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IMF Loans to Hungary, 1996–2008

Summarty: Hungary has been an IMF member since May 1982 and has since benefited from the IMF's lending instruments on 11 occasions. The IMF loans supported economic transformation (in the period between 1988 and 1993), facilitated Hungary in overcoming the transformation recession (in 1996) and helped to tackle economic crisis (in 2008). This paper analyses the two latter IMF loans in order to provide background context to Hungary's IMF negotiations, ongoing since November 2011.Ever since 1982, Hungary could always count on the efficient support of the IMF and – should this be necessary – this may be the case in the future as well. The Monetary Fund is a 'lender of last resort'; it is never a good sign when a country is forced to turn to the IMF instead of market financing. This can only be avoided with an adequate economic policy that allows the country to find permanent and continuous external financing 'with acceptable terms and conditions'.

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It is a well-known fact that Hungary became a member of the International Monetary Fund on 6 May 1982 (and as is customary, the World Bank shortly thereafter). Over the past three decades, public and professional attention only turned to the IMF when Hungary applied for a loan-otherwise, relatively few works dealt with the IMF or its relationships with Hungary (See Csáki, 1988; Brüll, 1993; Báger, 2011). Given the fact that Hungary has been in talks with the Monetary Fund since November 2011 on potentially taking out a new loan, we should review the credit relationships between IMF and Hungary-from the regime change until present day[1] (See Appendix).

On 6 May 1988, the IMF management approved a *stand-by loan of SDR 265.35 million,* to be disbursed in five equal instalments over the course of 12 months. The loan was not considered to be of a significant amount and *its primary objective was to support the reform processes that started in Hungary in 1988.* The conditions of the loan were primarily focused on the reduction of the budgetary deficit-the reason we could not call the fifth instalment of the loan was primarily because we did not comply with the budgetary adjustments we had committed to (See Báger, 2011, pages 105–106). The IMF wanted to support the regime change and the transformation to a market economy from the start, which is why it made a decision to disburse a small SDR 159 million standby loan to Hungary on 14 May 1990-the fifth instalment of which we could not call, because a new, and much larger (SDR 1.114 billion) 36-month loan agreement was concluded on 20 February 1991 under the extended credit line.

The fate of the three-year extended stand-by facility approved in 1991 was quite turbulent: On 23 March 1992, the IMF made

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a positive decision on the disbursement of the last instalment of the credit line approved for 1991-albeit it should have made a decision on the calls due in 1992 by the end of February-which failed to happen. During the talks of September-October 1992, the agreement was concluded on the disbursement of the remaining instalments of the extended stand-by facility based on the key figures approved. The main condition of the 1992 IMF loan-similarly to all previous IMF loans-was the substantial reduction of state income redistribution and the decrease of the volume of public finances in proportion to the GDP.[2] In the second half of 1993, there was no need to draw on the instalment due, and in 1994 the option to do so was no longer available-due to the increase of the budget deficit.

A UNIQUE 'PRECAUTIONARY' STAND-BY LOAN, 1996

Effective as of 1 January 1996, Hungary accepted the provisions of Article VIII of the IMF Articles of Agreement regarding the convertibility of the national currency. The IMF press release on the matter emphasised that: *"IMF members accepting the obligations of Article VIII undertake to refrain from imposing restrictions on the making of payments and transfers for current international transactions or from engaging in discriminatory currency arrangements or multiple currency practices without IMF approval"* (IMF, 1996/a). *The last paragraph of the press release contains the specifics of the Hungarian commitment: "By accepting the obligations of Article VIII, Hungary gives confidence to the international community that it will continue to pursue sound economic policies that will obviate the need to use restrictions on the making of payments and transfers for current international transactions, and thereby contribute to a multilateral payments system free of restrictions. The acceptance of the obligations of Article VIII comes after a new foreign exchange law took effect on January 1, 1996. As a result of this law and accompanying regulations, Hungary's exchange system is now free of exchange restrictions on the making of payments and transfers for current international transactions"* (ibid. – highlighting by the author: Gy. Cs.).

As is known, the fundamental goal of the Bokros-package launched in March 1995 was to manage the transformation crisis that had been delayed until that point. At the centre of the programme was the crawling-peg exchange rate policy introduced in the wake of the one-off devaluation, which was able to take the wind out of speculation against the Hungarian forint, to finance public debt at a predictable rate and to continuously reduce inflation (by 6 per cent per annum).[3] The Horn administration already began talks with the IMF in the autumn of 1994 on the possibility of taking out a stand-by loan. On 5 June 1995, *Michel Camdessus*, the Managing Director of the IMF at the time met with Prime Minister *Gyula Horn* in Budapest. Camdessus welcomed the measures adopted in March (i.e. the Bokros-package), and emphasised in the communication released by the IMF that the monetary fund's staff will cooperate closely with Hungary in the continued implementation of the programme. The IMF formulated five main objectives with regard to the 1996 budget (IMF, 1995):

- a substantial reduction in the government deficit, aimed (in concert with monetary, exchange rate, and income policies) at securing the government's objectives for inflation and the balance of payments;
- monetary and wage policies targeted at a significant reduction of inflation and the maintenance of international competitiveness within the framework of the crawling-peg exchange rate policy;

- structural reform of the public sector-that is, improved fiscal control mechanisms, a more efficient public administration, a broadening of revenue bases so as to reduce distortionary elements of the tax system, and adjustments in the social security system to safeguard its viability while providing adequate assistance to those in need;
- structural reform of enterprises and providing a renewed impetus to privatisation;
- an external current account balance consistent with no increase in foreign debt, without relying on exceptional inflows associated with privatisation.

