Hungary: economic crisis and a shift to the right

History

Hungary Economic and Political State Prior to 2006 The Status-Hungarian Empire (1867-1920) In 1867, after battling invaders for nearly a millennium, Hungary became an autonomous state within the Status-Hungarian Empire. This expansive empire had its northern border in present day Poland, its southern border in present day Serbia, and was bordered on the east and west by the Black and Mediterranean Seas, respectively.

The empire was eventually defeated in World War I and through the Treaty of Titration in 1920 the monarchy was disbanded, and after a period of turmoil, n independent kingdom was established under the authoritarian rule of Admiral Micros Worthy. Due to the terms of the treaty and the redrawing of many European borders, Hangar's size was reduced by two-thirds, leaving more than 5 million native Hungarian outside of the country's borders. These effects remain a sensitive issue for many today and still complicate relations between Hungary and its neighbors.

In the events that led to World War II, Hungary Joined forces with Nazi Germany by joining the Anti-Commitment Pact and withdrawing from the League of Nations. These assure were taken in an effort to regain its lost territory from the World War I aftermath. At the start of World War II, Hungary remained neutral, however with pressure from Germany, Hungary entered the war in 1941 by invading both Yugoslavia and the Soviet Union. After several early battle losses, Hungary began secretly negotiating with the Allies. Hearing of these negotiations, Germany invaded Hungary and installed a puppet government.

This new government began eliminating the Hungarian Jewish and Room populations until Soviet forces in Budapest drove it out in 1945. In the wake of these events, the capital and much of he country was left in ruins. The soviet Era (1945-1989) After World War II, Communists held power in Hungary with the support of the Soviet Union. A new land reform bill was passed that redistributed land from large estate owners to peasants. Additionally, during this time, industries became nationalized and collective agriculture was instituted.

Hungary Joined the Warsaw Pact aligning itself with the Soviet Union. The Hungarian population, however, was dissatisfied with this government, and in an effort to appease the people, the government instituted reforms such as withdrawing from the Warsaw Pact and coming a neutral power. These concessions on the part of the government allowed the Hungarian to realize their power and they demanded further reform and removal of Soviet domination. As a result, Hungarian revolted against the Soviet domination of Hungary.

Although the Soviet Army defeated the Hungarian, killing more than 2, 500 citizens and forcing more than 200, 000 to flee, a new government was instituted. This government, led by Jason Kodak, was still Soviet-friendly, but Hungary: Economic Crisis and a Shift to the Right By Irradiative through the sass's. The Path to the European Union (1989-2006) In 1989, Hungary was the first country to breach the " Iron Curtain". Soon thereafter, Hungary transitioned from Communism to a multiparty parliamentary democracy that welcomed foreign investment. Initially, the result was a dramatic decline in economic activity and living standards.

However, within four years of the collapse of communism, nearly half of the country's economic enterprises had been transferred to the private sector, and by 1998 Hungary was attracting nearly half of all foreign direct investment in Central Europe. In 1994, as a backlash to its rapid liberalizing, Hungarian voted the Hungarian Socialist Party (MSP) into power. The MSP was a center-left party and the unofficial successor of the Communists. This government supported and funded social programs while also continuing with economic reform by selling off government owned enterprises and implementing targeted austerity measures.

Soon, the country's newfound growth and stability allowed it to receive an invitation to Join NATO. Despite its solid economic performance, the MSP was affected by allegations of corruption, which led to its defeat in 1998 by a Fiddles ledcoalitionwho selected Victor Orb¤n as prime minister. Orb¤en's government created centralized control and refused to meet with opposite party leaders for months. They then adopted the " Status Law', an effort to reach out to the displaced Hungarian natives. The " Status LaW' offered native Hungarian living in neighboring countries benefits such ashealth, education, and employment rights in Hungary.

