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Crisis Management in Hungary during the 2020 Crisis

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Obsah

Abstrakt

This study investigates the economic response the COVID19 crisis in Hungary. We begin by setting out the socio-economic state of affairs prior to the crisis. After explaining the general protective measures taken, we arrive conclude that they were successful. We proceed by elaborating the economic crisis response measures and their impact. We conclude that the economic response was opaque and its size has kept on changing. We also conclude that the harm caused by the crisis puts Hungary in the middle range in an international comparison.

1. The state of the Hungarian economy prior to the crisis

The Hungarian economy was going strong prior to the crisis. Only a decade earlier, in 2009, Hungary had been the first EU economy ever to turn to the IMF under nominally Socialist Prime Minister Ferenc Gyurcsány. That loan amounted to a whopping 20% of GDP.

Following transition to illiberal, ethno-nationalist Prime Minister Viktor Orbán, the economy took off. Hungary's GDP growth rates prior to 2020 were at the top of the European league. The wage levels were also growing strong, although not as strong as the rest of the region.

Most of this growth was dependent on the following factors:

1.) **A massive inflow of European Union non-repayable cohesion policy transfers**, amounting to some 5-7% of GDP over a number of years. This is probably the most significant contributing factor. Given the fact that GDP growth averaged about 3.5% over Orbán's two terms, it begs the question of how large this would have been without the EU transfers.

2.) **Massive remittances** from the some 350,000 Hungarians working abroad, mostly in the European Union, and primarily in Austria, Germany and the United Kingdom. According to World Bank data, this amounts to around 3.5% of GDP annually.

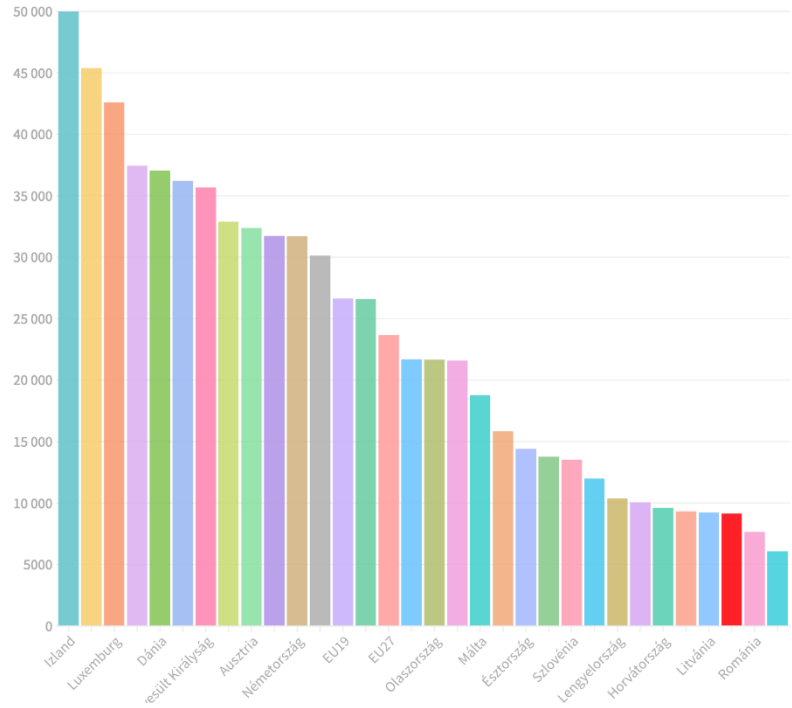
3.) **German investments**. Hungary was about to overtake Slovakia as the world's number one car producer, with Germany's BMW opening up a new production plant in Debrecen, centre of the East of Hungary. Mercedes is already active in the centre, Audi the West, and Suzuki in the North. (The fate of the new BMW plant is uncertain at the moment due to the virus.)

4.) **Generally positive global economic situation**. Hungary's economy is part of the Visegrad hintergrund of the German economy. Germany's growth is in turn dependent on exports to other regions, primarily China.

In 2019, the net growth rate of the average wage was 5.9% in Hungary. This is high in an international comparison, but lower than 6.8% in Slovakia, 7% in Estonia, 7.5% in Bulgaria, 8% in Poland, 9.4% in Latvia and a remarkable 14% in Romania.

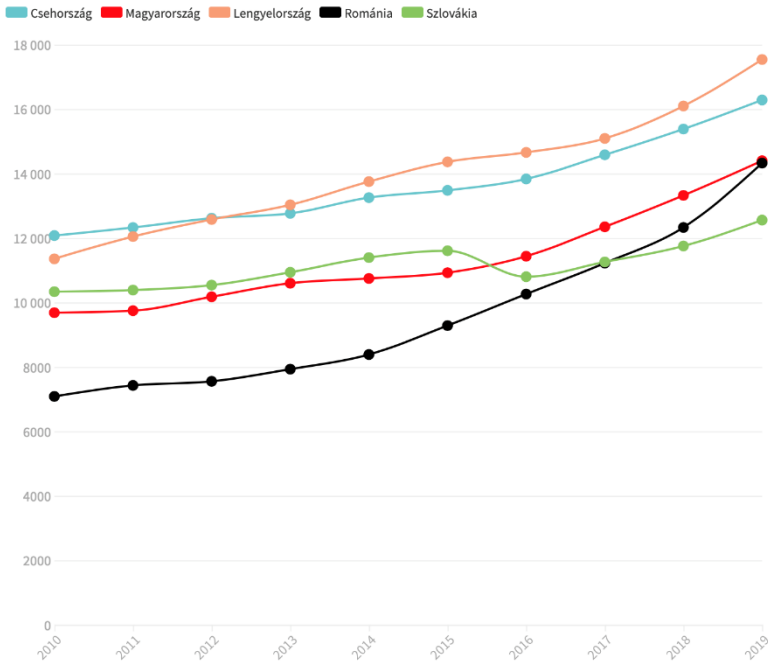
In euro terms, however, Hungary still has very low wages. Only Romania and Bulgaria have lower wages when expressed in euros.