Managing Director Camdessus *"said he would be prepared to recommend to the Executive Board that IMF financial support be provided for a government programme that would realise these objectives."* (ibid.)

Under these conditions, on 15 March 1996, the management of the IMF approved a stand-by loan in an amount of SDR 264.18 million (USD 387 million) (IMF, 1996/b).[4] The press release started off by emphasising that this concerns *"the next 23 months to support the Government's economic programme through end-1997. The Hungarian authorities do not intend to make any drawings and to treat the stand-by as precautionary"* (ibid.). The goal of the loan-supported economic policy was to consistently continue the economic policy started in 1995, as a result of which, the Hungarian government-supported by the IMF's analysis and projection-expected moderately dynamic growth and consistently declining inflation, increasingly manageable external indebtedness and disciplined fiscal management. The following structural reforms were set out in the stand-by arrangement: *"improving budget planning, monitoring and execution, and placing different levels of government on sounder financial footing; strengthening the social security system; restructuring and privatising state-owned enterprises, including banks; and continuing the liberalisation of international transactions"* (ibid.). The credit agreement did not forget about the needs of the social sector either, and stipulated that: *"The objective of the reform of the social security system is to generate enough savings to allow for a significant reduction in contribution rates, while ensuring the viability of the system. Reform of provision of medical services will be undertaken while ensuring adequate support to the truly needy"* (ibid.).

"On 15 March, after a lengthy period of yearning, it seems the Hungarian government was finally approved a loan, of which it is not planning to utilise a single forint" – was the introduction to the expansive article published in HVG on the credit arrangement (Réti, 1996). Interestingly, the article, which analyses the Horn administration's economic policy in a highly critical manner, considers the IMF loan inconsequential due to the upcoming OECD membership: *"The reduction of the interest rates of the loans to be taken out by the MNB could be more significantly impacted by Hungary's accession to the OECD, which-according to experts-could instantly do away with the 20-30 per cent interest premium the lenders otherwise charge to 'plain old transitional' Hungary"* (Réti, 1996, page 10). *Gusztáv Báger* calls the 1996 stand-by credit-without any further explanation-"an agreement of symbolic importance" (Báger, 2011, page 110). Although the statement is true, it does not define the purpose and point of this "symbolic" stand-by credit agreement, albeit, as referenced above, the IMF was well aware of the fact that Hungary had no intention of actually calling the credit. That is because on 7 May 1996, Hungary became the 26th member of the OECD after South Korea and the Czech Republic, ahead of Mexico and Poland. This was tremendously important in 1996; it was a sign of recognition

that Hungary, having overcome the crisis of transformation, was irrevocably on its way to becoming a member of the community of developed countries. This huge victory of prestige made financing our external debt considerably easier (and much cheaper), and improved Hungary's ability to attract capital even further. Nonetheless, joining the OECD was conditional upon concluding a two-year stand-by credit agreement with the Monetary Fund, in which Hungary undertook to continue the macro-economic processes launched in 1995.[5] One of the more interesting features of the 1996 credit agreement is that at this time the Monetary Fund did not have a precautionary stand-by arrangement on offer. This arrangement became a possible form of the stand-by credit after its overhaul in 2009, i.e. after the eruption of the crisis (IMF, 2012).

CRISIS LOAN, 2008

On 15 September 2008 one of the largest investment banks of New York with a history of 150 years, Lehman Brothers filed for bankruptcy, and the United States government did not bail it out. This date was the "date of birth" of the global financial crisis-although it had been obvious since the collapse of the American mortgage lending market in the summer of 2007 that the international currency and financial system was fraught with serious systemic errors. After 15 September 2008 a serious liquidity crisis quickly emerged on the international money markets; stock markets plummeted and international lending froze. The management of the IMF quickly assessed the situation and came up with a list of immediate potential clients. On 26 October 2008, the management released a statement on the fact that: *"The International Monetary Fund (IMF), which has announced its readiness to lend billions of dollars to support nations hit by fallout from the global financial turmoil, is holding talks with several countries about possible new lending programmes"* (IMF 2008/a). The statement named four countries: Iceland, Pakistan, Ukraine – and Hungary. At the same time, Dominique Strauss-Kahn, IMF Managing Director at the time announced that the IMF had reactivated the Emergency Financing Mechanism set up in 1995 (which had last been used by the IMF 10 years earlier during the South-East Asian financial crisis) and emphasised that the IMF has more than USD 200 billion of loanable funds and can draw on additional resources (ibid.).

On 26 October 2008, Mr. Dominique Strauss-Kahn issued a statement: *"An IMF staff mission and the Hungarian authorities, in close consultation with the EU, have reached broad agreement on a set of policies that will bolster the Hungarian economy's near-term stability and improve its long-term growth potential. The authorities' programme will ensure fiscal sustainability and strengthen the financial sector. A substantial financing package in support of these strong policies will be announced when the programme is finalised in the next few days. Participants will include the IMF, the EU, and some individual European governments, together with regional and other multilateral institutions. With Hungary's commitment to strengthened economic policies, we expect that banks and other financial institutions operating in the country will continue to provide adequate financing. The Fund's assistance, in the form of a Stand-By Arrangement, will be considered by the IMF's Executive Board for approval under the Fund's expedited procedures. The policies Hungary envisages justify an exceptional level of access to Fund resources"* (IMF, 2008/b).

