REPORT ON THE BALANCE OF PAYMENTS

2024
APRIL

'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

REPORT ON THE BALANCE OF PAYMENTS

2024

APRIL

Published by the Magyar Nemzeti Bank

Publisher in charge: Eszter Hergár

H-1013 Budapest, Krisztina körút 55.

www.mnb.hu

ISSN 2064-8707 (print)

ISSN 2064-8758 (on-line)

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: Judith Balázs, Ignác Forgó Balázs, Annamária Hegedűs, Péter Koroknai, Rita Lénárt-Odorán, Zsuzsa Nagy-Kékesi, Balázs Sisak, Daniella Tóth, Noémi Végh. The Report was approved for publication by Barnabás Virág, Deputy Governor.

The Report is based on information pertaining to the period ending 27 March 2024.

Summary

In conjunction with falling energy prices and weak domestic demand, the external balance indicators of the Hungarian economy improved significantly in 2023, as also observed in the region overall. Hungary's current account balance as a share of GDP rose by a record 8 percentage points last year. As a result of this increase, which was robust even by EU standards, the current account showed an annual surplus of 0.2 per cent of GDP, while the net lending of the economy jumped to 1.2 per cent of GDP.

The improvement in the external balance is mainly linked to the trade balance, and within this, in part, to improving terms of trade due to lower energy prices, and to lower imports, which reflect the decline in household consumption and corporate investment. In addition, a modest increase in the surplus in services also contributed to the surplus in external trade, which reached a level not seen in the past five years. Meanwhile, primarily as a result of rising interest expenses in the higher interest rate environment, the income deficit rose moderately, while the improvement in the external balance was also curbed somewhat by a shrinking transfer balance due to the subdued inflows of EU funds. Overall, however, by the end of 2023 the exceptionally high net borrowing observed in the previous year had turned into a significant net lending position.

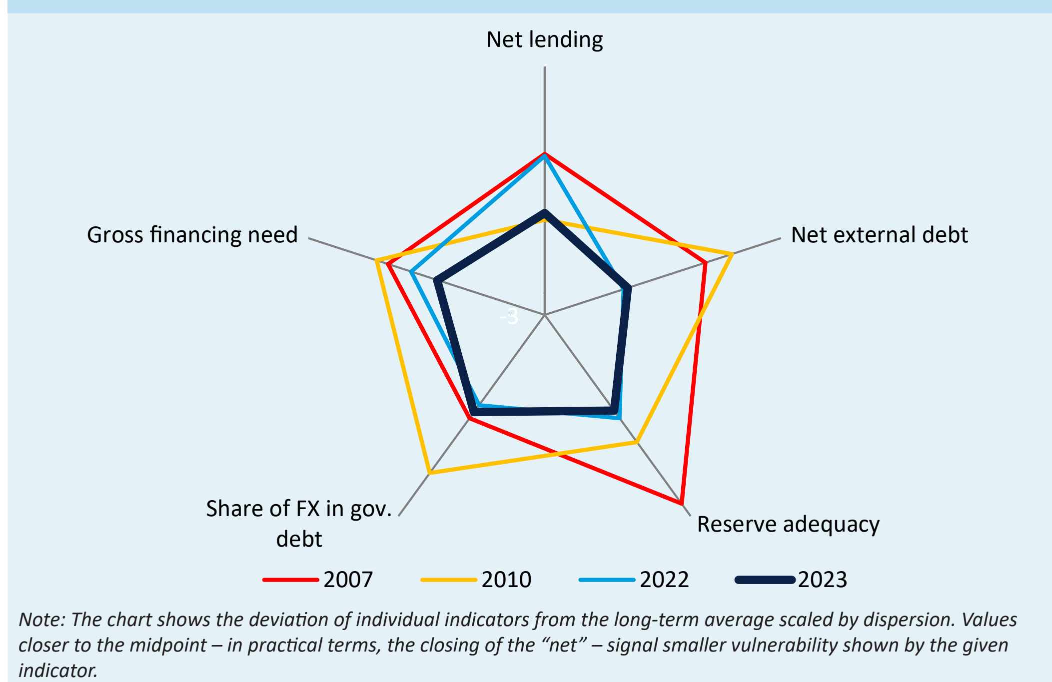
The improving external balance was also reflected in a decline in the economy's external financing. Falling energy prices and restrained domestic demand entailed a decline in the current account deficit and thus a fall in external borrowing, while – partly due to an increase in investment abroad and the domestic acquisition of a foreign-owned company – net FDI inflows were lower than in the previous year, but remained significant nonetheless. Banks and the general government were the primary contributors to the modest level of new debt liabilities and hence the moderate increase in the net external debt ratio; in respect of the general government, this was mainly due to the increase in non-residents' holdings of government securities, the central bank's discount bills held by non-residents and the foreign exchange reserve-reducing effect of the MNB's swap instruments. At the same time, the central bank instruments provided to banks did not represent a net inflow of funds at the level of the national economy, as they curbed the increase in banks' net external debt.

Key debt indicators relevant to the country's external vulnerability also developed favourably in 2023. Due to the contraction in net borrowing, net external debt only rose moderately in 2023, remaining below 12 per cent, i.e. close to its historic trough. The debt ratio was boosted by inflows of debt liabilities and the revaluation of stocks, which was partly offset by a substantial increase in nominal GDP. Short-term external debt – a key factor in the country's external vulnerability – fell by the end of 2023, while international reserves rose to a historic high, with these reserves substantially exceeding the level expected by investors in December 2023 (by EUR 7.7 billion).

The four-quarter decline in the economy's net borrowing in 2023 is linked to the rising net financial savings of the private sector. Households' net lending increased significantly by the end of 2023, while the lower capital expenditure reduced the borrowing requirement of the corporate sector. The budget deficit increased somewhat during 2023, primarily due to high inflation, low VAT receipts and a surge in interest expenses. At the same time, the public debt-to-GDP ratio decreased moderately, mainly reflecting nominal GDP growth. Due to foreign currency bond issues, the foreign currency debt ratio and non-residents' share in government debt rose moderately by the end of 2023.

As a result, relative to 2022, Hungary's external position has improved substantially in terms of almost all of the external vulnerability indicators (Chart 1). With the current account balance turning into surplus, the critically high – gross and net – external borrowing observed in 2022 fell sharply and thus poses a low risk, similar to that associated with the low external debt ratios, which are now consistent with those in the region, the constantly improving foreign exchange reserve adequacy and the relatively low foreign currency debt ratio.

Chart 1: Stylised depiction of Hungary's external balance position



Note: The chart shows the deviation of individual indicators from the long-term average scaled by dispersion. Values closer to the midpoint – in practical terms, the closing of the "net" – signal smaller vulnerability shown by the given indicator.

In the special topic in this report, developments in Hungary's external balance indicators are compared to those observed in the other countries in the region. After the significant deficit seen in 2022, the external balance of most regional countries improved strongly in 2023. On the side of the real economy, the improvement in the external position is primarily due to a decline in gross capital formation, i.e. the fall in investment and inventory investment which, in some countries, was also supported by an increase in savings. The substantial correction in the trade balance of the countries in the region mainly resulted from improved terms of trade amid falling energy prices and from weakening domestic demand. This was offset by the decline in the transfer balance observed in several countries and the rise in the income deficit, which was driven by interest expenses rising in parallel with the profit balance. In 2023, the net borrowing of countries in the region declined overall, while net FDI inflows remained significant. The domestic budget deficit remains above the levels typical in the Visegrád countries.

Contents

1 Real economy approach 7

1.1 External trade balance 7

1.2 Income balance 11

1.3 Transfer balance 12

2 Financing approach and debt ratios 14

2.1 Net external debt 15

2.2 Non-debt liabilities 16

2.3 Debt liabilities 17

2.4 Net external debt 19

2.5 Gross borrowing need 20

2.6 Reserve adequacy 21

3 Savings approach 23

3.1 General government 23

3.2 Households 26

3.3 Corporate sector 28

4 Comparison by region 30

4.1 A snapshot of Europe 30

4.2 Gross savings and investment 31

4.3 Net lending and its real economic factors 31

4.4 Trade balance 32

4.5 Income balance and transfer balance 33

4.6 Financing side developments 35

4.7 Financial savings by sector 35

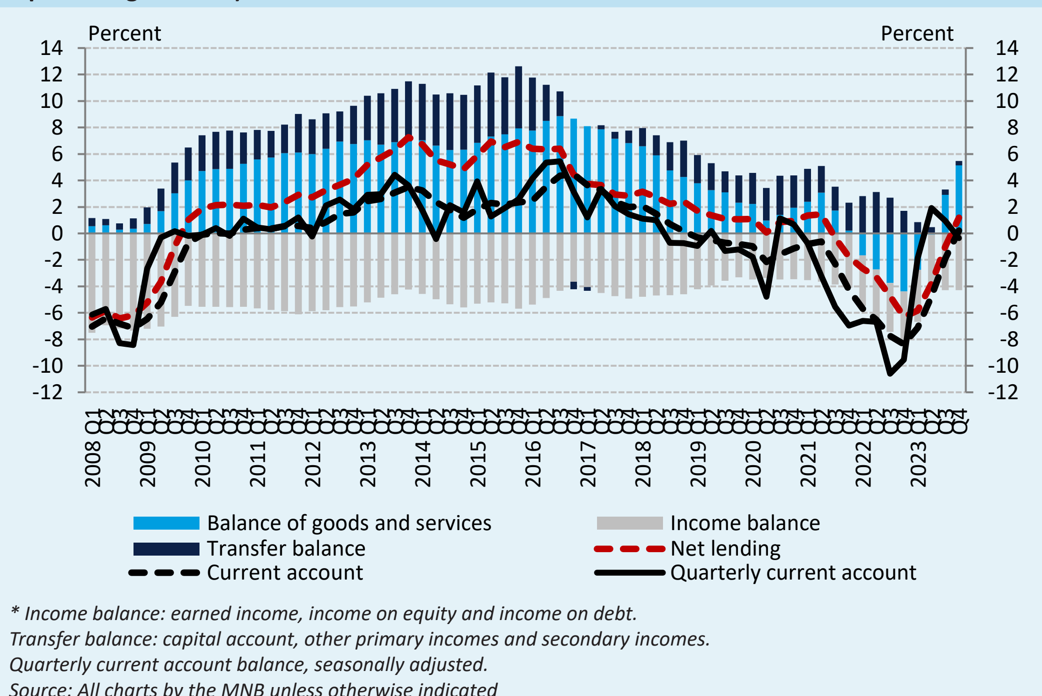
4.8 External debt indicators 36

1 Real economy approach

The key external balance indicators of the Hungarian economy improved at a record pace during the year. The increase in the current account balance was mainly linked to rising external trade, more specifically to an improvement in the terms of trade in conjunction with falling energy prices, but the decline in imports in the context of waning consumption and investment also fostered an improvement in the goods balance, while the beneficial effect of export growth gradually faded in a difficult international environment. Relative to the level at the end of the previous year, the surplus on the balance of services, which plays an important role in the foreign trade balance, rose somewhat as a proportion of GDP. This was partly offset by the widening income deficit amid rising interest expenses as a result of high inflation and the shrinking surplus on the transfer balance owing to the subdued inflow of EU funds. The exceptionally high net borrowing observed in the previous year had turned into a significant net lending position by the end of 2023.

In the real economy approach, following the significant imbalance observed in 2022, the external balance indicators of the economy improved at a record pace in 2023, with a surplus of 0.2 per cent of GDP on the current account registered for 2023 as a whole, while net lending reached 1.2 per cent of GDP (Chart 2). Seasonally unadjusted data show that net borrowing amounted to EUR 95 million in the fourth quarter, which was the net result of a current account deficit of EUR 561 million and a capital account surplus of EUR 466 million. Four-quarter data show that the improvement in the current account balance over the course of the year was driven by an increase in the trade balance. The steady, significant rise in the goods balance can be mainly attributed to the decline in energy prices and the contraction in domestic demand, partly offset by a gradual deterioration in the income and transfer balances, with the former coming to a halt in the last quarter. By the end of 2023, the income balance undermined the external position by 4.3 per cent of GDP, while the transfer balance improved it by 0.3 per cent of GDP. Overall, these developments led to a steady increase in the current account balance as a share of GDP during the year, with a moderate surplus at the end of the year.

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



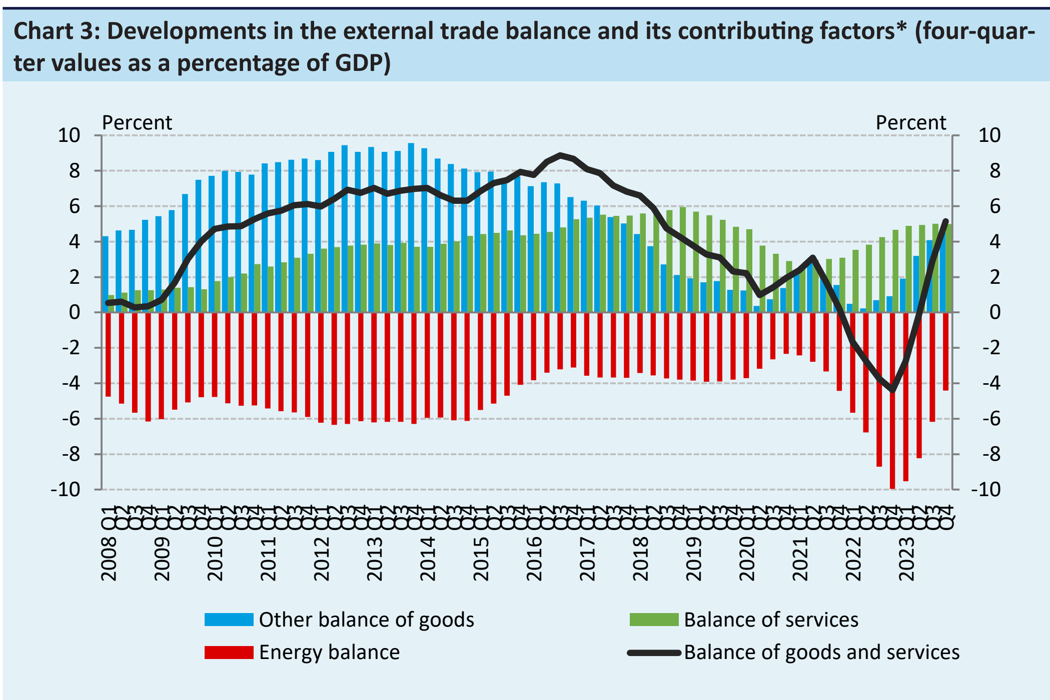
** Income balance: earned income, income on equity and income on debt.*
Transfer balance: capital account, other primary incomes and secondary incomes.
Quarterly current account balance, seasonally adjusted.
Source: All charts by the MNB unless otherwise indicated

1.1 External trade balance

The four-quarter trade surplus reached 5.1 per cent of GDP at the end of 2023, on the back of a continued and significant year-on-year improvement in the balance of goods and a stable services surplus (Chart 3). The balance of goods rose very rapidly during 2023, turning into a moderate surplus by the end of the year. This improvement was primarily linked

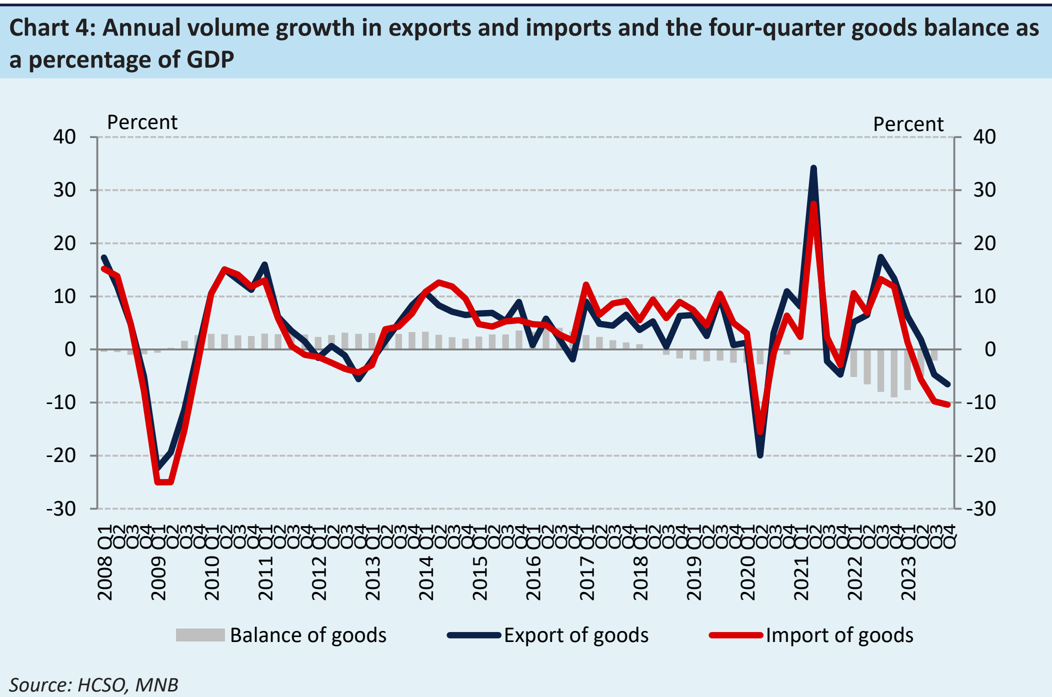
to the correction in the energy balance following the energy price shock in 2022, and secondly to a decline in other imports due to shrinking consumption and investment. Export growth also supported the goods balance in the first half of the year, but this effect faded in the second half of the year in the context of weak global economic activity. Together with the slower decline in domestic demand, this caused the rise that started in 2022 in the other balance of goods to decelerate by the end of 2023. The steady improvement in the services balance after the COVID-19 pandemic stabilised after the beginning of 2023; therefore, the four-quarter surplus at the end of 2023 amounted to around 5 per cent, a typical level for the year as a whole. The improvement in the balance of services until the beginning of 2023 was driven by dynamic growth in tourism and a recovery in the balance of transportation services. Tourism remained the most important sector in the services balance, and its role even increased somewhat in 2023.

Chart 3: Developments in the external trade balance and its contributing factors* (four-quarter values as a percentage of GDP)



The dynamics of goods exports moderated gradually during the year and turned into a decline in the second half of the year. Import growth was lower than export growth, which enabled the goods balance to improve steadily throughout the year (Chart 4). By the end of 2023, the annual real growth rate of exports fell from a level of above 10 per cent in 2022 H2 – associated with the post-pandemic recovery – to minus 6.6 per cent, reflecting the subdued demand shown by Hungary's main trading partners. As household consumption and investment slowed, the annual decline in imports accelerated over the year, and this development was also supported by the dampening effect of lower exports on imports in the latter half of the year. By the end of the year, the four-quarter decline in imports exceeded 10 per cent.

