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Shifting Paradigms for the Hungarian Economy and the MNB



Summary

As a result of the fresh, new approaches taken in economic policy, significant economic convergence occurred in Hungary in the past decade, and a sustainable internal and external balance was also achieved. Thus, the formula of “balance and growth” was applied successfully for the first time in the last hundred years. Consequently, Hungary faced the coronavirus pandemic and its economic effects with a strong immune system, and the recovery was rapid. However, even as the crisis subsides, work remains to be done: we need to restore balance and implement a turnaround in competitiveness to redirect the economy back to a sustainable path. In the competitive environment of the 21st century, economies which are able to harness emerging international megatrends by accentuating their own strengths will be the winners. Over the long term, Hungary can be among these winners, by correctly assessing the changing forces and using them to our advantage, while continuously strengthening competitiveness factors.

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INTRODUCTION

Over the past period of slightly more than ten years, the Hungarian economy and economic policy have come a long ways. The 2008 global financial crisis hit Hungary in a weak condition, causing serious problems (Matolcsy, 2020a). After 2010, however, the economy's immune system strengthened again, owing to the fresh, new approach in economic policy. Thanks to this, Hungary was able to overcome the economic difficulties caused by the coronavirus crisis quickly and successfully. Nothing illustrates this success better than the fact that the economy needed just six quarters to recover to its pre-crisis performance during the coronavirus pandemic, which triggered the most serious global crisis in the past 70 years; by contrast, this took six and a half years after 2008.

Nevertheless, even after successful crisis management and economic reopening, we must not be complacent. The post-Covid syndrome must be avoided, and a turnaround in competitiveness has to be completed. Hungarian economic policy must be shaped and recalibrated in this spirit. At the same time, emerging international megatrends also need to be taken into account. Recognising and utilising these developments, while remaining mindful of Hungary's special features, a winning economic strategy can be formulated that leads Hungary to successful economic convergence in the coming years and decades.

THE HUNGARIAN ECONOMY BETWEEN THE TWO CRISES

The 2008–2009 global financial crisis and the subsequent decade were an important turning point in economic history and for society as well. The complex challenges generated by the global economic crisis and the related responses continue to define everyday life, with profound geopolitical, social and political consequences. It was demonstrated once again that in difficult situations, sustainable development can only be ensured with an economic policy built on creative ideas, bold decisions and constructive cooperation.

The novel problems called for new, unconventional economic philosophy approaches and new attitudes from the various branches of economic policy. As a result of the misguided economic policy of the pre-crisis years, the turbulence in 2008–2009 swept over Hungary in a particularly weak state. Consequently, Hungary experienced one of the gravest crises in Europe until 2010 that wreaked havoc in the economy. After the dust settled, the fiscal turnaround launched by the incoming government after 2010, followed by the turnaround in monetary policy from 2013 paved the way for the healthiest business cycle in Hungary's modern history during the past decade. This is because in the past century, this was the first time when the formula of economic "growth and balance" was applied for a longer period of time, instead of choosing between either growth or balance (MNB, 2021d). One of the pillars of this economic policy revolution was that the overwhelming majority of reforms were implemented during the first third of the decade. Of the 56 most important reforms, 43 were completed or launched between 2010 and 2013 (including a tax reform, the opening up to the East, strategic agreements, the forint repayment of FX debt, the various Széll Kálmán plans and a host of other reforms). In 2010, six critical areas in the economy were reformed or started to be reformed, followed by twelve more in 2011, ten in 2012 and fifteen in 2013.