Two days later, the IMF bulletin published the specific amount of the imminent IMF loan-along with the expected commitment of joining international organisations.[6] The "Global Economic Crisis" tagline said it all and summed up the essence of the article: IMF, EU, and World Bank Line Up $25 Billion for Hungary (IMF, 2008/c). The brief summary of the article emphasises three points: Hungary has a comprehensive policy package to restore investor confidence; the programme's core measures aim to strengthen the financial sector; the fiscal steps to reduce government financing needs ensure debt sustainability. According to the article, the objective of the USD 25.1 billion financing package for Hungary is "to bolster its economy, hit by recent financial market turbulence." The press release repeats the contents of the statement made by Strauss-Kahn two days earlier, namely that the IMF is ready to lend Hungary USD 17.7 billion (= EUR 12.5 billion) under a 17-month Stand-By Arrangement, which would be adopted by the Board under the Fund's emergency procedures in early November. At this point, it was already clear that the EU would provide a loan of EUR 6.5 billion (= USD 8.45 billion) and that the World Bank would contribute to the tune of EUR 1 billion (= USD 1.3 billion) to the total loan package. Perhaps the most important sentence(s) of the article: *"Core measures under the programme are designed to improve fiscal sustainability and strengthen the financial sector. Specifically, the package includes measures to secure adequate domestic and foreign currency liquidity, as well as strong levels of capital for the banking system"* (ibid. – highlighting by the author: Gy. Cs.).

On 4 November 2008, the Hungarian government, with the signatures of Minister of Finance *János Veres* and MNB President *András Simor,* sent the letter of intent regarding the stand-by loan to IMF Managing Director Dominique Strauss-Kahn[7] (IMF, 2008/e), and as a result the IMF management reached a decision on 6 November 2008 (IMF, 2008/f).

The press release issued on the credit decision repeats the elements already described, and goes on to quote *John Lipsky,* Deputy Managing Director of the IMF at the time who announced the management decision, in length, who said: *"With the decline in global liquidity and increase in risk aversion, financial markets in Hungary came under intense pressure, given Hungary's high debt levels and significant balance sheet mismatches. Several government bond auctions failed, liquidity in the secondary bond market dried up, and bond yields rose sharply. At the same time, the stock market fell and the currency depreciated. Reducing financial market stress will require both a high degree of policy discipline and large external financing. The authorities' comprehensive set of policy measures, supported by the 17-month Stand-By Arrangement under the Fund's exceptional access policy, is designed to strengthen Hungary's economy and thereby foster a reduction in financial market stress. (…) Most important, the combination of accelerated fiscal adjustment and the introduction of a rules-based fiscal framework will help persuade investors that the government's short- and medium-term financing needs are being addressed"* (ibid.).

The appendix to the press release begins by presenting the economic situation, starting off with the fact that Hungary was among the first to suffer from the global financial crisis, primarily due to Hungary's extremely high public debt and significant balance sheet mismatches. *"Even though macroeconomic and financial policies had been strengthened since 2006, with substantial fiscal consolidation and tax administration improvements, Hungary was hit hard by the global deleveraging"* (ibid.). The three most important elements of the economic programme supporting the IMF loan were: the fiscal adjustment of 2.5 per cent of current GDP, bank capital enhancement and the necessity of external financing assistance. The press release concludes with a macro-economic projection, which calculates with a 1 per cent drop in GDP, a 4.5 per cent consumer price increase and an unemployment rate of 8.5 per cent[8] (ibid.).

Hungary had the option to call the facility in six equal instalments during the period between 12 November 2008 and 15 February 2010 (the latter deadline was extended by the IMF until October 2010). The loan will be repaid in eight equal instalments following a grace period of two years and three months. *"The amount drawn on was placed by the state at the MNB as a foreign exchange deposit and will only be converted into HUF if necessary. Part of the amount (to the value of HUF 600 billion) was used to finance the bank support package"* (Báger, 2011, p. 112). The first instalment, SDR 4.215 billion, was drawn by the MNB (on behalf of the state) effective as of 12 November 2008. Overall during the call period extended until 5 October 2010, Hungary called SDR 7.637 billion from the available SDR 10.5375 billion. The repayment obligation was SDR 1.903 billion in 2012, will be 3.8185 billion in 2013 and 598.31 billion in 2014, and these principal repayments will also incur SDR 70.85, 53.96 and 4.5 million in interest, respectively (IMF, 2012/c). The IMF loan was not simply one of the external funds available to our country in a global financial environment characterised by a shortage of funds, rather it was an especially cheap external fund. The costs of IMF loans are public and are available on the organisation's website and updated on a daily basis. The-variable-SDR interest rate is available on the homepage of the IMF website, to which a 0.5 per cent handling fee is added and an interest premium, which depends on the size of the loan: 100 basis points on the amount of credit outstanding above 200 per cent of the quota, and 200 basis points on the amount of credit outstanding above 300 per cent of the quota. During the period between the awarding and the calling of the loan the IMF deducts a commitment fee, which is refunded once the loan is called. At the time of the disbursement of the first instalment, the SDR interest rate was 2.71 per cent-therefore, if the entire loan amount were to have been drawn, it would have incurred an interest of 5.51 per cent.[9]