Figure 1 **Wages across Europe in euro terms** (Source: Eurostat)



On purchasing power parity, Hungary does even worse. Wages are significantly lower than in Poland or the Czech Republic and even Romania has managed to catch up. Only Slovakia managed to underperform.

Figure 2 **Wages in the Visegrád region in local currencies, PPP. Czechia, Hungary, Poland, Romania and Slovakia.** (Source: Eurostat)



Actual individual consumption in Hungary is the lowest in the EU with the exception of Bulgaria. Croatia is at the same level.

Unemployment levels were very low in Hungary at the beginning of 2020. However, these are lowered by a massive public works programme, 6% of the Hungarian workforce working outside of Hungary, as well as a very short period of unemployment support, three months, after which job seekers fall out of this category.

Figure 3 **The unemployment rate in Hungary** (Source: Central Statistical Office)

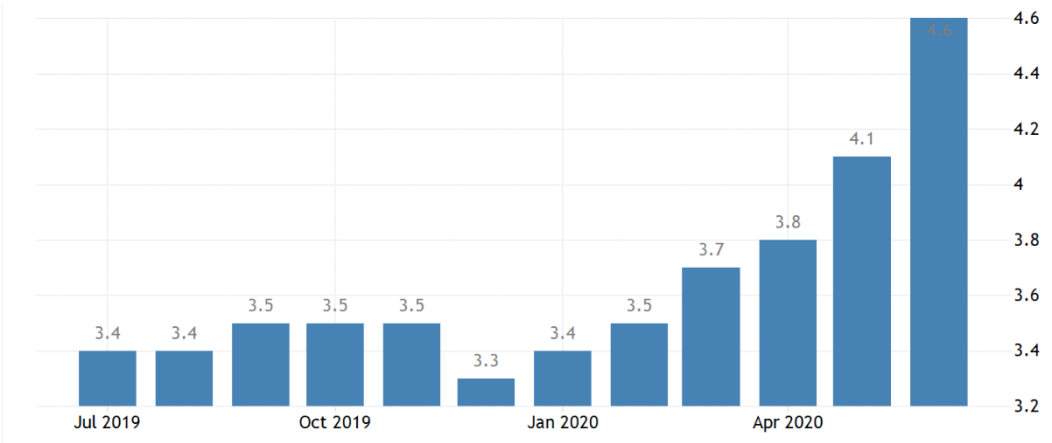
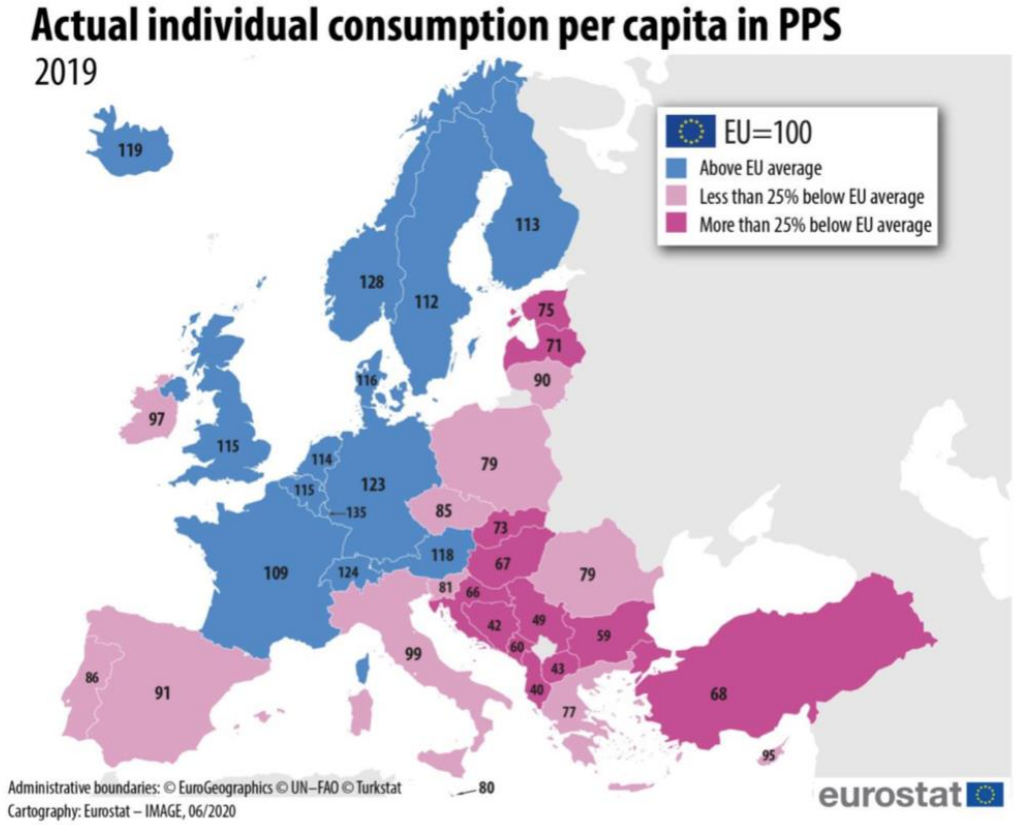


