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The end of the recession is unpredictable

The forecast prepared by GKI Economic Research Co. in co-operation with Erste Bank shows that both the depth and duration of the global recession are for the time being completely unpredictable. In 2009 the decline of GDP in the entire European Union will probably close to 2%, within this the downturn in Germany and consequently in Hungary will be somewhat deeper. At the moment it appears that the situation will most likely start improving in late 2009, but the actual developments could be more positive or more negative alike.

It is almost sure, that the deficit of the general government in Hungary will well below the Maastricht criterion in 2009. Strict monitoring of the IMF agreement makes the fulfillment of the 2.6% deficit target very likely. There is a risk on the revenue side stemming from the larger than originally planned decline of the economic activity and lower inflation, which cannot be outweighed by the expected higher wages – because of the decreasing employment. The reserve account of the budget will likely be insufficient to fully compensate for this. Nevertheless, the deficit can be reduced. If there is a need, some revenue items, e.g. the excise tax on fuel can be (temporarily) increased. Given the decreasing inflation, certain expenditure items can be partially frozen. At the same time, it is also essential to reduce the current account deficit, as the money market situation has made foreign financing very difficult and expensive. Practically, it is the shortage of funds that makes the reduction of external deficit indispensable. Improvement can be achieved through increase of the trade surplus and the EU transfers.

In 2009 the output of the Hungarian economy will shrink by approximately 2.5%. This will be attributable to two factors: first, the expected decline in the output of agriculture assuming average weather conditions following the sector's growth in 2008; second, the increasingly rapid decline in the rest of the business sectors, which started already in 2008. Industrial production is expected to decrease by 3%, but –after the significant decline in the first half of the year – fourth quarter could bring some growth compared with the low basis figures. The downturn in the construction sector – that started two years ago – continues in 2009 (although by only 3%). The scarcity of credit sources holds back the public, business and household investments. The competition that has been characteristic in most of the business sector becomes more intense due to the shrinking demand. This will likely result in bankruptcies in the category of smaller undercapitalized businesses and in large-scale acquisitions across the globe at a number of well-capitalized corporations. The shortage of funds will intensify the problem of debt chains. On the other hand, the terms of trade will improve by 1% in 2009.

Gross earnings will rise by about 4% in the business sector, while the public sector will see a 1% decline. Overall, this will yield a modest, approximately 1% drop in real terms. Inflation will fall rapidly in early 2009, as global energy and agricultural prices drop. The annual average price increase expected to be 2.8% (around 2.5% at the end of the year). The savings propensity of households will be rising. This will be attributable partly to unavoidable circumstances (limited access to credit and rising costs) and partly to interest (high yields and interests on deposits, rising down payments for loans, which, in turn, take longer to raise). Consumption expected to fall at a faster rate than real earnings (by about 2.5%). Investments will continue to decline in 2009, approximately to the level of 2004. This is due to the recession as well as the shortage (and unrealistically high price) of credit. Net EU transfers will be up from 1.5 billion euros in 2008 to 2.5 billion in 2009.

Forecast of GKI Economic Research Co. on Developments in the Hungarian Economy in 2009

	2006	2007	Jan-Oct 2008	2008	2009
				(estimate)	(forecast)
1. Volume of GDP (%)	104.1	101.1	101.5*	100.7	97.5
2. Industrial production (constant prices %)	110.1	108.1	100.4**	100.0	97.0
3. Investment in the national economy (constant prices %)	93.8	101.5	97.1*	98.0	97.0
4. Construction (constant prices %)	98.4	85.9	92.7	94.0	97.0
5. Retail trade (volume index)	104.4	97.0	98.1	98.5	97.0
6. Exports (current prices in euro %)	116.6	115.7	107.4**	106.5	100.0
7. Imports (current prices in euro %)	113.9	111.9	107.2**	106.0	98.0
8. Trade balance (bn. euros)	-2.4	-0.1	0.1**	0.0	1.2
9. Combined balance of the current and capital accounts (bn. euros)	-6.2	-5.4	-5.0*	-6.2	-3.0
10. Average exchange rate of euro (forints)	264.3	251.3	251.2***	251.2**	255
11. Deficit of the general government (cash flow basis, without local governments; bn. forints)	2034	1291	907.1***	907.1**	620
12. Index of average gross earnings	108.1	108.2	108.1	107.8	102.5
13. Consumer price index	103.9	108.0	106.3**	106.1	102.8
14. Consumer price index at the end of the period (corresponding month of the previous year=100)	106.5	107.4	104.2**	103.8	102.5
15. Rate of unemployment (at the end of the period, %)	7.5	7.7	7.8****	7.9	8.5

* Q I-III. 2008

** Jan.-Nov. 2008

*** Actual annual data

**** Sept.-Nov. 2008

Sources of actual data: CSO, NBH, MoF