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Real earnings will moderately, consumption significantly decrease

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 still unpredictable; but forecasts all over the world are more and more pessimistic. In Hungary real earnings decrease moderately, while consumption declines significantly. Investments in the business sector drop because of the limited demand and the scarcity of resources.

The bottom of the global recession is expected in 2009. This year a 2-3% decline is probable in the GDP of the EU in spite of numerous concerted international actions intended to stabilize the economy of the European Union. The growth rate of the Hungarian economy was 0.6% in 2008. In 2009 the output of the economy will decrease by 3-4%. This is a more pronounced decline than what was expected earlier and is a consequence of drop in external and internal demand.

It is practically sure that by the end of 2009 the deficit of the general government in Hungary will be below the Maastricht criterion (3%). 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 trade surplus and EU transfers.

Gross earnings will rise by about 4% in the business sector, while the public sector will see a 1% decline. Overall, this will yield an almost 1% drop in real terms. (In 2008 real earnings increased by 0.7%, thus in two years real earnings will remain basically unchanged.) Nevertheless, consumption and investments of households will perceptibly decrease because of the increasing burden of debt service, limited access to and rising costs of credit, plus strengthening propensity of households to save. Household consumption will decrease by about 3%, investments by about 5% – due to deteriorating market conditions and scarcity of sources.

Inflation will fall rapidly in early 2009, as global energy and agricultural prices drop. Price increases will be only around 2% by May. In the second half of the year inflation will probably accelerate as a result of the planned increase of VAT and excise duties, plus the weak forint – although the weak demand and the keen competition will limit the price increases. Thus, the annual average price increase is expected to be 3.3%, but by the end of the year it will be somewhat higher: around 4.4%.

Between the end of December and end of January the exchange rate of the forint against the euro weakened from 265 to 300; in early March it weakened further. Until the recent days this could be explained basically by international developments, since all the national currencies of the region weakened similarly. The weak forint substantially increases the debt service burden of those persons and firms whose liabilities are in foreign currencies, but is favorable for the tourist industry and for those firms that compete with imports. Its positive impact on the exports is limited by the exchange rate volatility.

In February – i.e. in the period of weakening of the forint – the central bank did not continue the policy of cautious rate cuts, but it is expected that the presently 9.5% base rate will be reduced during the rest of the year.

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

	2006	2007	2008	2009 (forecast)
1. Volume of GDP (%)	104.1	101.1	100.6	96.5
2. Industrial production (constant prices %)	110.1	108.1	98.9	90.0
3. Investment in the national economy (constant prices %)	93.8	101.5	97.0	95.0
4. Construction (constant prices %)	98.4	85.9	94.9	95.0
5. Retail trade (volume index)	104.4	97.0	98.2	97.0
6. Exports (current prices in euro %)	116.6	115.7	105.6	95.0
7. Imports (current prices in euro %)	113.9	111.9	105.6	93.0
8. Trade balance (bn. euros)	-2.4	-0.1	-0.2	1.5
9. Combined balance of the current and capital accounts (bn. euros)	-6.2	-5.4	-5.7*	-2.5
10. Average exchange rate of euro (forints)	264.3	251.3	251.2	280
11. Deficit of the general government (cash flow basis, without local governments; bn. forints)	2034	1291	907.1	620
12. Index of average gross earnings	108.1	108.2	107.5	102.5
13. Consumer price index	103.9	108.0	106.1	103.3
14. Consumer price index at the end of the period (corresponding month of the previous year=100)	106.5	107.4	103.5	104.4
15. Rate of unemployment (at the end of the period, %)	7.5	7.7	8.4**	8.7

* GKI estimate

** November 2008 – January 2009

Sources of actual data: CSO, NBH, MoF