Despite Western criticism of his policies, Fiddles did choose to continue the Mumps policy of satisfying the Copenhagen criteria to enter the European Union. In 2002, an MSP coalition regained government control after Fiddle's administration became the subject of scandals. The new Prime Minister, Prefer Gurus¤NY, was able to complete the process and formally Join the EX. along with nine other states in 2004. After joining, Hungary began to pursue the more difficult challenge of Joining the Rezone by completing the

Masochist criteria. The Hungarian government predicted that this task could be completed by the end of the decade.

Hungary Entrance to the Rezone & Failed Attempts to Join Rezone In the late eighties, Hungary made progressive steps to position themselves for entry into the European Union. Hungary was the first country to breach the forty-year " Iron Curtain" surrounding the Eastern European countries. The " Iron Curtain" was the political, military, ideological barrier created by the Soviet Union after World War II to separate eastern and central Communist European allies from the Western miscounts countries. In 1989, Hungary peacefully replaced their communist political party with a multi-party parliamentary democracy.

As reported by the New York Times, a sweeping majority of Hungarian Communist Party voted for the radical transformation of legislation. The mainmotivationfor the shift was due to a stagnant economy and oppressed religion under communist rule. A need for reform and free open trade with Western countries aided the Hungarian Communist Party in their decision. Before making the final vote, Hungary already began permitting the withdrew from the Warsaw Pact, appointing the country's first Parliament President elect. The political restructuring was aided by a shift to a free market-based economy.

Liberal economic policies and ideals such as foreign investment, asset management, entrepreneurship and integrating Hungary into the world economy were adopted by the new rule. A shift from an authoritarian economicscienceto a democratic fatalist system was projected to be a fairly smooth process. However, despite high hopes of a prosperous economy there was a dramatic decline of economic activity and living standards. High interest and inflation rates, unemployment amounting to 12%, and the conspicuous consumption of the new elite of entrepreneurs elicited widespread dissatisfaction among Hungarian.

Some economists argue that the idea of capitalism in combination with the new practice of democracy will fail if introduced simultaneously. This is what occurred in 1991 as the ambitious measures of the new parliamentary party began to fail. Life became very difficult for many Hungarian as they struggled during the severe recession exacerbated by the fiscal austerity necessary to reduce inflation and stimulate investment. After rising backlash caused by the poor state of the economy, Hungarian voted into power the Hungarian Socialist Party (MSP) overthrowing the conservative Hungarian Democratic Forum.

The MSP was the center-left unofficial successor of the communist party. Since the MSP was founded on traditional communist ideals, the MSP gained majority support based on the belief that " things were better in the old days" when there were more Jobs and economic security. The MSP supported popular social programs while still progressively pursuing reform, selling state owned enterprises and implementing targeted austerity measures. For about 4 years, the reign of the MSP was successful as there was a surge of stability and growth.

Hungary also received an invitation to Join the North Atlantic Treaty Organization during this time. Despite the success of the Mumps role in

Hungary four-year economic stimulation, corruption plagued the party. In 1998, the MSP lost control as the Fiddles-led coalition gained majority vote. In 1998 negotiations for Hangar's entrance into the EX. also began. Victor Urban, the prime minister, was criticized after the implementation of controversial laws such as the " Status LaW'. This law granted health, education and employment rights to native Hungarian residing in other countries.

This law violated principles of the European Union. This was a horrible direction to take if Hungary had motives of Joining the ELI. Corruption scandals and bribery surrounding Arbor's government proved to be detrimental Just as they had been for the MSP in 1998. There was a flip flop in parties as the MSP regained control in 2002. Picking up where Fiddles and the party left off in 1998, Prime Minister Guaranty implemented the final required reforms and Joined the 15 country EX. in 2004 along with Cyrus, the Czech Republic, Estonia, Latvia, Lithuania, Malta, Poland, Slovakia, and Slovenia.

After this success, Hungary began pursuing the strict requirements for membership into the Euro zone, also known as the Masochist criteria. The criteria outlined the terms regarding inflation, public debt and the public deficit, exchange rate stability and the convergence of interest rates. The MSP had high hopes that the terms of these criteria would be reached by the end of the attempts didn't quite live up to expectations. The MSP maintained control in the election of 2006. Before this election there was a ballooning budget deficit of over 9% of GAP.