MNB's usual quarterly report (MNB, 2008) was very cautious in its wording on 15 October 2008; it indicated the risks-macro-economic risks and those of the financial intermediary system as well-but did so with restraint.[10] With respect to the level of foreign exchange reserves (EUR 17.409 billion), the quarterly report indicates only a slight increase (ibid., p. 6). The report, naturally, made no references to the ongoing IMF negotiations. The MNB report for the second quarter of 2008 primarily focuses on the circumstances of the outbreak of the crisis and the appropriate monetary counter-measures (MNB, 2009). MNB's assessment clearly attributes Hungary's financial difficulties to the global economic crisis: explaining the increasingly difficult financing of public debt with the general aversion to emerging markets.[11] The central bank goes on to present the measures it has taken in the interest of ensuring interbank liquidity, emphasising the cooperation agreement concluded with the European Central Bank on 16 October 2008.[12] Strangely, the MNB quarterly report describes turning to the IMF differently than the public documents that had been available for three months at that point.[13] *"On 21–22 October, the exchange rate of the forint was subject to significant devaluation pressure in excess of a fundamentally justifiable magnitude. At its extraordinary meeting, the Council reacted with a decision to increase the base rate by 300 basis points. The aim of the rate increase was to maintain the* *stability of the financial intermediary system, to contain a further increase of capital outflows and devaluation expectations and to make speculation against the forint more expensive. In parallel with this decision, negotiations were held with the International Monetary Fund and other organisations, as a result of which, a total credit line of EUR 20 billion was provided to Hungary. On the one hand, the loan allows for the financing of public finances even under the most unfavourable market conditions, and on the other, it significantly increases the foreign exchange reserves of the central bank. As a result of these measures, Hungary's risk assessment improved and the vulnerability of the financial intermediary system decreased considerably. The exchange rate stabilised, speculative positions were eliminated, and even turnover was generated on the foreign exchange swap and government securities market, though at a lower rate than previously"* (MNB, 2009, p. 4).

Naturally, the stand-by arrangement stirred up a storm-in the press and politics alike. A particularly thorough and comprehensive article was published in Magyar Narancs, which presented the main issues in a precise and objective manner (Bogár László – Mészáros Bálint – M. László Ferenc, 2008). After outlining the situation in October 2008 and presenting Hungarian risks, the paper confirms that talks had already begun with the IMF and the EU/ECB on 9 October- as opposed to what was stated in the above quoted MNB report. *"On Thursday, 9 October, when the Hungarian forint and the shares of OTP took a huge dive one thing was clear: The National Bank and the government must display an immediate show of force." "Although the EUR 17.4 billion foreign currency reserves of the MNB represent a formidable counterweight, they could melt relatively quickly if the forint were to run away. If someone is in defense mode, they must adapt to and mimic the rhythm of their assailant, but initially everyone fights almost blindly, because the intentions and tactics of the speculator are unknown. It was difficult to guess how much money was needed to slow things down"* – said an influential politician within the Cabinet to Magyar Narancs. Therefore, the crisis committee that was convened that same night, consisting of the Prime Minister, the Minister of Finance and the Central Bank Governor has come up with several different scenarios and have also prepared for the worst case scenario. Since the European Union has no well-established crisis management methods, it was clear that only the IMF would be capable of averting the danger with respect to currency problems (ibid.). In spite of emergency measures on the part of the government and the MNB, the situation failed to improve and the pressure on the Hungarian financial system did not let up.[14] The Hungarian government securities market already dried up once in the spring of 2008 for three weeks; however, the situation on that particular occasion was overcome. In October, however, the external environment was much more adverse; the bankruptcy of Lehman Brothers on 15 September 2008 (and the concurrent announcement made by the US government that is was not going to bail out the esteemed 160-year-old investment bank) and the sovereign default of Iceland increased the money market risks experienced by emerging countries to an incredible degree. In mid-to late October 2008 it seriously looked as if Hungary had become the target of global speculative attacks. The agreement struck by the MNB and the ECB, and half of the EUR 12 billion bailout fund available within the EU at that time was not sufficient to stabilise the Hungarian money markets; the quick conclusion of an agreement with the IMF, as literally the only means to escape sovereign default, – became essential. *"First and foremost, the country was saved from sovereign default by the news of an IMF-ECB-*

World Bank loan agreement; the sobering power of this piece of news was just as great as the momentum of the brutal attack against forint launched on 8 October. The size of the credit line surprised analysts, who expected a package of around EUR 10 billion, calculating with the difference between the short-term debt portfolio of the country (app. EUR 26 billion) and the foreign currency reserves of the MNB (app. EUR 17 billion). The amount of the standby credit available until March 2010 was exactly twice this amount, of which 6.5 billion was provided by the EU, 12.5 billion by the IMF and 1 billion by the World Bank. The loan cost less than half (5–6 per cent interest depending on the tenor of 3–5 years) of what it cost to get open market funding on the government securities market in October (by promising yields of 13–14 per cent); therefore this loan under the current circumstances was not only a much needed bailout, but a source of significant savings" (ibid.).

