Macroeconomic and financial environment in 2020

The Covid-19 pandemic turned the world upside down in 2020, putting to the test not only health care, but causing interruptions in many areas of everyday life as well as the economy. Initially, it was the possibility of supply chain disruptions that caused worries, then the uncertainty resulting from the measures to stymie the spread of the virus that alarmed markets. The first, spring wave of the pandemic was like a cold shower for Europe and the USA, where unprecedented distancing measures limited free movement, practically bringing life to a standstill for a while. The summer offered a short time to take a breather and prepare for the next wave, which peaked between October and December in the developed world. Meanwhile, fiscal and monetary policies made great efforts to get the economy back on its feet, offering practically unlimited liquidity, low-interest loans, wage and investment subsidies, and tax credit. As a result of hard work, the first covid vaccines have been developed and authorized by December, to be followed by similar preparations very soon.

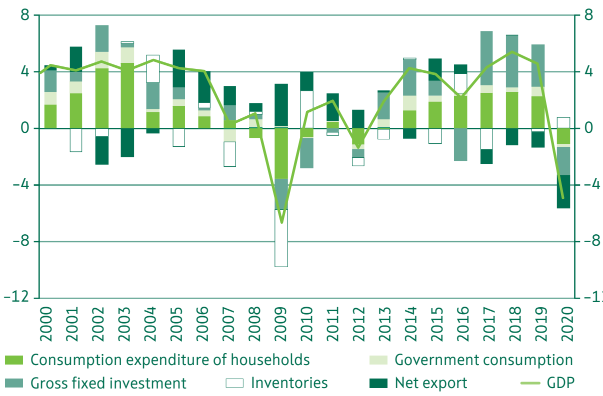
This was not a 'usual' financial crisis; the recession is very fast and huge, like never before. In 1Q 2020, the CEE region fared better than Western Europe, as the pandemic arrived somewhat later, and growth dynamic was in better shape in most parts of the CEE region than in the EZ. The second quarter brought big recession to all OTP countries. Countries where the share of the auto and related industry is higher have suffered a sharper drop in industrial production. The CEE region's countries were usually in a much better shape than in 2007, with a much better vulnerability profile. Economic policy reactions were extremely aggressive throughout the region. Until now, we have not detected large-scale capital flight from developing countries. The labour market and credit market reaction were not intense. Most countries showed a decent recovery in 3Q. Contrary to the initial expectations of a renewed recession due to second-wave lockdowns, almost all OTP countries posted positive q-o-q growth rates for 4Q 2020. This stems from the facts that (I) industry remained resilient (II) consumer sentiment did not collapse (III) the service sector adapted somewhat to the pandemic.

Among the countries where OTP is active, Serbia performed by far the best, with just 1% recession, due to strong investment activity and FDI inflows. GDP dropped between 3 and 5% in of the OTP universe countries; Hungary (–5.0%), Slovenia (–5.5%), Bulgaria (–4.2%), Romania (–3.9%), Russia (–3.1%), Ukraine (–4.0%). In these countries the value added of the manufacturing industry is relatively high, while that of tourism is less significant. Moldova (–7.0%) would also belong to this group if there had not been a major drought, which significantly worsened the performance of the really important agriculture sector.

While almost all industries have been negatively affected by the spread of Covid-19, it has had a bigger impact on some of them. Tourism is one of the sectors hardest hit by the coronavirus crisis, with some parts of the sector and some regions affected more than others. Most tourist facilities were closed during the peak of the crisis, with events cancelled or postponed. This is also true for the most tourism-driven OTP countries. Montenegro (–15.2%) and Croatia (–8.4%) suffered the biggest losses in this field.