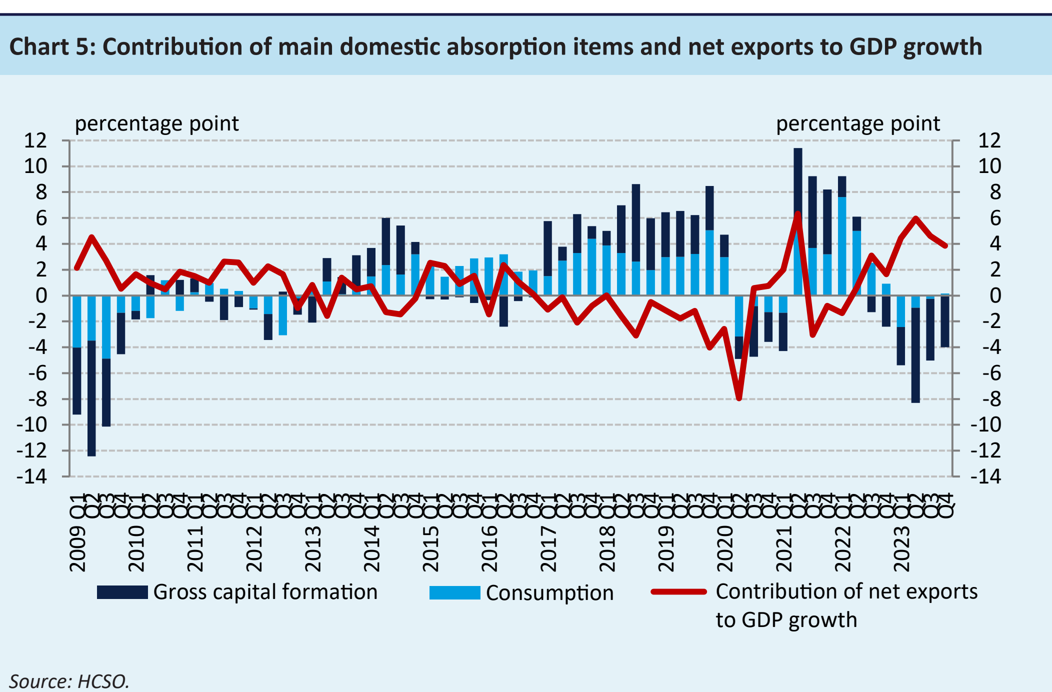
Chart 4: Annual volume growth in exports and imports and the four-quarter goods balance as a percentage of GDP



Source: HCSO, MNB

Although it declined in the fourth quarter, the positive growth contribution of net exports remained significant for the year as a whole. In the high inflation environment, the contraction in domestic demand which started in 2022 continued in 2023 as well, but the growth contribution of consumption turned moderately positive by the last quarter of the year, as real household income stabilised. By contrast, the growth contribution of gross capital formation (including investment and inventory investment) remained significantly negative, although it rose relative to previous quarters. Coupled with the weak performance of exports, this suggests that to a large extent the positive growth contribution of net exports is driven by the decline in gross capital formation.

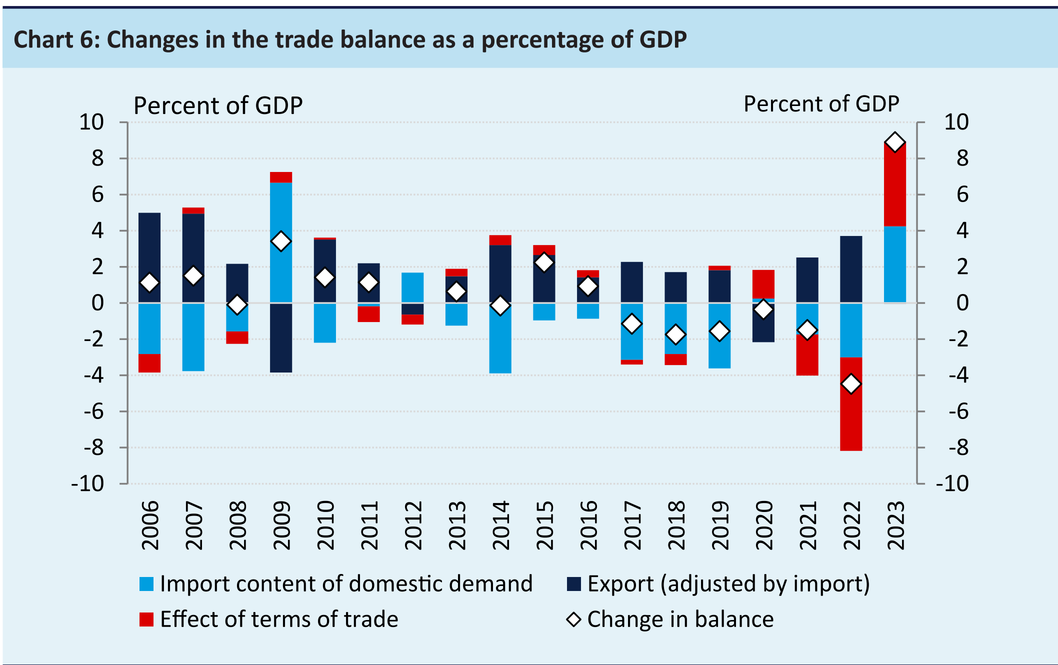
Chart 5: Contribution of main domestic absorption items and net exports to GDP growth



Source: HCSO.

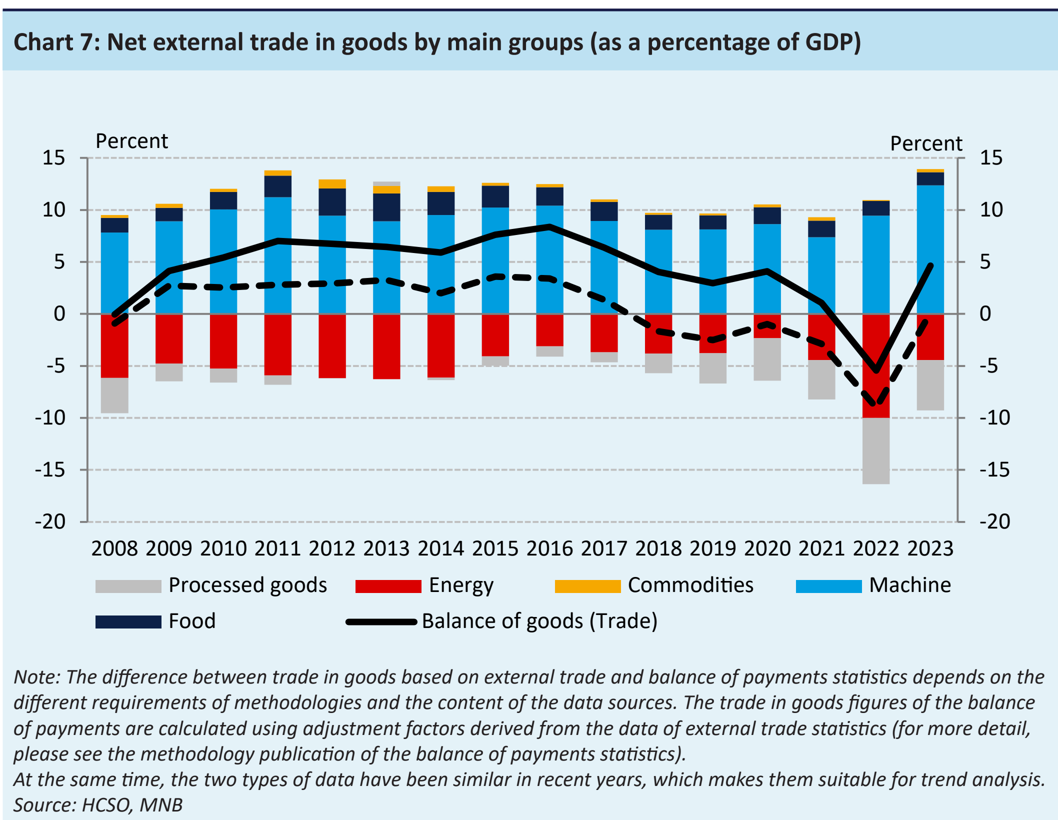
The foreign trade balance rose to a record high last year, reflecting an improvement in the terms of trade and moderation in domestic demand (Chart 6). The improvement in the terms of trade was mainly due to the correction in energy prices following the peak in 2022 owing to the war in Ukraine. In parallel with lower domestic demand in 2023, the ensuing fall in imports also boosted the trade balance. At the same time, the impact of exports net of imports was neutral for the year as a whole.

Chart 6: Changes in the trade balance as a percentage of GDP



In 2023, the rise of more than 9 percentage points in the goods balance as a share of GDP stemmed primarily from the decline in net energy imports, while the contribution of processed goods and machinery also developed favourably (Chart 7). Net energy imports fell by 5.6 per cent of GDP in 2023, consistent with the decline in natural gas and electricity prices and lower domestic energy consumption. The upswing in machinery exports that began in 2022 H2 continued in 2023 H1, as global semiconductor shortages and production chain disruptions eased. However, along with the historically still high energy prices in the region, weak external demand in conjunction with the war in Ukraine and tighter international monetary conditions brought this process into a halt towards the end of the year. Accordingly, the 2.9-percentage point contribution of machinery and equipment to the improvement in the ratio of the goods balance to GDP also partially reflects the fall in domestic demand. The impact of lower domestic demand was also strongly reflected in the 1.5-percentage point fall in net imports of processed goods.

Chart 7: Net external trade in goods by main groups (as a percentage of GDP)

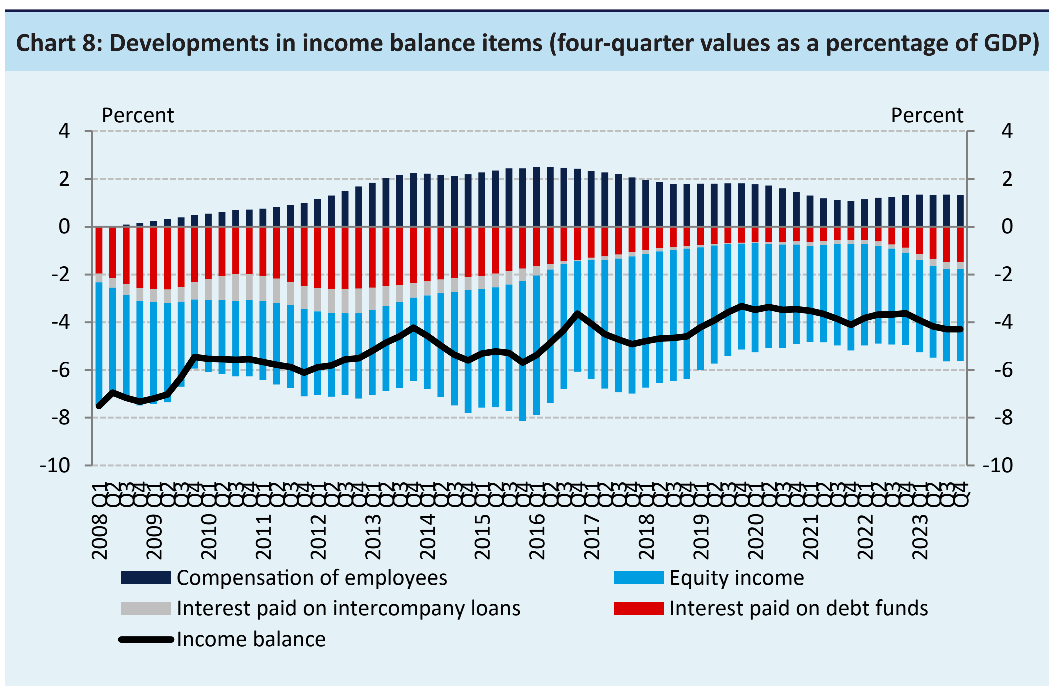


Note: The difference between trade in goods based on external trade and balance of payments statistics depends on the different requirements of methodologies and the content of the data sources. The trade in goods figures of the balance of payments are calculated using adjustment factors derived from the data of external trade statistics (for more detail, please see the methodology publication of the balance of payments statistics).
At the same time, the two types of data have been similar in recent years, which makes them suitable for trend analysis.
Source: HCSO, MNB

1.2 Income balance

Driven by higher net interest expenses, the deficit of the income balance increased in 2023, reaching 4.3 per cent of GDP by the end of the year (Chart 8). A large part of the income balance is composed of the profits of foreign-owned enterprises,1 the value of which did not change much during the year, standing at around 3.8 per cent of GDP, while the boosting effect of the high inflation environment on profitability was offset by subdued demand and rising extra-profit taxes. The change in the income balance was mainly driven by net interest on external lending and borrowing. Consistent with increases in domestic and international yields and the rise in external debt, net interest paid rose by 0.6 percentage point to 1.5 per cent, in parallel with an increase in net interest expenses on inter-company loans during the year. The earnings of employees working temporarily abroad remained at the low level of the post-pandemic period and, as in the past period, improved the indicator only moderately. As a result of these factors, compared to the level recorded in 2022, the deficit on the income balance increased by around 0.7 per cent of GDP by the end of 2023.

Chart 8: Developments in income balance items (four-quarter values as a percentage of GDP)

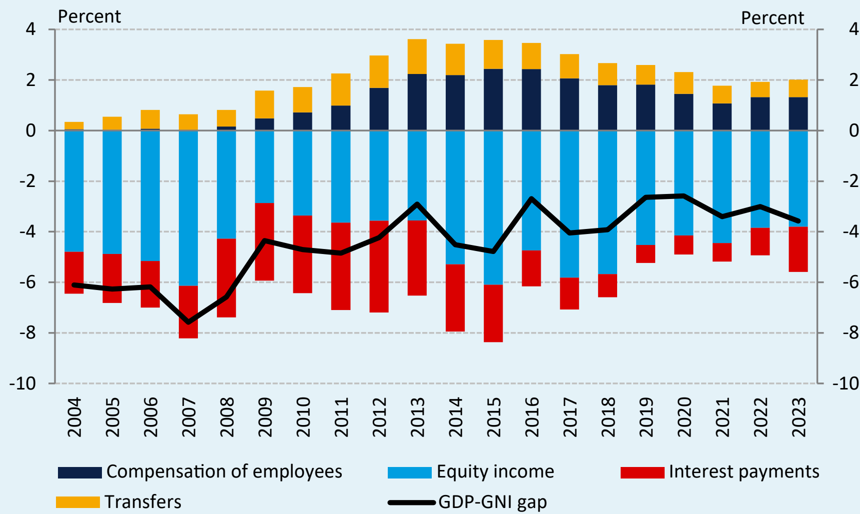


Box 1: The gap between GDP and GNI

In 2023, the gap between GDP and GNI increased: the disposable income of domestic sectors was below the income generated in Hungary by about 3.6 per cent of GDP (Chart 9). The difference between Gross Domestic Product (GDP) and Gross National Income (GNI) shows the balance of income flows vis-à-vis the rest of the world, which allows analysts to estimate the actual disposable income of domestic agents (excluding secondary income). The significant improvement in the indicator in 2008–2009 was mainly linked to a decline in the profitability of foreign-owned enterprises, which reduced the gap from over 6 per cent of GDP to 4 per cent of GDP, after which it fluctuated around 3–4 per cent, with minor swings. As a result of the COVID-19 pandemic, the decline in the compensation of the employees balance (with a drop in the income of Hungarian workers abroad) caused an increase in the gap between GDP and GNI. Despite the increase in extra-profit taxes and slack demand, foreign companies maintained their profitability in a high inflation environment in 2023 at the previous year's level. At the same time, the high domestic and international yield spreads and the rise in external debt led to a significant increase in the interest expenses of economic sectors. Overall, as the net result of the above effects, the GDP–GNI gap rose by 0.6 percentage point in 2023.

[1] Since quarterly data on the 2023 profitability of foreign-owned enterprises operating in Hungary are limited, information on quarterly profit outflows is based on estimates until the receipt of corporate questionnaires at the end of the summer. For more detail, see the publication "Methodological notes to the Balance of Payments and Investment Position Statistics".

Chart 9: Evolution of the GDP–GNI gap in Hungary (as a share of GDP)

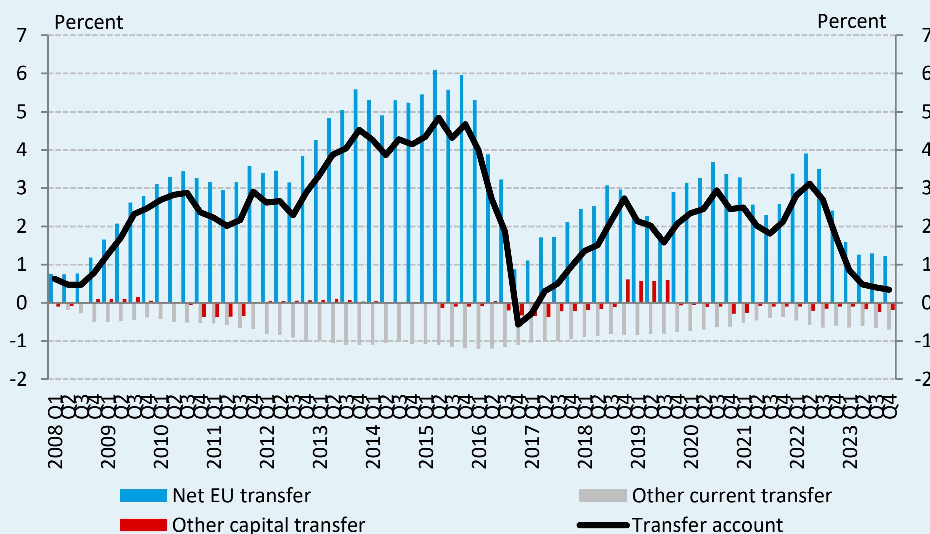


Note: As official GNI data (published by the HCSO) are not currently available for 2023, the balance of payments data release is based on primary income (for now, the profits of foreign-owned companies, excluding SPE companies, are estimates).

