

REPUBLIC OF HUNGARY
MARCH 2009

CREDIT GUARANTEE COUNTRY PROFILE:

IES/02: ATTACHMENT N

Country Rating	S/T Business Cycle Indicator	S/T Political Indicator	Debt Recovery
2B	↓	→	Debt recovery would prove more effective through the use of collection agents.

Credit Guarantee Experience

We are open for cover in this market without any restrictions. Our experience in this market has been favourable.

Political Highlights

- ❑ Chief of state since August 2005 is President Laszlo Solyom. The president is elected by parliament and has little power. The EIU had earlier expected Prime Minister Ferenc Gyurcsany to face an internal leadership challenge before the 2010 parliamentary election; however that is now unlikely after passing of the budget at the beginning of this year. Elections to the European Parliament will be held in June this year.
- ❑ Hungary is a multiparty democracy. In April 2006 the Government led by the Hungarian Socialist Party (MSZP), became the first to win re-election. The MSZP renewed the coalition with its junior partner, the Hungarian Liberal Party (SZDSZ), but the SZDSZ left the coalition in April 2008 following a dispute over reforms and the MSZP is now governing in minority.

Effects of the global financial and economic crisis

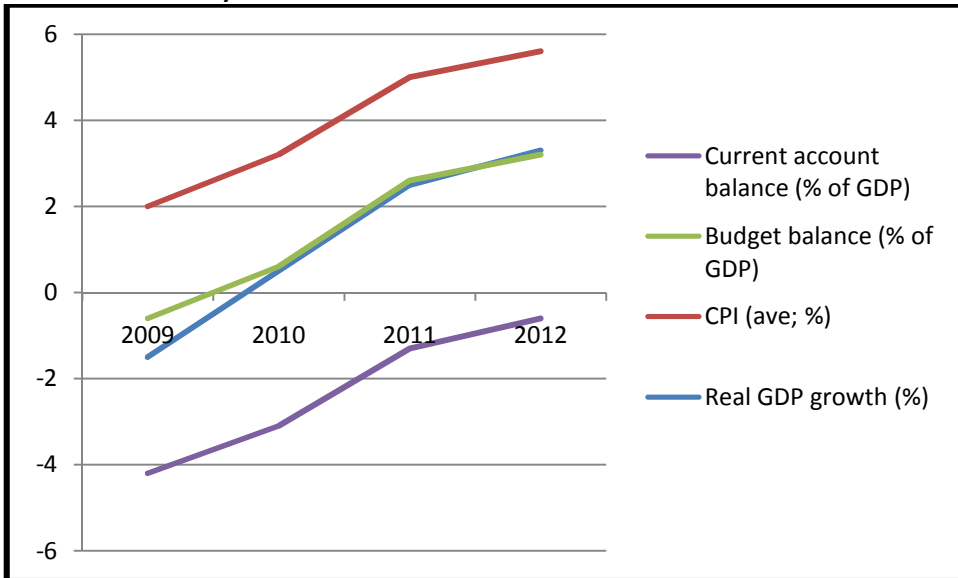
- ❑ Although Hungary's economy is not directly affected by the crisis in the US banking system, the resulting tightening liquidity will make it more difficult and expensive for Hungarian banks and businesses to borrow, leading to negative effects on exports and growth of the real economy.
- ❑ In October last year Hungary found itself particularly vulnerable due to its heavy debt burden and was the first EU member state to have sought a stand-by loan from the IMF since the financial turmoil in mid-2008. Public debt was estimated at 70.2% of GDP in 2007. Government financed itself in part with foreign currency loans and average Hungarians who also flocked in droves to banks for once-cheap loans in Swiss francs and euros to buy their cars and houses (*nearly 90% of loans to households in the year to October 2008 were in euros and Swiss francs*) found themselves with ever rising debt repayments due to currency fluctuations as concerned investors began pulling their money out of the country. About 60% of loans in Hungary are denominated in foreign currency, including €7.3bn or 9% of GDP represented by the home loans.
- ❑ The government obtained a support package for the country's banks, to be funded from the \$25bn credit line provided to Hungary by the IMF, the EU and the World Bank. The IMF-led bailout ensures that Hungary will be able to finance its large debts even if foreign investors' appetite for Hungarian assets does not improve this year. Implementation of policies must be consistent with the IMF programme so as to maintain investor confidence and minimise the depth of the economic downturn.
- ❑ Hungary's government has agreed on a plan to temporarily assist, with guarantees to those who have lost their jobs because of the economic crisis and have trouble repaying their home loans. The state guarantee will be up to two years on reduced installments for clients who request eased repayment conditions for loans taken before September 1, 2008. The Swiss National Bank said it will provide Swiss franc liquidity to Hungary's central bank, as the Eastern European country struggles to restore financial stability. The measure will be in place until the end of April.
- ❑ Ratings agency, Moody's lowered Hungary's local and foreign currency government bond rating to A3 from A2 in November 2008 after the country was forced to seek financial help of the IMF and EU to avert crisis. In February it kept the rating unchanged and says for now it's comfortable with Hungary's A3 debt status, but the country's economic outlook and large foreign currency-denominated private debt pose a risk.