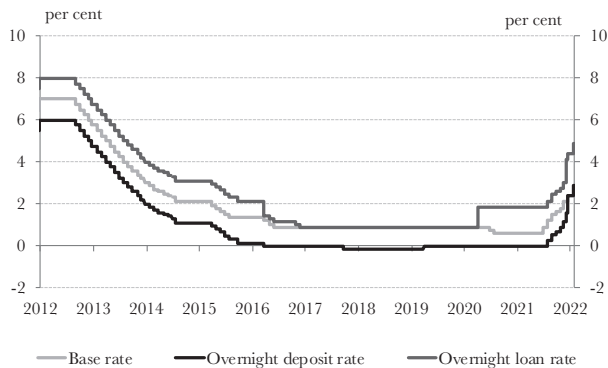
Budgetary turnaround

As a first step in its successful crisis management, Hungary managed to carry out a successful fiscal consolidation between 2010 and 2014, in parallel with fiscal and tax system reforms (Matolcsy, 2019). The tax reform that began in 2010 was implemented with a new philosophy. Its aim was to ensure fiscal balance and support economic growth. The parallel achievement of these two goals required an increase in employment and investments, which could be most efficiently achieved by cutting taxes on capital and labour. In other words, economic policy shifted its focus from taxes on labour and capital towards consumption taxes. As a result of the successful budget consolidation and lasting economic stabilisation that occurred after 2010, all of the Hungarian economy's employment indicators improved for the entire period. Thanks to the successful fiscal turnaround, Hungary exited the excessive deficit procedure after nine years, in 2013. Moreover, the fiscal turnaround also allowed the debt ratio to be reduced via the sustainable consolidation of the government budget deficit and the stimulation of economic growth.

Monetary policy turnaround

Monetary policy was completely realigned when the new leadership of the central bank took office in 2013. Reform of the central bank's policies was also strongly influenced by the efficient transformation of the institutional system, in particular integration of the financial supervisory authority into the central bank in late 2013. As part of the monetary policy renewal, the Magyar Nemzeti Bank (MNB) started its rate-cutting cycle in August 2012, reducing the policy rate in three stages by 610 basis points, from 7 per cent to the then-historic low of 0.9 per cent, over the course of four years (Chart 1). The substantial reduction in the base rate mitigated the risk of a deflationary environment and contributed strongly to the rise in output and the growth in lending, while economic balance was preserved and the economy's external financing capacity was also consistently positive.

Chart 1. Central bank base rate and the interest rate corridor



Source: MNB

Note: The chart shows the state at the time of the submission of the manuscript (31/01/2022).

In 2013, the central bank launched the Funding for Growth Scheme, which ended the credit crunch and made a huge contribution to putting SME lending on a more stable growth trajectory. This completed the turnaround in lending. In April 2014, the Self-financing Programme was announced, with which the MNB transformed its monetary policy instruments to encourage banks to keep their excess liquidity in long-term, liquid securities, i.e. government securities, rather than as a central bank deposit. This programme overhauled the financing structure of government debt. Furthermore, the MNB introduced a new monetary policy framework in the summer of 2016, by means of which it implemented a targeted, unconventional monetary easing policy while keeping the base rate sustainable and taking into account inflationary developments. The robust financing capacity that emerged through the post-crisis adjustment as well as the resulting drop in external debt and external vulnerability allowed the central bank's balance sheet to be reduced with targeted programmes and without jeopardising reserve adequacy. This all came at a time when most central banks in the world tended to expand their balance sheet totals to achieve their monetary policy goals (Csontos–Nagy–Kékesi, 2020).

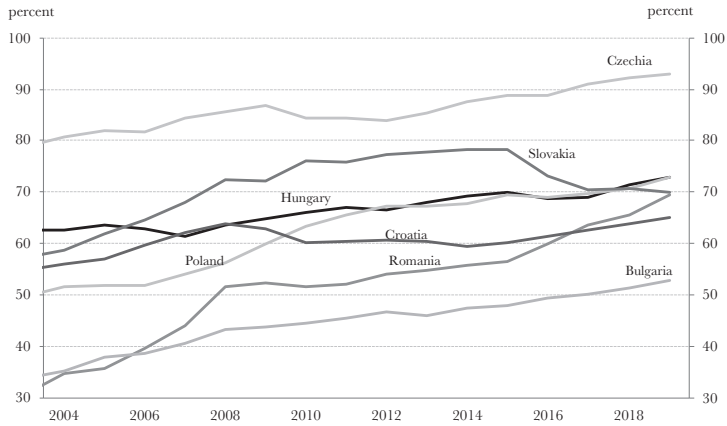
The turnarounds speeded up convergence

The decade of 2010–2019 began with a straightforward, positive national strategy, focusing on rebuilding the nation state and reorganising the market economy in accordance with Hungary's interests. This national strategy proved to be perfect, taking into account the 100 years after the Trianon Treaty and the national strategy performance of other countries in the CEE region. Instead of the earlier below-average ranking, Hungary's national strategy after 2010 was ranked the best in the CEE region. This laid the foundations for the exceptional crisis management results in 2020 and especially in 2021.