1.3 Transfer balance

The surplus on the transfer balance dropped to 0.3 per cent of GDP by the end of 2023, mainly due to lower net EU transfers (Chart 10). The use of net EU transfers has averaged around 2.0–3.5 per cent of GDP in recent years, but in 2023 the four-quarter net EU transfer balance fell to 1.3 per cent of GDP by the end of the first half and remained at around this level until the end of the year. This was due to the expiry of the 2014–2020 EU budget cycle and the delay in accessing the new seven-year cycle and the Recovery and Resilience Facility (RRF), which was set up to help with the recovery from the COVID-19 crisis. Meanwhile, the four-quarter balance of other current transfers and other capital transfers also deteriorated somewhat compared to the previous year.

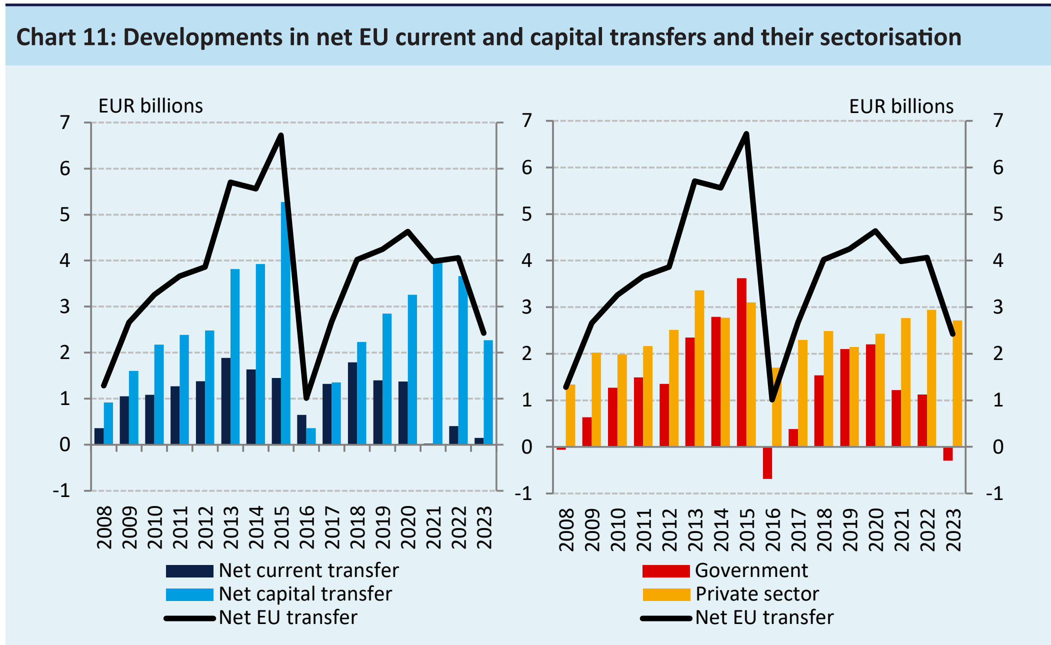
Chart 10: Developments in the transfer balance (four-quarter values as a percentage of GDP)



Net absorption of EU funds amounted to EUR 2.4 billion in 2023, just over half the level from previous years. In 2023, the general government became a net contributor, while the private sector's use of EU funds remained significant (Chart 11). Due to the EU budget cycle and the relevant rules, the use of EU transfers reached its trough in 2016 and

peaked in 2020. In 2023, both current and capital transfer inflows moderated compared to 2022, due to the new budget cycle and delays in accessing the RRF funds. At the sectoral level, in 2023 the fall in net absorption was concentrated within the general government, where it turned negative by the end of the year, meaning that the government's payments to the EU exceeded the funds received from it in 2023. At the same time, private sector absorption was only lower relative to the high levels of the previous two years, and at EUR 2.7 billion it still remained significant.

Chart 11: Developments in net EU current and capital transfers and their sectorisation

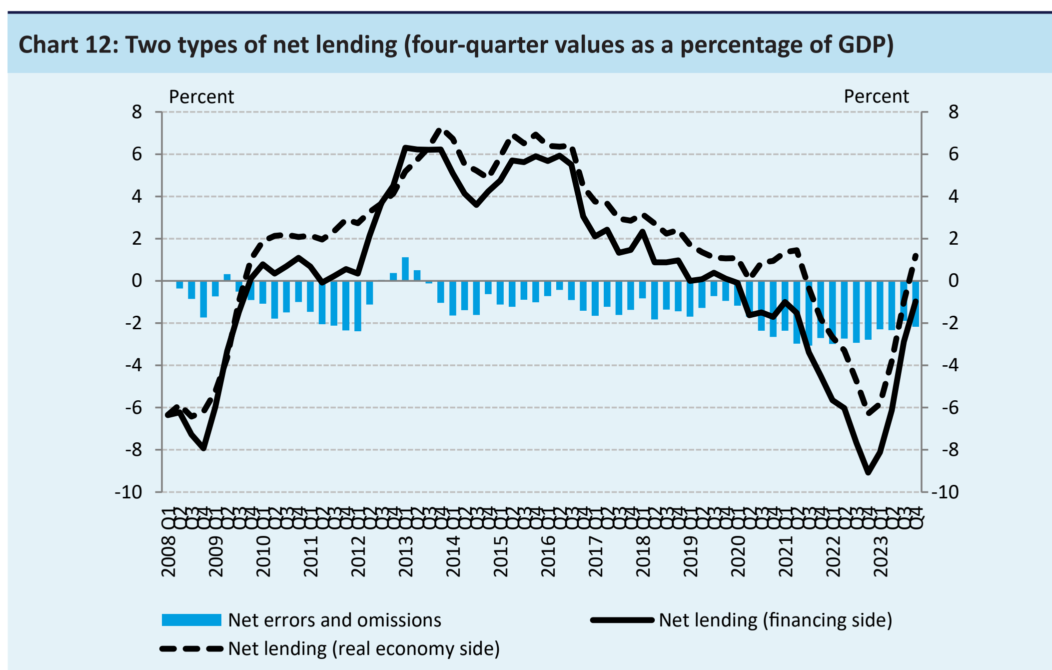


2 Financing approach and debt ratios

In 2023, net borrowing calculated on the basis of financing items dropped to around 1 per cent of GDP. As the current account deficit narrowed in parallel with the adjustment in energy prices, this was also reflected in lower external borrowing, while net FDI inflows declined compared to 2022, partly due to an increase in investment abroad and the domestic acquisition of a foreign company. On an annual basis, net external debt continued to rise moderately, driven by the general government and the banking sector. The increase in government debt was linked to higher non-resident holdings of government securities, the issuance of central bank discount bills and the reserve-reducing effect of the MNB's swap instruments. At the same time, the central bank instruments provided to banks did not represent a net inflow of funds at the level of the national economy, as they curbed the increase in banks' net external debt. With the decline in external net borrowing, the key debt indicators relevant to the Hungary's external vulnerability also showed a generally positive picture in 2023. Net external debt rose somewhat, amounting to almost 12 per cent of GDP. In addition to the debt-increasing effect of transactions, revaluation effects (yield declines which increased the market value of debt and exchange rate changes which reduced net foreign currency receivables) boosted the indicator somewhat, which was partly offset by a substantial increase in nominal GDP. The net external debt ratio of the private sector turned negative again, i.e. the sector's foreign assets exceeded its foreign liabilities at the end of 2023. Foreign exchange reserves stood at EUR 41.4 billion at the end of 2023, EUR 7.7 billion above the level of short-term external debt, a figure monitored closely by investors.

The economy's four-quarter net borrowing amounted to around 1 per cent of GDP in 2023 Q4, according to the financing approach. While the net position showed **net borrowing** based on financing data, the figure for the side of the real economy turned into a net lending position in excess of 1 per cent of GDP (Chart 12). Accordingly, the balance of errors and omissions, i.e. the difference between the real economic and financing balance indicators, was around 2 per cent of GDP, i.e. near the average from previous years.[2]

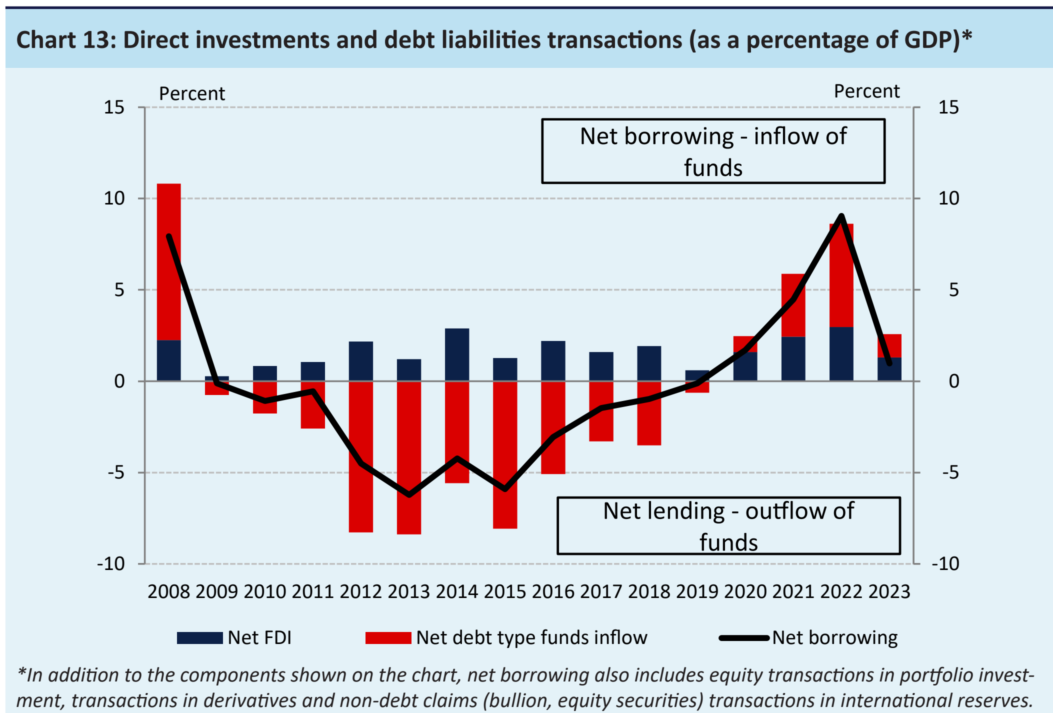
Chart 12: Two types of net lending (four-quarter values as a percentage of GDP)



In 2023, inflows of debt liabilities fell to nearly 1 per cent of GDP, while net FDI inflows also declined according to transactions (Chart 13). The economy's net external debt rose by around 1.3 per cent of GDP in 2023, driven by a simultaneous increase in foreign debt-generating liabilities of almost EUR 12 billion and external assets of EUR 9 billion. Foreign direct investment was mainly linked to reinvested earnings. The decline in net FDI inflows can be attributed primarily to domestic acquisitions of foreign-owned companies, while the investments of residents abroad continued.

[2] Trends in the balance of payments can also be analysed by examining the financing of real economy transactions. Indeed, the financial account shows what types of transactions were used by resident economic agents to finance transactions in the real economy that had an effect on net financial worth. The data in the real economy and financing approaches should in theory be consistent, but non-integrated data sources, incomplete monitoring and different treatment of exchange rates can lead to discrepancies, as shown in the "Balance of errors and omissions".

Chart 13: Direct investments and debt liabilities transactions (as a percentage of GDP)*

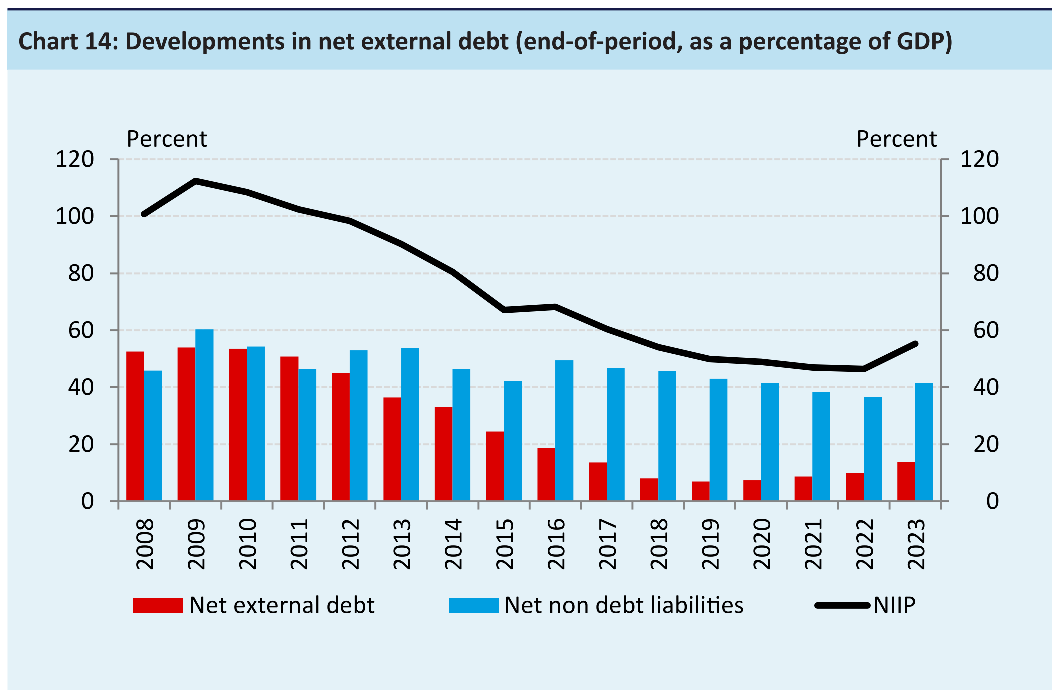


**In addition to the components shown on the chart, net borrowing also includes equity transactions in portfolio investment, transactions in derivatives and non-debt claims (bullion, equity securities) transactions in international reserves.*

2.1 Net external debt

In 2023, Hungary's net external debt as a share of GDP continued to increase as a result of rising non-debt liabilities and debt inflows (Chart 14). After slowing in 2022, the gradual decline in net external debt observed since the 2008 crisis, which includes external debt and non-debt liabilities (including indirect investment, portfolio holdings and derivative liabilities), turned into an increase in 2023, with the indicator rising to 55 per cent of GDP by the end of the year. Non-debt liabilities and the rise in external debt also contributed to the annual increase of almost 9 percentage points. The increase in net external debt as a percentage of GDP occurred in the sector of the general government, while the private sector as a whole recorded a decline. The indicator for the corporate sector dropped to a larger extent, while the banking sector indicator rose substantially. Accordingly, net external debt amounted to almost 12 per cent of GDP in 2023. The increase in non-debt liabilities was mainly linked to net FDI inflows. Net FDI inflows as a percentage of GDP rose during the year as the impact of continued net FDI inflows was not offset by GDP growth in 2023.

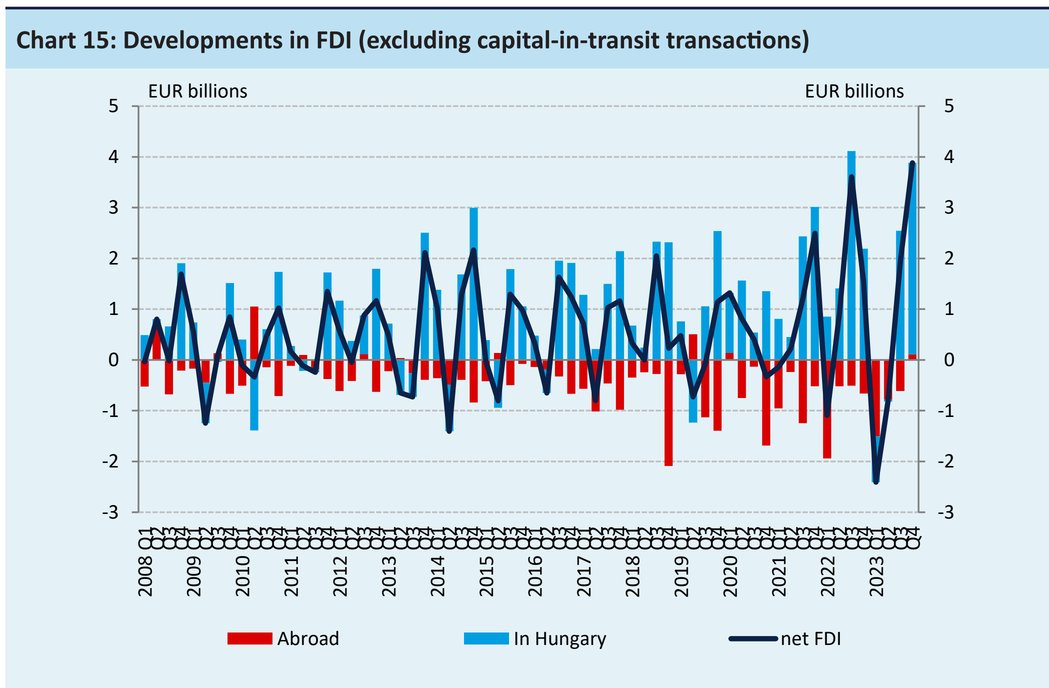
Chart 14: Developments in net external debt (end-of-period, as a percentage of GDP)



2.2 Non-debt liabilities

FDI inflows in Hungary were around EUR 5.6 billion in 2023, while net FDI inflows amounted to EUR 2.6 billion (Chart 15). Foreign direct investment in Hungary totalled around EUR 5.6 billion last year, showing a significant decrease versus 2022. Outward foreign investment by Hungarian participants increased by a total of EUR 3 billion during the year, bringing the total net FDI inflow to EUR 2.6 billion in 2023. In the first half of the year, net FDI outflows amounted to more than EUR 3 billion, partly related to a Hungarian financial institution's acquisition of a stake in a bank in a regional country and a bank in a Central Asian country, and partly to the domestic acquisition of a foreign-owned telecom company. Ordinary dividend payments approved at the beginning of the year reduced FDI shares (via the fall in reinvested earnings); nevertheless, most of these have not been paid yet, which in turn drove intercompany loans higher. Significant equity investment continued in the electronics industry in 2023, including battery and electric motors manufacturing and pharmaceuticals. FDI inflows, which had slowed in the first half of the year, accelerated in the second half, resulting in an unprecedented EUR 4 billion quarterly net FDI inflow in the fourth quarter. The trend observed after the financial crisis continued in 2023, with ownership shares and inter-company loans often contrasting in terms of the structure of direct investment (this is one of the reasons why the MNB considers inter-company loans as ownership shares and does not take them into account in external debt). As a net result, overall net FDI investment declined overall, relative to 2022.