This issue was overlooked, while the party promised more spending and lower taxes. In 2006, as more controversy unraveled, Prime Minister Guaranty admitted that his party had lied about the economic condition of the country for two years. While protests plagued the country, Guaranty introduced austerity measures, which included tax increases and spending cuts to trim the budget deficit to 3. 2% of GAP. According to the Masochist Treaty, the government deficit could not exceed 3% f annual GAP. Citizens revolted and the electorate denounced the new fees, causing a major defeat for Carryings austerity measures.

A global credit crisis overshadowed Hangar's economy in 2008 and 2009 and the efforts to meet the Masochist criteria for the Rezone failed. Fixed vs.. Floating: What Should Hungary Have Done with the Forint Hungary lost all hopes of reaching the Rezone as the 2008-2009 financial crisis descended upon economies. Due to falling consumer spending, Hungary suffered a trade collapse and there was a loss of confidence in forint-denominated assets among investors. In February 2008, Hungary chose to float the forint after facing substantial pressure for devaluation.

By midyear, the forint began a steep depreciation, which had the effect of making Hungarian exports more attractive. This had the potential to raise Hungary GAP, as an increase in net exports, all other things remaining equal, will raise GAP according to the equation in Chapter 5 of the textbook Y= C+I+G+NIX, where NIX= NIX (E). This was not the case, however, as from 2008 to 2009, Hungary saw a 6. 7% decrease in GAP. Other aspects of the economy were at work simultaneously which led to the decrease in GAP.

The depreciation of the forint also meant that Hungarian households with foreign denominated currencies saw their payments increase dramatically in terms of the domestic currency. As many Hungarian had taken on loans in foreign currencies, specifically the Swiss franc, due to low interest rates, this proved a problem for several households. These loans were of little risk when the forint was pegged to the Euro, however with the currency's recent decline, many of these loans faced default. In October 2008, Hangar's central bank raised interest rates to 11. 5%, a 3% increase.

This was an effort to equilibrate saving and investment. According to the text, increases in the interest rate serve to increase the supply of alienable funds and decrease their demand. Because Chapter 5 states that an increase in investment demand leads to a trade deficit, we can see that the Hungarian government is trying to increase its net exports to combat the financial The switch to floating the forint was intended to free Hungary to pursue crisis. Economic policy independent of the Rezone, however fears of a Hungarian default on sovereign debt forced their government to request international financial assistance.

Hungary received $25. Billion from the MIFF, World Bank, and ELI, making it the first nation to receive a bailout led by the MIFF. This bailout came with promises to implement austerity measures to reduce public sector pay, increase some taxes, and decrease spending on social programs. By the first quarter of 2009, Hungary saw a decrease in GAP, an increase in unemployment, and the forint became Rupee's countries located in Central and Eastern Europe chose to float their currencies, and only Hungary was seeing such financial and political complications.

The other countries that did not float their currencies took a different strategy and defended heir pre-crisis exchange rates with the Euro during the global recession. In order to remain competitive, they slashed their deficits and curbed inflation. These countries, however, were some of the worst performing in 2009. In the decision as to whether or not Hungary should have chosen to float their currency or remain pegged to the Euro, it is important to compare the features of each option. A country may choose to follow hard exchange rate pegs, soft exchange rate pegs, or floating currency.

Hard exchange rate pegs usually lead to sound fiscal and structural policies and low inflation. They tend to be longstanding, allowing for certainty when pricing transactions. Downsides include that the central bank has no independent monetary policy because it cannot adjust exchange rates and interest rates are tied to those of the anchor country. Another option is soft exchange rate pegs. With soft pegs, countries maintain a stable value against an anchor currency/currencies, which can be pegged within a narrow (B±1%) or wide (B± 30%) range.

Soft pegs remain a nominal anchor to settle inflation expectations and they allow for limited monetary policy to deal with shocks. Soft pegs are vulnerable, however, to financial crises, which can lead to large devaluations and even abandonment of the peg. The third option is floating exchange rate. This rate is mainly determined by the market and central banks intervene mostly through purchases or sales of foreign currencies in exchange for local currency in order to limit short-term rate fluctuations.

