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Hungary on Path to Shed Junk Grade and Shield Forint, Orban Says

By Zoltan Simon

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Hungary's Prime Minister Viktor Orban speaks during an interview at his parliament office in Budapest. Orban says Hungary will regain its investment grade by reaching an agreement with the banking industry on taxes and lending, phasing out foreign-currency mortgages and trimming the share of non-forint state debt.

Prime Minister Viktor Orban says Hungary is on track to regain its investment grade by reaching an agreement with the banking industry on taxes and lending, phasing out foreign-currency mortgages and trimming the share of non-forint state debt.

Orban also spoke about politics, the economy and foreign policy in a Dec. 12 interview in Budapest.

On foreign-currency debt, Hungary's sovereign debt rating, monetary policy:

"We're indebted to such a degree in foreign currencies that it questioned the country's true sovereignty and independence. Every government wanted to reduce this exposure and few were able to succeed, mine is one of them.

''Phasing out foreign-currency loans will cut this exposure, while at the same time we managed to finance a bigger share of state debt in forint. These two effects make the Hungarian economy much less exposed and vulnerable.

''I even dare say that if our economic results are maintained, we have an agreement with the banking industry and our exposure is cut, then sooner or later the Hungarian economy must be upgraded. It will also increase the maneuvering room of monetary policy.''

On speculative attacks:

''We had to fight back a very serious speculative attack in 2011, this is a point of reference for Hungarian policy makers whether in the government or the central bank.

‘‘There are always signs’’ for it. ‘‘So we always have to scan the horizon to see whether a storm is in the making. This is an instinct of Hungarian economic policy and is justified by the country’s size and the fact that we’re not a part of the euro area and we have our own currency.

‘‘Our size and the vulnerability that comes from that makes us extra careful and I’m happy if the central bank is working to ensure a solid monetary backdrop for the government.’’

On investments:

‘‘We have to look at the dynamics of foreign-direct investments and that’s improving every year.

‘‘We don’t want to squeeze out anyone, the reason we introduced sectoral taxes is so that we have more revenue, not less.

‘‘Hungary is giving the maximum aid allowed under European rules to car manufacturers. I counted with more dynamic growth in the car industry, better than it is currently. I’m not disappointed of course, the numbers are still imposing, but I see more opportunities than the German, Japanese, South Korean carmakers and first-round suppliers took advantage of in Hungary.

‘‘I also expected another big manufacturer to enter this industry but besides Mercedes this hasn’t happened. Of course Mercedes is great but we need other brands as well.

‘‘Hungary is a transparent country, it can be seen clearly where there are higher or lower taxes in the European context. In the sectors where we have high taxes we don’t think investors will come to Hungary. We have tax breaks where we’d like to see more investments, not just in the car industry but we’re also strong in chemicals, pharmaceuticals and IT investments.’’

On banks:

‘‘We’re also in talks with the banking industry on normalizing the size of the bank tax because that’s extraordinarily high in Hungary. This can be possible around 2016 or 2017 if we can strike a good agreement, whose chances are better than at any time since we came to power in 2010.

‘‘It’s a two-part package. One is cutting the burden of the banking industry and the other is boosting lending capacity. If there’s lending, the tax can be lower. This won’t happen in 2015 but after 2015 I can imagine it.

‘‘The last obstacle will be surmounted and the political establishment and the banking industry can come to a long-term agreement’’ once foreign-currency loans are phased out ‘‘by the middle of 2015.

‘‘The Slovenian example is a valuable and dangerous experience. That’s why we’re cautious. We separate the financial institutions we want to keep in state ownership permanently -- the MFB development bank, Eximbank and some sort of state ownership in savings banks -- from those where we don’t need state ownership in the long-term.

‘‘Budapest Bank won’t stay in state ownership permanently. And we bought MKB to clean it up and we put a 100 percent state guarantee behind its deposits and bonds.

‘‘There are smaller banks that want to leave Hungary or want to change their operational structure and only keep certain businesses. We’re ready to cooperate with these so that they can work optimally in Hungary, we’re ready to buy them.

‘‘But in two to three years, the state doesn’t want to keep banks that don’t need to be publicly owned, we want to clean them up and then we want to return them into private ownership. We’ll choose the method in due time: there’s the stock market, capital markets work well and we also have experience in privatization.’’

On the budget:

‘‘Economic growth is still insufficient to lead us out of budget deficits. I consider the ideal budget one that’s in surplus or at worst one that’s balanced. As long as the budget isn’t balanced, the Hungarian budget needs every penny.

‘‘The financing cost of Hungary’s state debt is continuously declining. So there’s an opportunity to cut taxes in line with the declining cost of debt financing and make available funds for economic growth. So it’s not hopeless to have a balanced budget.

‘‘There are uncertainties in the Hungarian budget and that’s why the Hungarian budget has much bigger reserves than is customary in Europe.”

On economic policy:

“The first and most important revolutionary constitutional change was the introduction of the debt brake which says that the debt level can’t go above 50 percent. And as long as we’re not at that level, we can’t approve a budget that doesn’t bring us closer to that level.

‘‘The second most important economic change was what we call workfare society, which means helping as many people living off welfare in the world of employment. That means a workfare society instead of a welfare society.

‘‘And the third important change is the fair sharing of the tax burden. This includes a tax system unknown in Europe: a combination of flat income tax and family tax. We combined tax breaks after children with a flat tax, which meant we needed a high value-added tax, which not only makes sense but we think is fair. And to this we added industry taxes and an action plan to cut taxes on employment.