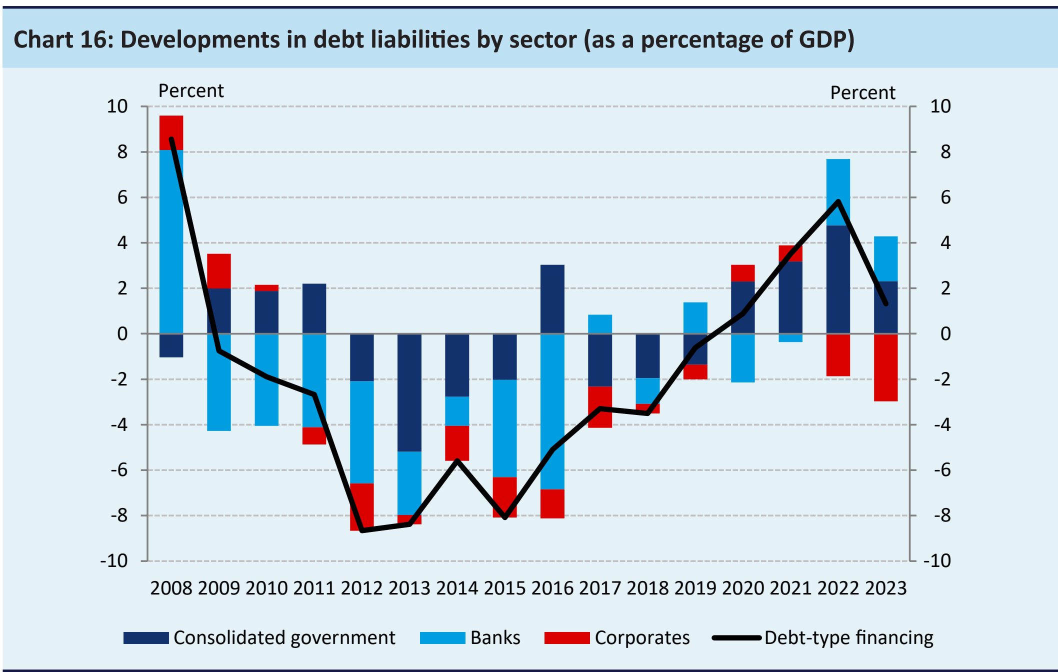
Chart 15: Developments in FDI (excluding capital-in-transit transactions)



2.3 Debt liabilities

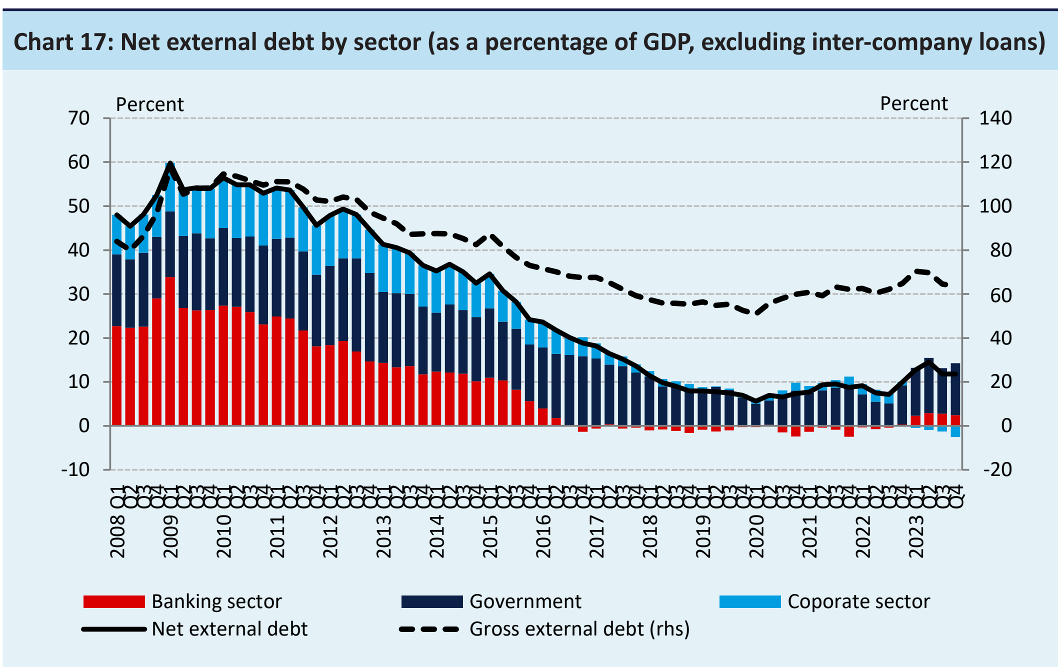
In 2023 as a whole, the net external debt of the economy increased by around 1.3 per cent of GDP due to transactions, with the general government and banking sectors contributing, while the corporate sector indicator declined (Chart 16). In 2023, in line with the consolidating net borrowing, the economy's external debt inflows were substantially lower than in the previous year: as a result of transactions, the net external debt of the consolidated general government rose by EUR 4.6 billion and that of the banking sector by EUR 3.9 billion, while the corporate sector indicator dropped by around EUR 5.8 billion. The net external debt of the general government was boosted by the increase in the foreign holdings of HUF-denominated government bonds. The issuance of central bank discount bills – aimed at easing swap market tensions – in excess of the previous year-end value, also raised the level of the government's net external debt. These were partly offset by the absorption of EU transfers. The increase in non-residents' holdings of foreign currency debt securities due to the issuance of foreign currency bonds raised the level of both external liabilities and foreign exchange reserves, and thus did not affect net external liabilities. The MNB's swap instruments providing euro liquidity reduced the foreign exchange reserves, which had a neutral effect on net external debt at the macroeconomic level, but tended to increase the net external debt of the general government. The MNB's swap instruments provided the banking sector with foreign currency liquidity, while reducing foreign exchange reserves, and thus improved the net debt ratio of banks. For the banking sector, the increase in debt outpaced the growth in foreign assets, reflected in an increase in net external debt of almost EUR 4 billion. The net external debt of companies fell sharply, in line with the decline in the sector's borrowing requirement.

Chart 16: Developments in debt liabilities by sector (as a percentage of GDP)



The moderate increase in net external debt was linked to the banking sector in addition to the general government, while the corporate sector indicator declined (Chart 17). The year-on-year increase in net external debt as a percentage of GDP occurred against the backdrop of rising indicators for the banking sector and the general government, including the MNB. Banks' net external debt peaked in the middle of the year and started to decline in the second half of the year, mainly owing to transaction activity. After a temporary decline in the third quarter, the government's net external debt increased again in the last three months of the year, reaching close to 12 per cent of GDP at the end of December. In addition to the dynamics of debt inflows described above, the evolution of the stock-flow indicator of the general government was also affected by revaluation effects related to changes in the exchange rate and yields. In the first half of the year, both transaction and revaluation effects contributed to the increase in stocks. In the third quarter, in addition to net external debt repayments, revaluation effects also reduced the government's net external debt ratio. In the fourth quarter, as debt increased due to transactions, revaluation also added substantially to the government's net external debt through falling yields. The government's foreign currency bond issues, maturities and redemptions covered both gross debt and receivables, and were therefore neutral to the net external debt of the general government.

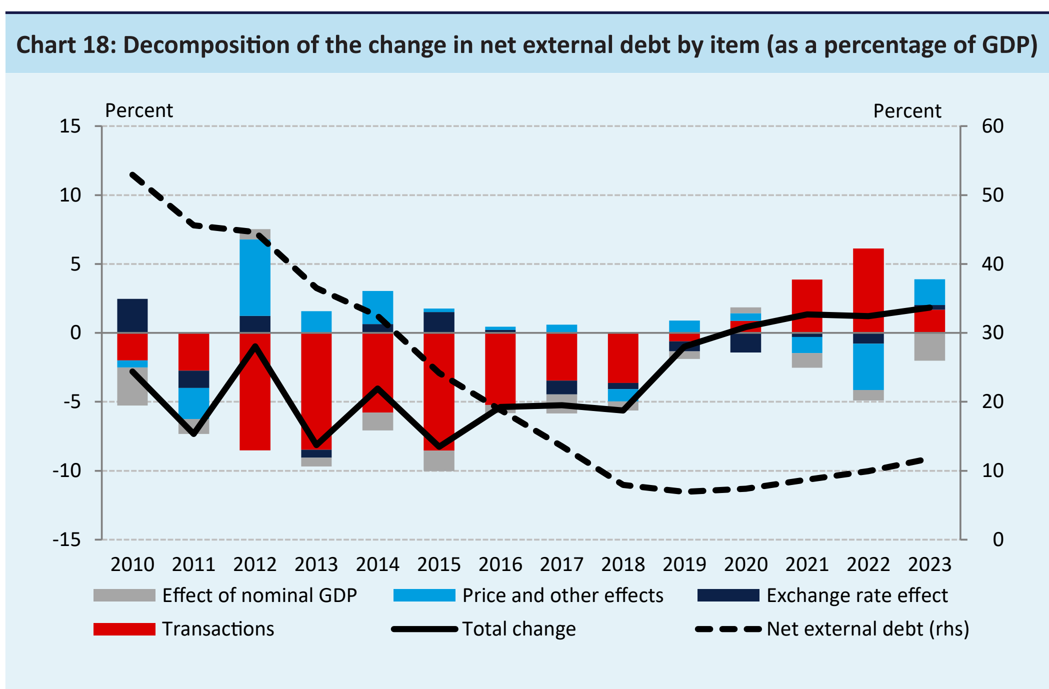
Chart 17: Net external debt by sector (as a percentage of GDP, excluding inter-company loans)



2.4 Net external debt

In conjunction with the contraction in net borrowing, net external debt rose only moderately during 2023 and remained below 12 per cent, i.e. close to its historic trough. The increase in the debt ratio was driven by the fact that the debt-increasing effect of debt-type inflows and stock revaluations was partly offset by a substantial expansion in nominal GDP (Chart 18). The net external debt accumulated in the years before the 2008 crisis fell by 46 percentage points in the 2010s, mainly due to an outflow of debt liabilities, with nominal GDP growth also contributing to the improvement, albeit to a lesser extent. Following a significant decline after the crisis, the debt ratio remained stable at a low level of around 7–8 per cent of GDP between 2018 and 2021, before rising in line with the economy's net borrowing in 2022 to reach 9.4 per cent of GDP at the end of 2022, which is somewhat above its historical low. However, with a significant improvement in the external position and the substantial growth in nominal GDP, Hungary's net external debt increased only moderately in 2023 to almost 12 per cent of GDP, broadly in line with the regional average. The debt inflows observed during the year and the revaluation effects (yield declines which increased the market value of debt and exchange rate changes which reduced net foreign currency receivables) boosted the indicator somewhat, which was partly offset by a substantial rise in nominal GDP.

Chart 18: Decomposition of the change in net external debt by item (as a percentage of GDP)



Box 2: Changes in external debt from different perspectives

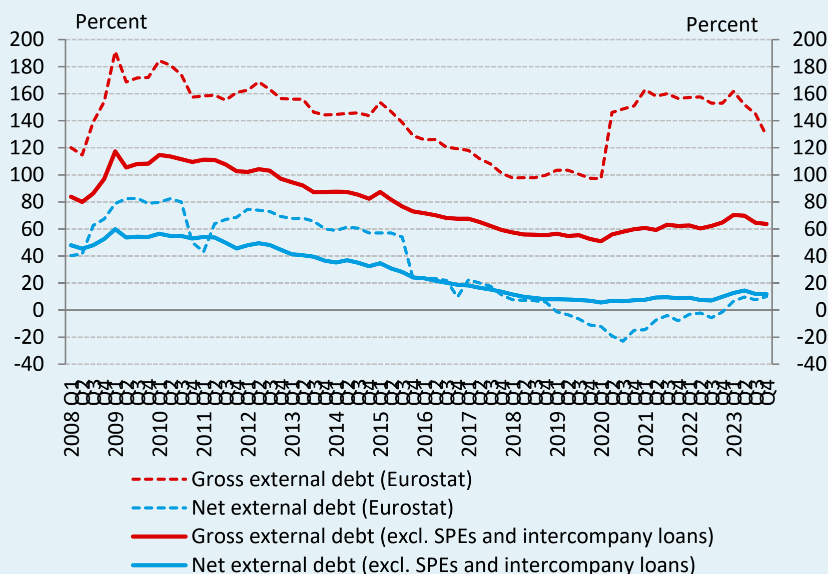
Net external debt remains at a consistently low level, regardless of the inclusion of SPEs and inter-company loans, but the gross external debt ratio including SPEs and inter-company loans is still substantially higher than the underlying debt ratio. For economic reasons, the MNB's analyses and publications analyse debt indicators without SPEs (special purpose entities) and inter-company loans, considering gold reserves as liabilities to non-residents,3 in order to present the underlying processes. However, the indicators calculated together with these factors are available only in the Eurostat database at the international level. SPEs have no real economic activity in the country and typically have fewer than five employees. Their activities generally have no impact on the country's net external debt; since they have external receivables of the same amount as their liabilities, they only have a significant impact on gross debt indicators. Based on their fundamentals, inter-company loans are generally considered non-debt liabilities (see the April 2014 Report on the Balance of Payments for more detail) rather than debt liabilities, and accordingly, balance of payments statistics recognise inter-company loans under FDI investments.

[3] From an economic perspective, fundamental developments in the dynamics of debt ratios are not affected by the switch between gold bullion and unallocated gold accounts, and thus this effect is excluded from the time series.

Including SPEs and inter-company loans, net external debt has increased in excess of the net external debt according to underlying trends in recent years. Net external debt calculated by Eurostat stood at 10 per cent at the end of 2023, bringing the two indicators close together again for the first time since 2018 (Chart 19).

However, the gross indicators show a significant difference in level between the two methodologies, with a sharp jump in gross external debt in 2020, which partially adjusted in 2023. This underpins that the indicator – which takes into account SPEs that do not pursue real economic activity in Hungary – and its changes reflecting individual factors, obscure real economic developments.

Chart 19: Developments in net and gross external debt (as a percentage of GDP)

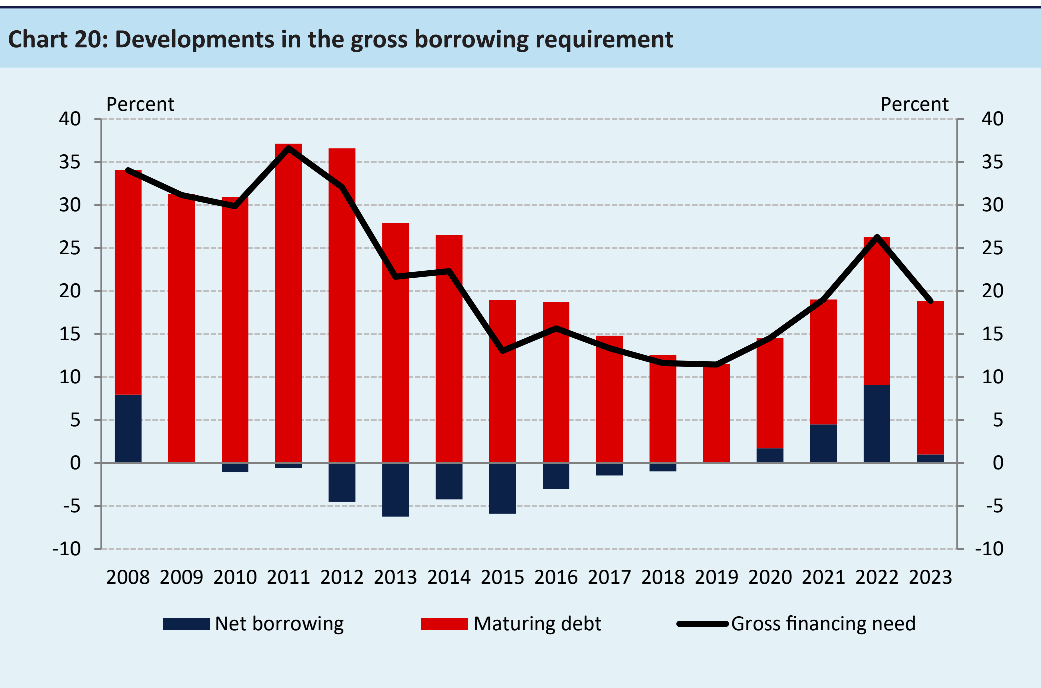


Source: Eurostat, MNB.

2.5 Gross borrowing need

In parallel with the improvement in the external balance, Hungary's gross external borrowing need dropped substantially in 2023 (Chart 20). After a gradual decline since 2011, gross borrowing need increased between 2020 and 2022 as the external position turned into net borrowing. Subsequently, it declined and dropped to 2021 levels in 2023 as the external position improved. The annual net borrowing of Hungary, calculated from the items of the financial account, amounted to 1 per cent of GDP. At the end of December 2022, short-term external debt – i.e. debt maturing in 2023 – was close to 18 per cent of GDP, reflecting a moderate increase from the previous year. Overall, the gross borrowing need of the Hungarian economy showing the Hungarian economy's external liabilities to be renewed in a given year – the sum of the two values – fell to 19 per cent of GDP.