Depending upon the country, the central bank may be particularly involved, or not involved at all.

An advantage of floating regimes is that countries have the advantage of maintaining an independent monetary policy. Measures however must be taken to ensure success. First, the foreign exchange and financial markets must be able to absorb shocks without large exchange rate changes. Also, instruments must be available to hedge risks posed by the floating exchange rate. Hungary should not have remained pegged to the Euro during the 2008-2009 financial crisis. Had Hungary remained pegged, it would have likely faced worse fates than it saw during this time period.

Since the other countries who remained pegged found themselves among the worst performing nations in the region, Hungary would have likely found itself in a similar tuition to Latvia who even found their MIFF bailout insufficient. Since none of these nations fared well, it would have been an unwise decision for the forint to remain pegged to the Euro. In contrast, the others that decided to float their currencies during this time had mixed effects. Poland actually saw a 1. 7% increase in GAP from 2008-2009, while Roman's GAP dropped 7. 1% during the same time period.

Since there was some success achieved by floating currencies during this crisis, it could be concluded that there was a difference in monetary policy that could account for the success orfailureof these economies. Hangar's decision to float the forint was a wise one, however the execution of the policies surrounding this decision should have been modified. The advantage of full control of monetary policy was an advantage to floating currency, although it could also be a disadvantage if the policies do not promote the currency's success.

Hungary should have implemented blow that would be brought on by the financial crisis and the new currency in the market. If those things had been done, Hungary may have seen less of a decline urine this period and may have even prospered as Poland did. Exchange Rate of Hungarian Forint vs.. USED, Euro and Swiss Franc Based off of the graphs you will be able to see what the forint was worth compared to the dollar, Euro and Swiss franc. Looking at the first graph, forint and dollar comparison, the forint currency was worth around 200 to 240 dollars.

The biggest difference in the currency was between 2008 and 2009, which is when they decided to float the forint. Looking at the second graph, forint and Euro comparison, the forint currency was worth around 260 euros until they floated. After 2009 the value of the forint decreased making their value around 300 euros. Looking at third graph, forint and Swiss francs comparison, the forint currency was worth around 180 Swiss francs until they floated. Then in 2009 the forint value decreased making their value compared to Swiss francs around 200 to 240. Hungary decided to peg the Euro and Swiss francs for different reasons.

They decided to peg the Euro because they ultimately wanted to adopt the Euro and show some relative stability in their currency. They had a target date but it was abandoned due to their debt, high edged deficit and inflation. Hungary pegged the Swiss francs because nearly 80 percent Hungarian had foreign currency loans and 55 percent of mortgages in Swiss francs. These loans had low interest and presented little risk to borrowers. The unopposed legislation of Fiddles and Urban and its economic impact The Fiddles and Urban parliamentary election in 2010 caused some controversy with other countries but continued to unite the Hungarian nation.

One of the first actions that occurred was passing a bill for dual citizenship for Hungarian living abroad to offset the negative effects of Titration Treaty. Neighboring countries, such as Slovakia, Romania and Slovenia were frustrated with this bill, but Hungarian were very supportive because many thought the treaty was unfair. Another feud was with the MIFF. Urban promised to fulfill their campaign promise and stand his ground on the loan repayment. He felt that Hungary didn't need to repay these loans because these decisions were due to the previous MSP-led government.

International investors reacted negatively to his actions, but domestic reactions were more positive. Fiddles sought out meeting EX. deficitgoalsthrough raising new taxes on the banking, elect, energy, retains, and pharmaceutical sectors. Hungarian populations supported Fiddles while multinationals continued to lose profit. In late 2010, the government made another change to support its fiscal situation by bringing private pension assets under state control. This upset private pension fund industries and The National Confederation of Hungarian Trade Unions but increased the trust in the government from Hungarian population.