The Hungarian press commented on the ongoing talks between the IMF and Hungary in the last week of October and the first days of November following the publication of the IMF communications. *"The government only struck a deal with the IMF by the end of last week, also intended to boost confidence by the latter. Moreover, there is still a need for a five-party agreement, because the Washington-based international financial organisation requires Parliamentary approval"* (Csabai, 2008, p. 9). At the 30 October session of Parliament Minister of Finance János Veres described the conditions of the IMF loan including all the commitments the government intended to undertake to manage the crisis, and lay the foundations of sustainable growth in the medium term, to be recorded in the letter of intent to be sent to the IMF. At the five-party talks Ferenc Gyurcsány, in the words of HVG, *"was trying to drum up support for the mega loan agreement to be signed with the IMF"* (Csabai, 2008, page 8 – highlighting by the author: Cs. Gy.). At this point, experts estimated the mega loan to amount to USD 12.5 billion-unaware of whether the financial assistance by the European Commission should to be included in this amount or not.

During the four weeks (9 October to 4 November 2008) of loan negotiations, political debates were subdued-the borrowing put an end to this restraint. During the discussion on the 2009 budget, the critical situation of Hungary was already apparent, a fact that was mirrored by the proposed budget bill. Naturally, the opposition parties vehemently criticised the draft budget foreshadowing stagnation-at the same time, however, SZDSZ that has previously withdrawn from the government coalition and the opposition-party MDF have indicated their willingness to vote in favour of the budget (See Farkas, 2008/a). Considering that at those budget debates the IMF was not mentioned at all-29 October marked the first instance-today it is entirely conceivable that this part of the budget debate was based on a five-party behind-the-scenes agreement. Of course, both political sides were quick to utilise the announcement of loan talks to further their own merits, and at the same time, to criticise the other side. 29 October 2008 was the first time Prime Minister Ferenc Gyurcsány spoke publicly about the IMF loan. In an interview given to M1 [Hungarian state television channel], he said that on the night of 9 October 2008, MNB President András Simor called the Monetary Fund, while the government contacted the EU. According to the Prime Minister, *"Hungary was granted a loan by the International Monetary Fund several times its quota, because overall we did what we did well";* in other words, he and his fellow ministers, *Gordon Bajnai* and János Veres have a great ability to enforce their interests. The PM stated: the credit facility serves as show of 'deterrent force' which says *"it is useless to attack us while we have such allies"*. The Prime Minister referred to the fact that attacks were launched against the Hungarian forint and OTP in the second week of October (Origo, 2008). The opposition was quick to strongly criticise the government's decision. *"Ferenc Gyurcsány has sat Hungary on the cutty-stool as it is the only EU Member State that is forced to apply for a loan from the IMF"* – declared Fidesz spokesperson Péter Szijjártó. He added, it is very clear that *"inadequacy, impotence and hesitance of governance"* are what forced the Gyurcsány administration to apply for the loan, *"while all other EU Member States had found the appropriate solutions for the crisis"*, adding: *"What Ferenc Gyurcsány accomplished with the past six years of governance is that we fall into the same category as the Ukraine, Belarus and Pakistan"* (ibid.). In the last two weeks of talks, however, opposition criticisms were definitely more subdued.[15]

Prime Minister Ferenc Gyurcsány and Minister of Finance János Veres both contributed greatly to the difficulties surrounding the IMF loan and the ensuing unfounded political debate, after both exclaimed that "we are not going to spend" the money; its only purpose is to stabilise the position of Hungary on the foreign and money markets (See Farkas, 2008/b). These were obviously senseless statements, because the IMF loan (and the additional ECB and World Bank loans) allowed Hungary to finance the renewal of its external debt for exactly half the price of the 9-10 per cent-interest euro loans available to it at the time.

A few days after the IMF management decision and the drawing of the first loan instalment, the debate took an 'interesting' thematic turn. It is not surprising that the opposition utilises an IMF loan to criticise the government: since the very beginning of its operation, the IMF has been a 'lender of the last resort'; member countries only turn to it for loans if they are unable to ensure financing from the international money markets or are only able to do so at an unrealistically high cost (which is unsustainable in the long-term). This is why applying for an IMF loan in itself indicates a grave economic situation- and nothing is simpler than for the current opposition to blame the current government for this situation.[16] However, in Hungary, it was the *"agreement with the Monetary fund"* and the making of the letter of intent public that became the issues of political debate. In Gusztáv Báger's excellent analysis covering all relevant issues, we should pay attention to two typically subdued remarks by the author: *"(The letter of intent and its annex are public.)"* and *"No separate loan agreements have been executed."* (Báger, 2011, p. 111 – highlighting by the author: Gy. Cs.). The two sentences are not very uplifting in the context of the political debate on the IMF loan; therefore, they refer to the two statements understandably "modestly" handled by Gusztáv Báger.