Chart 20: Developments in the gross borrowing requirement



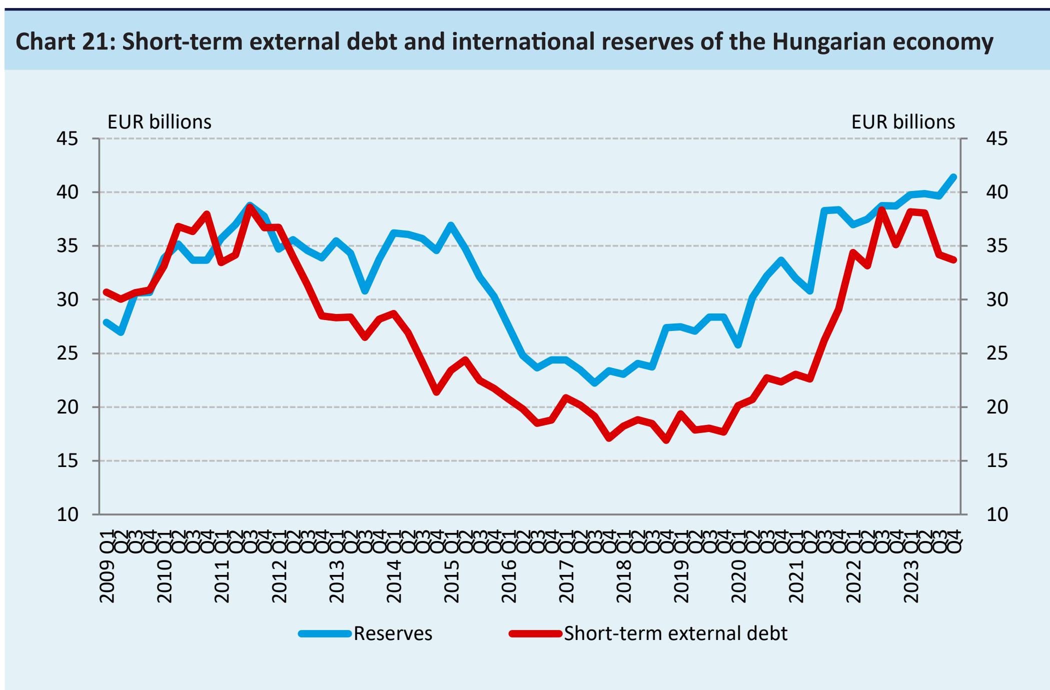
2.6 Reserve adequacy

International reserves stood at EUR 41.4 billion at the end of 2023, up significantly from EUR 39.7 billion at the end of September. Developments in the reserves were influenced by numerous factors, the most important of which were the following:

- The net reserve-increasing effect of EU *funds* amounted to EUR 2.2 billion, which, besides the RRF loan, was primarily related to the inflow of 2014–2020 cohesion funds.
- The *net FX financing operations of the Government Debt Management Agency (GDMA)* reduced the reserves by a total of EUR 0.3 billion. Based on the financing data of the GDMA, gross foreign currency borrowing in the final quarter of the year (excluding RRF loans, which are stated under EU funds) was not significant. In November, a private offering of a USD 500 million bond was announced. There was also a small amount of foreign currency borrowing. However, the amount of the borrowing was exceeded by the value of a maturing foreign currency bond and foreign currency interest payments.
- The reserve-reducing effect of the *Hungarian State Treasury's foreign currency transactions* amounted to EUR 1.1 billion.
- Due to changes in the exchange rate, the *revaluation* of reserve items denominated in currencies other than the euro increased the reserves by nearly EUR 0.1 billion.
- The *utilisation of the swap facility providing euro liquidity at the end of the quarter* and the balance of international *repo drawdowns* lowered the level of reserves compared to the end of September 2023.

At the end of 2023 Q4, the MNB's international reserves exceeded the level of short-term external debt, which is closely monitored by investors, by EUR 7.7 billion. At end-December 2023, international reserves and short-term external debt amounted to EUR 41.4 billion and EUR 33.7 billion, respectively; in other words, the steep rise in the level of the reserves was coupled with a decline in short-term debt. The leeway above the Guidotti-Greenspan indicator, which is closely followed by both the central bank and investors, amounted to EUR 5.5 billion at the end of September 2023, which significantly improved reserve adequacy (Chart 21).

Chart 21: Short-term external debt and international reserves of the Hungarian economy



In 2023 as a whole, the MNB's international reserves increased significantly, rising by EUR 2.7 billion. The reserve-increasing effect of EU transfers and the issuance of foreign currency bonds by the GDMA were partly offset by the Hungarian State Treasury's foreign exchange expenditures and the combined decline in the MNB's swap and repo holdings. At the end of 2023, foreign exchange reserves rose to EUR 41.4 billion from EUR 38.7 billion at the end of December 2022, mainly due to the following factors:

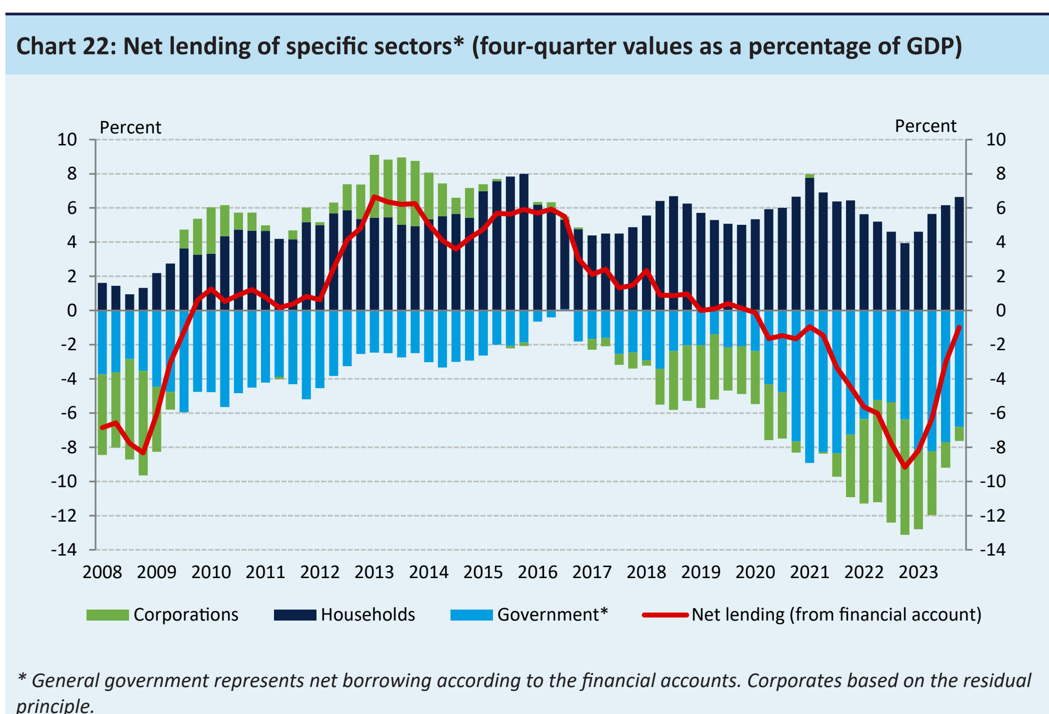
- *Receipts from the European Commission* and annual netted *payments* affecting the foreign exchange reserve exceeded EUR 4 billion.
- The increase in reserves was driven by the *net foreign currency financing* (including interest payments) *of the GDMA,* amounting to EUR 2.8 billion. The bulk of foreign currency funding was raised by the issuance of foreign currency bonds. Another contributor was the GDMA's launch of the Euro Commercial Paper Programme in July, under which it envisaged issuing a foreign currency instrument with a maturity of up to one year for the purposes of liquidity management, which was implemented during the year. To a smaller degree, funds were also raised by foreign currency borrowing.
- The above items were somewhat offset by the negative balances *of the Hungarian State Treasury's foreign currency expenses of* EUR 2.5 billion.
- The facility linked to the hedging of *net energy imports* reduced the level of reserves.
- The combined effect of *swaps providing euro liquidity* to the banking system and the *international repo drawdowns used to finance them* also had a reserve-reducing effect.

3 Savings approach

In 2023, the substantial contraction in the economy's four-quarter net borrowing was mainly driven by gradually rising net financial savings in the private sector. Households' net lending rose to a high level by the end of 2023 amid subdued consumer spending, while the net borrowing of the corporate sector declined as a result of a fall in consumption expenditure. Primarily owing to high inflation, low VAT receipts and a surge in interest expenses, the budget deficit increased somewhat over the course of 2023. Nevertheless, mainly reflecting nominal GDP growth, the public debt-to-GDP ratio declined slightly. As a result of foreign currency bond issues and non-residents' share in government debt, by the end of 2023 the foreign currency debt ratio increased moderately.

In 2023 Q4, the net borrowing of sectors under the savings approach continued to fall substantially, driven by the improving financing position of the private sector, while the general government deficit declined (Chart 22). The change in the financial savings of individual sectors is ultimately reflected in their external financing, and thus changes in the external balance can also be captured as the sum of the sectors' savings, which also corresponds to processes on the financing side. Based on preliminary data, the annual net borrowing of the consolidated general government increased up until the middle of the year and declined by the end of the year. The narrowing government deficit was mainly linked to gradually decreasing but still high energy and other expenditures, and falling tax revenues were also affected by shrinking domestic demand and falling investment in the high inflation environment. As the pace of price increases slowed, real wage dynamics gradually improved over the year, but households cut back substantially on consumption expenditure to offset the inflation loss, which resulted in an increase in households' net savings. At the same time, the net borrowing of the corporate sector declined steadily in 2023, mainly due to a fall in inventory investment, but also reflecting subdued investment activity and the stabilisation of operating profits at high levels.

Chart 22: Net lending of specific sectors* (four-quarter values as a percentage of GDP)



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

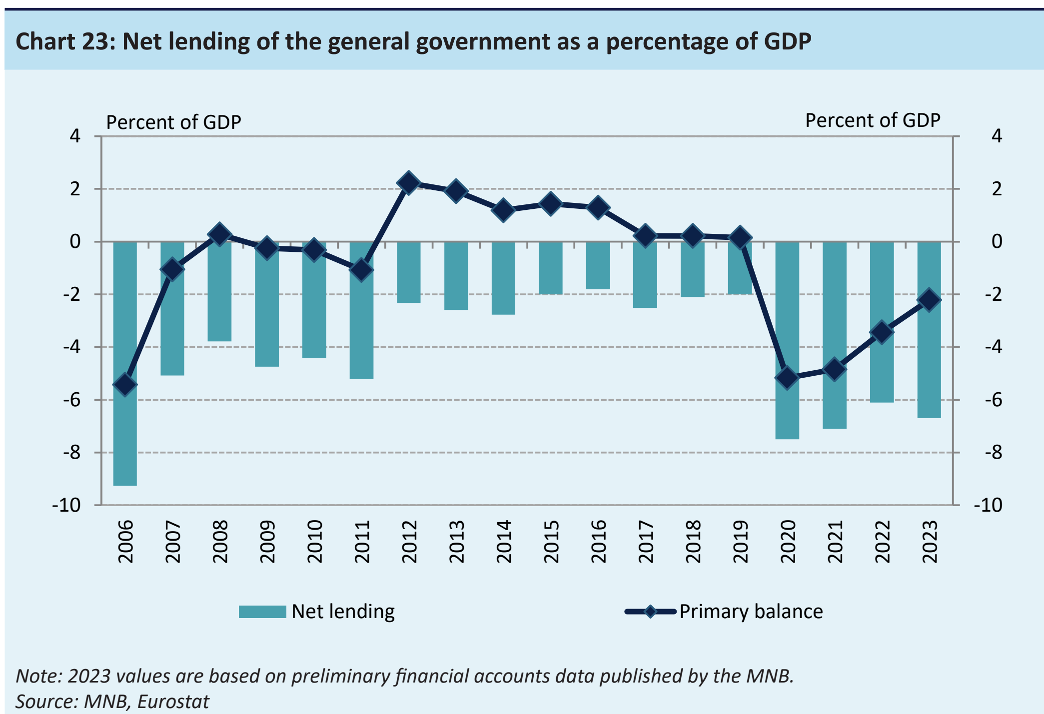
3.1 General government

In 2023, the net borrowing of the general government increased compared to the previous year due to high inflation, low VAT receipts and high interest expenses. According to preliminary financial accounts data, net borrowing by the general government amounted to 6.7 per cent of GDP in 2023[4] (Chart 23). Based on preliminary data, the accrual-based

[4] Data regarding the ESA balance of the budget is not yet available for 2023, but in general, there is only a minor difference between preliminary net lending data calculated according to the financial accounts and the ESA balance.

deficit exceeded the budget deficit target, which was raised to 5.2 per cent, by 1.5 percentage points, and the previous deficit in 2022 by 0.5 percentage point in 2023. The deviation from the amended Budget Act was mainly due to lower tax revenues and rising interest expenses in the higher inflation environment. As a result of falling consumption due to high inflation, net VAT receipts increased by just 2 per cent, over HUF 1,000 billion below the budgeted amount. As a further negative fiscal effect of the high inflation environment, government interest expenses rose by nearly HUF 1,500 billion from 2.8 per cent of GDP in 2022 to around 4.5 per cent of GDP in 2023.

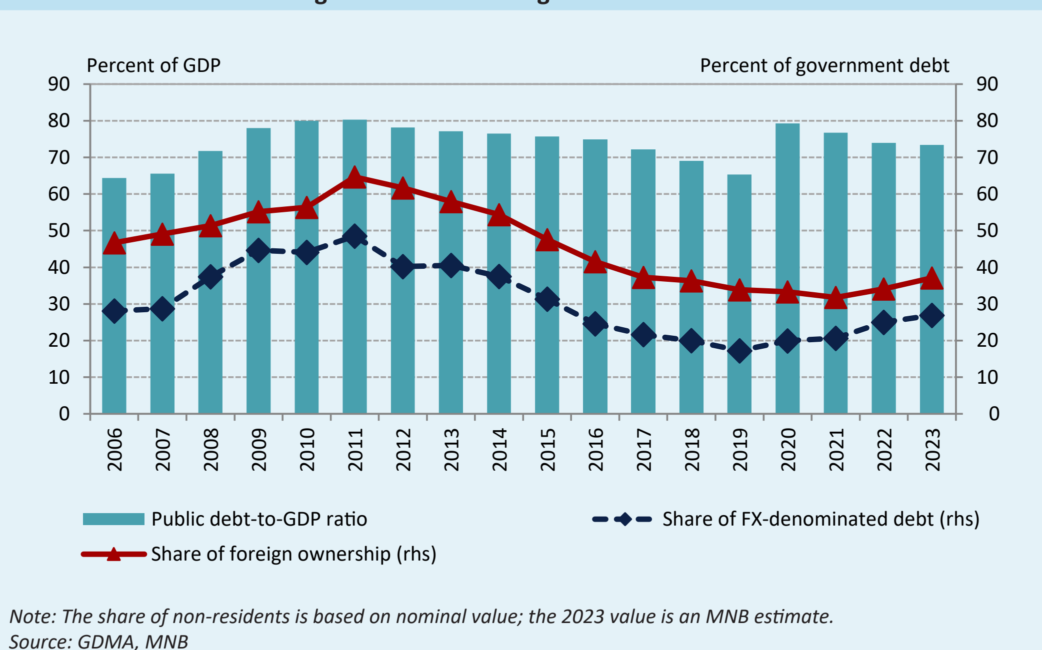
Chart 23: Net lending of the general government as a percentage of GDP



Note: 2023 values are based on preliminary financial accounts data published by the MNB.
Source: MNB, Eurostat

Gross public debt fell to 73.4 per cent of GDP by the end of 2023, while the foreign currency debt ratio and the share of non-residents in government debt rose somewhat due to foreign currency bond issuance (Chart 24). The 0.6-percentage point decline in the public debt ratio relative to end-2022 was mainly supported by a high GDP deflator, while it was offset by a high budget deficit, the increase in the debt of Eximbank, which is classified as public debt, and the deceleration observed in the real economy. In 2023, the Government Debt Management Agency issued more than HUF 2,840 billion in foreign currency in net terms, including wholesale net foreign currency bond issuance of around HUF 1,740 billion. As a result of the foreign currency bond issues, the foreign currency debt ratio rose to 26.9 per cent from 25 per cent in 2022. The share of foreign ownership in public debt may have increased to around 37 per cent by the end of 2023 from 34 per cent at the end of 2022.

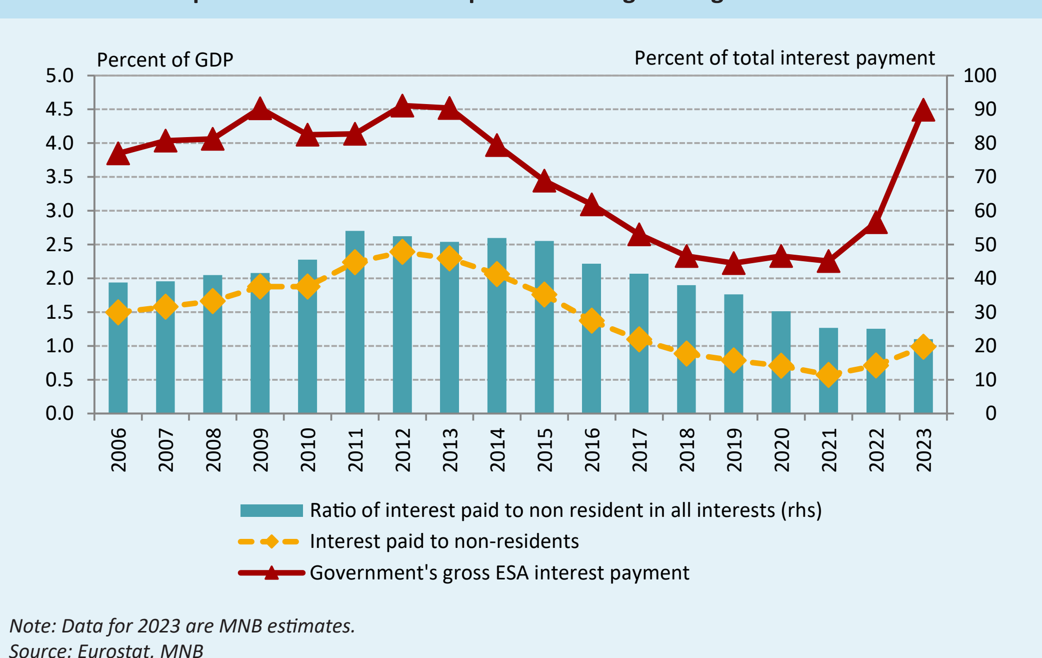
Chart 24: Developments in gross government debt, including changes in the share of non-residents and the share of foreign currencies in budget debt



Note: The share of non-residents is based on nominal value; the 2023 value is an MNB estimate.
Source: GDMA, MNB

Public sector interest expenses rose sharply to 4.5 per cent of GDP in 2023, mainly due to high inflation, with only a minor increase in interest paid to non-residents (Chart 25). Public sector interest expenses increased by 1.7 percentage points compared to 2022, primarily due to high inflation and an increase in interest rates linked to inflation expectations. A significant part of the higher interest expenses of the government was transferred to domestic participants, in particular, households. In 2023, government interest paid to non-residents fell to 22 per cent of total interest expenses, corresponding to 1 per cent of GDP. As a result of the low level of non-residents' share in government debt, interest payments to non-residents have almost halved since 2012, improving the current account balance.

