

June 5, 2005.

The deficit is higher than planned but lower than last year

According to the forecast made by GKI Economic Research Co. in cooperation with Erste Bank, this year the growth of the Hungarian economy will be somewhat slower than last year. At the same time real earnings will grow dynamically, while the savings of households will also increase faster than earlier. The deficit of the general government will be lower than in 2004 but higher than originally planned.

After the 4.1% growth in the 4th Qtr 2004 the Hungarian economy expanded by 2.9% in 1st Qtr 2005. The growth rate has declined in the eurozone as well: from 1.5% to 1.3%. Even the relatively modest performance of the Hungarian economy is due mostly to the service sector - partly to public administration. All productive sectors have slowed down with the sole exception of the construction sector. In the industry in the 1st Qtr the expansion of the exports was slower than the increase of domestic sales, which is a very rare situation. Even the domestic sales increased mainly as a result of the energy production.

At the same time investments gained momentum after the stagnation in the 4th Qtr of 2004, although this was only due to motorway constructions. Investment in the manufacturing industry started to grow again - although slowly - after the drop at the end of last year. In the 1st Qtr construction type investments increased altogether by 12%, while machinery investments by less than 3%.

At the beginning of the year the number of people employed stagnated: increased in the business sector and declined in the public sector. The unemployment rate increased by 1.2 percentage points to 7.2% compared to the corresponding period of the previous year. In the rest of the year the rate will decrease - partly due to seasonal factors - nevertheless, the annual average is expected to be 6.5% that is higher than the last year's 6.1%, although still better than the EU average.

In 2005 average gross earnings will grow by 7% in the business sector and by 9.5-10% in the public sector. (The latter would be around 8% without the deferred payment of last year's 13th month salary). Real earnings will grow by 5% this year.

After the large drop at the beginning of the year, inflation will stagnate with some fluctuation. It probably decreased in May, but in the next months may increase moderately - depending, among others, on the crude oil prices. The annual average probably will be around 3.8%. The forint that was very strong in March has weakened since by about 5% and is expected to strengthen again during the rest of the year. The base rate of the central bank was reduced to 7.25% at the end of May. The 2% benchmark interest rate of the ECB and the favorable evolution of the inflation make further reduction of the central bank base rate possible.

The deficit of the general government reached in the first four months of the year 70% of the annual target. This is partly due to certain one-off expenditures; nevertheless, the actual deficit will certainly surpass the annual target. In other words, in 2005 the deficit according to the methodology accepted by the EU will be 4% of GDP, larger than the targeted 3.6%, but smaller than the 4.5% of 2004.

Forecast of GKI Economic Research Co. on Developments in the Hungarian Economy in 2005

	2003	2004	Jan.-March. 2005	2005 (forecast)
1. Volume of GDP (%)	102.9	104.2	102.9	103.5
2. Industrial production (constant prices %)	106.4	108.3	101.7	105
3. Investment in the national economy (constant prices %)	103.4	107.8	106.8	106
4. Construction (constant prices %)	102.0	106.8	111.7	109
5. Retail trade (volume index %)	109.0	105.7	103.0	103.5
6. Exports (current prices in euro %)	104.4	115.3	109.7	112
7. Imports (current prices in euro %)	105.9	113.2	108.0	111
8. Trade deficit (□ bn.)	4.2	3.9	0.6	4.0
9. Combined deficit of the current & capital accounts (□ bn.)	6.4	6.8	-	6.9
10. Average exchange rate of euro (in forints)	253.5	251.9	247.1*	247
11. Deficit of the general government (on cash flow basis without local governments; billion forints)	1054	1284.1	710**	1160
12. Index of average gross earnings	112.0	106.1	113.7	108
13. Consumer price index	104.7	106.8	103.7**	103.8
14. Consumer price index at the end of the period (corresponding month of the previous year=100)	105.7	105.5	103.9**	103.9
15. Rate of unemployment (at the end of the period %)	5.5	6.3	7.2***	6.3

* January-May

** January-April

***February-April

Source of actual data: Central Statistical Office. National Bank of Hungary. Ministry of Finance