Mihály Varga, Fidesz Member of Parliament (at the time) on 17 November 2008 said the following at the Parliamentary session in his pre-agenda address: *"it was the Prime Minister who not so long ago assured us that once the agreement is concluded, they will present it to the members of the Hungarian Parliament as well. Allow me to quote several of the Prime Minister's statements! On the 4th of November in Madrid, he said: a process is beginning which will end in the conclusion of a loan agreement. This may take several days or even weeks. On the 31st of October, Ferenc Gyurcsány once again assured us, this time on a radio programme that they will make the agreement public, and he repeats this in an earlier press statement as well. This is complemented by a statement by the Minister of Finance, who said: knowing the contents of the IMF agreement is a realistic, though not timely* *need – János Veres said this to be precise on the 2nd of November"* (Varga, 2008). Following the strong criticism of the person of Prime Minister Gyurcsány and repeatedly calling his credibility into doubt, he continued: *"Here it is (…) It is a question of is there an agreement or isn't there. Wouldn't it have been more elegant for you to say, I was wrong? Or perhaps say that you had been misinformed by the IMF staff? But no, instead you come with accusations and keep slandering the people who have previously said: if there is such an agreement, it must be shown to the Hungarian public"* (ibid. – highlighting by the author: Gy. Cs.). Minister of Finance János Veres replied on behalf of the Prime Minister, and emphasised that the opposition parties were also provided information on the letter of intent at the closed session of the National Assembly's Budget Committee-prior to the decision of the IMF management. He added: *"You know perfectly well that it was precisely due to the high interest in Hungary that, in contrast with previous procedures and general rules of proceedings, prior to the directorate meeting, we informed the Parliament committee of the Hungarian conditions and the contents of the letter of intent, and that as soon as it was possible, we also informed the public thereof. The honourable MP knows full well that in this regard we have held a professional discussion about the type of contract and agreement to be concluded, which information has been disseminated to the members of the parliamentary committee in its entirety, as was the fact that the loan amount was not going to be called, rather transferred to the foreign currency reserves of the National Bank of Hungary, under the first phase, concurrently with the decision"* (Veres, 2008). In terms of the issue of the *"contract"*, the Minister of Finance said the following in response to the question of the MP: *"In connection with the issue of how an agreement can be established – and I am sure the lawyers can define this much more precisely than I can –: if anyone here thinks that there is only one type of agreement to be concluded, namely the kind where the two parties sign their names on the last page, they are obviously wrong. I don't want to be the one to hand down information about this, after all I am not a lawyer, so I just want to say, that there are several ways in which an agreement can be concluded, and it will be still binding on all the parties, on the lender as well as the borrower, just as it would if it were to be concluded under different circumstances. Whatever is concluded as a result of a letter of intent and a decision is also a contract, and the public parameters and public conditions are transparent and are there for all to see, regardless of those involved, on the website of the IMF and ever since the decision was made, the conditions are available on the website of the Ministry of Finance as well"* (ibid. – highlighting by the author: Cs. Gy.).

The above presented parliamentary debate was a not so cheerful manifestation of Hungarian political folklore. The Monetary Fund operates on the basis of the Anglo-Saxon legal order-ever since the start of operations in 1946-and any given loan agreement between a member country and the IMF is concluded on the basis of the letter of intent by the former and the management decision made based on the letter. In Anglo-Saxon legal systems, the letter of intent is of binding force and it is on the basis of this that the IMF management decides on the disbursement of the loan. In the letter of intent, the member country applying for a loan presents the economic policy measures it is looking to take, in other words, explains what it needs the financial assistance of the Monetary fund for-this means that the borrowing country exclusively takes responsibility for the economic policy programme related to the IMF loan. According to the continental interpretation of law, agreements signed by both parties do not exist in the IMF's practice. The debate presented clearly shows that neither *Prime Minister Gyurcsány, nor Member of Parliament Mihály Varga were aware of how the Monetary Fund operates* and that their experts/advisors failed to brief them on this, *while Minister of Finance János Veres was unable to accurately explain the situation to the Parliament's plenary session!*

As far as the political 'debate' regarding the letter of intent is concerned, we must note that in the past the Monetary Fund did not make these letters of intent public, but recently they have been made available on the IMF homepage, in the *What's New* column. The letter of intent in question was posted on the IMF website dated 4 November 2008, i.e. the date of the management decision, was also posted on the site two days later as an appendix to the Staff Paper and was also featured in the document published on the site on 17 November (along with the Staff Report and the minutes of the management meeting) (IMF, 2008/g). At the same time, it is also well-known that the press release and its appendix always contains the main economic policy measures the member country undertakes in the letter of intent, as well as the macroeconomic consequences-expected by the IMF-thereof during the term of the given loan. At the same time, given the nature of the IMF's decision-making system-since indirectly all member countries are represented in the management, the monetary authorities of every member country are familiar with every document related to every loan-the representatives of all member countries are familiar with the documents related to all the loans. As a result, being familiar with the exact text of the letter of intent does not convey any new information in the borrower member state, just as keeping them secret does not mean that the given member state wants to keep its economic/financial troubles secret from the monetary authorities of the rest of the member states. Moreover, the IMF "greeted" the Hungarian credit application in a rather multi-faceted manner (see IMF, 2008/a, IMF, 2008/b, IMF 2008/c, and IMF, 2008/d). And in a truly unusual manner, the IMF- officially-announced the main details of the standby credit line to be disbursed to Hungary on 26 October 2008, about which the board of supervisors "only" made a decision on 6 November. As a result of the political debate that was spurred around the "contract" and the letter of intent in Hungary, which was rare albeit not unheard of in the history of the Monetary Fund, the Hungarian letter of intent signed on 4 November 2008 was also independently uploaded to the website of the IMF (IMF, 2008/e)-with a comment described under note no. 20 obviously with reference to the debate.

* * *

As in the case of relationships between the IMF and any of the member countries, there may be disagreements and debates in the relationship between the IMF and Hungary. It is also clear that the IMF did not always understand every real problem of transforming economies applying for loans. Our experiences show that in the period from 1982 to 2008, Hungary could always count on the efficient support of the IMF. We have no reason to doubt that-should this be necessary-this may be the case in the future as well. Of course, the Monetary Fund is a 'lender of the last resort'; it is never a good sign when a country is forced to turn to the IMF instead of market financing. This can only be avoided with an adequate economic policy that allows the country to find permanent and continuous external financing 'with acceptable terms and conditions'.

