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Statement by Mr. Schwartz and Mr. Calderón-Colín on Hungary
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Executive Board Meeting 05/52
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Nearly a year after gaining access to the EU and pledging its adherence to the EMU in 2010, it is not clear whether the authorities have realized the significance of their commitments given the path of policy implementation they have adopted. It appears from the report that, after being mentioned frequently as a good example of economic transition during the nineties, the current policies are not well suited to attain the degree of economic convergence required to be a part of such group or benefit from it. Economic performance in the EU has been difficult in recent years and this group requires that new members contribute in an efficient and positive manner. Unless further fiscal consolidation, a clear definition of monetary targets, the abandonment of exchange rate targeting and further progress in the structural front are attained, it does not seem plausible that Hungary will retain the current level of market confidence. If the gap between Hungary and its peers continues widening, as the day in which the euro would be adopted is nearer, markets will eventually price their assessments.

The pursuit of economic policies to prepare the economy for the monetary integration should be a priority. Among Maastricht criteria, currently, Hungary only meets that of public debt, but given the fiscal path it seems likely that it will also fail it in the near future. Achievement of the other criteria appears difficult given the lack of commitment in fiscal issues and the absence of prudent macroeconomic policies.

The degree of economic consolidation, as stated by staff, is lower due to accounting and methodological issues. A continuous lack of achievement of fiscal targets, the higher risk to miss them this year due to the possibility of overspending given the political cycle and the level of GDP considered in the budget, call for an accurate use of expenditure controls and use of reserves. The recent discussion on Public Investment acknowledged the benefits that PPPs can bring and also set out its limitations. The cases of Brazil and Colombia were presented as good examples of PPPs management, including provision of resources for future payments.

We are surprised to hear from staff a justification for considerable large current account deficits such as the current and expected for the next years in Hungary. Recent financial crises have highlighted the risks and vulnerabilities of such levels of deficit. Considering that only approximately 40 percent of the current deficit is financed by FDI, the risk is higher. We wonder if—abstracting from the case of Hungary—such justification for large current account deficits is shared among different area departments within the Fund. It would also be interesting to know whether catch-up models are used consistently also in other emerging market reports.

On the monetary side, as staff, we are concerned that indicating the markets what the authorities consider the appropriate level of exchange rate could undermine the effectiveness of the inflation targeting framework. Before further refinements to the current framework, we consider that a more clear signal from the central bank stating inflation as its main and only objective could contribute to deter misunderstandings or loss in credibility. With respect to the financial assessment and its recommendations, we don't think that informing borrowers of the foreign exchange risk would be enough to reduce vulnerabilities. Additional provisioning should be considered, in line with EU prudential directives.

On the structural front, progress should be aimed to prepare the economy for convergence and the adoption of the euro. Good examples of efficient and positive use of EU funds are available and Hungary should take advantage of these resources. They are a luxury that not many emerging countries can afford in their quest for economic improvement.