Chart 25: Developments in the interest expenses of the general government

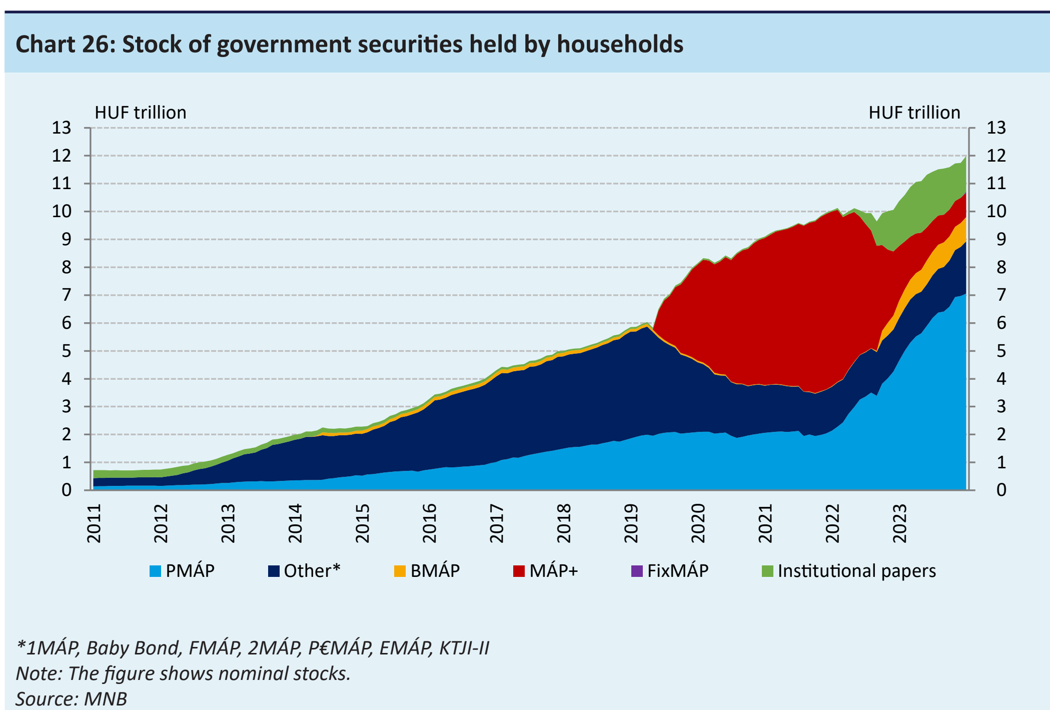


Note: Data for 2023 are MNB estimates.
Source: Eurostat, MNB

2023 saw the dominance of the inflation-protected Premium Hungarian Government Securities in the retail government securities market, with households' government securities savings rising substantially over the past year (Chart 26). In the uncertain economic environment of 2022, the stock of government securities held by households

stagnated overall, but as inflation rose towards the end of the year, demand for Premium Hungarian Government Securities (PMÁP) started to increase. The scheme, which preserves the real value of households' savings, attracted inflows of around HUF 2,700 billion in 2023, bringing its stock to nearly HUF 7,000 billion by the end of the year, accounting for nearly two thirds of the household government securities portfolio. By contrast, there was an outflow of almost HUF 1,400 billion from MÁP Plus last year. In 2022, the stock of the popular Discount Treasury Bills (DKJ) declined by HUF 200 billion, as households typically invested larger maturing amounts in other products offering more attractive interest rates than the falling short yields. At the same time, nearly HUF 350 billion flowed into the BMÁP, which is linked to the performance of the DKJ yield, but offers a premium above it. The stock of 1MÁP moderately declined in 2023, while the stock of the baby bond, the 1- and 2-year KTJ, the EUR-denominated P€MÁP, and then the EMÁP that replaced the latter, increased; thus, overall, the stock of these securities increased by around HUF 260 billion. In the high inflation environment of 2023, households increased their savings substantially, and government bonds played a major role in this increase, providing stable domestic financing for the general government.

Chart 26: Stock of government securities held by households

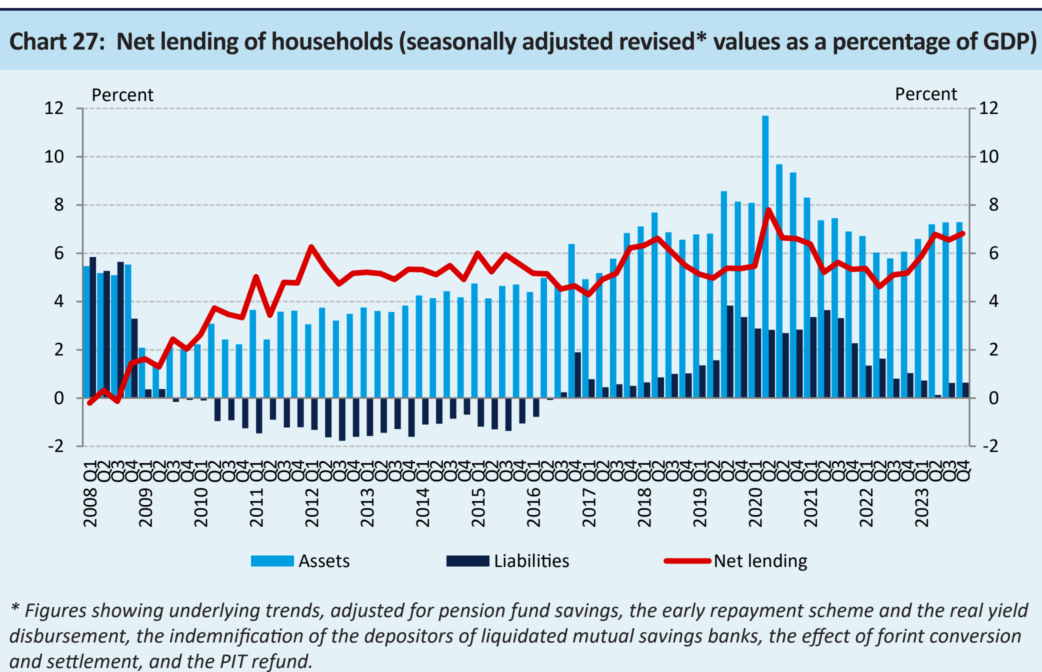


**1MÁP, Baby Bond, FMÁP, 2MÁP, P€MÁP, EMÁP, KTJI-II*
Note: The figure shows nominal stocks.
Source: MNB

3.2 Households

According to underlying trends, after a rise observed in the middle of the year, households' net lending stabilised at above 7 per cent of GDP in 2023 Q4 – the level recorded in 2020, during the COVID-19 pandemic (Chart 27). In 2020, during the coronavirus pandemic, the population accumulated a substantial amount of forced savings, most of which households used to increase their consumption after the restrictions were lifted: this explains the surge in savings in early 2020 and the subsequent decline, which may have contributed to the increase in inflation. From 2022 H2 onwards, there was an adjustment to the impact of the energy crisis and rising inflation on the back of the Russia-Ukraine war by cutting back on consumption, which contributed significantly to the increase in households' financial savings. On the borrowing side, in addition to the slowdown in real estate loans, the relatively stable growth of baby loans within other loans also slowed substantially during the year, following the restructuring and possible termination of the programme.

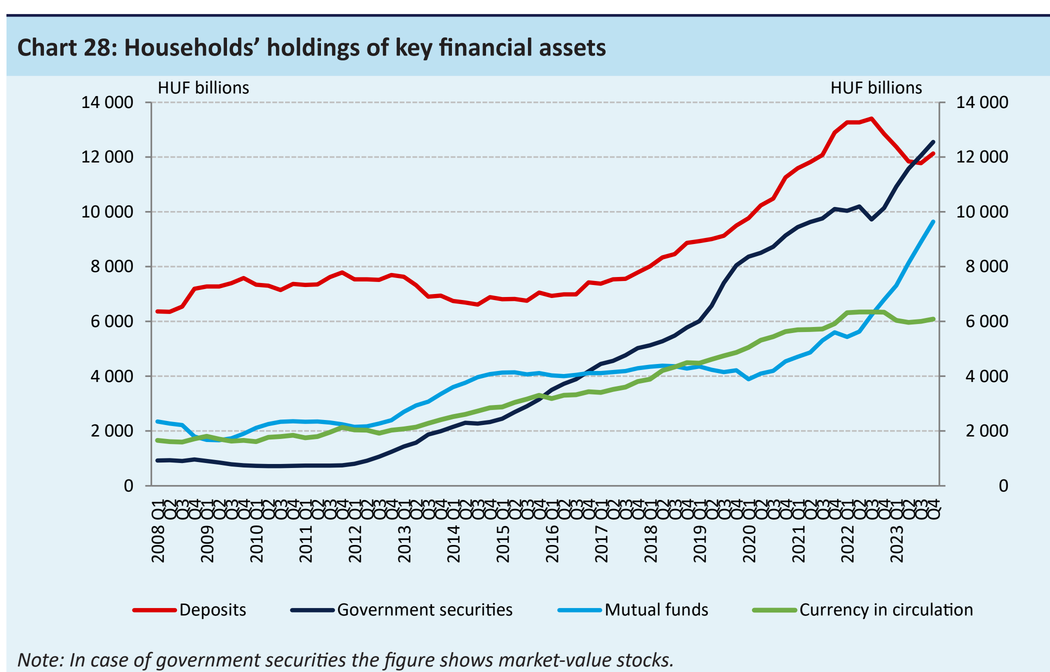
Chart 27: Net lending of households (seasonally adjusted revised* values as a percentage of GDP)



** Figures showing underlying trends, adjusted for pension fund savings, the early repayment scheme and the real yield disbursement, the indemnification of the depositors of liquidated mutual savings banks, the effect of forint conversion and settlement, and the PIT refund.*

In 2023, the growth rate of the holdings of government securities and investment fund units accelerated, while the decline in deposits stopped and turned into an upward trend by the end of the year (Chart 28). Cash holdings fell by around HUF 150 billion at the beginning of 2023, which may be explained by the fact that the high inflation led households to exchange some of their accumulated cash for interest-bearing assets, and declining retail sales also had an impact on lower cash holdings. The steady increase in households' direct holdings of government bonds observed since 2012 continued at a slower pace in 2021. However, starting from 2022 H2 and mainly in response to rising inflation, households shifted their new savings primarily into inflation-linked, higher-yielding government bonds, and also reallocated some of their available liquid assets. Thus, the stock of government securities held by households expanded by nearly HUF 2,400 billion in 2023. The stock of investment fund units increased by nearly HUF 2,200 billion over the year, as savings flowed into bond funds, which have become attractive investments as their backward-looking yields increased. Demand for government bonds was influenced both by the high inflation environment and developments in the yields of alternative investment options, which also affected the size and structure of purchases. Deposit balances declined for most of the year due to high inflation and low retail deposit rates, while they rose again in the last quarter thanks to moderating inflation and government transfers (e.g. pension supplements).

Chart 28: Households' holdings of key financial assets

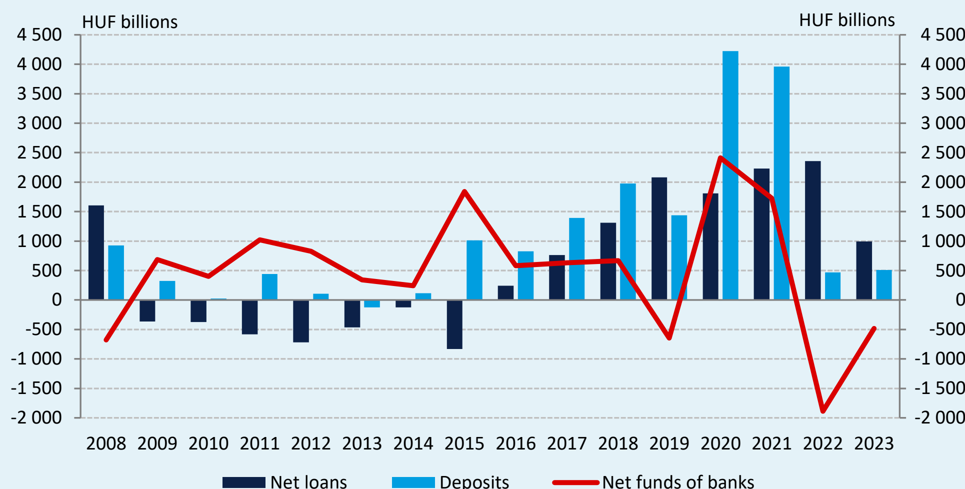


Note: In case of government securities the figure shows market-value stocks.

Box 3: Changes in the bank loans and deposits of the private sector

In 2023, annual private sector deposit inflows stagnated at a low level, but net private sector withdrawals from banks declined due to a significant fall in net bank borrowing. In the years after the 2008 financial crisis, the private sector steadily reduced its bank loans in net terms, i.e. repayments exceeded the amount of new borrowings. Together with a smaller degree of deposit placement, this implied that the private sector increased the funds available to banks. 2016, however, saw a turnaround in lending with net borrowing by households and the corporate sector rising steadily; this was only temporarily slowed by the 2020 COVID-19 pandemic (Chart 29). At the same time, as borrowing increased, the private sector also expanded its deposit placements, and accordingly, banks' funds from households and the corporate sector typically continued to grow until 2021. 2022 marked a turning point in this process: while borrowing continued to expand moderately, deposit taking moderated due to portfolio shifts into assets offering higher returns than deposits, presumably because of rising inflation. Thus, the net decline in liabilities to the private sector contributed to banks' increasing external borrowing as seen in the balance of payments. Outflows from banks to the private sector continued in 2023, but at a much slower pace than a year earlier, as deposit inflows remained low in the high inflation environment (reflecting a larger decline in deposits by households and rising deposit inflows by corporates), while net borrowing by both households and corporates fell.

Chart 29: Changes in the bank loans and deposits of the private sector

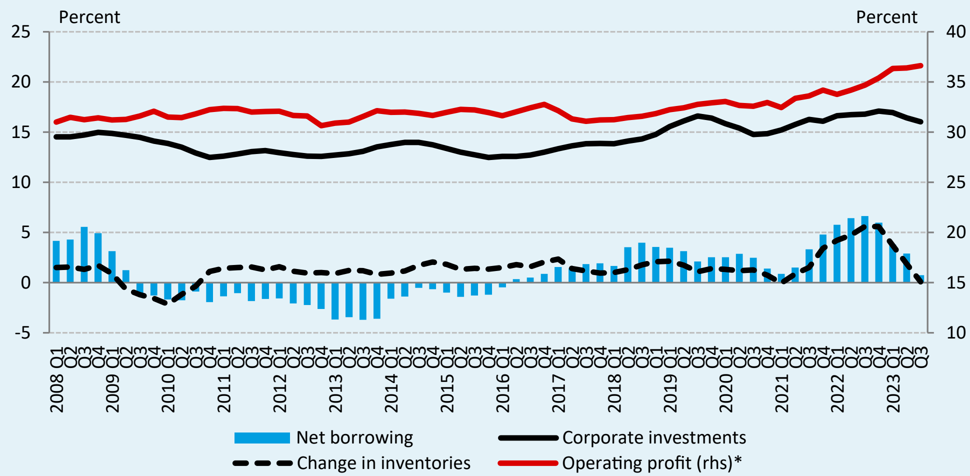


3.3 Corporate sector

The net borrowing of non-financial corporations fell sharply in the context of a declining investment rate and falling inventory investment. The four-quarter operating profit of the corporate sector as a percentage of GDP stabilised at a high level during 2023, which may have been supported by a combination of lower energy prices and significant annual price increases. At the same time, with external demand increasingly unfavourable and household consumption subdued due to high inflation, the sector's investment expenditure as a share of GDP declined, while its inventory investment – which had advanced to a record high by the end of 2022 – fell to nearly zero in 2023. As a result of the above, the four-quarter net borrowing of companies decreased significantly overall as a percentage of GDP by 2023 Q3 (Chart 30).[5]

[5] Financial accounts for 2022 Q4 will only be published after the editorial deadline for this report.

Chart 30: Net borrowing of non-financial corporations and its main factors (four quarter GDP-proportionate values)



** Indicator adjusted for companies' interest and shareholder incomes. Data related to the borrowing requirement are only available until the third quarter.*
Source: HCSO, MNB

4 Comparison by region

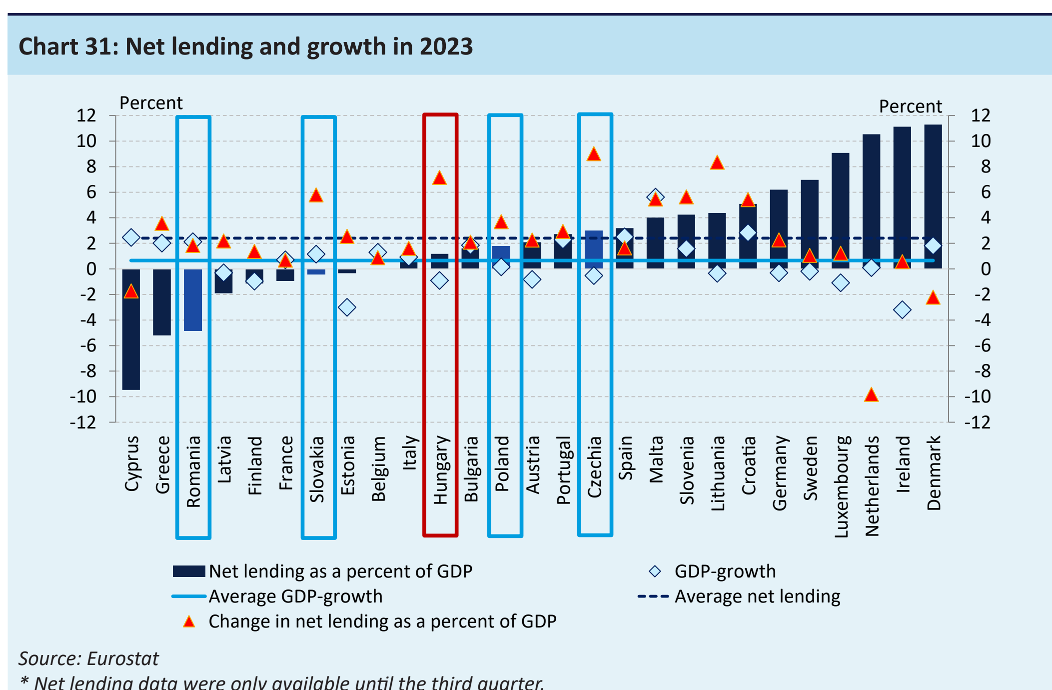
After the significant deficit seen in 2022, the external balance of most countries in the region showed a marked improvement in 2023. The decline in gross capital formation, including the increase in inventories, was reflected in an improvement in the external position, which was also supported by an increase in savings. The improvement in the external balance of the region was mainly due to a substantial correction in the trade balance, partly driven by falling energy prices and partly by weakening domestic demand due to high inflation. The services balance stabilised at high levels in Poland and Romania, as well as in Hungary. The transfer balance declined in most of the countries in the region. The deficit on the income balance was driven by rising interest expenses in parallel with the profit balance, which continues to weigh heavily on external positions across the region. In 2023, the net borrowing of the countries in the region decreased significantly, and by the end of the year, Poland and the Czech Republic exhibited an outflow of resources. Net direct investment by the region's countries remains significant. In Hungary and Romania, the net borrowing of the general government exceeded 6 per cent of GDP, while the Czech figure was below 3 per cent of GDP.