APPENDIX

Loans provided to Hungary by the International Monetary Fund, 1982 – 2012, SDR million (as of 31 May 2012)

Loan type	Date of loan approval	Date of the disbursement of last instalment	Amount approved, SDR million	Amount drawn, SDR million
Stand-by arrangement	6 November 2008	5 October 2010	10,537.50	7,637.00
Stand-by arrangement	15 March 1996	14 February 1998	264.18	0.00
Stand-by arrangement	15 September 1993	14 December 1994	340.0	56.70
Stand-by arrangement	15 September 1993	14 December 1994	340.00	56.70
Extended financing facility	20 February 1991	13 September 1993	1,114.00	557.24
Compensatory financing facility	16 January 1991	16 January 1991	226.2	226.2
Stand-by arrangement	14 March 1990	19 February 1991	159.21	127.37
Stand-by arrangement	6 May 1988	6 May 1989	265.35	215.4
Stand-by arrangement	13 January 1984	12 January 1985	425.00	425.00
Compensatory financing facility	15 December 1982	15 December 1983	72.00	72.00
Stand-by arrangement	8 December 1982	8 January 1984	475.00	475.00

Source: http://www.imf.org./external/np/fin/tad/exfin2.aspx?memberkey1=415&data1Key=2012-05-31. Downloaded on: 9 July 2012

Notes

1 The table included in the Appendix contains the main data of all loans provided to Hungary by the IMF.

2 By 1993 the budgeted deficit of public finances was 6.9 per cent of the GDP, and according to the conditions of the IMF loan this should have dropped to 5.3 per cent by 1994 calculating with real growth of 1–3 per cent.

3 By the beginning of 1996 the macro-economic results of the programme were already apparent, which, however, did not prevent the "fall from grace" of the Minister of Finance, Lajos Bokros. The temporary increased customs duty applied for 18 months-in line with the rules of the WTO-was an important part of the Bokros package, as were a number of specific measured designed to cut back on budgetary spending. The speeding up of the privatisation process, the "mass" privatisation of public utility companies at the end of 1995, was quite unfairly not regarded as part of the Bokros package, although the nearly USD 4 billion proceeds generated from the privatisation played a fundamental role in reducing the external debt. At this time, Hungary had the strongest ability to attract capital and the massive FDI flowing into the country made financing the current account deficit unproblematic. These circumstances contributed to the extremely rapid success of the Bokros package: In 1995–1996, Hungary embarked on a clearly export-driven growth path, the fruits of which we were able to enjoy until 2000–2001.

4 At this point, Hungary's quota was SDR 754.8 million (USD 1,105 million), i.e. the amount of this stand-by loan was equal to only 35 per cent of our quota (at the time).

5 In addition, this is also the explanation for the remarkably low amount (and the remarkably low

ratio compared to the quota) of the stand-by loan approved: apart from 'offering guarantees', the IMF only wished to tie up very few of its resources, and Hungary was indifferent to the amount of the 'loan' it did not wish to call down.

[6] On the very same day, the IMF also released its press release on the loan package for Hungary (See IMF, 2008/d). The very last paragraph was also of equal significance: "We will continue assisting the Hungarian authorities on how to adapt to the current global financial turmoil and to catalyse financing as needed," said Strauss-Kahn" (ibid.).

[7] The Letter of Intent is available on the IMF website (IMF, 2008/e). The cover page has an interesting comment: "The following item is a Letter of Intent of the government of Hungary, which describes the policies that Hungary intends to implement in the context of its request for financial support from the IMF. The document, which is the property of Hungary, is being made available on the IMF website by agreement with the member as a service to users of the IMF website."

[8] A few days after the awarding (and disbursement) of the loan the detailed report of the staff of the IMF (Staff Report) was published on its website, providing a 27 page summary (and an additional 13 pages of tables) of the opinion of the staff of the IMF on the situation and prospects of the Hungarian economy. Attached to this paper as an appendix is the Hungarian letter of intent-which was made public for the first time by the IMF in this specific format (IMF, 2008/g).

[9] Author's own calculation-based on the following formula: 0.2x2.71 + 0.1x4.71 + 0.7x5.71 + 0.5 = 5.51. The commitment fee was only a temporary burden for the borrower and, therefore, shall not be taken into account.

[10] "The MNB paid special attention to assessing the impacts of international trends on Hungary and identifying the possible risks. Within the operating environment of the Hungarian financial system, the risks identified in the "Report on Financial Stability" published in April had strengthened in the recent period. Owing to increasing global risk premiums, the unfavourable liquidity conditions of the domestic financial sector may become permanent, economic growth may remain at a low level due to external and internal factors, and the risk-based competition between banks could become fiercer. Entering the second year of the subprime mortgage crisis, the financial markets continue to be characterised by uncertainty. Meanwhile, the ongoing adjustment in the financial sector has contributed to negative effects on the real economy. At the same time, the domestic financial sector has significant capital reserves; its shock resilience is strong. The domestic interbank market is functioning smoothly, and there is adequate forint liquidity in the financial system. Though the conditions for accessing foreign funding have clearly deteriorated, funding liquidity has not dried up. While credit portfolio quality has declined, the ratio of non-performing loans to the total portfolio remains low. It is important to emphasise that although the profitability of the domestic banking system was declining, it is still high in European comparison, and that its capital reserves are significant" (MNB, 2008/a, p. 5).