The main achievement of the successful, positive national strategy implemented after 2010 is that the nation state was rebuilt, and thus the nation as a cohesive force was created (Matolcsy, 2021e). This is sustainable in the long run as it is built on a broad-based social consensus.

Thanks to the turnaround in economic policy, this was the first time when the formula of economic “growth and balance” was used for a sustained period of time in the past 100 years. By 2019, the Hungarian employment rate, which had been at the bottom of the rankings, had risen to the top of the region and above the EU average, which is an outstanding performance. Economic growth was more than 2 percentage points higher than the EU average, while the country's balance indicators also improved. Hungary's level of economic development climbed from 66 per cent to 73 per cent of the EU average, once again overtaking Poland and Slovakia (Chart 2).

Chart 2. GDP per capita in the region as a share of EU average



Note: Adjusted for purchasing power parity

Source: Eurostat

The MNB’s programmes accounted for almost one half of the GDP growth between 2013 and 2019, and thus the central bank made a massive contribution to Hungary’s sustainable convergence. At the same time, the improvement in the Hungarian economy’s balance position was reflected in all key indicators. The MNB also achieved unparalleled success in meeting the inflation target: for almost 90 per cent of the 2017–2020 period, inflation was within the central bank’s tolerance band, which is exceptional even by international standards. In cooperation with the government and the Hungarian Banking Association, household FX loans were phased out, removing a heavy burden from the shoulders of Hungarian economic agents. The central bank also improved the powers and efficiency of the financial supervisory authority, and regulation in the banking system underwent a major change as well, leading to much better, and in many cases even certified, products for customers, while banks’ capital position and resilience to shocks improved. The budget deficit steadily fluctuated around 2 per cent, government debt contracted considerably, and the share of FX debt shrank to below 20 per cent.

The next step may be a turnaround in competitiveness

Despite the unprecedented decade, there is still much to be done for the long-term sustainability of economic growth. In addition to its primary mandate for the achievement and maintenance of price stability, the MNB supports the economic policy of the government with the instruments at its disposal. In the course of this, the MNB facilitates Hungary’s sustainable convergence by improving competitiveness with the expertise it has available. The MNB’s Competitiveness Programme set out 330 proposals in 12 areas in

order to fully develop the country's growth potential and catch up with the most advanced economies in a sustainable manner (MNB, 2019). In the future, Hungary's growth model needs to be enhanced. The country's strengths need to be preserved and its reserves must be utilised.

This is important because based on the example of the economies that have successfully completed a digital transformation (e.g. Estonia), this area can be assumed to provide one additional per cent of GDP compared to the existing GDP (Matolcsy, 2021c). Targeted economic protection measures should be used to preserve the successful growth formula from recent years. Dynamic investments, rising consumption and growth in excess of the European Union average by 2–3 per cent based on advanced technologies, high capital intensity and double-digit credit expansion should be maintained. Sustainable convergence requires balance and growth at the same time.

CENTRAL BANK RESPONSES TO THE CORONAVIRUS PANDEMIC

Like other countries in the world, Hungary was confronted by an unexpected global public health crisis in early 2020. The coronavirus pandemic and the ensuing economic turmoil posed enormous challenges for the society and all members of the economy. However, the world had learned its lesson from the previous crisis, and so a financial crisis was successfully averted.

During the 2020 crisis, Hungary had strong immunity, adequate room for manoeuvre in economic policy and stable fundamentals, thanks to the earlier economic policy changes. Since 2013, the central bank's measures have made the financial system much healthier than before. The MNB's measures contributed strongly to crisis management: the central bank's targeted programmes provided HUF 11,400 billion in financing to a wide range of economic actors until the end of 2021.