Economic Highlights

- ❑ The population of Hungary was estimated at 10 million in 2008.
- ❑ The Hungarian economy is forecast to contract 2.4% in 2009 compared to a contraction of about 1.4% estimated for 2008 due to a downturn in Hungary's main export markets in Western Europe and a tightening of lending conditions. The European Bank for Reconstruction and Development projects a 2% economic contraction in Hungary in 2009. The economy is expected to return to positive growth in 2010 as the euro zone recovers.
- ❑ Inflation is projected to fall to 3.2% in 2009 and 2.7% in 2010 from 6.1% in 2008, as commodity prices fall and domestic demand falters. The National Bank of Hungary has a 2 to 4% medium-term inflation target.
- ❑ The current account deficit is expected to narrow to €6.4bn in 2009 from €7.8bn in 2008. The drop in domestic and export demand will hurt profitability and result in a cut-back in investments, a drop in production and layoffs. The arm of the country's Central Statistics Office, Ecostat, sees investments falling 3.2%, exports dropping 4.5% and imports declining by 5.9% in 2009. Ecostat projects the biggest fall in export demand for machinery, electric equipment and automotive sectors.

- Prime Minister Ferenc Gyurcsany aims to further reduce the general government deficit- one of the conditions to foreign lending -to 2.6% from this year's revised target of 3.4% of GDP. Ecostat estimates the general government deficit at 3.1% of GDP in 2009.

EIU forecasts for key indicators



- The Forint (HUF) is expected to trade around 300 to the euro in the first half of the year and firm by 20-30 forints by year-end due to improvements in external financial conditions.
- Industrial production contracted 7.2% y/y in October 2008, the largest decline in 16 years. The growing number of layoffs are in construction businesses, automobile and electronics manufacturers (including Suzuki and Nokia).
- The number of company liquidations in Hungary rose 17% y/y in 2008, including 32% y/y during the Q4'08. A total of 11,504 companies were liquidated with a record 3,400 companies in Q4'08. 9,715 companies were wound up in Hungary in 2008. Despite this, an all-time high 48,500 companies were founded in Hungary in 2008, surpassing the previous record set in 2004 by almost 10,000. According to a company director, the increase in company start-ups could be deceptive as there are sectors in which the founding of companies is not indication of economic growth, but of fraud. In the construction industry, for example, companies with unpaid bills often shelter their jobs and instruments in new companies.
- Hungary joined the EU in 2004 but preparations for joining European economic and monetary union (EMU) and attempts to regain and sustain catch-up growth rates above the EU average will pose tough policy challenges in the coming years. The EIU expects Hungary to be ready for accession to the EMU only in 2013-14.

Trade Developments

- Major exports: machinery and equipment, other manufactures, food products, raw materials and fuels and electricity.
- Major imports: machinery and equipment, other manufactures, fuels and electricity, food products and raw materials.
- Main trading partners: Germany, Italy, France, Austria, UK, Romania, Poland, China and Netherlands. About 80% of Hungary's exports are now directed to the EU. Austria is the third largest foreign investor in Hungary after Germany and Holland.
- South African exports to Hungary totaled R112m in 2006 and R240m in 2007. South Africa's main exports to Hungary include iron ore, steel, coal, fruit and vegetables, spices and cut flowers. Hungary's main exports to South Africa include machinery, electronic equipment and meat (pork) products. South Africa is accorded GSP (generalised system of preferences) GSP status by Hungary.

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