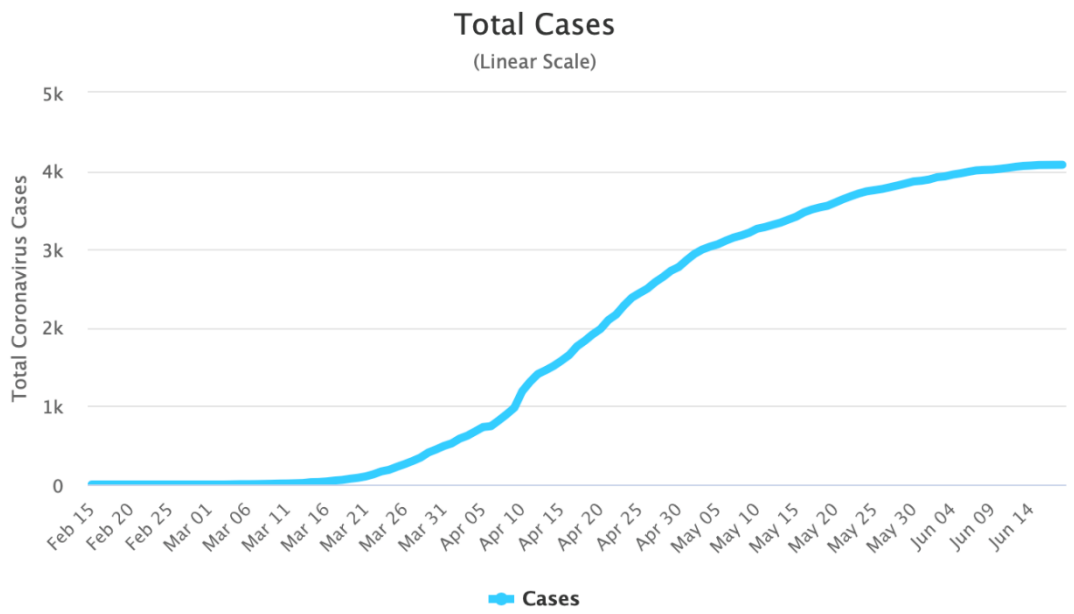
Figure 4 **Actual individual consumption as a percentage of EU average, 2019** (Source: Eurostat)



2. General response to COVID19

The first officially registered case of COVID19 in Hungary is dated in the middle of February. The following chart demonstrates the evolution of proven cases:

Figure 5 **Total registered corona virus cases in Hungary** (Source: Worldometer)

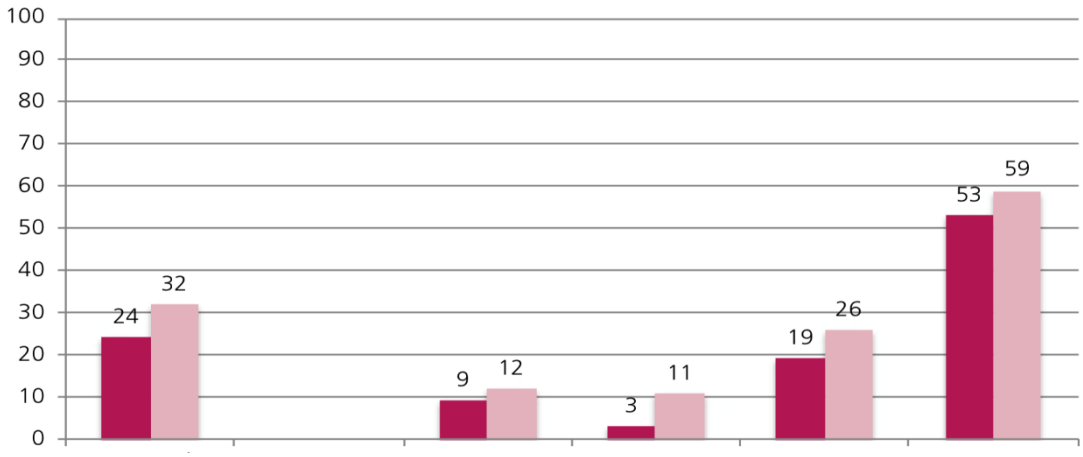


It is important to add that Hungary carried out far too few tests, and thus these figures should be treated as the lower bound. Actual infections are likely to be significantly higher.

By the middle of March, the government ordered a partial lockdown of the economy. This included:

1.) A total **sealing of the borders**, with only Romanian guest workers allowed to transit as they piled up at the Austrian border to return home to Romania. Interestingly enough, work visas were issued to some 25 000 seasonal agricultural workers in spite of the epidemic, primarily Ukrainian citizens.
2.) **Home office** for as many employees as possible. There is no accurate information as to what percentage of overall employees this affected, but a survey-based estimate is 32%.

Figure 6 **Home office amongst male and female employees with different levels of education: all, primary, vocational, secondary, university.** (Source: Fodor-Gregor-Koltai- Kovács, Fes 2020)

