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The Chairman's Summing Up at the Conclusion of the 1982 Article IV  
Consultation with the Hungarian People's Republic  
Executive Board Meetings 82/156 and 82/157, December 8, 1982

On the occasion of the first Article IV consultation with Hungary, Executive Directors also considered and approved requests for a stand-by arrangement and for a purchase under the compensatory financing facility. Much of the discussion therefore focused on the efforts made by the Hungarian authorities to improve the balance of payments position. It was generally recognized that the high level of external debt, together with the high proportion of short-term debt and renewed pressures on the current account since 1981--which reflected in part delayed and too timid adjustment measures--were among the main reasons for the very serious liquidity problems facing Hungary in the first quarter of 1982, although it was also noted that events in other countries had indirectly contributed to these difficulties. The large capital outflow in early 1982 gave the Hungarian authorities no option but to accelerate substantially the improvement in the current account vis-à-vis the convertible currency area.

Directors welcomed the new initiatives of economic reform and the strengthening of demand management policies aimed at external adjustment since 1979, although they observed that the tightening of policies had initially been rather gradual and that slippages had occurred in 1981 and early 1982. Directors considered that policies had been markedly changed in the right direction with the new measures introduced in the course of 1982, and they commended the Hungarian authorities for their determination and for their flexibility in the formulation of economic policy.

Directors noted that the brunt of the adjustment effort had until recently been borne almost entirely by investment, and they expressed concern about the longer-term implications for the competitiveness of the economy. However, they observed that the measures adopted since mid-1982 to restrain the growth of real private incomes meant that consumption was currently bearing a greater share of the burden of adjustment. Directors referred in particular to the commitment to a 4-5 per cent decline in real wages in the 1983 plan, which they regarded as a courageous decision and an important element in the program for the coming year. In this context, while welcoming the recent increases in prices of some subsidized goods and the adjustment of various fuel prices for consumers, many Directors stressed the need for a further major reduction in subsidies as well as for further corrective price adjustments.

With respect to credit policy, it was felt that the easy availability of credit to enterprises had contributed to the country's difficulties in 1981. The gradual tightening of credit policy, especially since mid-1982, was welcomed. It was noted that most borrowing interest rates for enterprises were positive in real terms, but that deposit rates were becoming increasingly negative in real terms. Higher deposit rates for

households were considered desirable as a way of preventing a decline in the savings rate. Directors also stressed the importance of reorganizing the financial market and developing investment instruments. They welcomed the containment of the state budget deficit below the level foreseen in the budget plan in 1982 and the further cut envisaged in 1983. It was noted, however, that further and durable improvement of the budget would depend very much on the success of efforts to reduce the burden of subsidies, which remained excessive and continued to account for about 30 per cent of budget expenditure.

Turning to the balance of payments, Directors welcomed both the marked reduction in the current account deficit achieved in 1982 and the planned surplus for 1983. They expressed appreciation for the fact that the bulk of the improvement had been brought about through demand restraint and through measures designed to stimulate exports or to raise productivity. However, a number of Directors regretted that part of the improvement had been the result of administrative measures aimed at reducing imports. They attached considerable importance, therefore, to the commitment in the letter of intent to eliminate these restrictions during 1983. A number of Directors also noted with regret the restrictions maintained abroad that seriously hampered Hungarian exports and made the adjustment process much more difficult. Directors noted the depreciation of the forint by 7 per cent in July 1982, and more recently by a further 4 per cent in two stages, and welcomed the intention of the authorities to continue to follow an active exchange rate policy in the months ahead. Given that the projected increase in exports had struck a number of Directors as rather ambitious and perhaps too optimistic, and in view of the commitment to eliminate import restrictions, Directors considered an active exchange rate policy to be of crucial importance.

Directors stressed that, even if the target of a US\$600 million surplus on current account in convertible currencies was achieved in 1983, the liquidity position would remain precarious. In view of the high level of debt and heavy burden of maturities foreseen for 1983 and beyond, it was recognized that the external situation would remain heavily dependent on the attitudes of foreign lenders, which reinforced the importance of implementing a strong adjustment program that would bolster the confidence of foreign lenders in Hungary's policies and prospects. Directors emphasized the need for the authorities to take additional adjustment measures if developments in export and capital markets should turn out to be more unfavorable than expected. The provision of adequate information on economic developments and policies in Hungary was also viewed as desirable, as lack of information could contribute to a lack of confidence on the part of foreign lenders.

Executive Directors supported the Hungarian authorities' determination to pursue the reform of the economic system at the same time that they were making more immediate policy adjustments. In this connection, Directors attached great importance to the desirability of transferring resources from the less efficient to the more dynamic sectors and enterprises of the economy as well as to the need for promoting greater domestic and foreign competition.