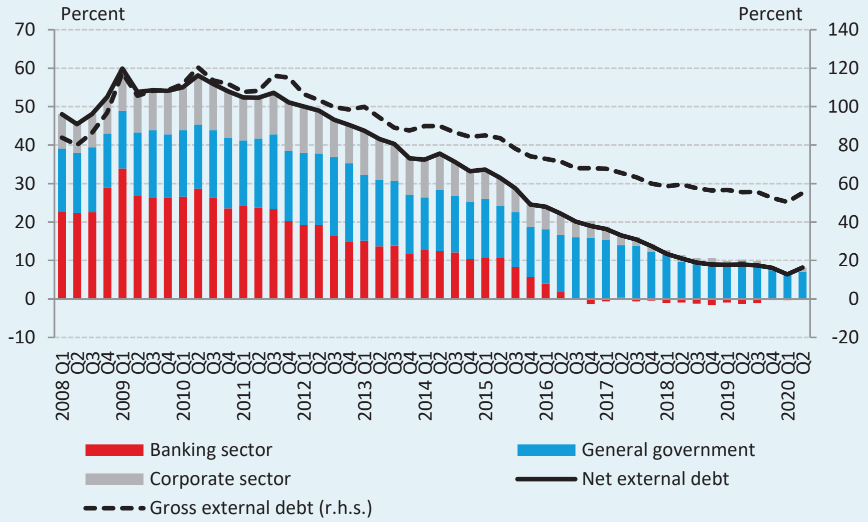
Following its low in Q1, net external debt increased in Q2, primarily owing to net debt inflows, but revaluation and the change in GDP also made contributions. From its low of 6.4 percent at end-March, the net external debt-to-GDP ratio rose to around the end-2019 value, i.e. to 8.2 percent in Q2. Inflows of debt liabilities resulted in a rise of 1.2 percentage point in the net external debt-to-GDP ratio, while revaluation effects and the decline in nominal GDP elevated the indicator by 0.4 percentage point and 0.1 percentage point, respectively. The revaluation was primarily related to the fact that the fall in forint yields contributed to an increase in the value of non-residents' government securities holdings (Chart 16).

Chart 16: Components of the change in net external debt (values excluding intercompany loans as a percentage of GDP)



The increase in the net external debt of both the general government and the private sector contributed to the rise in the debt-to-GDP ratio (Chart 17). The net external debt of the general government including the MNB rose by 0.8 percent of GDP, primarily because the expansion in FX reserves fell short of the increase in the external liabilities of the state, due to the costs of containment measures and the decline in the forint liquidity-providing FX swap. At the same time, the drop in non-residents' HUF-denominated government securities holdings supported a decline in net external debt. FX bond issues by the state added to both the FX reserves and foreign liabilities and thus did not change the level of net external debt. The foreign liabilities of the state also rose because of the higher prices of non-residents' government securities holdings and the associated revaluation, occurring as a result of the decline in yields. The fall in corporations' external assets exceeded the decline in liabilities, which was primarily related to the repayment of commercial loans, and thus the sector's net external debt rose by 0.4 percentage point, following a decline of a similar degree in the previous quarter. The increase in banks' net external debt was attributable to a larger fall in foreign financial assets, while the decline in loan debts was offset by one bank's bond issue in April.

Chart 17: Breakdown of net external debt by sectors and gross external debt (as a percentage of GDP, excluding intercompany loans)



In Q2, Hungary's gross external debt advanced to 55.1 percent of GDP. The rise in this indicator was entirely related to the general government including the MNB, mainly reflecting the effect of the FX bond issues by the general government in April and June. On the whole, the gross liabilities of the private sector remained practically unchanged, as the effect of the decline in the corporate sector's liabilities related to the repayment of commercial loans was offset by an increase in the banking sector's gross external debt, which was partly related to the issuance of bonds by banks. In addition to transactions, revaluation of the outstanding debt – due to a fall in yields and through the price changes of government securities – also contributed to the increase in gross external debt.

3.2 Foreign exchange reserves and reserve adequacy

Compared to end-March 2020, the level of FX reserves increased by EUR 4.4 billion in 2020 Q2, and amounted to EUR 30.2 billion at end-June. The changes in reserves were affected by various factors, the most important of which were the following:

- The *net FX financing of the Government Debt Management Agency (ÁKK)* raised the reserves by EUR 3.2 billion in total. In April, the ÁKK issued new euro bond series with maturities of 6 and 12 years with a nominal value of EUR 1 billion each, followed by a 15-year green bond issued in a value of EUR 1.5 billion in June.

- The reserve-increasing effect of EU funds was nearly EUR 0.7 billion, resulting primarily from the payment of performance-based invoices of the 2014–2020 EU programming period and to a lesser degree from agricultural subsidy programmes.

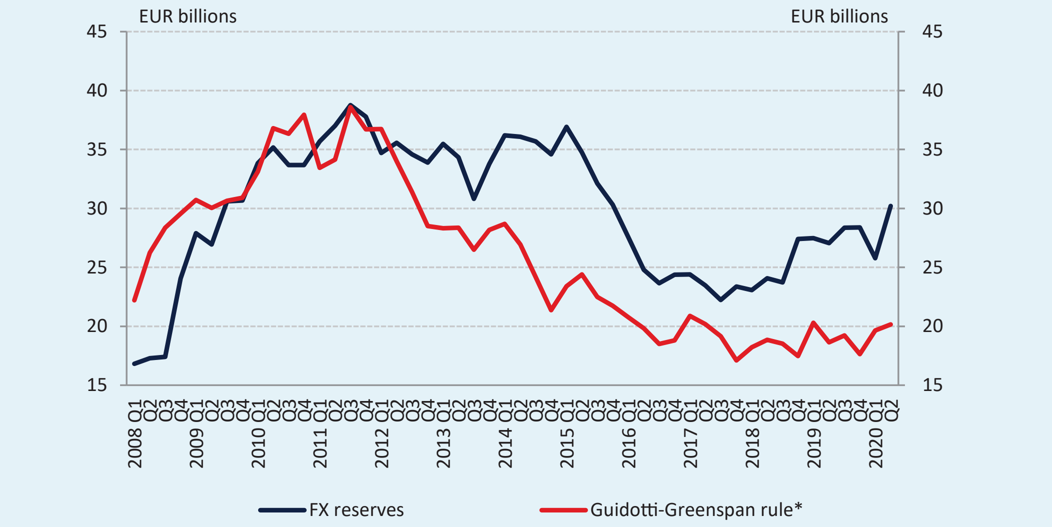
- The reserve-reducing impact of the *FX transactions of the Hungarian State Treasury (MÁK)* was primarily attributable to the equipment purchases by the government related to managing the public health emergency, which were mainly paid in foreign currency.