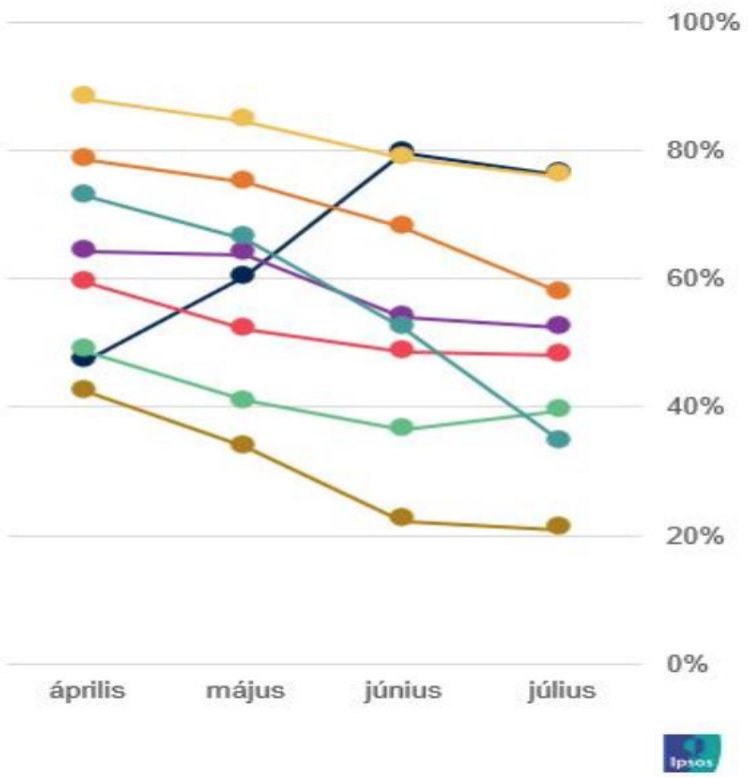


3.) The **closing of all schools** and universities. The Prime Minister initially resisted, but public opinion and the example of other European countries forced him to give in. Education moved online overnight, with the Prime Minister indirectly admitting that preparations for digital education in previous years had largely been a failure. This admission, however, did not lead to any serious effort to make up for this lack of preparation. Digital education took placed largely unsupervised and uncoordinated, with no support to poorer segments of society left cut off.
4.) The **suspension of all non life saving healthcare provision**. At the height of the crisis, some 30 000 hospital beds were emptied out, officially to make way for coronavirus patients. The opposition charged that this was an unnecessary move, resulting in the deaths of many patients who had been in critical conditions. Another charge was that the move was necessitated by the superspreading of the virus in hospitals amongst patients in critical conditions. No independent investigation has been carried out to substantiate these claims.
5.) The introduction of **separate shopping hours** for the elderly and the young.
6.) Incoherent communication on the wearing of masks in public spaces.

The Hungarian National Assembly also voted to give the government emergency powers, a move vehemently opposed by the parliamentary opposition. Part of these powers also included the suspension of the parliament itself, although de facto it continued its sessions. The emergency powers have since been returned.

We have a survey available about the actual behavioural responses of the population:

Figure 7 **Behavioural responses: frequent hand washing, avoiding handshakes, avoiding public transport, more chemicals at home, hand sanitizer, face mask, avoiding personal contact , keeping children away from public** (Source: Szonda Ipsos)



The measures were gradually lifted at the beginning of June. There is widespread awareness of a possible second wave, but no indication so far of it emerging. Human traffic from the rest of the world is still restricted, with the countries being categorised into green, yellow and red states. Most of the EU is green, while the United States is currently categorised as red.

There were some additional peculiar features of the response to the virus in Hungary. There was widespread militarisation of society during this crisis. Daily press briefings were held by two officials in uniform plus a civilian. Military was commandeered to 71 firms that were deemed to be of strategic interest, including ones in the following sectors: pharmaceutical, financial, energy, etc. Most of these were state owned enterprises, but others were not. The list included, for instance, the automotive supplier Bosch and the retail chain Auchan, but not other firms in the related industries. The official explanation was that the military could theoretically take over the operation of these firms in a situation of crisis, leaving commentators bewildered about how the military would have professional or technical expertise to do so.

The situation was exploited to take control of one particular firm, Kartonpack of Debrecen. The packaging enterprise had been disputed between the state and its owners, which included an entrepreneur that that been banned from managing the firm on account of his conviction in e major corruption scandal a decade or so earlier.

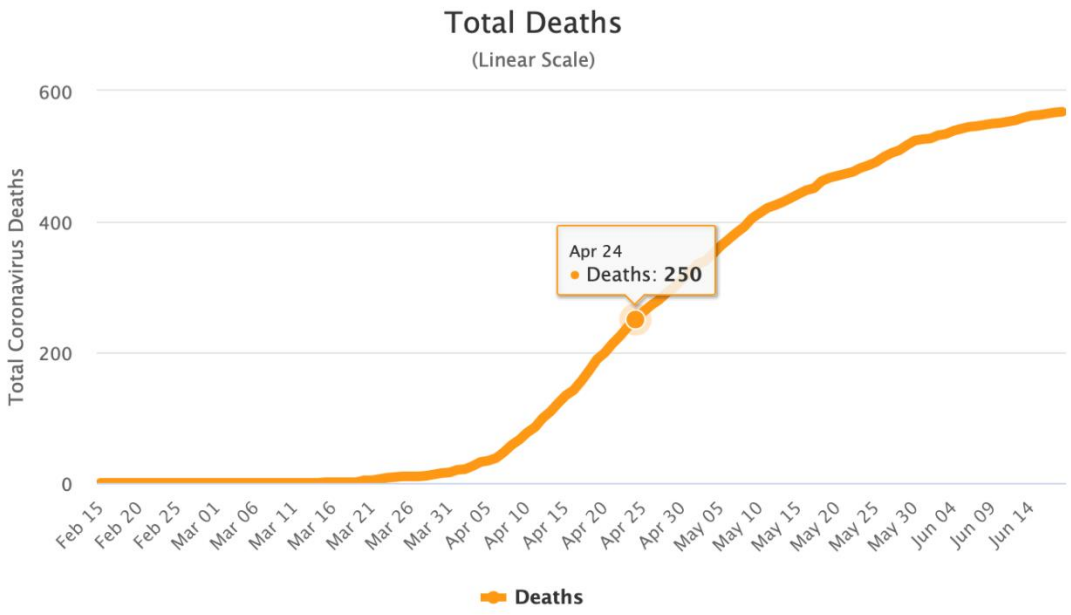
It is also significant that militarisation fits into the government's rhetoric of a permanent 'defense' against external enemies. Expressions such as 'war against the crisis', 'unlike in peacetime', and other militaristic language was consciously used in the communication.