Thanks to the quick, coordinated measures, the Hungarian economy was successfully restarted and was one of the quickest to recover in Europe. Owing to the central bank's determined steps, the prolonged, creditless recovery experienced earlier was successfully avoided.

The MNB responded to the crisis quickly in a targeted manner

The MNB responded with proper timing and massive firepower, fostering a rapid economic recovery (MNB, 2021d). The Bank faced several challenges, as the stability of the markets had to be preserved, economic stimulus measures were necessary to aid the recovery, and new challenges involving the primary objective, price stability, also had to be addressed. This required an even more complex, targeted and flexible monetary policy response than before.

From the central bank's perspective, the first stage of economic protection involved two main tasks:

- stabilisation of domestic financial market developments, and
- provision of the necessary liquidity under favourable conditions and at appropriate maturities to all economic actors.

To this end, the MNB modified its instruments and introduced several coordinated, targeted measures that focused on both the short and long segment of the yield curve (e.g. government securities purchase programme, long-term collateralised credit instrument, mortgage bond purchase programme). The MNB used the programmes to extend liquidity to the economy in the amount of HUF 11,400 billion until the end of 2021. In addition, the government and the MNB immediately introduced measures to maintain lending, in response to the new risks arising in the coronavirus pandemic. Such measures included temporary easing of capital requirement regulations and provisional tightening of liquidity and financing requirements targeting FX financing risks in Hungary. In line with the MNB's proposal, the moratorium on repayments introduced by the government eased the liquidity shortages of households and companies alike, and supported the maintenance of consumption and investments, immediately after the lockdowns started.

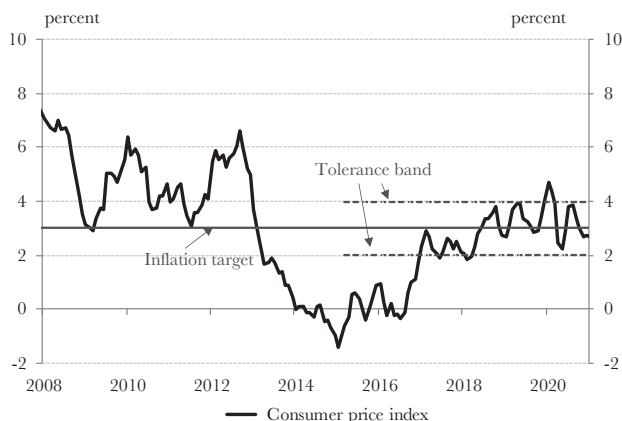
Following successful financial stabilisation, in the second phase of protecting the economy against the pandemic, restoring economic growth was the focus. Supporting this was also of key importance for the central bank, as economic recovery is also needed to achieve the inflation target. In the summer of 2020, the central bank cut the base rate twice, by 30 basis points in total, to 0.6 per cent. The interest rate cuts helped the rapid recovery of Hungarian economic growth.

As part of the phase promoting economic growth, on 20 April 2020 the MNB launched the latest extension of its Funding for Growth Scheme (FGS), FGS Go!. Due to the strong interest in this scheme, the MNB increased the available amount of FGS Go! to HUF 3,000 billion in several steps. Thanks to the MNB's Bond Funding for Growth Scheme, the liquidity of the corporate bond market expanded considerably during the coronavirus pandemic, and therefore companies now consider raising funds on the bond market as a genuine alternative to financing from bank loans. The Bank also paid dividends of HUF 250 billion to the government budget twice to contribute to the management of the coronavirus crisis and successfully jumpstart the economy.

The results of the crisis management

Overall, the MNB remained committed to maintaining price stability even during these difficult times, and successfully achieved its primary objective. The trend seen since 2017 was not interrupted in 2020, despite the coronavirus pandemic, and the consumer price index stayed within the central bank's tolerance band for almost the entire year (Chart 3). In 2020, average annual inflation was 3.3 per cent, and thus the central bank maintained price stability in Hungary.

