

## Further interest rate cut is expected

**According to the forecast made by GKI Economic Research Co. in cooperation with Erste Bank, the Hungarian economy - after a slowdown in the first quarter of 2005 - will grow more dynamically. Inflation will not decrease further in the rest of the year. Real income will grow fast and the savings of households will expand much more than earlier. External balance will improve.**

The Hungarian industry - after a less than 2% growth in the first quarter - increased its production by approx. 9-10% in April and May. This is equal to the pace of the Estonian or Lithuanian industrial growth and by far outpaces the 3-4% growth of the Czech and Slovakian industry or the performance of the stagnating Polish industry. The industrial average of the EU was around 0.4% in April-May. In the first five months of the year the export of the Hungarian industry increased by 6.3%, its domestic sales by 5.1% compared with the corresponding period of the last year. The growth was especially fast in the production of telecommunication equipment, construction materials and motor vehicles. Two regions were responsible for the bulk of the expansion: the Middle-Transdanubian and the Northern Hungarian.

The growth of the retail trade accelerated as well: after the 3.4% of the first quarter the average growth in April and May jumped to 6.5%. In May the increase of the earnings accelerated both in the private and public sectors. First time this year the increase was faster in the private sector. In the first five months of the year real earnings increased by almost 5% in the private sector. In the public sector the increase was similar, not taking into account the delayed payment of the last years 13th month salary (if we include this item, the increase is 15%). Households save somewhat more than in the corresponding period of the last year, while their borrowings have declined significantly. Thus, net savings of households are increasing strongly: after the near zero in 2003 this year they will reach more than 3.5% of GDP.

Exports expanded much faster than imports in the last several months. The foreign trade deficit expected to be not more than three fourth of the last year's figure. In the balance of payment, however, a large part of this improvement will be eliminated by the outflow of interest- and profit-type earnings. A large part of this profit will be reinvested and the inflow of fresh capital will increase as well. This year the total inflow of foreign direct investment in all probability will surpass the last year's amount of 3 billion euros.

Inflation will not decrease further in the rest of the year, but in 2006 it may be around 2.5%. Forint continues to be very strong. All this makes probable further decrease of the base rate of the central bank in small steps during the year. A 6% base rate is expected by the end of the year.

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

	<b>2003</b>	<b>2004</b>	<b>Jan.-May 2005</b>	<b>2005 (forecast)</b>
1. Volume of GDP (%)	102.9	104.2	102,9*	103,5
2. Industrial production (constant prices %)	106.4	108.3	105,4	106
3. Investment in the national economy (constant prices %)	102.5	107.9	106,8*	106
4. Construction (constant prices %)	102.0	106.8	113,5	109
5. Retail trade (volume index %)	109.0	105.7	104,6	103,5
6. Exports (current prices in euro %)	104.4	115.3	111,9	112
7. Imports (current prices in euro %)	105.9	113.2	105,7	109
8. Trade deficit (□ bn.)	4.2	3.9	1,1	3,0
9. Combined deficit of the current & capital accounts (□ bn.)	6.4	6.8	1,3*	6,5
10. Average exchange rate of euro (in forints)	253.5	251.9	247,4**	247
11. Deficit of the general government (on cash flow basis without local governments; billion forints)	1054	1284.1	988**	1160
12. Index of average gross earnings	112.0	106.1	111,5	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	103,8**	103,9
15. Rate of unemployment (at the end of the period %)	5.5	6.3	7,1***	6,8

\* First quarter

\*\* January-June

\*\*\*Second quarter

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