Ironically, in the years preceding the virus crisis, the Hungarian government had been criticised for its spending spree on football stadiums by citing how many respirators could have been bought for hospitals instead. Thus at the beginning of the crisis, not unlike most other governments, the Hungarian foreign minister found himself in an international hunt for respirators. By June he had acquired some 10 515 of these. 10 097 are invasive, 418 non-invasive. The average price of a respirator was €56 647. For a population of ten million, this volume is generally regarded as more than adequate.

3. The impact of the lockdown

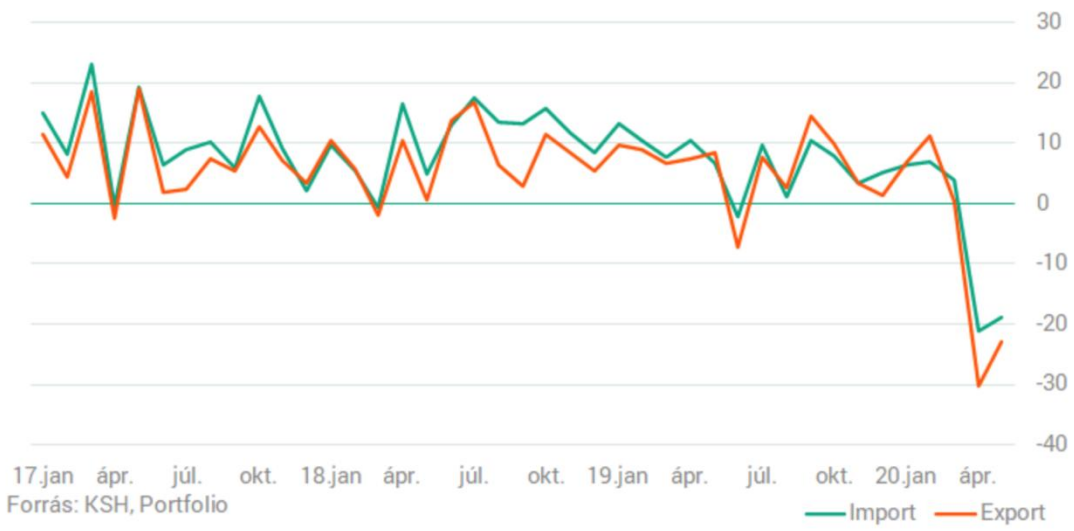
The result of the lockdown was a successful limiting of total deaths to below 600. Hungary's total population is below ten million. Thus we can conclude that measures of protection against the virus were largely successful.

Figure 8 **Total deaths from COVID19 in Hungary** (Source: Worldometer)



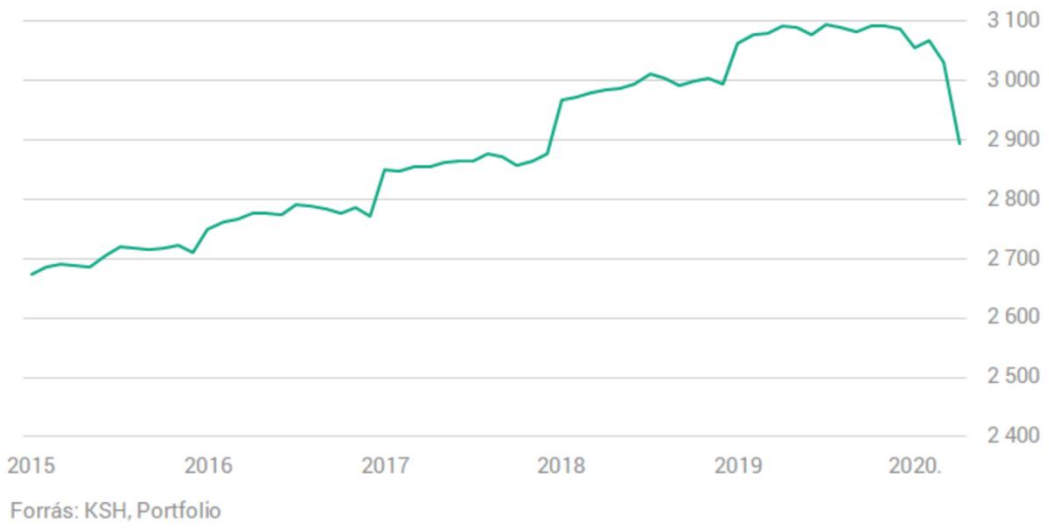
Hungary is one of the most open economies in the world; therefore it is highly dependent on both exports and imports. The sealing of the borders and disruptions in transnational production chains caused a massive fall in both imports and exports:

Figure 9 **Hungary's imports and exports** (Source: Central Statistical Office)



The drop in economic activity caused by the pandemic is also reflected in the severe job losses in this period. According to the figures from the Central Statistical Office, some 172,000 jobs were lost in March and April of 2020. Interestingly, a slow reduction in total employment had already been observable prior to the lockdown, which puts the total number of losses from the peak at around 200 thousand.

Figure 10 **Total number of persons employed in firms over 5 employees** (Source: Central Statistical Office)