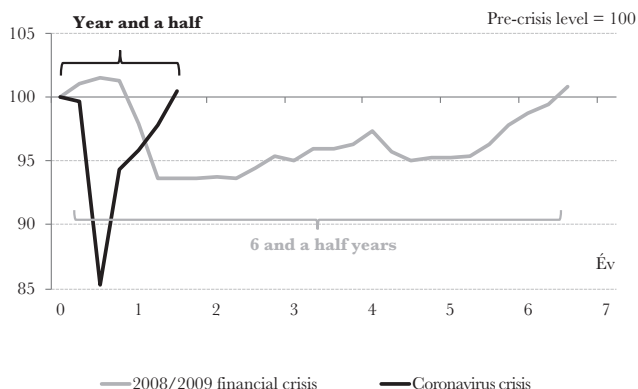
Chart 3. Inflation developments



Source: HCSO

The Hungarian economy returned to its pre-crisis levels in six quarters, whereas after 2008 this took six and a half years (Chart 4). Employment reached new historic highs in May 2021, whereas after 2008 the labour market recovery lasted for five years. Consumption recovered in just seven quarters, while, after 2008, due to the FX lending trap, this took over 10 years. The investment rate of around 20 per cent was among the worst in 2010, while today's rate of over 27 per cent is among the best by international standards. After the 2008 financial crisis, Hungary experienced a total meltdown in its credit market, and it took 10.5 years for lending to resume in earnest. By contrast, thanks to the central bank's successful protection measures, credit markets recovered in the year of the pandemic, after having repelled the effects of the coronavirus pandemic.

Chart 4. GDP recovery after the 2008/2009 crisis and coronavirus crisis



Note: Based on seasonally and calendar adjusted data

Source: HCSO

CONDITIONS HAVE CHANGED AS THE CRISIS SUBSIDES AND ECONOMIES RECOVER

As the crisis subsides, life is returning to normal. From the second quarter of 2021, more and more economies opened up again thanks to the progress in vaccination programmes. Hungary was able to lift the restrictions 1–1.5 months earlier than the EU average in 2021, thanks to the country's high vaccination levels by European standards and the quick, efficient economic policy responses.

Crisis management was successful, the economy was restarted, and now it is time to shift the focus to new challenges. There are 3+1 areas where balance needs to be restored:

- inflation,
- the labour market,
- competitiveness,
- the balance position.

This will help avoid the post-Covid syndrome, and the next decade can be won as well.

Inflation

Inflation is on the rise globally, which is related to the timing and speed of economies' reopening. Inflation appeared earlier wherever the economy recovered faster. In Hungary, inflation returned sooner because of the rapid recovery of the economy and the quick resurgence in demand. Apart from the spikes in inflation, the outlook has clearly risen, driven by both external and domestic factors. Persistent increases in commodity prices and freight costs indicate a higher external inflation environment. Furthermore, Hungary's inflation is also elevated by the rapid wage growth despite the pandemic, the tight labour market and the pick-up in domestic consumption, coupled with the rise in inflation expectations.

As the outlook improves, the Hungarian economy is now faced with a new situation, which requires determined action by the central bank. Now, the primary task is to prevent prolonged inflationary effects and anchor inflation expectations. Persistently high inflation erodes purchasing power and people's accumulated savings, retarding the process of recovery. Currently, 56 per cent of households' financial assets are not protected against inflation. It would be a mistake to underestimate the risk of prolonged high inflation.

Therefore, monetary policy has proactively entered into a new phase, to ensure price stability and support the return to a sustainable economic growth trajectory. Taking this into account, the central bank began its tightening cycle in June 2021, raising the base rate in eight steps to 2.90 per cent (until the finalisation of the manuscript at the end of January 2022). The tightening cycle needs to be continued until the outlook for inflation stabilises around the central bank target in a sustainable manner and inflation risks become evenly balanced on the horizon of monetary policy. The central bank also started to

gradually phase out its crisis management instruments: in June, the MNB announced the termination of the FGS Go! programme as the allocated amount had been depleted, and as a next step, use of the long-term collateralised credit instrument was also terminated effective as of the date of the July monetary policy meeting. After this, the MNB started to gradually phase out the government securities purchase programme in late August. In view of swap market developments, the decision was taken to gradually phase out the swap instrument providing forint liquidity.