- The change in the stock of the forint liquidity-providing FX swap instrument also reduced the reserve level.

- The aggregate impact of other items added to the reserves.

At the end of 2020 Q2, the MNB's international reserves exceeded the level of short-term external debt, which is closely watched by investors, by EUR 10 billion. At end-June 2020, international reserves and short-term external debt amounted to EUR 30.2 billion and EUR 20.2 billion, respectively. The rise in both the debt based on original maturity and the debt whose maturity became shorter contributed to an evolution of short-term debt that slightly exceeded that of the previous quarter. Compared to the level of EUR 6.1 billion at end-March, reserve adequacy compared to short-term external debt thus increased significantly in 2020 Q2: the leeway above the Guidotti–Greenspan indicator, which is closely followed both by the central bank and investors, was EUR 10 billion at end-June (Chart 18).

Chart 18: Short-term external debt of the Hungarian economy and foreign exchange reserves



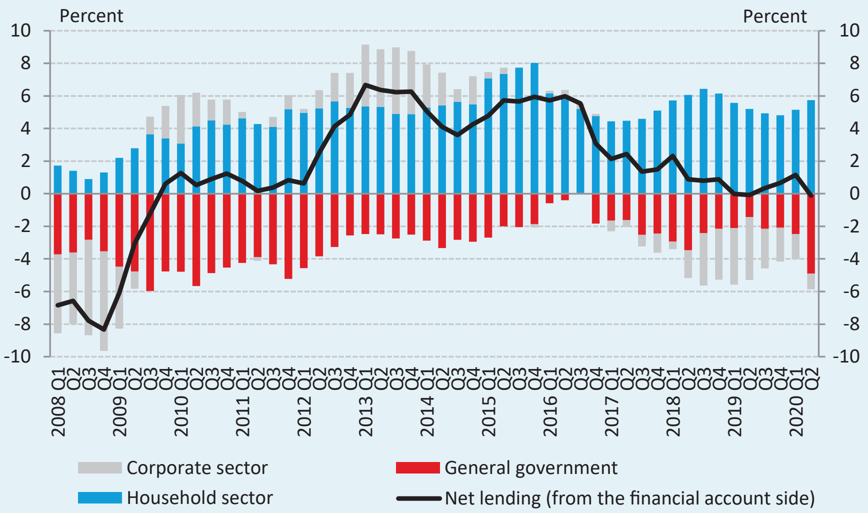
** Guidotti–Greenspan indicator: short-term external debt based on residual maturity.*

4 Sectors' savings approach

Changes in the external balance position according to the savings of sectors were determined by the significant Q2 deficit of the general government, the impact of which was partly offset by the improving savings position of the private sector. Protection against the pandemic, economic protection measures and declining tax revenues were factors behind the surge in the deficit. The rise in households' net savings was attributable to the decline in consumption, while the decrease in the corporate net borrowing was caused by the downturn in investment activity. Significant financial asset accumulation and a slower expansion in loans outstanding contributed to households' increasing net lending. In view of the uncertainty created by the pandemic, it was primarily savings held in liquid financial assets that rose, but households' share purchases also reached a high level following the plunges on the stock exchanges. Although at a slower pace, households' government securities holdings increased further during the quarter, which was attributable to the purchases of long-term MÁP+ securities.

According to the developments in the sectors' savings, the high deficit of the general government contributed to the decline in the net lending position, which was partly offset by the improving position of the private sector (Chart 19). The fiscal deficit increased as a result of the costs of coronavirus pandemic prevention measures, economic protection measures and the decline in tax revenues in parallel with the contraction of the economy: the four-quarter government net borrowing was close to 5 percent of GDP. In parallel with that, in view of the downturn in consumption and investment, the financial saving position of the private sector improved: households' four-quarter net financial savings approached 6 percent of GDP, while corporate net borrowing fell to below 1 percent of GDP.

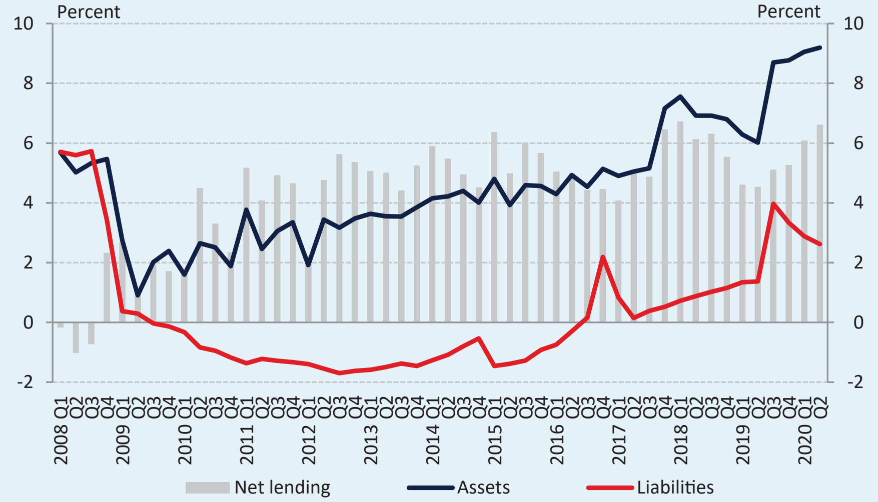
Chart 19: Net lending of specific sectors* (four-quarter values as a percentage of GDP)



** General government represents the net borrowing according to the financial accounts. Corporations based on the residual principle.*

Both the high financial asset accumulation and the decline in net borrowing contributed to the rise in households' net financial savings (Chart 20). Households' financial assets accumulation increased considerably during the quarter, reflecting the effect of the downturn in consumption and the precautionary savings in view of the more uncertain income and labour market prospects as a result of the pandemic. According to seasonally adjusted data, the expansion in household loans outstanding continued more slowly, which may also have been affected by the cautiousness due to the pandemic. Prenatal baby support loans are still popular. Their borrowing may have partly increased the financial assets as well, which may also have had an impact on the continued high financial asset accumulation.