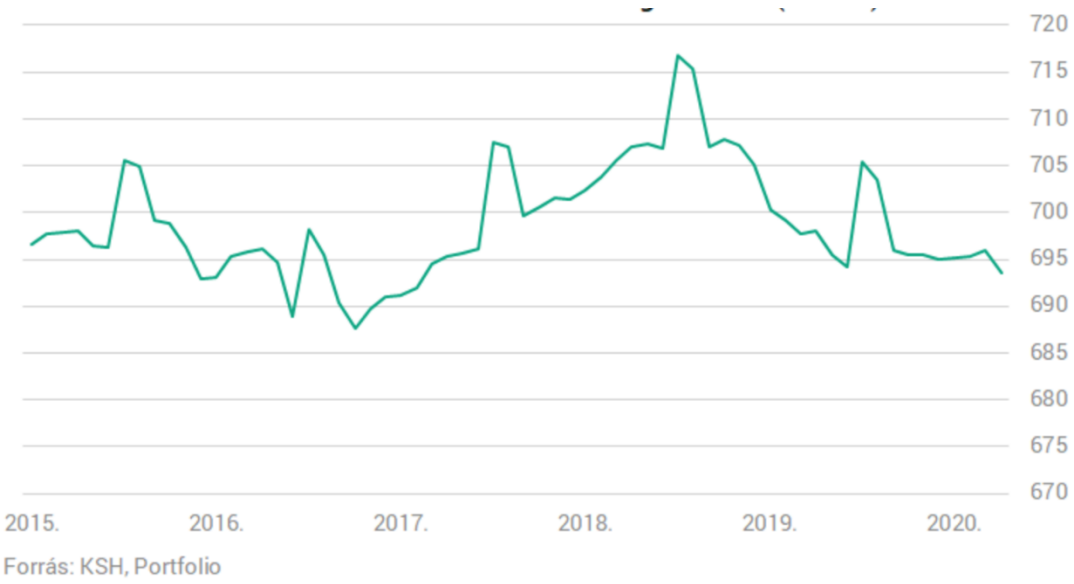


We have no accurate information about firms employing less than 5 people. It is likely that this sector has been hit quite severely, as they are rather vulnerable small firms for the most part.

The sectors that were hit the hardest were the hospitality sector with some 45 000 job losses, followed by 35 000 in retail, 30 000 in industry, and 11 000 in retail.

The state sector by and large stayed stable in the same period:

Figure 11 **Employment in the state sector in Hungary** (Source: Central Statistical Office)

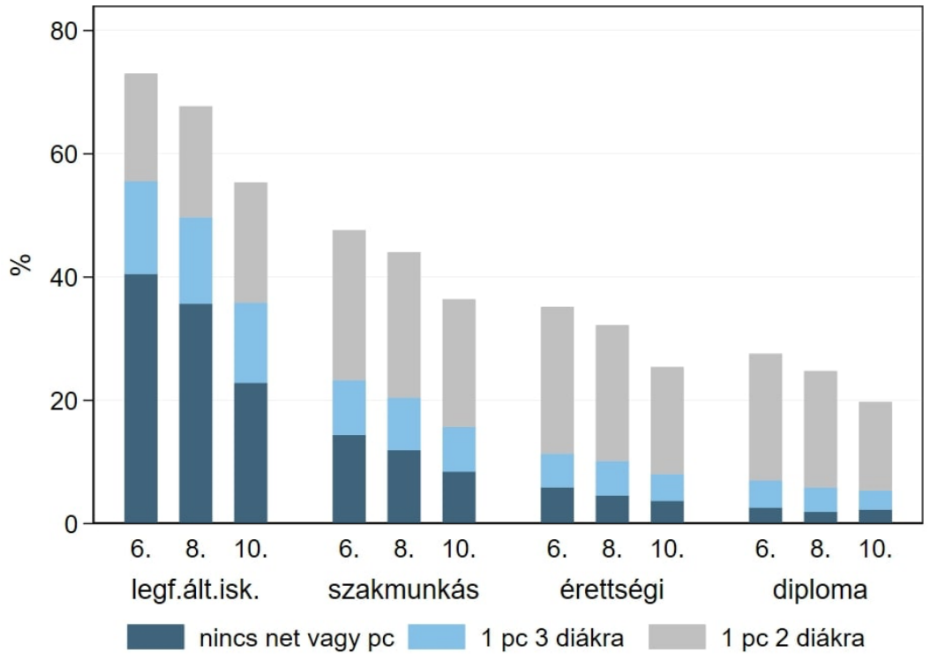


There are no official figures for the number of employees whose pay was reduced. The government claimed in the middle of July that some 260 thousand jobs were preserved by government crisis measures. The official headline unemployment figure increased from 3.3% at the beginning of the year to 4.6% in June.

It is striking how digital education was not monitored in this period. While we have survey-based knowledge that a significant segment of the student population did not have access to relevant technology and internet service, the government ignored the plight of this very exposed segment of the population.

However, a study by Zoltán Hermann exposed that there are indeed huge digital inequalities present in Hungary:

Figure 12 **Limited access to online education** (Source: Hermann)



