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Decreasing inflation, weak forint

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. Domestic inflation decreases faster than expected earlier, although the forint is much weaker than last year.

The January prognosis of the European Commission forecasts an almost 2% decline of GDP in the EU during 2009; within which the contraction will be somewhat stronger in Germany and smaller in Hungary. The forecast of GKI is more pessimistic: it expects a 2.5% decrease of GDP in Hungary but – in accordance with the opinion of the European Commission – anticipates some improvement by the end of 2009. Much stronger decline is expected in the Baltic States, Ireland and UK. In Bulgaria, Slovakia and Romania – where the growth rate in 2008 was more than 6% – 4-6 percentage points slowdown is expected.

It is almost sure, that the deficit of the general government in Hungary will be well below the Maastricht criterion in 2009. Strict monitoring of the IMF agreement makes the fulfillment of the deficit target very likely. Most probably the government will counterbalance the shortfall of the revenue caused by the deeper than expected recession and lower than planned inflation; moreover it will regroup certain items in the budget (or in the tax system). The European Commission forecasts 2.8% general government deficit for Hungary, which is much smaller than the 4.4% average of the EU and is the tenth smallest deficit in the EU-27. The fast reduction of the balance of payments deficit became inevitable as well, because in the present money market situation the access to foreign sources is both difficult and costly. In fact, the scarcity of sources compels the reduction of the external deficit. The improvement will take place due to increase in the trade surplus and the EU transfers. This year the balance of payments deficit as a percentage of GDP expected to be around the European average.

Gross wages are expected to grow by 4% in the business sector and to decrease by 1% in the public sector, which altogether means a minimal decrease of real earnings. Nevertheless, the consumption and investments of households will decrease perceptibly because of the growing burden of amortization of debt, contraction of credit sources and rising borrowing costs. At the beginning of 2009 inflation decreases rapidly – as global energy and agricultural prices drop. The annual average price increase is expected to be 2.3%, but at the end of the year it will be somewhat higher: around 2.5% – because of the lower basis. In the conditions of low demand and strong competition an eventual increase of the VAT would have limited impact on the prices.

Between the end of December and end of January the exchange rate of the forint against the euro weakened from 265 to 300. This was due mainly to international developments, since the currencies of other nations in the region weakened similarly. In January the Central Bank continued its cautious cuts in the base rate; this policy is expected to be continued during the year.

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

	2006	2007	Jan-Nov 2008	2008	2009
				estimate	(fore- cast)
1. Volume of GDP (%)	104.1	101.1	101.5*	100.7	97.5
2. Industrial production (constant prices %)	110.1	108.1	98.9**	98.9**	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	93.8	94.0	97.0
5. Retail trade (volume index)	104.4	97.0	98.2	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**	270
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	108.2	108	102.5
13. Consumer price index	103.9	108.0	106.1**	106.1**	102.3
14. Consumer price index at the end of the period (corresponding month of the previous year=100)	106.5	107.4	103.5**	103.5**	102.5
15. Rate of unemployment (at the end of the period, %)	7.5	7.7	8.0***	8.0***	8.5

* Q I-III. 2008

** Actual annual data (2008)

*** Q IV. 2008

Sources of actual data: CSO, NBH, MoF