May 31. 2010.

After recession, before substantive growth

According to the forecast of GKI Economic Research Co. prepared in co-operation with Erste Bank, following the end of the recession in statistical terms in the first quarter, there will be an approximately 1 per cent GDP growth in 2010, which will be the consequence of increasing external demand and investments financed by EU funds.

In May the European Commission raised its autumn forecast for the EU from 0.7 per cent to 1 per cent, whereas the figure for Hungary was changed to stagnation from the 0.5 per cent decrease that had been projected earlier. However, according to the Central Statistical Office data released in the meantime Hungary's GDP grew somewhat in the last quarter of 2009 compared with the preceding one and it was followed by a further 0.9 per cent GDP growth in the first quarter of 2010 being one of the highest rate in the EU. As a consequence, an approximately 1 per cent growth is forecast for Hungary this year.

In May the Greek crisis and its uncertain resolution caused distrust in the euro and the EU leading to the weakening of the euro vis-?-vis major currencies. In many EU member states the interim improvement of the general government balance was put on the agenda, which causes the drop of domestic demand in the countries concerned. It has a negative impact on trade within the EU as well. However, the weak euro helps exports beyond the EU borders, which is favourable for instance for German and hence Hungarian exports.

The programme of the new government does not tell much about the economic policy steps to be taken. Obviously, the Greek crisis narrows the room of manoeuvring for the new government; restrictions are the agenda in almost all European countries. Under such circumstances the general government deficit - which, in theory and with deliberate government measures could be close to the 3.8 per cent target approved of by the Parliament - may not reach 5 per cent of the GDP even if consolidation expenditures and the related structural reforms are taken into account.

As a consequence of the formation of the new government, changes in the organisational structure of the administration and staff, government decision making is likely to slow down substantially for some time, however, investments and projects co-financed by the EU may speed up based on the decisions made earlier. Unemployment has already reached its peak; in the next months some improvement is expected due to seasonal effects (there will be additional employment in agriculture, construction and tourism).

The Hungarian rate of inflation was 5.7 per cent in April, the highest in the EU. However, if not adjusted for the tax changes, the price index was only 1.5 per cent. In the first half of 2010 the rate of inflation will still be above 5 per cent, but it will moderate to 3-3.5 per cent by the end of the year, and it may drop below the 3 per cent targeted by the National Bank of Hungary by the end of 2011. As a consequence of the Greek crisis, the Hungarian currency will be weaker than what had been expected before, but - if economic policy is aligned with international financial trends - the forint will be stronger than in these days: a HUF/EUR annual average exchange rate of HUF270 is expected in 2010.

The balance of the current and capital accounts continues to climb out of the red: the EUR6.5 billion deficit in 2008 was followed by an EUR1.4 billion surplus in 2009, which may further increase in 2010. The foreign trade surplus decreases somewhat since domestic demand slightly improves and slowly expanding profits also imply higher repatriation. EU transfers can be higher as well.

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

	2008	2009	March 2010	2010 (forecast)
1. Volume of GDP (previous year=100)	100.6	93.7	100.1	101
2. Industrial production (constant prices. previous year=100)	98.9	82.3	104.5	104.5
3. Investment in the national economy (constant prices. previous year=100)	97.0	91.4	93.6	103
4. Construction (constant prices. previous year=100)	94.9	95.7	89.8	101
5. Retail trade (volume index. previous year=100)	98.2	94.8	95.4	98
6. Exports (current prices in euro. previous year=100)	105.6	81.1	116.9	110
7. Imports (current prices in euro. previous year=100)	105.6	75.3	112.1	111.5
8. Trade balance (EUR billion)	-0.2	4.0	1.3	3.5
9. Balance of the current and capital account (EUR billion)	-6.5	1.4	-	1.8
10. Average exchange rate of euro (forints)	251.2	280.6	268.4*	270
11. Deficit of the general government (cash flow basis. without local governments; billion forints)	909	918.6	637*	1200
12. Index of average gross earnings	107.5	100.5	105.7	103
13. Consumer price index (previous year=100)	106.1	104.2	105.9*	104.3
14. Consumer price index at the end of the period (corresponding month of the previous year=100)	103.5	105.6	105.7*	103.3
15. Rate of unemployment (at the end of the period. per cent)	8.0	10.5	11.8**	11.0

* January-April 2010
** February-April 2010
Sources of actual data: HCSO, NBH, MoF