In our special topic focusing on international comparison, the developments in Hungary's external balance are presented relative to the countries in the region. In terms of balance of payments figures, Hungary should be compared primarily to countries which are at a similar level of development and face similar challenges. For this purpose, the most ideal group of countries comprises countries in the region which acceded to the European Union at the same time, plus Romania, which joined the EU later but has been quick to catch up in recent years.

4.1 A snapshot of Europe

In 2023, the external position of the Hungarian economy improved markedly compared to the EU (Chart 31). The net borrowing of most EU countries improved substantially in 2023 as economic growth decelerated. Falling energy prices and weaker domestic demand, combined with high inflation, led to an improvement in the external position in most European countries, which was dampened somewhat by a slowdown in exports due to the uncertain external environment. The fall in external and internal demand was accompanied by a slowdown in economic performance in all European countries, although the extent to which the dynamics slowed down varied considerably across countries. The Hungarian economy is projected to contract by 0.9 per cent of GDP in 2023, coming in last place among the countries in the region and the fourth lowest in Europe. By contrast, the improvement in Hungary's external position was one of the highest in the European countries, and its level is also favourable: it is significantly higher than in Romania and Slovakia among the countries of the region, while remaining close to the European average.

Chart 31: Net lending and growth in 2023



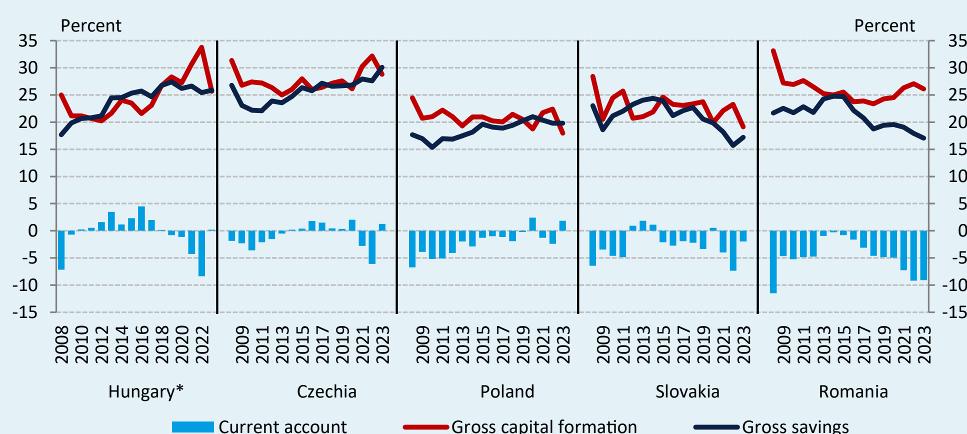
Source: Eurostat

** Net lending data were only available until the third quarter.*

4.2 Gross savings and investment

The narrowing of the current account deficit in 2023 was typically driven by a decline in gross capital formation in the countries of the region (Chart 32). The current account balance is the difference between gross savings (the difference between income and consumption) and capital formation (investment and inventories). Following the financial crisis of 2008, the current account balance improved in all CEE countries amid falling investment rates and gradually expanding gross savings as a result of balance sheet adjustment. Since the middle of the previous decade, however, this improving trend has been reversed in most of the countries in the region, with the current account balance declining. The deterioration was halted in a few countries by falling domestic demand during the COVID-19 pandemic, but the current account balance deteriorated again in 2021 with reopening. While in 2022, the deteriorating external balance indicators in the countries of the region were mainly due to the strengthening of gross fixed capital formation (although savings also declined in several countries), in 2023, the decline in investment activity was reflected in an improvement in the external balance, with the exception of Romania. In addition, slowing inventory growth contributed significantly to the improvement of the external balance. The stocks accumulating before 2022 H2 may reflect the disruption of economic relations in the context of the pandemic, a shortage of chips and the significantly higher cost of natural gas procurement. However, over the course of 2023, inventory investment slowed significantly in the countries of the region, and started to decline in Slovakia, Romania and Hungary by the end of the year. Savings rates in Hungary and Poland remained relatively stable in 2023 at around 2022 levels, while the Romanian figure declined and the Czech and Slovak figures improved. The savings rates in Slovakia and Romania, on the other hand, moved on a downward trend, which, together with high capital expenditure in Romania, induced a significant increase in liquidity needs, while Slovakia has a very low investment rate of below 20 per cent, which resulted in a lower borrowing requirement. As a result, current account balances have increased significantly in most of the countries in the region, while Romania maintained a large deficit.

Chart 32: Developments in gross savings and investment (investment and inventory) rate (as percentage of GDP)*



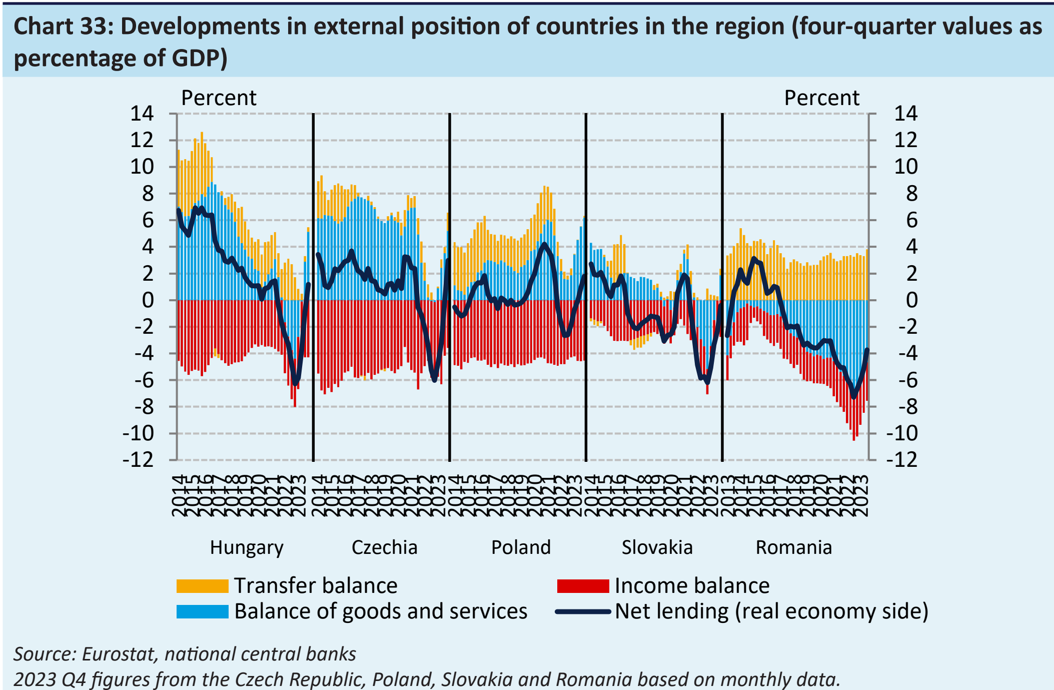
Source: MNB, HCSO, WEO
** For 2023 the gross savings rate is derived from the total investment and current account data. For the rest of the region, the balance of payments in 2023 is estimated on the basis of monthly data.*

4.3 Net lending and its real economic factors

In 2023, the improvement seen in the external balances of the countries of the region is mainly due to a significant correction in the trade balance (Chart 33). According to real economic data, the four-quarter net external position improved significantly in all countries of the region over the past year. In Slovakia and Romania, net borrowing improved from the trough of 6–7 per cent of GDP in 2022, but the pace of the improvement was below the Hungarian level. Therefore, external borrowing was still necessary in 2023 Q4 in Slovakia and Romania. In the Czech Republic, the path of the external balance indicator has been very similar to that in Hungary over the past two years, turning from a trough at

the end of 2022 to a surplus in 2023 with a rapid improvement. In Poland, on the other hand, the deterioration in net borrowing had come to a halt by mid-2022, and the external position had turned into net lending of close to 2 per cent of GDP by 2023 Q3.

Chart 33: Developments in external position of countries in the region (four-quarter values as percentage of GDP)



Source: Eurostat, national central banks
2023 Q4 figures from the Czech Republic, Poland, Slovakia and Romania based on monthly data.

Developments in the external balance indicators were determined by the following factors:

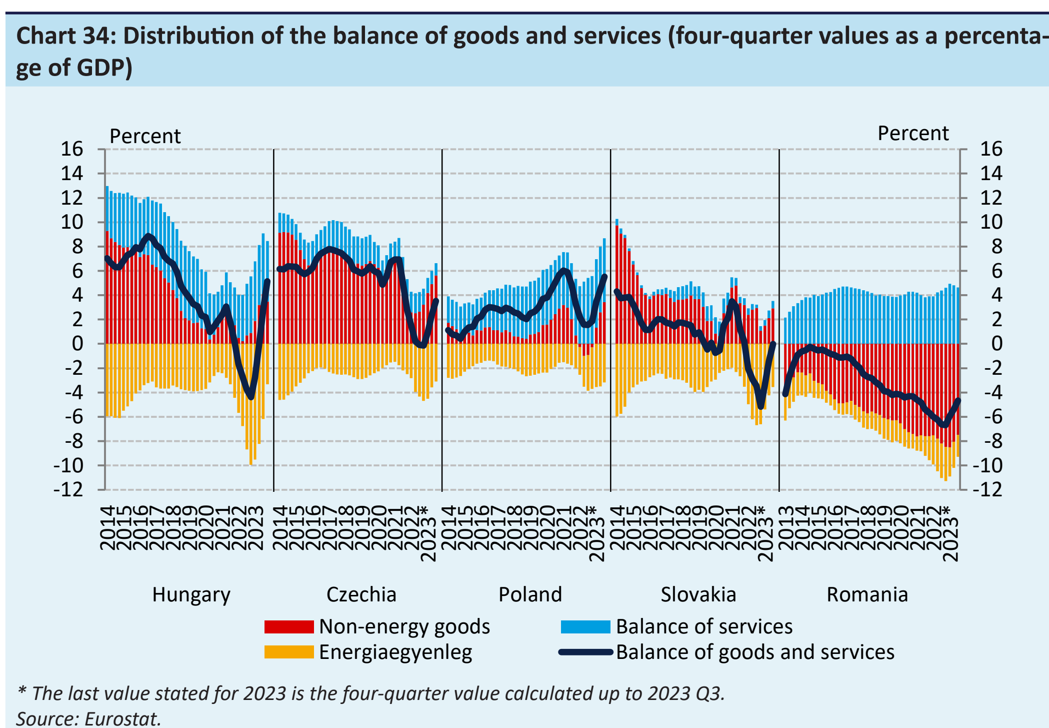
- The ratio of the **balance of goods and services** to GDP rose sharply in 2023, as energy imports adjusted to falling energy prices, accounting for most of the improvement in the external balance. The fall in energy imports and the slowdown in imports as domestic demand weakened led to a rapid improvement in Hungary, the Czech Republic and Slovakia. The Romanian and Polish economies were less affected by energy price fluctuations, due to significant domestic energy production. For Hungary, Poland and Romania, the surplus in services stabilising at high levels contributed significantly to the trade balance.
- **Income imbalances** in the region's countries generally undermine the external position of the economy. The income balance deficit in 2023 increased in most countries in the context of expanding corporate profit balances and higher interest expenses.
- The positive contribution of the **transfer balance** to the external balance declined in all the countries of the region except Romania. In the year to 2023 Q3, the transfer balance as a share of GDP was highest in Romania, followed by the Hungarian and Czech indicators. In the other Visegrád countries, the transfer balance dropped to a level close to equilibrium. EU transfer inflows slowed in Hungary and Poland, but accelerated in the rest of the countries.

4.4 Trade balance

In 2023, Hungary recorded the largest increase in the goods balance, but the normalisation of energy prices led to a substantial improvement in the indicator in all countries in the region (Chart 34). In 2022, a sharp rise in energy imports due to the surge in energy prices, combined with a slowdown in exports in the context of weakening global activity, led to an overall deterioration in the trade balance. This could not be offset by falling imports amid the contraction in domestic demand resulting from the rising cost of living. In 2023, however, normalising energy prices and the continued weakening of domestic demand led to an overall adjustment in the balance of goods across the region as a whole. The pace and extent of the improvement was determined by exposure to energy prices: the Hungarian and Slovakian balances, which are heavily dependent on energy imports, showed the largest improvement from their historical lows in 2022, while Poland and Romania, which have significant energy supplies, saw only smaller fluctuations in their energy balances. At the

same time, the non-energy goods balance also improved substantially, mainly due to lower imports as consumption and investment slowed. The surplus on the balance of services continued to boost the trade balance substantially across the region, but especially in Poland, Romania and Hungary. In 2023, the services balance in the countries of the region stabilised at the previous, generally high, level. Overall, the trade balance improved significantly in all countries of the region, reflecting the fall in energy prices and subdued domestic demand: in Hungary, Poland and the Czech Republic, it turned into a surplus ranging between 3 and 6 per cent of GDP, while in Slovakia it rose to nearly equilibrium. By contrast, the Romanian indicator showed a deficit of almost 5 per cent of GDP, despite the improvement.

Chart 34: Distribution of the balance of goods and services (four-quarter values as a percentage of GDP)



** The last value stated for 2023 is the four-quarter value calculated up to 2023 Q3.*
Source: Eurostat.

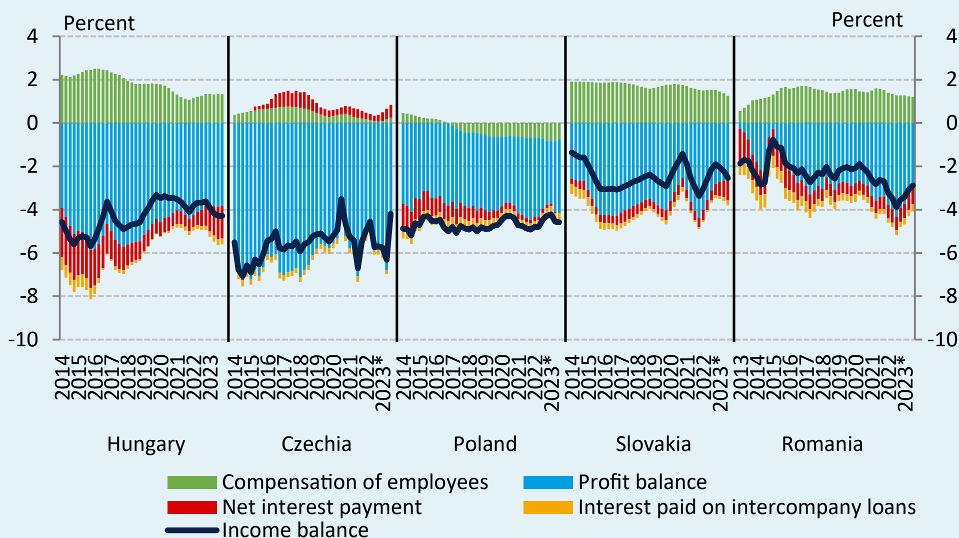
4.5 Income balance and transfer balance

The income balance in the countries of the region generally shows a substantial deficit mainly related to the profit balance, but its development varied across countries in 2023 (Chart 35). Based on four-quarter values up to the third quarter, the deficit on the income balance narrowed markedly in the Czech Republic and Romania, while it deteriorated in the other countries.

- The income balance of workers temporarily working abroad tends to reduce the income deficit, with the exception of Poland where even before the war in Ukraine there was a significant number of Ukrainian workers,[6] whose income in Poland exceeds that of Polish workers temporarily working abroad. Developments in the remuneration of employees reduced the income balance deficit in the Czech Republic and Hungary, but worsened it in Slovakia and Romania.
- Rising interest expenses, in line with higher yields, contributed to a widening income balance deficit in most of the countries in the region, but improved the indicator in the Czech Republic (thanks to its net external assets position).
- Foreign companies have built up significant production capacities in all countries in the region; accordingly, the profit balance of foreign companies accounts for the largest part of the region's income balance deficit.[7] The Czech Republic and Slovakia had the highest and lowest deficit on the profit balance, while Hungary was in the middle of the range.

[6] https://www.nbp.pl/en/publikacje/raport_inflacja/iraport_november2019.pdf
[7] Since quarterly data on the 2023 profitability of foreign-owned enterprises operating in Hungary are limited, information on quarterly profit outflows is based on estimates until the receipt of corporate questionnaires in September 2024. For more detail, see the publication "Methodological notes to the Balance of Payments and Investment Position Statistics".

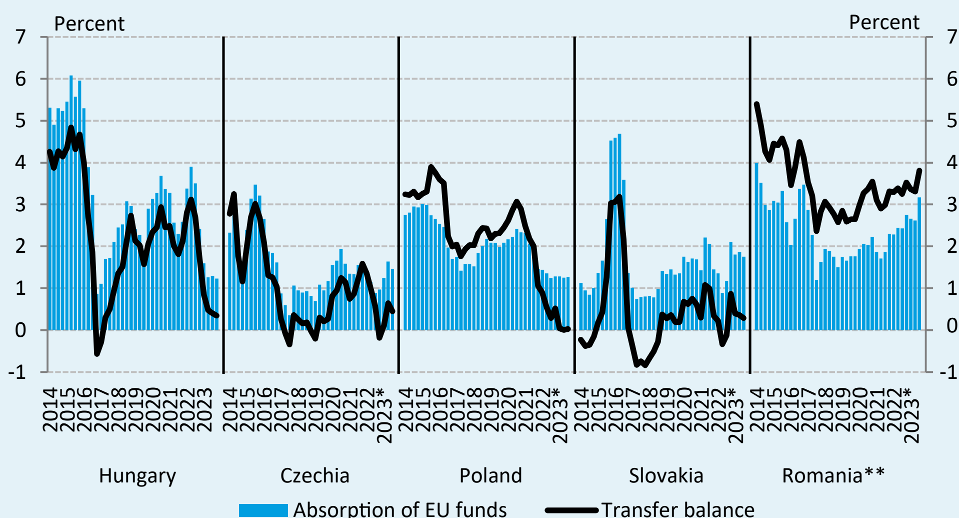
Chart 35: Developments in the components of the income balance* (four-quarter values as a percentage of GDP)



** The value stated for 2023 is the four-quarter value calculated up to 2023 Q3.*
Source: Eurostat

Inflows of EU transfers slowed down in 2023 in Poland and Hungary compared to the previous year, while Romania and Slovakia saw a significant acceleration last year (Chart 36). By the end of 2023, the absorption of EU funds in both Hungary and Poland fell to a low level compared to previous years, mainly due to the end of the 2014–2020 budget cycle and the different timing of the drawdown of funds (Chart 45). The Czech Republic, Romania and Slovakia have also started to draw down Recovery and Resilience Facility (RRF) funds in recent years, while Hungary and Poland only accessed advances from REPowerEU, which are mostly loan-related and therefore do not affect transfer receipts. In Romania, uniquely among the countries compared, in addition to EU transfers remittances from long-term expatriates also improved the transfer balance significantly.