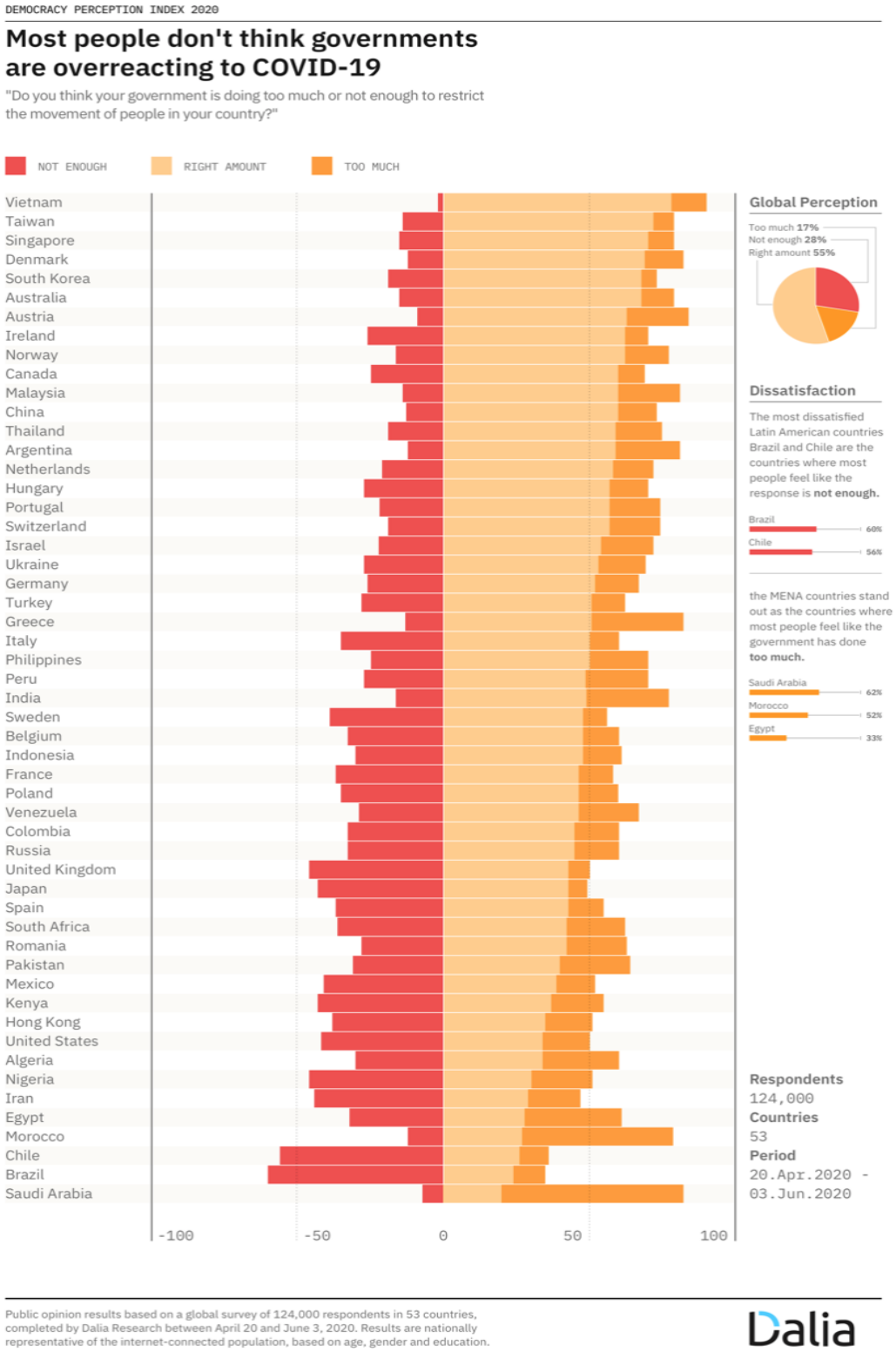
2. ábra Korlátozott hozzáférés az online távoktatáshoz évfolyam és az anya iskolázottsága szerint, 2017, százalék

The graph indicates that access grew with the lower completed educational level of the mother (elementary, vocational, secondary, university degree). Dark blue represents the complete absence of internet or PC, light blue three students per one pc, grey two students per one pc.

Based on this graph we can conclude that a significant proportion of students were effectively excluded from education during the lockdown, or their access was severely hindered. Since this was marked amongst the most disadvantaged groups, the lockdown increased inequalities of opportunity.

Most Hungarians were satisfied with the way the government handled the crisis:

Figure 13 **Satisfaction with government crisis response** (Source: Dalia Democracy Perception Index 2020)



4. The domestic economic response

The economic response of the Hungarian government underwent continuous changes during the course of the crisis.

At the beginning, in the middle of March, a first version of the response plan was published. This consisted of:

1.) An **Epidemic Defense Fund** to finance direct measures reacting to the crisis, including purchasing of medicine and medical equipment, building of emergency medical facilities, at HUF 633bn,
2.) an **Economic Defense Fund** at HUF 1346bn, with five pillars: employment preservation, employment creation, sectoral support, enterprise finance and the 'protection' (sic!) of families and the elderly. The latter includes a rise in pensions, but only to the extent of a single week, divided over two years, starting only from 2021.
3.) **off balance sheet** easing of credit repayments, easing of credit conditions etc. at HUF 7-8000bn.

A large part of the funding for the Economic Defense Fund was to come from austerity in certain other parts of the budget, including a massive, 1000bn cut to the budgets of local governments, educational institutions and political parties. It would include wage support, and the lowering of certain taxes on small enterprises. In the communication of the government, all crisis response taken together would amount to as much as 20% of GDP. By far the larger part of this would be made up of off budget items.

Over time, it became clear that the budgeting of these funds would change somewhat. The Epidemic Defense Fund has spent HUF153bn on extra wages for health workers, and HUF609bn on the purchases of medical instruments. Thus at HUF761bn it exceeded its planned budget.

The off budget items, on the other hand, have shrunk in size. They included HUF3600bn on a moratorium on loans, HUF1694bn on new capital guarantee and loan programmes, as well as HUF1500bn on the continuation of an already existing subsidised loans (funding for lending) programme for small and medium sized firms. Altogether, the off budget items would amount to HUF6794bn, lower than the previously foreseen amount.

Most change was implemented in the Economic Defense Fund. Most of what had previously been a part of it is now funded by European Union resources the HUF volume of which has increased due to the depreciation of the Hungarian forint during the course of the crisis. The items now financed from EU resources includes:

- Wage support (HUF200bn)
- Job creation (HUF80bn)
- R&D sector wage support (HUF32bn)
- Support for SMEs (HUF78bn)
- Digital literacy trainings to retain employment (HUF7bn).

All in all HUF397bn, all from EU funds.

The EDF now includes a HUF160bn item, consisting of tax cuts that had already been part of the budget plan back in 2019, for instance the 2% cut in social security contributions. It also includes surprising items, such as funding for the Chinese built Belgrade-Budapest train line and the national space programme. The explanation for these incongruities is the following: the government first raided the budgets of state and local government institutions, then received the go ahead from the European Commission that it can finance a large part of the expenditure from EU resources, and in turn started to funnel back spending to state expenditure unrelated to the virus. All along, the size of crisis spending remained at 20% of GDP, consistently communicated in the media by government politicians.

