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Demand on export markets and EU funds can support recovery

According to the forecast of GKI Economic Research Co. prepared in co-operation with Erste Bank a 6.5 per cent drop of GDP is expected this year and stagnation is to come in 2010. Despite the tax raise, inflation accelerates only moderately, external disequilibria improve markedly, and internal disequilibria are in line with international requirements.

The Hungarian economy has probably reached the bottom of recession: compared with the preceding quarter, some growth is expected in the fourth quarter of 2009; however, in comparison with the corresponding period of the previous year, some little growth is likely only in the second half of 2010.

In September the output of industry and construction was 3.7 per cent higher than in August. Monthly fluctuations are considerable in both sectors. However, in industry, the increases are usually higher than the declines: in December, too, there can be some growth compared with the same month in 2008 and the trends for next year are linked to the European business cycle. It is somewhat promising that the GDP of Germany - Hungary's main export market - may grow by more than 1 per cent according to the most recent forecasts, however, the question is to what extent the improvement of recent months is the result of one-off factors (such as the cash for clunkers schemes used to stimulate car sales). Upswing in the construction sector is to come in 2010 only - due to the temporary growth at the end of last year - however, its expansion next year (about 6 per cent) will be more marked than that of industry (3-4 per cent). Still, it will be not the result of business or household investments, but infrastructure development projects co-financed by the EU. In the third quarter the number of homes completed was less by almost one-fourth than a year before, and throughout 2009 it may drop below 30 thousand, and close to 20 thousand in 2010 - half the peak of 2004. Actually this is the level of 2000 (prior to the introduction of the housing support scheme).

Imports decline much more than exports because domestic demand contracts. In 2010, however, imports will grow more than exports (in euro terms) as domestic demand stabilises and the terms of trade deteriorate due to rising global energy prices. Consequently, the foreign trade surplus contracts, however, in the balance of the current and capital accounts it will be offset by the increase of EU-transfers. In 2009-2010 Hungary will probably not need net external financing, because the loans already taken will be used either to lift foreign exchange reserves or to repay loans borrowed earlier.

In 2009 real incomes are likely to drop by 4-5 per cent because real earnings fall by 2 per cent, employment by 3.5-4 per cent, the 13th month pension was abolished and family subsidies do not increase in nominal terms. In 2010 real incomes are expected to stay flat. Consumer prices were 4.9 per cent higher in September than one year before; this price index is lower than expected before and by the end of 2010 the rate of inflation can drop to about 3 per cent. Despite the considerable contraction of the economy, the general government deficit will be around 3.9 per cent of GDP in 2009. In 2010 a 3.8 per cent deficit is expected, similar to the official target. International money markets would tolerate a substantially higher deficit only if this implies one-off capital spending and restructuring, and if a programme to achieve a sustained decrease of the deficit - supported by structural reforms - is elaborated.

Forecast of GKI Economic Research Co. on Developments in the Hungarian Economy in 2009-2010

	2008.	2009. I-IX. hó	2009 (forecast)	2010 (forecast)
1. Volume of GDP (previous year=100)	100.6	92.8	93.5	100
2. Industrial production (constant prices, previous year=100)	98.9	79.0	84	103.5
3. Investment in the national economy (constant prices, previous year=100)	97.0	92.9	93	106
4. Construction (constant prices, previous year=100)	94.9	97.3	96.5	106
5. Retail trade (volume index, previous year=100)	98.2	95.6	95	100
6. Exports (current prices in euro, previous year=100)	105.6	76.8	86.5	104
7. Imports (current prices in euro, previous year=100)	105.6	70.7	80	106.5
8. Trade balance (EUR billion)	-0.2	3.3	4.5	3.0
9. Balance of the current and capital account (EUR billion)	-6.5	0.6*	0.5	0
10. Average exchange rate of euro (forints)	251.2	282.7**	280	265
11. Deficit of the general government (cash flow basis, without local governments; billion forints)	909	1047.7**	1000	870
12. Index of average gross earnings	107.5	101.2	101.5	101
13. Consumer price index (previous year=100)	106.1	104.0**	104.2	103.5
14. Consumer price index at the end of the period (corresponding month of the previous year=100)	103.5	104.7**	105.3	103
15. Rate of unemployment (at the end of the period, per cent)	8.0	10.4***	11	10.5

* first half of 2009
** January-September 2009
*** August-October 2009
Sources of actual data: HCSO, NBH, MoF