Chart 20: Net lending of households (seasonally-adjusted, revised* values, as a percentage of GDP)

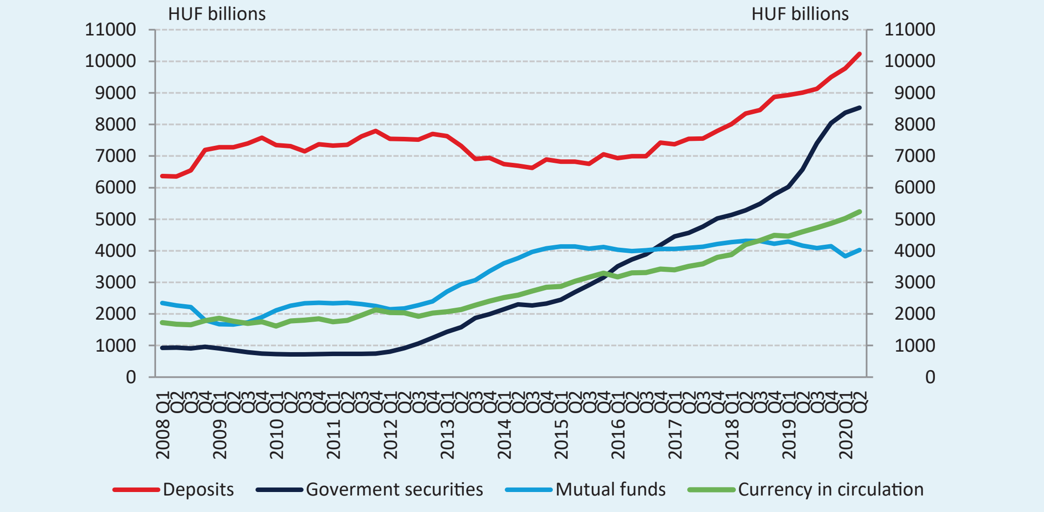


** Figures showing underlying trends, adjusted for the impact of pension savings, the early repayment scheme and the real yield payment, the indemnification of the depositors of liquidated mutual savings banks as well as the forint conversion and settlement. Time series adjusted separately.*

During Q2, due to the uncertainty created by the pandemic, it was primarily the savings held in liquid financial assets that increased (Chart 21). The Q2 impact of the coronavirus pandemic affected households' asset allocation decisions considerably. There was buoyant demand for easily available forms of savings: households' cash holdings grew by more than HUF 200 billion, and the increase in current account deposits also significantly exceeded the value for the same period of the previous year. With the mounting uncertainty, interest in longer-term securities and investments that are more sensitive to short-term market developments showed a mixed picture during every single month of Q2. With the feed-through of the impacts of the pandemic, the sales of mutual fund shares, which suffered serious price losses due to the impacts of the virus on the economy, accelerated in April. Then, for the remainder of the quarter, in parallel with lower mutual fund share prices, financial assets already started to return to investment funds. Following the stock exchange falls in April, there was also an upswing in demand for equities, which was attributable to the lower prices as well as the favourable opportunity to open a position.

During the quarter, with the fund withdrawals in April, net purchases of retail government securities decelerated. The popularity of MÁP+, the new government security, was unbroken in Q2 as well, and the expansion in the holdings exceeded HUF 400 billion, while holdings of other government securities fell. The decline in the shorter-maturity One-Year Hungarian Government Securities (1MÁP) exceeded HUF 200 billion, and the Premium Hungarian Government Securities (PMÁP) also decreased by some HUF 80 billion. On the whole, households' government securities holdings increased by approx. HUF 150 billion, thus continuing to contribute to financing the state from domestic sources.

Chart 21: Developments in households' key financial assets



5 Income of foreign-owned companies

The special topic of the Report on the Balance of Payments discusses the developments in the income of foreign-owned companies. According to actual incoming data, which are still incomplete due to the COVID-19 situation, the profit of foreign-owned companies as a proportion of GDP declined in 2019, reaching the lowest level in the past six years. The drop in profits was also reflected in lower reinvestments, although their level remains high: foreign-owned companies continued to invest most of their earned income in Hungary. Foreign-owned companies' return on equity fell in the main sectors. The income balance deficit was also reduced by the fact that – in contrast to the decline in the previous year – the profits of companies owned by residents and operating abroad expanded. Looking at profit rates in a regional comparison, as a result of the decline in foreign-owned companies' income, return on equity decreased to a level below the average of the neighbouring countries, while the dividend payout ratio in Hungary continues to be low in regional terms. The decline in the profits of foreign-owned companies operating in Hungary was also reflected in the decrease in the difference between GNI and GDP to below 3 percent, which still corresponds to the regional average.

5.1 Introduction

In the September balance of payments data release, the previous, estimation-based data for corporate income in 2019 are replaced by actual figures on the basis of the received annual data reports. In the balance of payments, until the release of the September data following the reporting year, incomes in the corporate sector are based on estimates, which are replaced in the Q2 data release by actual figures calculated on the basis of questionnaires prepared about corporate and bank incomes.[3] At the same time, in connection with the 2019 incomes it is necessary to mention that in view of the pandemic situation the deadline for preparing the corporate reports was extended until end-September. It also means that the data currently available for the 2019 corporate incomes are more uncertain compared to previous years, as not all companies submitted their reports by the deadline for data submission. Nevertheless, actual figures concerning the corporate sector's profitability in the previous year continue to be first available during the September data release.

According to the data, the balance of profits in the income account was lower than the preliminary estimate. The difference is mainly attributable to the fact that the profit of foreign-owned companies operating in Hungary declined, in contrast to the growth expectations based on the expansion in export revenues. The balance of payments statistics contain extraordinary corporate income related to current operating performance, excluding outliers, i.e. one-off profit/loss items. This is due to the fact that – based on the methodology of the balance of payments[4] – the profit/loss realised outside current operating performance (for example, from exchange rate revaluation) does not form part of the incomes. Profit/loss items stemming from sources like this are stated among the changes in stock in the financial account. In Section 5.2, we first review the incomes of foreign-owned non-financial corporations and banks, and then examine the background of the changes in profits in 2019 (Section 5.3). Thereafter, we present companies' profits shown in the balance of payments, as well as their after-tax profit (Section 5.4). Finally, the current Report on the Balance of Payments closes with a regional comparison.