Labour market

The Hungarian economy restarted in second quarter of 2021. After reopening, the phase of economic recovery became much faster, which may potentially lead to renewed labour shortages in certain sectors. The first signs of this are already visible, as the share of firms where the lack of available labour represents a potential constraint on production is increasing.

Labour market tightening further fuels the already dynamic expansion in wages. Within the CEE region, the highest wage growth was in Hungary in 2020, and it did not slow down in early 2021. The high wage share in Hungary may translate into a competitive disadvantage for SMEs over the long run. This can already be seen in the fact that small enterprises exhibit slower wage growth early in the year, showing that these firms have little room to increase wages due to their dented profits. Consequently, persistently high wage growth may place these predominantly Hungarian businesses at a competitive disadvantage compared to larger, typically foreign companies over the long run.

Competitiveness

The key to winning the 2020s is to increase the real value of gross value added per capita, in other words to improve productivity. A continued improvement in productivity requires that all relevant reserves be utilised. This is what the MNB's 330-point competitiveness programme is about, as well as the 50-point crisis management programme and the 10-point restarting programme. A complete turnaround in competitiveness is necessary for convergence and for successful crisis management in the future

Balance position

The recipe for the economic success in the past decade was maintaining balance and growth at the same time. Although balance became less important due to the challenges faced last year, this was only temporary. The balance indicators that deteriorated in 2020 need to improve in 2021 and 2022. The task is not simply to restart economic growth and convergence: a sustainable convergence path needs to be devised, with the tools and resources of the recovery. The financial resources necessary for this are already available.

THE IMPORTANCE OF THE GLOBAL MEGATRENDS DETERMINING ECONOMIC DEVELOPMENTS IN THE 21ST CENTURY

The 21st century is strongly determined by global economic and geopolitical megatrends. The momentum generated by these megatrends could benefit the country that turns out to be the best performer of the century. Hungary also needs to ensure balance and growth in this new world, which means that it is crucial to identify and continuously monitor the main megatrends.

Deglobalisation and localisation

Super-globalisation, i.e. the age of economic value creation that eliminates the framework of nations, is now being replaced by deglobalisation, i.e. local and regional production (Manfredi-Sánchez, 2021; Matolcsy, 2020b; Sharma, 2016). In the global production organisation, production and service activities are built on international outsourcing and low stocks. The coronavirus crisis highlighted just how fragile these global value chains are (OECD, 2020; Nandi et al., 2021; Handfield et al., 2021). Therefore, multinational corporations may shorten global value chains during the economic recovery, making them more regional, and increase their reserve stocks. This process is strengthened by the heightened tensions in international trade relations, as the world has entered a long “Cold War” due to the rivalry between the USA and China.

Localisation developments are supported by the fault lines within the euro area, exacerbating the strains between northern and southern Member States. Due to the institutional shortcomings of the euro area, common monetary policy leads to development for the north and more lagging behind for the south. This is not helped by further increase in indebtedness (Matolcsy, 2021d). A larger amount of money does not solve the qualitative issues with money. A separate euro would be needed for the north and the south. This seems to be impossible today, but it is still the beginning of the decade. New central bank digital currencies may provide a theoretical opportunity for broadening Europe’s monetary room for manoeuvre and introducing a dual exchange rate regime.

Existing euro area members are interested in new joiners being appropriately mature before entering the currency area. Until the appropriate foundations are established, there is no guarantee for a successful and safe introduction of the euro (MNB, 2020). The past year has shown that the forint outperformed the euro in repelling the financial and economic consequences of the coronavirus pandemic. This would not have been possible with the euro, as the central bank was able to use more targeted instruments during its crisis management with the forint. It is in Hungary’s best interest to ensure that the switch from the forint to the euro is safe and thus successful.

Digitalisation and the data revolution

Digitalisation changes everyday life. The information economy has been rapidly developing due to the coronavirus, which may not only help spread the innovations of today’s Fourth Industrial Revolution in the economy and society as a whole, but may also contribute to the

emergence of the Fifth Industrial Revolution based on artificial intelligence. Although this could lead to the disappearance of low-skilled jobs, many new, high-skilled jobs are being created. A good example for this is the reduction of human labour in certain sectors, while new occupations emerge, such as programming and data science (Shah et al., 2015). Skills- and practice-oriented specialised and further training can ensure that workers remain flexible in the new world, and increasing the number of graduates is also crucial. As a result of mass digitalisation, data is replacing raw material as the major resource of the 21st century, and its protection is a key responsibility (Seele–Lock, 2017).