It is also significant that the terminology fits into the government's rhetoric of a permanent 'defense' against external enemies. Expressions such as 'war against the crisis', 'unlike in peacetime', and other militaristic language was consciously used in the communication.

Most attention was focused on the Economic Defense Fund. However, accurate information was hard to come by. Details were leaked in a piecemeal fashion, proved to be at a preliminary stage of project development, were often contradictory and ambiguous, and were sometimes later revoked or modified. It was to consist mostly of wage support programmes, direct support to firms, as well as allowances on tax payments. The financing for the programmes was to come from austerity measures on ministries, universities, local governments and political parties.

In the middle of June, when the virus reseeded, the government started the emptying out of the Economic Defense Fund. This continued with a second batch in July. Altogether some HUF570bn has been diverted elsewhere, some 43% of the original amount. The target areas of this diversion range from the Hungarian Village Programme, through bus and rail transport, waste management, gas procurements, recapitalization of the Paks Nuclear Energy Company, and so on.

All in all we can conclude that the structure and effective volume of economic crisis response has remained highly opaque during the entire period of the crisis.

GDP figures

Based on available data on disruption caused by the virus, as well as the economic response of the government, we are faced with a surprisingly divergent range of forecasts about GDP growth for 2020 in Hungary.

We have a factual figure of positive 2.2% growth for the first quarter. There is also a forecast available for the second quarter from the Finance Ministry, estimating the slump at -9.9%.

As for the entire year, the Hungarian National Bank is the most optimistic of all, insisting on a positive growth figure between 0.3% and 2%. The Finance Ministry is more pessimistic, calculating with a negative 3% slump. The Reuters consensus of market analysts averages at -5.1%, while the updated forecast of the European Commission stands at -7%. Naturally, much depends on whether there is a second wave of the virus, but these forecasts reckon with a third and fourth quarter rebound, without a second wave.

5. Response to EU Crisis management

The European Union responded by proposing a €750 billion Reconstruction Fund. Of this, €500 billion would take the form of non-repayable support, and €250 so called corona bonds. The European Commission would issue 3-30 year bonds at and AAA rating, which it would pass on, in case of demand, to member states.

The novelty of these bonds is that they are to be issued jointly by the union. This would diversify the varying risks ratings of member states, allowing riskier states (such as Italy) to access cheaper loans. This would in turn prevent these states from running up an even larger mountain of debt as a consequence of the corona virus crisis. Such an instrument had previously been greatly resisted by the richer member states, which had considered themselves less risky and therefore could issue debt with a lower yield. The so-called Frugal Four (Austria, Denmark, Netherlands and Sweden) still resisted. However, the breakthrough moment came with Chancellor Angela Merkel, formerly a staunch opponent, switched side to back the plan.

There was also a proposition by financier George Soros for a perpetual bond. However, this proposal was quickly rejected by EU leaders. There are serious concerns about Soros' proposals. Given longer-term uncertainties, it would be very difficult to price in such a paper. The current market conditions (low inflation as well as low, sometimes even negative yields) are unlikely to persist over a very long-term horizon. While very long-term bonds by Austria for instance have been successful, ones issued by Argentina have been a disaster. It is questionable whether investors would really be interested in such an instrument. It is also not clear who would be the issuer. The recent exit from the Union by Britain begs the question of longer-term payments in case the European Union would shrink further or disappear altogether.

The rejection by the EU did not stop Viktor Orbán, however, from including the Soros proposal in his latest 'national consultation' (a frequently held referendum of sorts, but of dubious methodology, representativeness and reliability) on the European plans.

In his first radio interview, Orbán sounded skepticism about the European solution. He claimed that issuing bonds is a problematic way of financing, as it is not based on any existing achievement, but on future promises. Loyal journalists did not press him on why he is not concerned about this same aspect in the case of massive loans he is taking from Russia to finance the extension of the Paks nuclear power plant, or from China to build the Belgrade-Budapest high-speed train route, amongst other similar megaprojects. He does not give interviews to non loyal journalists.

Orbán also expressed his worry about a potential default by weaker Southern European economies, in which case Hungarian citizens would be forced to foot the bill.

He also criticized the distribution of the amount, calling it 'absurd and perverted' that richer member states would receive more than poorer ones. The reason for this is the actual impact of the crisis. Richer member states such as France, Spain and Italy were hit harder by the virus. Amongst others, they have large tourist industries, which were completely halted. At the same time relatively poorer Central and Eastern European member states (with the exception of Slovakia and Romania) were affected relatively less by crisis. Whether this was due to their professional and early response, or also because of previous universal vaccinations, still needs to be established. However, the fact of the matter is that this time around it was richer member states that were affected more.

Still, according to this arrangement, Hungary would be the recipient of some €15 billion: 8.1bn in direct support and 6.9bn in loans. Even when netted out, this is a generous amount that can be invested into the Hungarian economy. As a comparison, Hungary currently issues longer-term debt with higher yields than the expected yield on the AAA corona bonds: 2.02% for ten-year treasuries, and 2.36% for fifteen year ones. Yields on an even longer-term bond would approach 3%.

At the European summit on crisis response, Orbán threatened to veto, insisting that any rule of law conditionality could not be part of the final text. In the actual text, however, a mild reference to rule of law does appear, but experts are divided over how strong this wording is. The European Commission insists that it is indeed tough wording, while Orbán returned home claiming triumph. The European Parliament, which still has to discuss the plan, has issued a five party declaration (which includes Fidesz's grouping, the European Peoples Party) in which they call for a stronger wording.

Figures

Literature