5.2 Income of foreign-owned companies in the balance of payments

In 2019, the balance of foreign-owned companies' income declined to below 6 percent of GDP. As the value of dividends paid to owners increased slightly, the drop in income was primarily reflected in lower reinvestments. During the 2008–2009 crisis, the profit of foreign-owned companies as a proportion of GDP fell in parallel with the slowdown in demand. Nevertheless, foreign-owned companies' dividend payments were around 4 percent of GDP, and thus almost the entire income produced was disbursed as dividends.[5] This may have been attributable to the significant worsening in growth prospects after the crisis and to parent companies' liquidity needs. Since 2013, the value of foreign-owned companies' income produced has also become higher, in line with the acceleration of economic growth. At the same time,

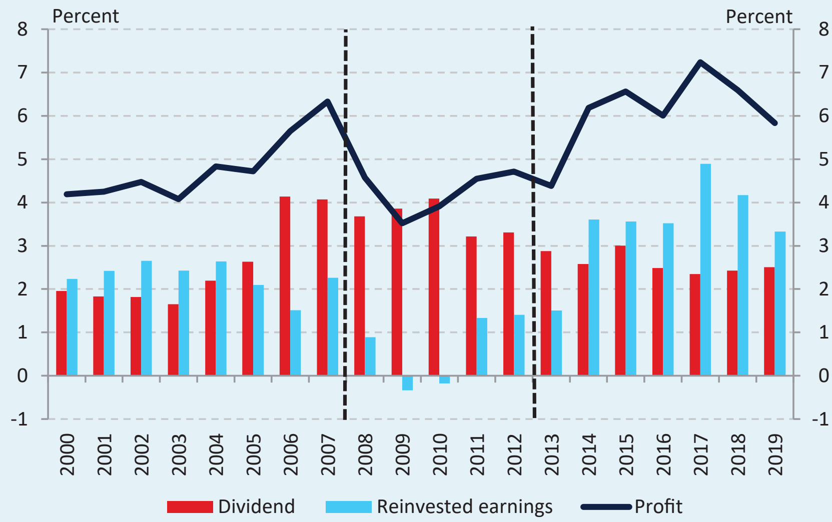
3 For more details, see: Hungary's balance of payments and international investment position statistics, MNB (2014).

4 Balance of Payment Manual, 6th edition

5 Companies usually vote on and pay dividends from their previous year's profit, and thus in fact the dividend payments of the given year should be compared to the previous year's profit. However, since the stocks included in the balance of payments data are influenced by the transactions of the given year, we present the profit of the given year together with the dividend payments of the same year.

the higher income was accompanied by subdued dividend disbursements, significantly raising the value of reinvestments, and thus of FDI inflows as well. In addition to EU funds, the high level of reinvestments has played a major role in the dynamic expansion in corporate investment in recent years. External demand, which facilitated the dynamic expansion in exports as well, also contributed to the increase in foreign-owned companies' profitability. In 2019, however, compared to the peak in 2017, the income of foreign-owned companies declined further, falling to below 6 percent of GDP. In parallel with that, the level of reinvestments dropped in the past period, although it corresponded to more than 3 percent of GDP even in 2019, with dividend disbursement fluctuating around 2.5 percent.[6] A substantial part (more than 94 percent) of foreign-owned companies' profits was produced by non-financial corporations.

Chart 22: Foreign-owned companies' income and its utilisation[7] (as a percentage of GDP)



5.3 Comparison of the profitability of banks and non-financial corporations

While banks' profit rate remained practically unchanged in parallel with the expansion in lending and improvement in the macroeconomic environment, the profit rate of non-financial corporations fell slightly. Prior to the 2008–2009 crisis, the value of companies' and banks' profits calculated as a percentage of their FDI equity was close to 10 percent and 13 percent, respectively. Following the outbreak of the crisis, the profit rate of non-financial corporations declined, but that of banks decreased to a greater degree only in 2012, and thus the profit rate of banks became lower than that of companies. Following a slight rise, foreign-owned banks' profit rate according to the current operating performance concept was close to 9 percent in 2018, remaining at the same level in 2019 as well. The favourable rates of the past three years are attributable to banks' balance sheet cleaning and the upswing in lending in line with the economic cycle. Following a rise to nearly 12 percent after the crisis, in 2018–2019 the profit of non-financial corporations fell to 9 percent, corresponding to the level of banks, which may have been attributable to the strong wage growth and significant investment expenditures (Chart 23).

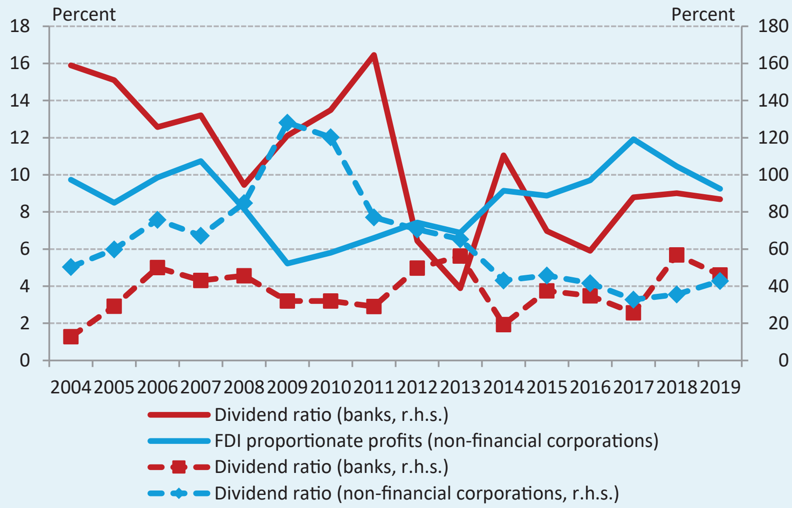
Non-financial corporations' dividend payout ratio continues to fluctuate around the historically low level of previous years, whereas banks' dividend disbursement dropped considerably last year, following a surge in 2018. Banks' dividend payout ratio was below that of companies in the previous years, but in 2018 a reversal took place: companies invested

6 Since reinvested earnings, related to the normal business operations, are the difference between the profit earned and the dividends paid, the applied COPC adjustment and the treatment of superdividends have a major impact on the value of reinvested earnings (for more details, see the July 2017 Report on the Balance of Payments).