Chart 36: Absorption of the transfer balance and EU transfers in the countries of the region (as a percentage of GDP)

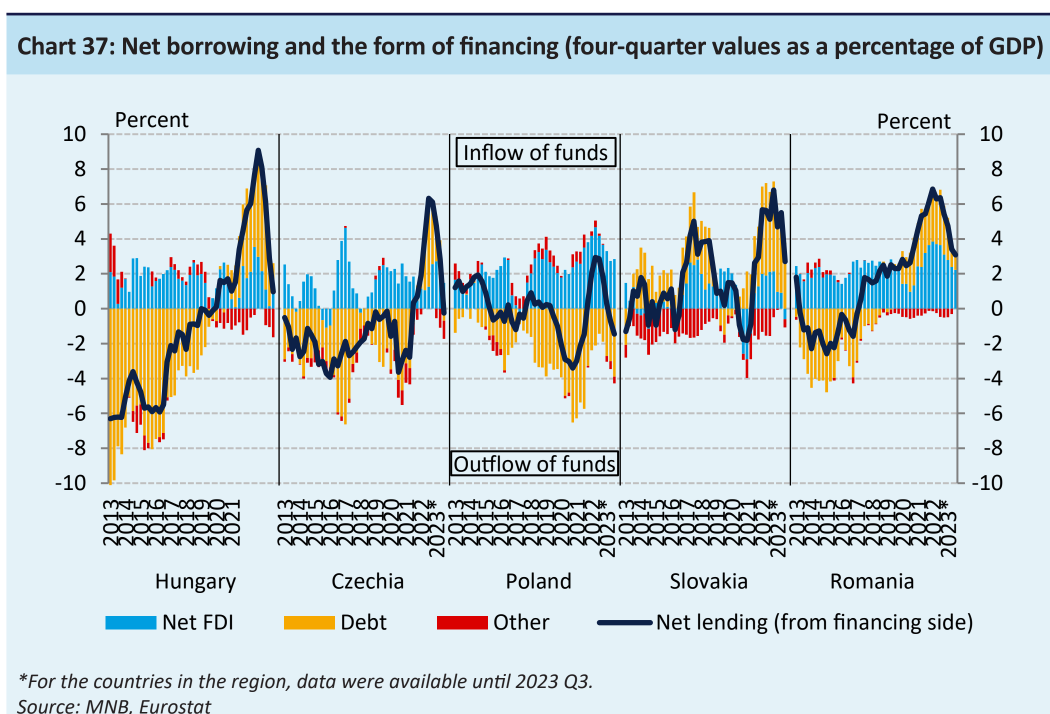


** The last value stated for 2023 is the four-quarter value calculated up to 2023 Q3.*
*** Secondary income data are incomplete for 2018–2019.*
Source: Eurostat

4.6 Financing side developments

The financial balance shows a rapid and significant decline in the net borrowing of the countries of the region in 2023 (Chart 37). The largest improvements in the borrowing requirement were observed in the Czech Republic and Hungary, while Slovakia and Romania, with high net borrowing, saw a smaller decline in their absorption. For Poland and the Czech Republic, net borrowing turned into net lending in 2023, amounting to 1.4 and 0.2 per cent of GDP, respectively. As regards the types of the liabilities, the main contributor to the improvement in the external balance in the region was the decline in external borrowing (in the case of Poland, the reduction of net external debt), while net FDI inflows slowed compared to previous periods, but remained significant. Romania financed itself more from net FDI and less from debt. In the case of Hungary and the Czech Republic, there were also significant outflows through other items related to portfolio outflows.

Chart 37: Net borrowing and the form of financing (four-quarter values as a percentage of GDP)

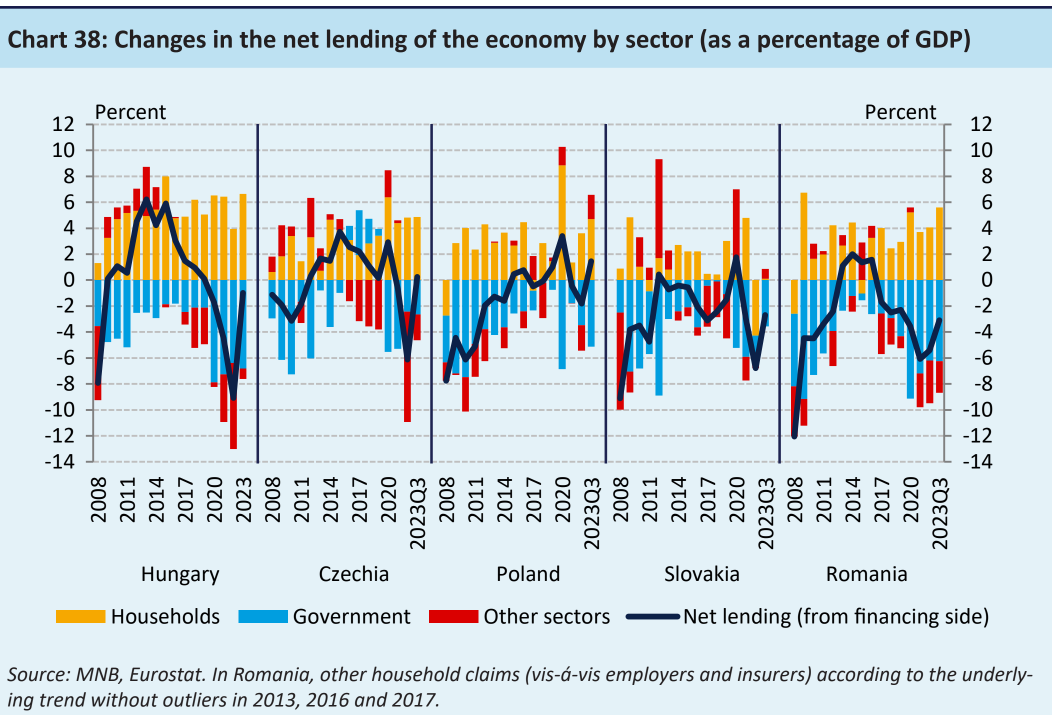


**For the countries in the region, data were available until 2023 Q3.*
Source: MNB, Eurostat

4.7 Financial savings by sector

In terms of the evolution of the financial position of the sectors, similar trends were observed in 2023 in the countries of the region: net financial savings of the private sector increased, while fiscal deficits typically continued to rise (Chart 38). The external financing position of the countries of the region improved significantly in 2023, mainly as a result of a decline in the net borrowing of companies and an increase in the net lending of households. Consumption fell uniformly in the region in 2023, while inflation reduced the real value of income less and less, allowing households' financial savings to improve substantially, with the exception of the Czech Republic, where savings increased only moderately. Hungarian households continued to hold the highest net financial savings among the countries under review. In 2023, high inflation and a slowdown in investment reduced domestic demand in the countries of the region, which also entailed lower tax revenues. In addition, the budget deficit typically continued to widen as energy expenditure gradually declined, but nevertheless remained high. In Hungary and Romania, the deficit thus remained historically high in 2023, while in the other three countries it may have been more subdued.

Chart 38: Changes in the net lending of the economy by sector (as a percentage of GDP)

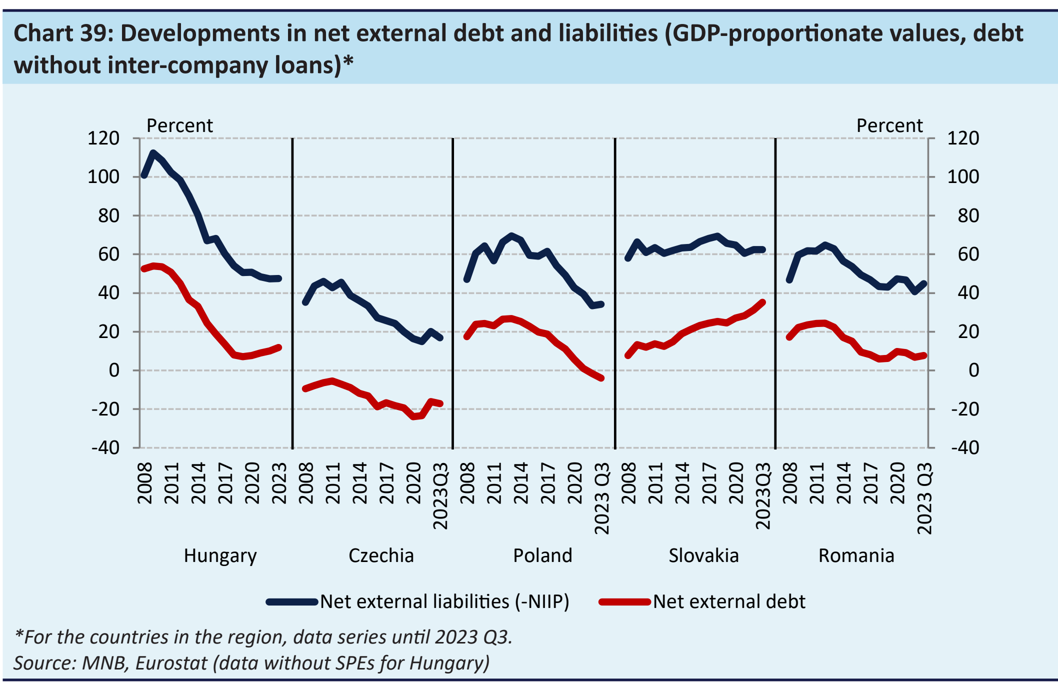


Source: MNB, Eurostat. In Romania, other household claims (vis-á-vis employers and insurers) according to the underlying trend without outliers in 2013, 2016 and 2017.

4.8 External debt indicators

In 2023, the net external debt and debt ratios of the countries in the region are mixed, while Hungary's ratios continue to be broadly in line with the regional average (Chart 39). The decline in net borrowing typically had a positive impact on external debt indicators, which was also supported by the effect of economic growth. The improving trend in Poland since 2017 continued unabated in 2023 for net external debt, while net external liabilities turned somewhat upwards. In Romania and Slovakia, on the other hand, both net external debt and net external liabilities increased in 2023, while the Czech Republic's indicators declined. As regards GDP-proportionate ratios, the Czech Republic remained the best performer in the region for both indicators, while Slovakia recorded the highest indicators. Hungary's net external liabilities amounted to around 48 per cent of GDP at the end of 2023, while its net external debt remained below 12 per cent of GDP, still close to historical lows. Looking at the longer-term trends, Hungary's external debt indicators have improved the most over the past decade, but all of the countries in the region except Slovakia recorded significant declines in both indicators.

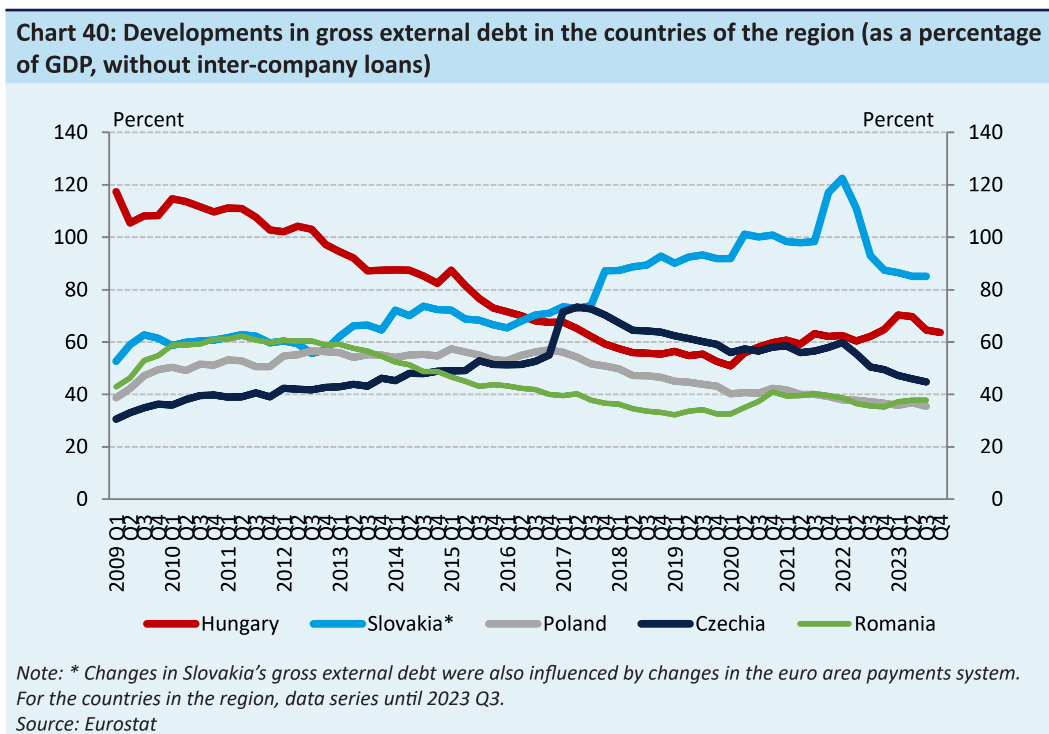
Chart 39: Developments in net external debt and liabilities (GDP-proportionate values, debt without inter-company loans)*



**For the countries in the region, data series until 2023 Q3.*
Source: MNB, Eurostat (data without SPEs for Hungary)

Consistent with the favourable external balance, gross external debt excluding inter-company loans declined in most countries in the region as a percentage of GDP (Chart 40). While at the onset of the financial crisis, Hungary's gross external debt was very high by regional standards, by 2016 the post-crisis adjustment lowered the debt ratio below the Czech and Slovak levels, bringing it into the middle of the regional range. The Hungarian and Czech ratios were similar until 2021, but after that a gap developed between the gross external debt levels of the two countries, which closed somewhat last year. In Slovakia, gross external debt developments were also influenced by TARGET-2 stock changes related to the country's participation in the euro area and the ECB's liquidity expansion.

Chart 40: Developments in gross external debt in the countries of the region (as a percentage of GDP, without inter-company loans)



*Note: * Changes in Slovakia's gross external debt were also influenced by changes in the euro area payments system. For the countries in the region, data series until 2023 Q3.*
Source: Eurostat

List of charts

Chart 1: Stylised depiction of Hungary's external balance position 4
Chart 2: Developments in the net lending position and its components (four-quarter values as a percentage of GDP) 7
Chart 3: Developments in the external trade balance and its contributing factors* (four-quarter values as a percentage of GDP) ..8
Chart 4: Annual volume growth in exports and imports and the four-quarter goods balance as a percentage of GDP 9
Chart 5: Contribution of main domestic absorption items and net exports to GDP growth 9
Chart 6: Changes in the trade balance as a percentage of GDP 10
Chart 7: Net external trade in goods by main groups (as a percentage of GDP) 10
Chart 8: Developments in income balance items (four-quarter values as a percentage of GDP) 11
Chart 9: Evolution of the GDP–GNI gap in Hungary (as a share of GDP) 12
Chart 10: Developments in the transfer balance (four-quarter values as a percentage of GDP) 12
Chart 11: Developments in net EU current and capital transfers and their sectorisation 13
Chart 12: Two types of net lending (four-quarter values as a percentage of GDP) 14
Chart 13: Direct investments and debt liabilities transactions (as a percentage of GDP)* 15
Chart 14: Developments in net external debt (end-of-period, as a percentage of GDP) 16
Chart 15: Developments in FDI (excluding capital-in-transit transactions) 17
Chart 16: Developments in debt liabilities by sector (as a percentage of GDP) 18
Chart 17: Net external debt by sector (as a percentage of GDP, excluding inter-company loans) 18
Chart 18: Decomposition of the change in net external debt by item (as a percentage of GDP) 19
Chart 19: Developments in net and gross external debt (as a percentage of GDP) 20
Chart 20: Developments in the gross borrowing requirement 21
Chart 21: Short-term external debt and international reserves of the Hungarian economy 22
Chart 22: Net lending of specific sectors* (four-quarter values as a percentage of GDP) 23
Chart 23: Net lending of the general government as a percentage of GDP 24
Chart 24: Developments in gross government debt, including changes in the share of non-residents and the share of foreign currencies in budget debt 25
Chart 25: Developments in the interest expenses of the general government 25
Chart 26: Stock of government securities held by households 26
Chart 27: Net lending of households (seasonally adjusted revised* values as a percentage of GDP) 27
Chart 28: Households' holdings of key financial assets 27
Chart 29: Changes in the bank loans and deposits of the private sector 28
Chart 30: Net borrowing of non-financial corporations and its main factors (four quarter GDP-proportionate values) ..29
Chart 31: Net lending and growth in 2023 30
Chart 32: Developments in gross savings and investment (investment and inventory) rate (as percentage of GDP)* 31
Chart 33: Developments in external position of countries in the region (four-quarter values as percentage of GDP) 32
Chart 34: Distribution of the balance of goods and services (four-quarter values as a percentage of GDP) 33
Chart 35: Developments in the components of the income balance* (four-quarter values as a percentage of GDP) 34
Chart 36: Absorption of the transfer balance and EU transfers in the countries of the region (as a percentage of GDP) .34
Chart 37: Net borrowing and the form of financing (four-quarter values as a percentage of GDP) 35
Chart 38: Changes in the net lending of the economy by sector (as a percentage of GDP) 36
Chart 39: Developments in net external debt and liabilities (GDP-proportionate values, debt without inter-company loans)* ..36
Chart 40: Developments in gross external debt in the countries of the region (as a percentage of GDP, without inter-company loans) 37

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.

REPORT ON THE BALANCE OF PAYMENTS

April 2024

Print: Prospektus Kft.

H-8200 Veszprém, Tartu u. 6.

mnb.hu

©MAGYAR NEMZETI BANK

H-1013 BUDAPEST, KRISZTINA KÖRÚT 55.