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Waiting for the bottom

According to the forecast of GKI Economic Research Co. prepared in co-operation with Erste Bank, the bottoming out of the Hungarian economy is still to come, GDP is likely to drop by about 6.5 per cent this year. Agriculture and export-oriented industries will suffer the greatest losses. The second half of the year will see a stronger HUF than before and accelerating inflation.

The drop in industry slowed down by the end of spring 2009. Although in May output growth was modest totalling 2.6 per cent compared to April, GKI's index that aggregates industry's business cycle indicators has been growing since April. The cyclical indices of the EU as well as Germany - Hungary's most important export market - also indicate somewhat declining pessimism. Nevertheless, there has been no signs of industrial recovery yet and it is not clear which industries could recover first. Construction output in volume terms declined further in May (by 3.3 per cent compared to April) and the industry became markedly divided: whereas civil engineering expanded by 7.9 per cent in the first five months of 2009, the construction of homes experienced steep fall (-24.1 per cent). The value of contracts already signed is 26 per cent higher than one year before, which anticipates growth in output; however, this process may start only in 2010, and mostly in civil engineering. In May contraction in retail trade turnover did not accelerate further, but from July on the decline will probably gain momentum again. For the whole year, the greatest drop is expected in the sales of furniture, electronic devices, construction materials and passenger cars. In the first five months real earnings were down by 2.2 per cent, in 2009 2.5 per cent overall decline is forecast. As a consequence of rising unemployment, decreasing credits and the increasing propensity to save (which is enforced rather than totally voluntary), the disposable income of households decreases more than real earnings.

By June general government deficit climbed to 0.9 per cent of GDP; for 2009 a 3.8 per cent deficit is forecast. In the first five months imports dropped more than exports: the resulting EUR1.5 billion foreign trade surplus is considerable. This trend is likely to continue until the end of 2009, thus an EUR2.8 billion surplus is expected, which corresponds to 3.1 per cent of GDP. Since foreign trade balance is more favourable than in the previous years, the annual external financing requirement also drops, to about 2.2 per cent of GDP.

In the second half of 2009, the consumer price index will temporarily increase as a result of the increase of VAT and excise tax rates; the December-December index will climb close to 7 per cent. The annual average rate of inflation is expected to total 5 per cent - reconsidering this figure is justifiable if and when the actual impact of tax increases can be assessed. The international inflationary wave - the likely result of economic stimulus packages adopted in many countries - will be imported in the Hungarian economy only from the middle of 2010. Hungary's assessment by international investors turned better as a result of improving external and internal disequilibria: this and the generally more optimistic investment climate helped the successful issuance of bonds denominated in euro. At the end of July - in a period of quiet capital and money markets - the National Bank of Hungary reduced its reference rate by 100 base points. This step was welcomed in the external financing environment and thus far the exchange rate of the forint to the euro was left virtually untouched. Until the end of 2009, further cuts in the reference rate are expected, by December it may be close to 7 per cent. The exchange rate of the forint to the euro is expected to average HUF270-HUF275 in the second half of 2009 with smaller volatility than in the first six months; the annual average exchange rate is projected to total some HUF280.

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

	2006	2007	2008	January-May 2009	2009 (forecast)
1. Volume of GDP (previous year=100)	104.1	101.2	100.6	93.6*	93.5
2. Industrial production (constant prices, previous year=100)	110.1	108.1	98.9	76.7	82
3. Investment in the national economy (constant prices, previous year=100)	93.8	101.5	97.0	92.3*	92
4. Construction (constant prices previous year=100)	98.4	85.9	94.9	93.1	93
5. Retail trade (volume index, previous year=100)	104.4	97.0	98.2	96.2	95
6. Exports (current prices in euro, previous year=100)	116.6	115.7	105.6	73.5	86
7. Imports (current prices in euro, previous year=100)	113.9	111.9	105.6	69.3	82.5
8. Trade balance (EUR billion)	-2.4	-0.1	-0.2	1.5	2.8
9. Balance of the current and capital accounts (EUR billion)	-6.2	-5.4	-7.8	0.3*	-2.0
10. Average exchange rate of euro (forints)	264.3	251.3	251.2	287.5***	280
11. Deficit of the general government (cash flow basis, without local governments; billion forints)	2034	1291	907.1	816.4**	960
12. Index of average gross earnings	108.1	108.2	107.5	101.4	102.4
13. Consumer price index (previous year=100)	103.9	108.0	106.1	103.3**	105
14. Consumer price index at the end of the period (corresponding month of the previous year=100)	106.5	107.4	103.5	103.7**	106.8
15. Rate of unemployment (at the end of the period, per cent)	7.5	7.7	8.0	9.8****	10.5

* first quarter 2009
** first half year 2009
*** January-July 2009
**** March-May 2009
Sources of actual data: HCSO, NBH, MoF