7 From an analytical standpoint there is a trend change in the time series: since 2008 the profit (and thus the reinvested earnings as a residual) only contains the profit/loss according to the current operating performance concept (COPC). However, it can be presumed that the profit items not related to the current operating performance and stemming from a major shift in exchange rates increased after the crisis, and thus the time series presumably remains comparable to the previous period as well. It may represent an additional break that since 2013 superdividends have been eliminated from the foreign profit and have been recognised as capital withdrawal rather than as dividend payment, which thus influences the distribution of corporate profit between dividend payment and reinvestment.

most of their profits in Hungary, while banks disbursed significant dividends to their owners. The underlying reason for banks' higher dividend payout ratio may be that there was no longer any need for capital injections to make up for the losses suffered during the crisis, and thus a larger portion of the profit could be disbursed as dividend. In 2019, banks' dividend payments declined again, practically approaching the degree of non-financial corporations' dividend payout ratio. Following a gradual decline since the crisis, the latter increased gradually in the past years. rising to 43 percent by last year. This means that the reinvestment ratio was high in both sectors in 2019, which may have been attributable to the favourable growth prospects and an expected further rise in incomes: in order to reach higher profits in the future, foreign owners invested the larger part of their earned income in Hungary.

Chart 23: Profit of foreign-owned companies and banks as a percentage of FDI equity, and as a percentage of dividends disbursed

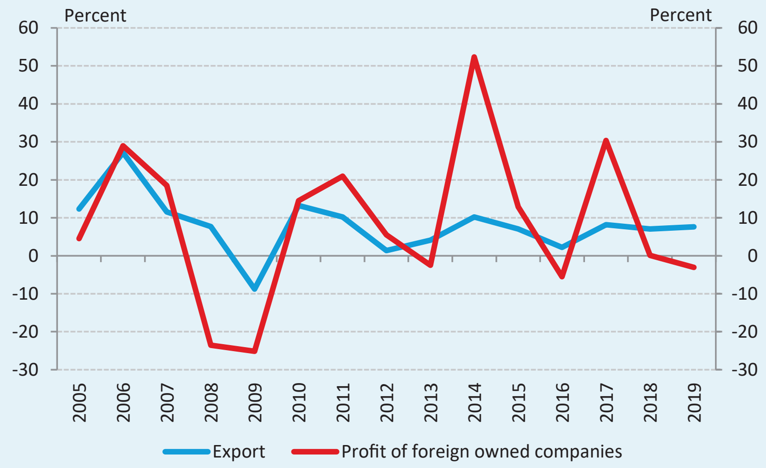


Note: FDI proportional to income is a value calculated from the year-end stock.

5.4 Factors underlying developments in corporate profits

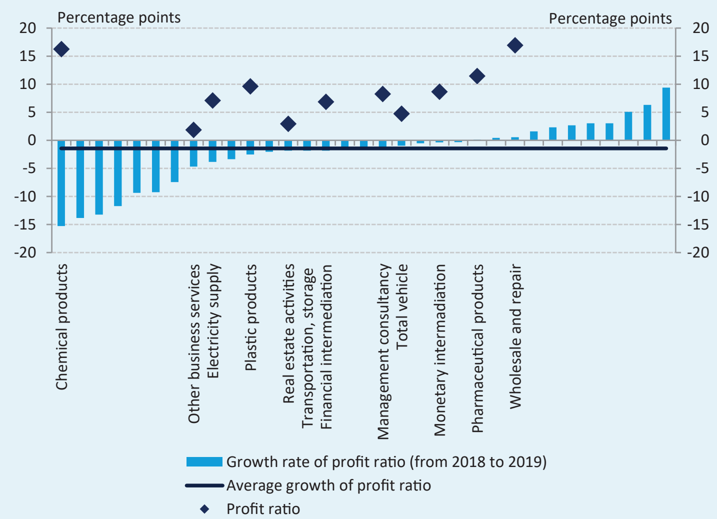
The decline in corporate profits occurred despite a slight increase in export dynamics in 2019. As many of the foreign-owned companies are active in the export-oriented sector, and based on past experiences as well, it is justified to compare foreign-owned companies' profit to the export performance. While the co-movement had previously been very close, after 2013 export dynamics tended to indicate only the direction of changes in corporate profitability; the separation was mainly attributable to one-off factors (Chart 24). This correlation weakened further in 2019: export dynamics accelerated slightly, while corporate profits declined compared to the previous year's level. The cyclicality observed in recent years may also have contributed to the decline in corporate income: an outstanding year is typically followed by a fall in profitability. On the whole, as of 2013, great differences between the growth rates of the two indicators were mainly observed in the years when profitability was especially high, whereas the difference usually narrowed in the years of profit declines. By contrast, a slight opening between the two indicators was seen in 2019 compared to the difference in 2018.

Chart 24: Profit of foreign-owned companies (in HUF) and developments in exports (change compared to the previous year)



In 2019, return on equity declined in the main sectors, of which the production of chemical substances, other business services and the manufacturing of electronic products are worth highlighting. Following the previous year's average 1-percentage point decline, foreign-owned companies' profit rate as a proportion of FDI equity fell by 1.5 percentage points on average between 2018 and 2019. Although roughly half of the sectors were loss-making and half of them profitable (Chart 25), corporate profits dropped in most sectors with high invested foreign capital exceeding EUR 2 billion (indeed, there was one major sector as well where the fall exceeded 15 percentage points). Of the major sectors, the profitability of trade and pharmaceutical production increased, whereas the largest decline in profits was suffered by the other services sector. At the same time, the production of chemical substances as well as the financial and insurance sectors also lost some of their profitability, and the decrease in the profitability of other business support services was also significant compared to 2017. Accordingly, on the whole, the average profit rate of foreign-owned companies operating in Hungary declined to below 10 percent in 2019, which is below the levels typical in the previous two years. As in the previous two years as well, the profit rate of vehicle manufacturing, where foreign investment is the highest, fell in 2019. As a result, it became one of the lowest among the sectors where FDI is high.