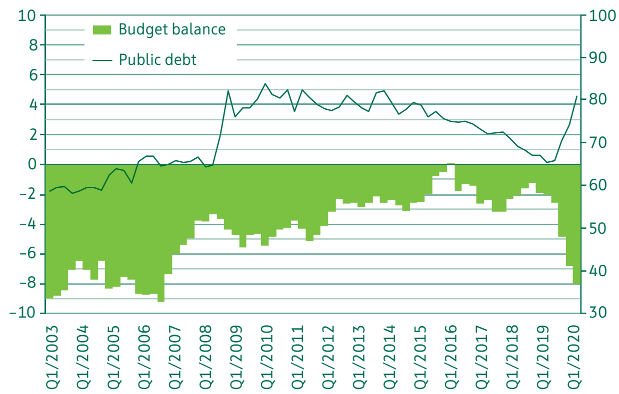
Year 2020 was dominated by the pandemic also in Hungary, where the epidemy, and thus the lockdowns started later. Based on detailed data, the economy sank into 5.0% recession; the smaller-than-feared contraction owes a lot to the supportive fiscal policy and to the fact that restrictions in the fourth quarter were not as tight as in the spring. Hungary's budget deficit slightly exceeded 8.0% of GDP, and public debt ballooned to 81% of GDP. The lockdowns hit the labour market hard, but most of this effect proved to be transitory, except for some sectors.
The recent years' double-digit increase in wages has significantly decelerated, but household saving rate has markedly increased, because of a drop in consumption. Despite the economic downturn and the lockdowns/restrictions, dwelling construction hit a ten-year high.

Use side decomposition of the GDP growth (%)



Source: KSH, OTP Research

Public debt and deficit (in % of GDP)



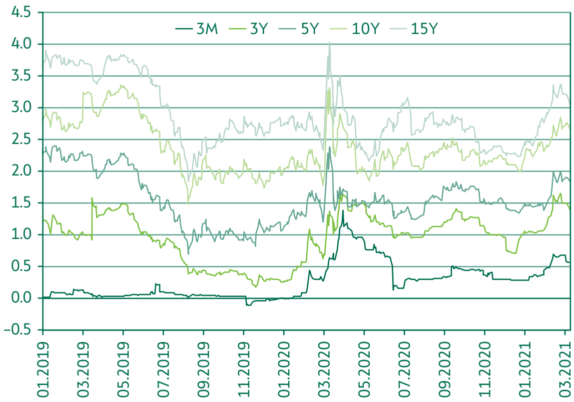
Source: KSH, OTP Research

Despite the coronavirus, both retail (14%) and corporate loan (nearly 13%) volumes expanded in 2020. Within retail loans, the subsidized 'baby loan' was the engine of growth, the volume of which has jumped by 130%. Despite the declining new business figures stock of the personal loans surged also by 12% thanks mainly to the moratorium which resulted in lower instalments. Housing loans increased by 10%, while home equity loans shrank by almost 5%.

In Hungary, inflation slowed to 3.3% from 3.4% in 2019. Constant tax core inflation, which is particularly monitored by the MNB, accelerated to 3.7% from 3.4% in 2019. In the second quarter, due to the collapse in oil prices, inflation slowed to 2.2% from 'above-4% territory' at the beginning of the year. After reopening, the inflation has started to pick up again in the summer months. Due to the lockdown measures, there has been a significant rearrangement in the structure of demand; decreased services and increased demand for products. The latter, supplemented by the weakening forint exchange rate, contributed significantly to the rise in industrial goods inflation.

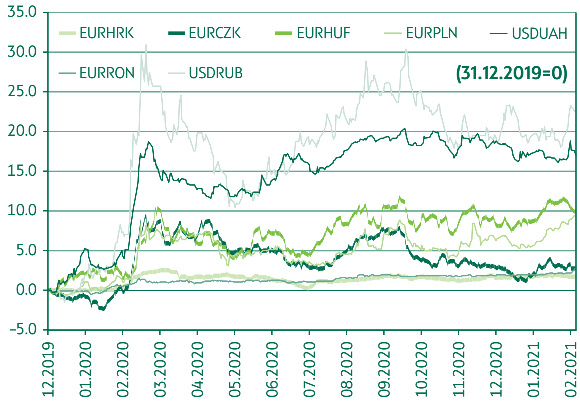
As a result of the changed external environment, Hungary's monetary policy adjusted it' monetary policy tools. Amid the stronger risk appetite at the time when the covid crisis broke out, the forint weakened, trading at 360 versus the euro, before the exchange rate stabilized, though with marked volatility. The EUR/HUF stood at 365 at the end of the 2020, almost 10% higher than a year earlier. Due to the rising budget deficit, it is becoming increasingly important for monetary policy to provide cheap financing to government and the corporate sector through asset purchase programs.

Hungarian yield curve (%)



Source: MNB, AKK, OTP Research

Exchange rate development in the CEE countries



Source: Reuters, OTP Research