[11] "While previously emerging markets were just brushed by the side-wind of the crisis, after September, the government securities considered a 'safe haven' (e.g. German, American) up until that point and investment targets considered risky for any reason separated sharply. The decline in the willingness to take risks led to severe problems in the operation of financial markets, primarily in the foreign exchange swap and government securities markets, and for shorter periods liquidity disappeared completely" (MNB, 2009, p. 4).

[12] "The MNB attempted to alleviate the market turmoil by expanding its set of instruments

and with other, non-interest measures. On 10 October, it introduced two-way FX swap quick tenders providing euro and forint liquidity to manage this market turmoil. On 16 October, the MNB and the European Central Bank concluded a cooperation agreement under which the MNB introduced an overnight FX swap standing facility providing new euro liquidity. The central bank has also intervened on the government securities market and has come to an agreement with Primary Dealers on the joint assumption of roles. In accordance with this, both parties support the equilibrium of the demand and supply side of the government securities market by reinforcing market demand, and MNB, for its part, supports it by introducing new credit instruments" (ibid.).

[13] See for instance Prime Minister Ferenc Gyurcsány's-quoted-television interview from 29 October 2008 (Origo, 2009), as well as the IMF documents-also quoted-from October 2008 (IMF/2008/a, IMF, 2008/b and IMF, 2008/c).

[14] "Over the next few days everyone's worst fears seemed to have come true; none of the measures taken by the government seemed to have any effect. The Cabinet re-wrote the draft budget, withdrew its tax cut bill, cut its government security issuance, gave a government guarantee on deposits, and made it possible for pension funds to purchase government securities instead of shares. However, the weakening of the forint did not stop there and repeatedly crossed the 280 mark; the shares of OTP dipped HUF 1 thousand below their book value, and the BSE underperformed the stock exchanges of the world that were already in the red at the time. Considering that even the EUR 5 billion currency swap of the MNB and the European Central Bank helped, and no one could be certain that the fall would stop after the 3-per cent base rate hike of the National Bank of Hungary on 22 October, there was an increasing need for assistance from the IMF (László Bogár – Bálint Mészáros – Ferenc M. László 2008).

[15] "Although the Monetary Fund always confers with the decision-makers of a given country, there are signs that they managed to include the opposition through various channels, or at least conveyed the sense to their leaders that the country was in big trouble and that they should be more permissive with the minority cabinet. The MDF and the liberals seemed to be ready to vote in favour of the budget-Károly Herényi, MDF faction leader said on Klubrádió [commercial radio station in Hungarian widely perceived to be leftward leaning in terms of political orientation] "we must overcome the foolish issue of who is going to support the budget". The two smaller parties were expected to get the support of the MSZP faction to pass the budget ceiling bill. Although the Fidesz have not let up with their criticism of the Cabinet, Viktor Orbán conspicuously eased up on his tough-guy rhetoric (on 22 October he was still demanding that Gyurcsány step down) and turned the floor over to his Minister of Finance, Mihály Varga, known for his precise negotiating skills, and let Lajos Kósa take charge of the anti-Gyurcsány outbursts" (László Bogár – Bálint Mészáros – Ferenc M. László, 2008).

[16] "Democratically elected governments are not re-elected if they are forced to apply for an IMF loan" goes the old saying-and quite rightly so. This is also the result of the fact that in addition to the opposition's successful emphasis on the responsibility of the government, and that IMF loan conditions always contain austerity measures, devaluation increases inflation, etc.

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Hungary repaid ahead of schedule yesterday (12 August) all of its outstanding debt, worth â‚¬2.15 billion euros, owed to the International Monetary Fund from a 2008 emergency loan programme, the Economy Ministry said in a statement. The central European country, which used a â‚¬20 billion euro aid deal from the IMF and the European Union to avoid insolvency as the crisis gripped its markets in 2008, has been at odds with the Fund under its current government, which took power in 2010.Â Based on a summary by the country's debt agency, Hungary had been due to repay the equivalent of â‚¬913 million to the IMF in each of the third and fourth quarters and another â‚¬299 million in the first quarter of 2014, an election year. IMF Survey online. November 6, 2008. Loan part of financing package with European Union, World Bank. Program aims to restore confidence in Hungary's financial markets. Cuts in budgetary expenditures needed to ease short-term financing pressures.Â Apart from Hungary, the IMF has been discussing with a number of other countries about loans to help them fend off the impact of the global financial crisis, which has triggered a worldwide economic downturn. The IMF approved a $16.4 billion loan for Ukraine on November 5. The IMF approval makes $6.3 billion immediately available and the remainder in five installments subject to quarterly reviews. BUDAPEST (Reuters) - Hungary repaid ahead of schedule on Monday all of its outstanding debt, worth 2.15 billion euros, owed to the International Monetary Fund from a 2008 emergency loan programme, the Economy Ministry said in a statement. The central European country, which used a 20 billion euro aid deal from the IMF and the European Union to avoid insolvency as the crisis gripped its markets in 2008, has been at odds with the Fund under its current government, which took power in 2010. Prime Minister Viktor Orbanâ€™s government, which faces an election in 2014, has sought to end what is has po