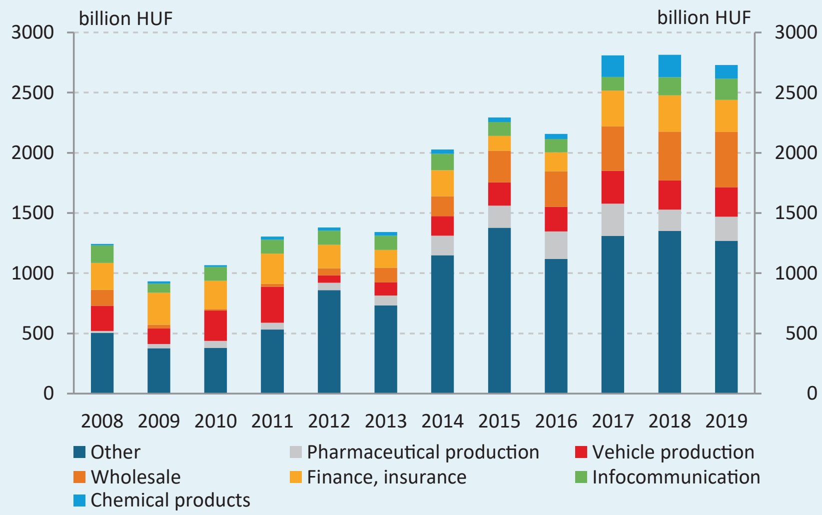
Chart 25: Growth in the profit of foreign-owned corporations as a proportion of FDI in selected sectors in 2019



Note: The sectors with FDI stock over EUR 2 billion were specified by name.

Foreign-owned companies' profit on FDI is relatively concentrated: six sectors account for more than half of the profit. Corporate profits increased in a wide range of sectors in 2017, with outstanding profitability in the six largest sectors. By contrast, in 2018 it was the income of sectors with lower invested capital that grew to a greater degree, whereas the share of the largest sectors within the total profit declined slightly as a result of deterioration in the profitability of pharmaceutical production. In 2019, the improving profitability of the information and communication sector, trade and pharmaceutical production added to the aggregate profitability of the sectors that have the highest weight in terms of income, whereas the profitability of other sectors declined compared to the previous year. Nevertheless, of the smaller sectors, construction tripled its profit, while agriculture and the utilities companies also improved their profitability. On the whole, the income of large sectors continues to account for more than half of the total profit of foreign-owned companies operating in Hungary, which means a relatively high concentration.

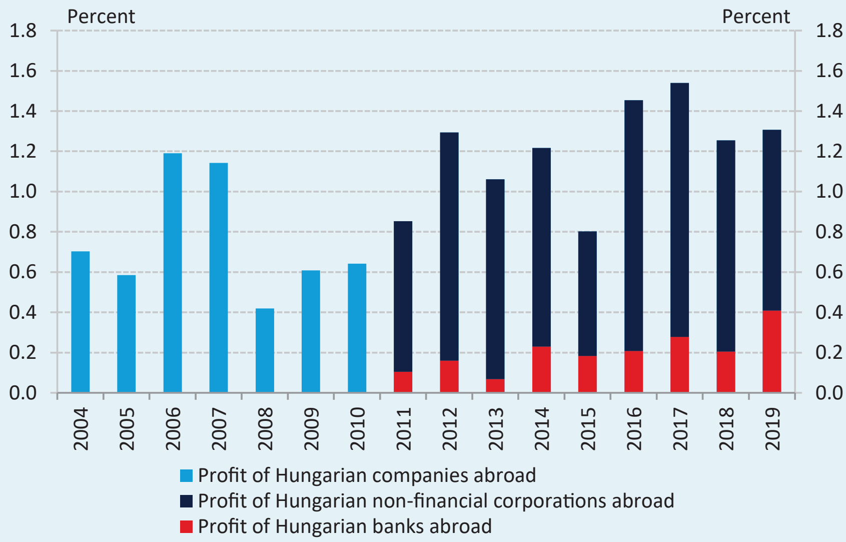
Chart 26: Profits of foreign-owned companies



In parallel with a decline in the income of foreign-owned companies operating in Hungary, the profit of resident companies' foreign affiliates rose in 2019, also contributing to the decrease in the deficit. In addition to the income of foreign companies operating in Hungary, the profits of companies operating abroad and owned by residents also have to be taken into account in the income account of the balance of payments.[8] Starting from a relatively high level in 2017, as a proportion of GDP these profits declined considerably, dropping by nearly 0.4 percent of GDP in 2018, before increasing slightly again in 2019. This was a result of the fact that banks' profits doubled compared to previous years' average, while the profit of non-financial corporations declined by 0.15 percent of GDP. The modest rise in income last year was the result of these two contrasting effects.

8 Based on analytical considerations, in the income account we present the primary incomes, except for other primary incomes, which in the former methodology formed part of unrequited transfers, and thus we state them in the transfer balance.

Chart 27: Profits of companies operating abroad and owned by residents (as a percentage of GDP)



5.5 After-tax profit of foreign-owned companies

In 2019, companies' after-tax profit was again similar to the income according to the 'current operating performance concept' shown in the balance of payments, i.e. the difference between the two indicators typical of the previous years – and attributable to one-off items – remained moderate. In 2019, both indicators declined slightly from the previous year's level and were around 5 percent of GDP (Chart 28). In line with international regulations, the statistics show only foreign-owned companies' profit/loss according to the current operating performance concept. This means that one-off effects, which are typically related to revaluation, are excluded,[9] and thus the profit/loss – according to the current operating performance concept – in the balance of payments is much more stable. Since the crisis, items outside of current operating performance have typically reduced corporate profits, and thus the exclusion of these items resulted in higher income (and thus in higher reinvested earnings) and a larger deficit of the income account in the balance of payments statistics. The outliers in 2015 and 2016 of a multinational company operating in Hungary had a strong impact on the changes in after-tax profit/loss, while the income according to the balance of payments excluding one-off effects was stable. The difference between the two indicators narrowed considerably in 2017, and then, in 2018, there was no one-off, high-amount non-recurring item that could have affected the income significantly, and thus the after-tax profit/loss and the profit/loss according to the current operating performance concept shown in the balance of payments reached similar levels. In 2019, the levels as a proportion of GDP of both the profit/loss according to the balance of payments (related to current operating performance) and the after-tax profit/loss declined. Just like in 2018, the difference between the two indicators remained insignificant, indicating that in 2019 there was no one-off, high-amount item that might have diverted after-tax profit/loss from the value according to the current operating performance concept.

9 Such one-off impacts at corporations are the losses from exchange rate revaluation and at credit institutions the early repayment at preferential exchange rate or the settlements related to household loans.