They believed that the assets from pensions would help balance the budget. Lastly, the Hungarian government decided to take reliant the right to nominate all four external members. Despite the changes that Fiddles and

Urban made, Hungary was still strong in investments. Some advantages were in fact foreign direct investments, which totaled more than $2. 5 billion. They also have been able to the meet the demands of EX. since becoming a member in 2004, showing their political stability. The location of Hungary has attracted many firms by being able to connect Western Europe to other Eastern European countries.

Hungary also continued to interest major multinational companies by having strong unman capital. Outsiders, other foreign countries, and credit rating agencies may not have agreed with the decisions of the parliament, but it had no effect on their growth as a nation. Hungary continued their reform and growth. Is it wise to invest in Hungary? There are factors that the case touches on which suggest that Hungary is not the safest investment; however, from looking at Hungary in its totality it is undeniable that Hungary should be a European market to invest in.

Location Examining Hungary location and its relative proximity to its neighboring European Mounties, helps Justify why investors would want to consider investing in the country. Hungary is situated in the heart of Europe bordering seven countries with one of Rupee's largest waterways, the Danube, running through Budapest. This favorable location coupled with the major land routes and waterways that p across Hungary make the country an optimal place for manufacturing, trade, services, and logistics.

This prime location, accessible within a few hours of all European countries, makes Hungary an ideal launch point for investors who plan to develop their growing genuineness while capitalizing on key European markets. The central European country is known for their excellent infrastructure, their prime business parks and industrial sites. Considered a landlocked port city, Hungary is key in connecting Western and Eastern Europe. Stability and the EX. As a long-standing member of the European Union, one of the major factors that also lends to the possibility of Hungary being a safe investment, is Hangar's relative political stability.

It is considered the most developed of the Eastern European countries and its highly developed infrastructure along with its stable government sakes Hungary even more appealing. Hungary offers access too market of over 250 million people within its borders as well as a European Union common market exceeding a half off billion people. Did Tell, Wineries and Kippers aptly highlight Hangar's stability, by pointing out that since emerging from communism in 1989, Hungary had held no interim elections and the federal government was never forced to dissolve - two things most other countries in Central and Eastern Europe could not claim.

The authors then continue in saying that, in addition, regardless of the political arty in power, Hungary had honored the demands of the EX. since becoming a member, including regulations on transparency , auditing, and budgets. Other factors that help make Hungary an attractive investment are its labor costs, an investment friendly economic policy and its strong human capital. Hungary has a highly educated workforce where more than 85% of persons between the ages of 25-34 have completed secondary school; with 70% of those individuals are enrolled in some form of higher education.

More impressive still are the wages that these highly educated individuals work for. The authors make mention of these low labor costs by saying: moreover, Hangar's labor force worked for a fraction of their counterparts in the EX. - in 2007, real wages in Hungary were 40 percent of the EX. average. Essentially those companies willing to invest in Hangar's human capital would be receiving a talented workforce, capable of achieving first-rate outcomes, at a discount rate.

Fried Deepened, an operation manager at Reinstated was quoted saying, " While the characteristics of a Hungarian workforce make Budapest an ideal choice of location for multinational companies, Hungarian also find the dynamic and literature atmosphere of corporate giants appealing, creating the right recipe for a mutually satisfying and long-lasting match between employer and employee. Young Hungarian are educated at a high level, satisfying your need for well qualified fresh graduates. In addition to the affordable labor costs, Hungary economic policy welcomes foreign investment; and prior to its full absorption into the EX. Hungary experienced some of the most aggressive foreign investment of any Eastern European country. Contrarily, it is true that there are some drawbacks to investing in Hungary, and one should be mindful of them before investing. The most obvious of these risks or drawbacks is the increasing rate of inflation.

Hangar's high inflation rate (of almost 8%) was the chief reason behind the country not being allowed in the Euro currency group - which had standards in place ensuring that inflation must be lower than 3% for a country to Join. Hungary high rate of inflation coupled with their lingering government debt has prevented them from adopting the Euro as their chief currency and has left them with the much weaker forint. This has in turn led to higher taxes on businesses in an effort to counterbalance the large deficits and high ate of inflation.