‘‘We call this the Hungarian model and it’s like a bumblebee. Scientists say a bumblebee shouldn’t be able to fly based on its weight, size and wingspan. And yet it does. The Hungarian model is such a bumblebee.

‘‘Economists say they can prove that based on what we do we can’t meet so many goals, that we can’t make a prosperous, growing economy that creates jobs. And the reality is that we can. We can post economic growth in excess of the European average; it can reduce employment; and simultaneously it can cut state debt and keep the budget deficit in check.

‘‘The question is what kinds of taxes we can cut. Our decision is that on the one hand we need salary increases and on the other tax cuts. This involves wage increases that don’t threaten economic competitiveness, stretched out over a number of years. This includes increases for teachers, law-enforcement officers and then government workers. We’ll cut taxes by boosting tax breaks for families with children.”

On poverty:

“We disagree with the statements that point to a poverty tendency. We think the opposite is true, poverty declined in Hungary in every dimension in 2013 and continued to do so in 2014. It can’t be otherwise since a large share of the poor, hundreds of thousands, lived on welfare. And welfare is less than 50 percent of the public works employment wages that we pay today.

‘‘These international statistics don’t take into account in-kind support, which are a strong feature of the Hungarian welfare system, such as free meals in schools and free textbooks.

‘‘The tendency is good. We have to boost the speed of transfer from welfare to payrolls. No one is satisfied with the current situation. And discussing what can be done better is a worthwhile debate to have.’’

On the timing of tax cuts:

‘‘Its time will come. It’s constantly a matter of debate whether we’re there yet, whether we should do it in the middle of next year or in 2016. But we’re also waiting for this moment, searching for it, and we’ll do it. The question is only which taxes to cut.”

On the outlook for economic growth:

“The environment around the Hungarian economy is causing uncertainty. We have to go with a conservative script, which says that the European environment will mean stagnation for Hungary, so this will impact Hungary.

‘‘Hungary lost 17 percent of its exports destined for Russia because of sanctions and the Ukrainian situation. And no one can say whether this will get worse.

‘‘The 2.5 percent GDP growth estimate for next year is a conservative one.’’

On acquisitions:

‘‘Hungary’s biggest company is Mol, in which we bought back a 25 percent stake from the Russians. We bought via E.ON the right to negotiate Hungary’s gas contract, which was previously done by Russians and Germans. We bought the gas storage facilities which are indispensable for Hungary's energy independence.

''We bought back the large gas distribution systems in Budapest as well its water works. We bought back businesses necessary for garbage collection. These were all done to ensure the security of utility services.

''There were acquisitions that boosted state assets in the markets, these included buying back Raba on the stock market and also purchases in the banking industry.

''The latter ones I don't consider permanent acquisitions. These assets can be later mobilized while public utilities will remain in state ownership permanently.''

On foreign policy:

''Hungary's foreign policy fits into the EU's foreign policy, that means it has solid international backing.

''It's a new challenge for all of us how fast a foreign policy driven by commercial, investor, financial interests and human rights considerations was replaced by a foreign policy based on geopolitics. This is a serious intellectual challenge for Europe.

''Hungary's foreign policy doctrine has three pillars: the American doctrine, the EU doctrine and the Russian doctrine. The American doctrine can be summed up as military alliance, economic cooperation and political sovereignty; the European doctrine as political, economic and military alliance. And the Russian doctrine is respect for international law while keeping open opportunities for economic cooperation.

''Hungary's national interest on Russia is that we have to stick to principles of international law and shape economic sanctions depending on the situation. We shouldn't throw sanctions out of the tool box but the EU should also start talks with Eurasian countries at the same time.

''It can be expected of Hungary that it be as loyal as it can to Europe's common foreign policy and for it to not damage its efficiency.

''The U.S., in response to the geopolitical situation, has come up with an action plan, which they recently announced publicly, and it involves two dozen countries. This is fundamentally trying to influence alleged corruption in these two dozen countries.

''This is the land of freedom fighters. And there's public feeling in Hungary that sees a sovereignty problem in all of this. It feels that this is an attempt to influence from the outside the sovereign decisions of a freely elected parliament.''

On energy:

‘‘We’ve closed the South Stream dossier. We have to change tracks quickly. We need a gas pipeline that stabilizes the western Balkans and serves Hungary’s national interest and Hungary’s energy industry as well. We’d like a pipeline through Serbia to Hungary. We want a solution that solves the Serb, Bosnian problems and it’s important that it be an EU country at the other end as well, that means Greece.’’

On domestic politics:

‘‘Checks and balances only have meaning in the United States, or in presidential systems, where there are two identical sovereigns, that is a directly elected president and legislature. In Europe, this isn’t the case, there’s only one sovereign, there’s nowhere to ‘check it or balance it,’ because all of the power is delegated by parliament. In these instances it’s much more appropriate to talk about cooperation rather than checks and balances. Checks and balances is a U.S. invention that for some reason of intellectual mediocrity Europe decided to adopt and use in European politics.

‘‘But there’s nothing to do now, it’s going to stay this way as long we’re here. So I can only nod that when I move my offices out of parliament and into a (former) monastery it will mean the strengthening of checks and balances.”

“There are checks and there are balances in European democracy, but the whole system isn’t built on this but on the distribution of the people’s sovereignty by parliament.

‘‘Hungarians welcomed illiberal democracy, the fact that in English it means something else is not my problem. In the Hungarian context, the word liberal has become negative. Liberal democracy has no or very little support in Hungary. What I want to say is that it’s not true that a democracy can only be liberal. There’s democracy in Hungary period, it doesn’t need any modifiers.”

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