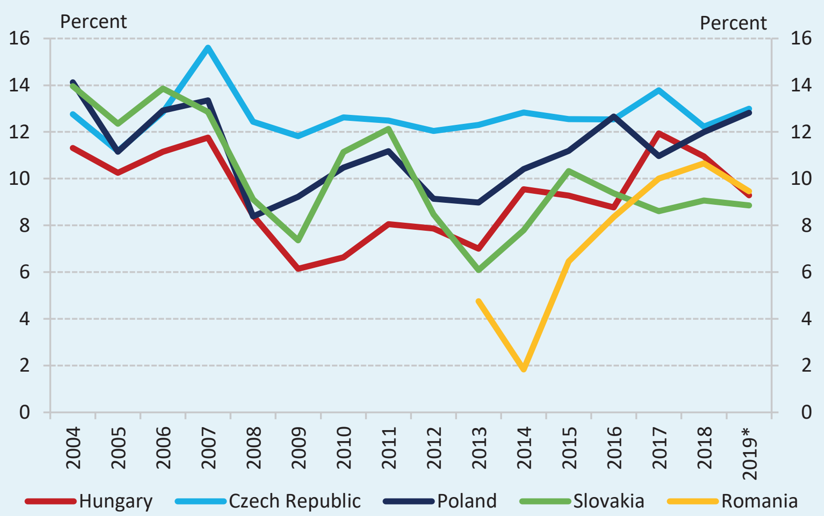
Chart 28: Profits from current operating performance and based on the profit/loss after tax* (as a percentage of GDP)

** The profit realised by foreign-owned corporations has a negative impact on the income account, in line with the income account of the balance of payments.*

5.6 International comparison

In 2019, foreign-owned corporations' profitability declined to around the levels seen in Slovakia and Romania, while the Czech and Polish indicators rose to much higher levels. Presumably due to the significant impact of international developments, the profitability indicators previously showed significant co-movements across the countries of the region. Following the crisis, the ratio of foreign-owned corporations' income to FDI equity holdings declined in several countries of the region, but since 2013 the return on FDI increased in all the countries of the region. Preliminary data suggest that the rate of return expanded in the Czech Republic and Poland as well in 2019, whereas the indicator fell slightly in Romania and Slovakia. As a result of the decline in the profit rate of foreign-owned companies in Hungary seen in the past two years, the indicator decreased to around 9 percent, similar to the figures for Slovakia and Romania.

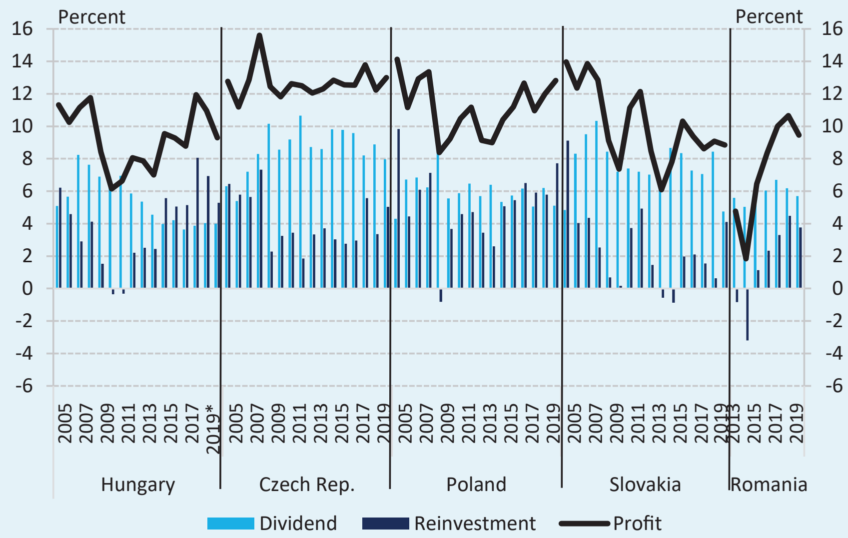
Chart 29: Return on FDI equity investment (value of the profit realised on the FDI stock relative to total FDI stock)



*Source: Eurostat * The 2019 value for the countries of the region is presumably an estimate only.*

Foreign-owned corporations reinvest more than half of their profits not only in Hungary, but already in Poland as well (Chart 30). While an increase in profits previously typically entailed an expansion in dividend disbursements in the countries of the region, dividend disbursement as a proportion of equity declined in Hungary over the past period of more than ten years.[10] According to preliminary data, similar to the trends seen in Hungary, the increase in profitability in Poland in 2019 entailed a rise in reinvested earnings instead of an increase in dividend disbursements. As a result, more than half of the income produced is reinvested by the foreign-owned companies operating in Hungary and now also by the ones operating in Poland. Based on available data, the increase in profits was reflected in a rise in reinvestments in the Czech Republic as well. The decline in profits affected both reinvestments and dividend disbursements to similar degrees in Romania. Although foreign-owned corporations' domestic reinvestments decreased, their level is still considered high in a regional comparison.[11]

Chart 30: Breakdown of FDI earnings in the countries of the region (as a percentage of FDI equity)



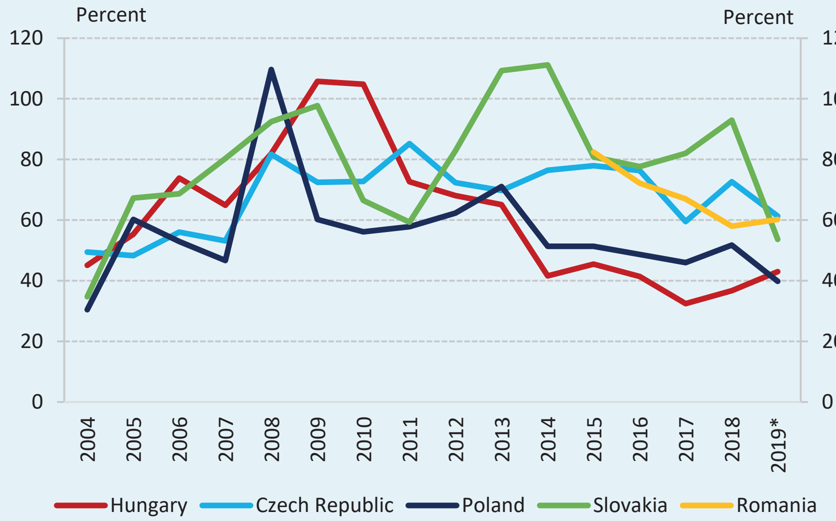
*Source: Eurostat * The 2019 value for the countries of the region is presumably still based on estimation.*