International experiences show that a persistently high investment rate of about 25–35 per cent of GDP is required for economic convergence (Matolcsy, 2021a). The most important driver of sustainable convergence is the expansion of productivity, which is best increased by digital investments. If there are few digital investments and the share of construction projects is high, there is little room for boosting productivity. Even in today's crisis, those who previously focused more on the digital transition were better off. Mass digitalisation requires significant investments, which calls for raising huge amounts of fresh capital.

In digital finance, the MNB set an example by introducing the instant payment system in March 2020. In recognition of the successful introduction of the system and the unparalleled Hungarian model in the international arena, the MNB received the prestigious prize of the Central Banking Institute on 22 March 2021 (MNB, 2021c).

Transformation of the monetary system: central bank digital currency

The 21st century not only brings breakthroughs in production due to the digital revolution, the same can be seen in the financial system as well (Matolcsy, 2020c). As the coronavirus pandemic spread, reducing cash use became even more important (Boar–Wehrli, 2021), and this may lead to renewed calls to provide households and non-financial actors with electronic access to central bank money. As a result of the financial revolution, access to money will be generally quick, cheap and secure.

As cash use is reduced, the next step in financial evolution could be central bank digital currencies (Auer–Böehme, 2020). Central bank digital currencies will allow central banks to enter into more direct relationships with real economy actors, thus enabling them to more easily influence the latter's savings and investment decisions (BIS, 2018). This new type of money could fundamentally alter the way financial systems work and money is created. Therefore, several central banks are studying the issue of central bank digital currencies and their potential applications (Chart 5). In order to join other central banks spearheading central bank digital currency research, the MNB published a comprehensive volume of studies in July 2021 (MNB, 2021a).

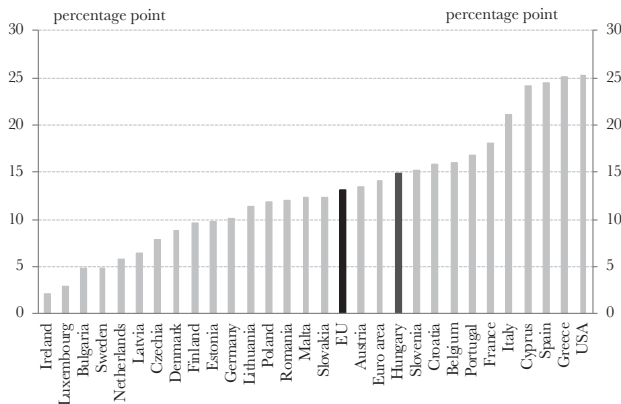
Chart 5. Countries researching central bank digital currency



Source: Edited by MNB based on Auer et al. (2020), CBDCTracker (2021) and central banks' websites
Sustainable debt management and tax reform

With the outbreak of coronavirus crisis, nations around the world went on a spending spree, increasing their government debt (Chart 6). According to the proponents of the modern monetary theory, the size of government debt does not matter anymore, because low interest rates mean that any debt can be repaid. The EU and the euro area may follow in the footsteps of Japan, where the debt-to-GDP ratio is over 260 per cent, around half of which is on the central bank's balance sheet (Matolcsy, 2021b). At the same time, debt will always be debt, and sustainability issues may resurface as the crisis subsides. Even a slight but persistent rise in inflation could suddenly change central banks' policies. Interest rate hikes could quickly make it difficult to finance debt, including government debt, hampering sustainable growth.

Chart 6. Change in government debt as a share of GDP between 2019 and 2020



Source: Eurostat, OECD

Dynamic, sustainable growth requires appropriate debt management as well as a competitive, growth-friendly tax regime and a sufficiently diversified financing system. Hungary has made great strides in establishing a growth-friendly tax regime in the past ten years. The idea behind a tax system encouraging employment and investments is that tax centralisation should shift from taxes on labour and capital towards consumption taxes: in other words, income is taxed when spent rather than when it is earned (Matolcsy–Palotai, 2018). The next step in the development of such a competitive tax regime could be the national taxation of cross-border digital services and the more active application of green taxes on polluting activities.

