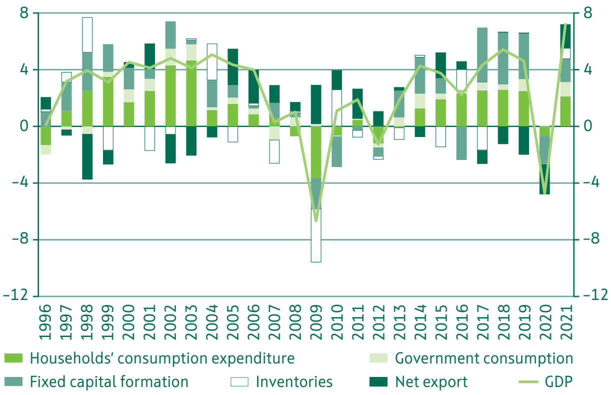
Macroeconomic and financial environment in 2021

2021 was not an easy year either. The operational environment of the financial sector were driven by the economic and labor market recovery following the deep recession of 2020, but new waves of epidemics and soaring energy prices in the second half of the year were strong headwinds. Luckily as vaccination programs progressed, less drastic measures proved sufficient to contain the epidemic, so the economic impact of the spring and autumn lockdowns of 2021 was much more modest than a year earlier.

By the middle of 2021, GDP in most economies had reached pre-Covid levels, with economic growth in the OTP countries typically falling between 4-7% for the year as a whole, but the Montenegrin and Moldovan economies were able to grow at double-digit pace. At the same time, employment also reached the level of the end of 2019, so labor shortage, one of the main problems of the pre-Covid period returned to the region. The recovery also brought an unexpected guest, not seen for decades in the developed world: high inflation. To offset the effects of the epidemic many fiscal and monetary measures have been implemented to support the economy. These measures kept demand strong, however the structure of consumption shifted sharply from services to goods. While in 2020, this meant that demand for some products exploded, while for others it fell sharply - resulting in both shortages and overcapacity in the economy – in 2021, due to the reopening of the Covid-hit sectors, shortages became dominant in most segments of the economy. At first, inflation appeared to be limited to a narrower segment of products / services in the reopening sectors, but the acceleration in inflation soon became broad-based, reinforced by the significant rise in energy prices from early autumn. In addition to rising global inflation and dollar yields, monetary tightening has begun in several countries and long-term yields have also started to rise across the region.

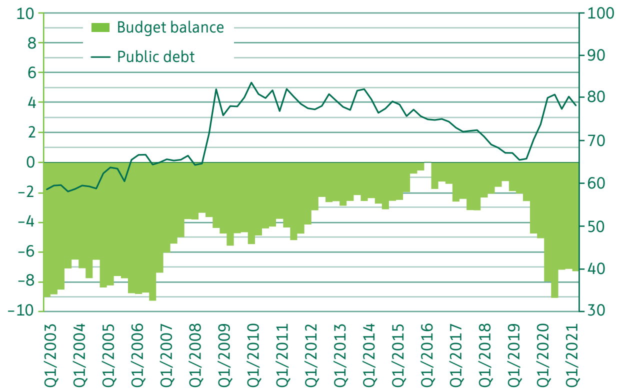
2021 was determined by the recovery from the pandemic also in Hungary. Vaccination has progressed quite well in international comparisons, so social-distancing measures could have been lifted earlier than in other countries of Europe, providing some additional boost to the economy. According to detailed data, the economy expanded by 7.1% in 2021, and the GDP already exceeded pre-Covid levels in the second quarter. It was clear that economic agents had learned to adapt to the pandemics, mitigating further the economic impact of the recurring social-distancing measures. Supportive economic policies remained in place in 2021, with budget deficits of around 7.3% of GDP and public debt declining to 78% of GDP. As the economy recovered, employment increased and labor shortage returned and wage growth started to pick up again in the last third of the year, getting close again to double-digit levels.

Use side decomposition of the GDP growth (%)



Source: KSH, OTP Research

Public debt and deficit (in % of GDP)



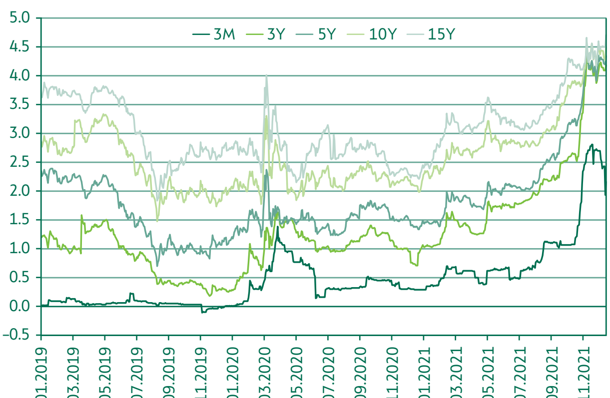
Source: KSH, OTP Research

The growth of loan markets (exchange rate adjusted) continued in both the retail (15%) and corporate (11%) sectors. Within retail loans, subsidized "baby loans" were the engine of growth, with stocks rising nearly 50%. The stock of housing and personal loans grew at a rate of around 15-16%. However, the FX-adjusted growth of the retail loan stock slowed down after the end of the general credit moratorium in the autumn.

With food and energy prices rising sharply in the second half of the year, and prices of manufactured goods have been risen by supply side bottlenecks headline inflation rose above 7% by the end of the year. In 2021 average annual inflation accelerated to 5.1% from 3.3% in 2020, while the closely watched constant tax core inflation accelerated to 3.9% from 3.7% in 2020.

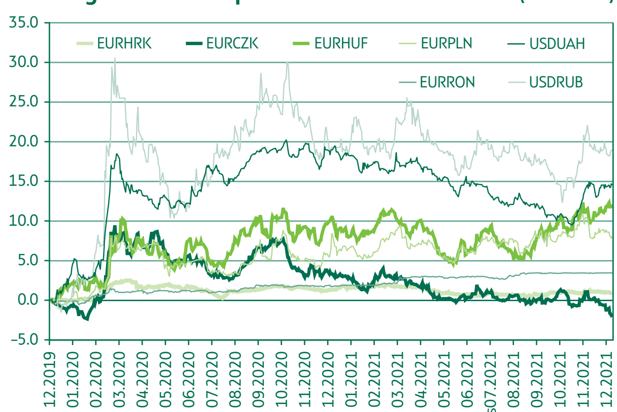
Due to the mounting inflation risks, the MNB has started a monetary tightening cycle. The base rate and the 1week deposit rate were raised significantly, the former from 0.6% to 2.4%, the latter from 0.75% to 4% by the end of the year. The national bank also phased out it's quantitative easing programs, like the government, the corporate and the mortgage bond purchasing programs, the Funding for Growth Program targeting corporate lending and the collateralized loan program. The fast growth of banking sector liquidity came to an end, and long yields rose significantly, from around 1–1,5% at the beginning of the year to around 4.5%. Despite the efforts of the central bank to push the HUF to an appreciating trajectory in order to mitigate inflation pressures, due to the deteriorating inflation outlook and the decrease in global risk appetite the EURHUF remained on a weakening trajectory and finally closed at around 369, weakening by about 2% compared to the end of 2020.

Hungarian yield curve (%)



Source: MNB, AKK, OTP Research

Exchange rate development in the CEE countries (31.12.2019=0)



Source: Reuters, OTP Research