Dividend disbursement as a proportion of income in Hungary remains among the lowest in the region, which is reflected in the high value of reinvestments. At the same time, the ratio of disbursed dividends to profits typically declined in the countries of the region in 2019 (Chart 31). Prior to the crisis and in some years following that, foreign-owned companies' dividend disbursement as a proportion of income increased, reaching its highest value in 2009–2010. As a result of the increased liquidity demand of foreign parent companies due to the crisis and of the decline in the growth prospects of the countries of the region, corporations in several countries also paid dividends to their foreign owners from the retained earnings accumulated from previous years' profits. The dividend payout ratio declined in all the countries from the middle of the decade, dropping to the greatest degree in Hungary, where foreign-owned corporations disbursed a mere 35 percent of their earned income as dividends in 2018. In 2019, some change took place in the previous trends: while the foreign-owned companies operating in Hungary spent more (43 percent of their income) on dividend disbursement than in the previous years, the ratio of dividend disbursement fell considerably in several countries. In this respect, the greatest change took place in the case of companies operating in Slovakia, where the previous year's high dividend payout ratio of 93 percent declined to 54 percent, while the Polish indicator was around the Hungarian level. Overall, reinvestment by foreign-owned corporations is still high in Hungary compared to the region.

10 However, from 2013 the accounting of superdividends in Hungary may have played a role in this.

11 The treatment of superdividends may also increase reinvested earnings as a percentage of profit, because by reducing the profit it raises the role of the reinvested earnings as a percentage of income, while it reduces that of dividends. Hence, this may also contribute to the higher reinvestment, as a percentage of profits, by foreign-owned companies operating in Hungary. With regard to other countries of the region, no information is available whether they take into account the recommendations of the IMF concerning the application of superdividends.

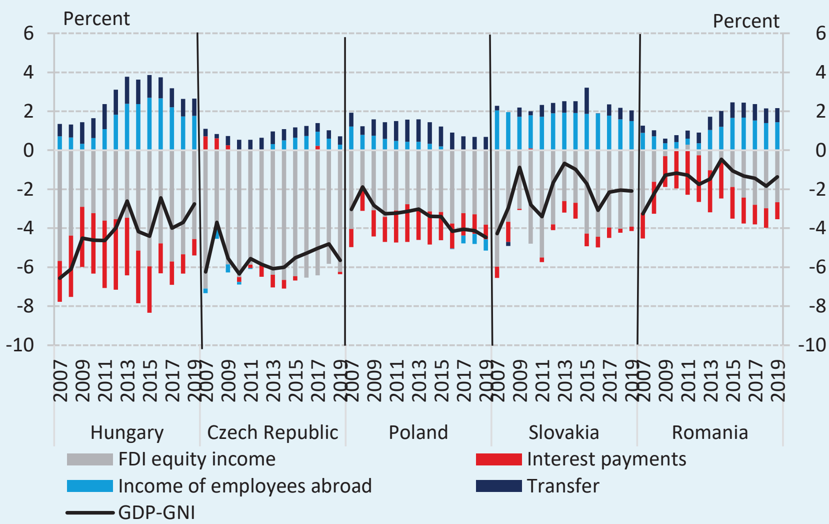
Chart 31: Ratio of dividend payments to profit



*Source: Eurostat * The 2019 value for the countries of the region is still partly based on estimation.*

The GDP–GNI gap declined significantly in Hungary in 2019, remaining near the regional average (Chart 32). The difference between gross domestic product (GDP) and gross national income (GNI), i.e. the GDP–GNI gap, is the result of summing up the income payments vis-à-vis the rest of the world. The factors of the indicator are: interest payments related to the rest of the world, net profit of foreign-owned companies, income of people employed abroad and foreign transfers (recognised among primary incomes). In view of the significant FDI in the countries of the region, the value of income is below the value of the gross domestic product. At the same time, the net income of people employed abroad and EU transfers typically reduce the difference between GDP and GNI in the countries of the region. Following the crisis, as a result of companies' improving profitability, profit outflows related to equity increased considerably in the countries of the region, which was partly offset by the rise in the income of those employed abroad and transfer inflows. In addition, the steady decline in interest expenditures also contributed significantly to the narrowing of the GDP–GNI gap. As a result of the decline in foreign-owned corporations' profits, the difference between GDP and GNI decreased in Hungary in 2019. In the Czech Republic and Poland, in parallel with a rise in foreign-owned companies' profits, the declining income of those employed abroad also resulted in the widening of the GDP–GNI gap.

Chart 32: Decomposition of the difference between GNI and GDP (as a percentage of GDP)



*Source: Eurostat * The 2019 value for the countries of the region is presumably still based on estimation.*

List of charts

Gábor Bethlen

(15 November 1580 – 15 November 1629)

Prince of Transylvania (1613–1629), elected King of Hungary as Gábor I (1620–1621), one of the most prominent personalities of 17th century Hungary. At the beginning of his career he loyally served the Princes of Transylvania Zsigmond Báthory, Mózes Székely, István Bocskai and Gábor Báthory. When Gábor Báthory contemplated alliance with the Hapsburgs, he turned against him and got himself elected to the throne of the principality. During his reign, he consolidated the position of Transylvania setting both the economy and the cultural life of this part of Hungary on a path of development later generally referred to as the 'golden age of Transylvania'.

The twenty-five years preceding the rule of Bethlen were heavy with external and internal wars leaving the population considerably thinned out. Bethlen set out to stabilise the domestic situation, to consolidate his power and to rebuild Transylvania with great patience. He established a centralised state apparatus and concurrently sought to strengthen the financial status of the principality. He ordered an accurate statement of treasury revenues, had the lands and properties granted since 1588 reviewed and ratified only those which had been awarded in recognition for service to the country.

To promote industry and trade, Bethlen encouraged an economic policy of mercantilism and settled foreign craftsmen in the country. Instead of taxation, he relied on the more rational utilisation of other means deriving from his status as prince in building his rule. He developed precious metals mining, invited renowned specialists from abroad and strove to boost trade. Gábor Bethlen minted coins of a stable value and regulated the multidirectional trade in goods by prohibiting exports of key merchandise.

Gábor Bethlen attempted to form an international anti-Hapsburg coalition among western and eastern European countries. In order to strengthen his ties with the Protestant Powers, on 1 March 1626 he wed the sister of George William Elector of Brandenburg, Catherine of Brandenburg, and in 1626 he joined the Westminster alliance of the Protestant Powers.

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