Green finance

Climate change has undoubtedly become one of the greatest challenges for humanity in the 21st century. Its signs and detrimental consequences can be acutely felt every day (IPCC, 2021). At the same time, it has also become clear that the previously pursued growth model is not sustainable, and a transformation of economic structure is needed that can ensure achievement of the national economy's objectives while preserving natural resources. Climate-related risks have a major direct and indirect impact on how the economy operates, and so they can influence financial stability and the monetary policy stance as well (BIS, 2020; NGFS, 2021). Therefore, sustainable growth requires not only the promotion of innovation and digitalisation but also the use of green solutions.

The natural, social and economic developments entailed by climate change shape the central bank's tasks arising from its mandate. Extreme weather events impact price levels, real economy output and labour supply, while the transition to a green economy represents a huge financing requirement on the financial markets; thus, climate-related risks both directly and indirectly jeopardise the primary objective of the central bank, i.e. the achievement and maintenance of price stability. Meanwhile, physical and transition risks affect companies' profitability, and thus also their creditworthiness along with the performance of other related financial assets, and may ultimately undermine the stability of the entire financial intermediary system. Moreover, several central banks also have a mandate pertaining to the real economy: therefore, they must address the challenges related to the implementation of environmental sustainability.

It is no coincidence that major central banks are also focusing on environmental sustainability (Dikau–Volz, 2019). It can be safely stated that the MNB recognised the importance of this topic in good time: it introduced several practical measures in recent years, thereby setting an example and pioneering such efforts at the international level. The Green Programme launched in 2019 as the flagship project and featuring a substantial supervisory aspect deserves special mention. The programme focuses on measures aimed at financial system stability and a favourable financing environment, but it also covers the promotion of climate-consciousness and the reduction of the MNB's own ecological footprint as well.

In a historic step, with its decision on 28 May 2021 Hungary's Parliament gave statutory authorisation to the MNB to support the government's policies related to environmental sustainability. The foundations of this new central banking approach were laid by the green

monetary policy toolkit strategy announced on 6 July 2021 (MNB, 2021b), the main thrust of which is to provide a uniform framework and to point out the potential ways for the MNB to incorporate climate protection and environmental sustainability considerations into its monetary policy instruments. This can contribute to the green transition and the establishment of a financial intermediary system efficiently and broadly integrating environmental aspects, which is crucial for Hungary's sustainable convergence.

Halting climate change and the transition to a green economy model requires not only pledges but also action, as soon as possible. The aim of the two pioneering initiatives, the FGS Green Home Programme and the Green Mortgage Bond Purchase Programme, is to facilitate green mortgage loans, i.e. loans extended for homes with the appropriate energy efficiency. The two programmes can make a targeted contribution to the construction of modern homes and the emergence of a more uniform stock of properties, which is key from a sustainability and a national economy perspective as well.

SUMMARY

As a result of the economic policy renewal, significant economic convergence has taken place in the last decade, while a sustainable internal and external balance has also been achieved. As a result, Hungary faced the coronavirus pandemic and its economic effects with a strong immune system and the recovery was rapid.

However, as the crisis subsides, more work remains to be done: we need to restore balance again and implement a turnaround in competitiveness to redirect the economy back to a sustainable path. In the competitive environment of the 21st century, economies which are able to harness emerging international megatrends by accentuating their own strengths will be the winners. Deglobalisation processes require that the role and structures of local cooperation be revisited, as they should be made sustainable. Investment in digital solutions offers a great competitive advantage to the countries that recognise the importance of this in time and focus their resources on such efforts. As part of this, the financial system could be transformed when central bank digital currencies appear. Tax regimes need to be revised, and debt must be made sustainable. Besides economic balance, the economy's ecological sustainability also has to be ensured, as this is the only way to achieve genuinely sustainable growth. Central banks have a huge part to play in this. By recognising and utilising international megatrends and strengthening the factors that promote competitiveness, Hungary can be among these economies.

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