

## Getting out from the hole

**According to the forecast prepared by GKI Economic Research Co. in co-operation with Erste Bank the Hungarian economy will bottom out from the last year's "hole" by the end of 2008. This year real earnings will already grow – although slowly. If the global financial market stabilizes, the forint interest rates may decrease.**

Although in the spring 2008 both the global economic and the domestic political conditions deteriorated, the performance of the domestic economy is not bad in the first months of the year. The industrial production and the exports accelerated, the drop in the construction industry and retail started to slow down compared to the last months of 2007. The balance of the foreign trade of goods became positive, the deficit of the general government decreased. In the last three months inflation is slowly but steadily abating. Wages in the competitive sector are growing faster than previously agreed, the forint is relatively strong. On the other hand, interest rates are increasing.

The industry continues to be export oriented, its main driving force is the production of electric machinery, electronics and motor vehicles. Domestic sales of the manufacturing industry decreased. It is expected that during the year the industrial exports will slow down. On the other hand, the decline in the domestic sales of industry will come to a halt – both in investment and consumer goods. The output of the construction industry continues to lag far behind the level of the same period of the previous year, but in February it increased by 6% compared to January. Significant change is expected from the expansion of EU supported investments in the infrastructure in the second half of the year. In the first two months of the year in the retail trade the sales of food products decreased by less than 1% compared with the corresponding period of the previous year, but the sales of other products declined by 4%. The number of guest-nights in commercial accommodations increased by 3%, but within this the guest-nights of domestic tourists declined.

Since December 2007 inflation has been slowing down by a monthly average of 0.2%. In 2008 the annual average inflation is expected to be around 6-6.5%, declining to approximately 5% by the end of the year. At the same time the price of food and household energy may increase by far more than 10% (given the global price hike, the price of the natural gas for household heating may go up 30%, the electricity tariff approx. 10%; the tariff of district heating may increase by 10-15% in the second half of the year).

The increase of the gross wages in the business sector is for the time being by far higher than the upper limit of the 5-7.5% band recommended by the National Interest Reconciliation Council. In the year as a whole – at an approx. 6.2% inflation – real wages will increase by 0.5-1%, but in the public sector will stagnate. The real value of pensions will increase by 1%. The number of people employed will moderately increase in the business sector, decrease in the public sector. Unemployment that between summer 2007 and now increased from 7% to 8.1% started to decrease a bit recently.

In 2008 the growth rate of the economy will be lower than in any other new EU member state. The economy as a whole after the last year's 1.3% will grow by 2.5-3%, but the combined performance of the sectors other than the agriculture and public services will expand by 3-3.5%. While in the first quarter the growth rate was close to the last year's 1.3%, the growth rate in the fourth quarter will be close to the 3.5% expected for 2009.

**Forecast of GKI Economic Research Co. on Developments in the Hungarian Economy in 2008**

	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>Jan.-Febr. 2008</b>	<b>2008 forecast</b>
1. Volume of GDP (%)	104.1	103.9	101.3	-	102.7
2. Industrial production (constant prices, %)	107.3	110.1	108.1	109.7	106
3. Investment in the national economy (constant prices, %)	106.4	98.0	100.3	-	104
4. Construction (constant prices, %)	116.6	98.4	85.9	76.7	102
5. Retail trade (volume index, %)	105.8	104.4	97.0	97.3	101.0
6. Exports (current prices in euro %)	111.4	116.6	115.7	117.4	110
7. Imports (current prices in euro %)	108.3	113.9	111.9	113.8	109
8. Trade balance (billion euros)	-2.9	-2.0	-0.3	0.1	0
9. Combined balance of the current & capital accounts (billion euros)	-5.3	-5.2	-4.0	-	-3.5
10. Average exchange rate of euro (in forints)	248.0	264.3	251.3	259.4*	257
11. Deficit of the general government (cash flow basis without local governments; billion forints)	984.4	2034	1291	508.1*	1050
12. Index of average gross earnings	108.8	108.1	108.2	105.1	107.7
13. Consumer price index	103.6	103.9	108.0	106.9*	106.2
14. Consumer price index at the end of the period (corresponding month of the previous year=100)	103.3	106.5	107.4	106.7*	105
15. Rate of unemployment (at the end of the period %)	7.3	7.5	7.7	8.0**	7.5

\*January-March

\*\* Q1 2008 average

Sources of actual data: CSO, NBH, MoF