2nd May 2011

Everything seems to be fine

According to the forecast of GKI Economic Research Co., in 2011 growth and equilibria of the Hungarian economy seem to improve significantly. The convergence programme presented to the EU promises lasting improvement, and money market acceptance of the programme is still favourable. The planned fiscal consolidation may be achieved in 2012; however, structural changes are expected to play a much smaller role in it than declared previously. Markets and international organizations are likely to react negatively to this, and the effects of this reaction may already be felt in 2011.

The Hungarian economy will grow at a rate of around 2.5 per cent in 2011. This is a significant acceleration compared to last year's 1.2 per cent, and it is about 0.7 percentage points higher than the expected EU average for 2011. The acceleration compared with 2010, however, will be generated almost entirely by agriculture (weather factors), as last year's 15 per cent drop in the agricultural sector caused a GDP decrease of around 0.5 percentage points. If the weather will be average in 2011, it will raise the growth rate by a similar extent. In the region the GDP growth rates of only Romania and Slovenia are expected to be slower than that of Hungary. The basis of economic growth is mainly agriculture, whereas other factors contributing to it are very limited. The main engine of growth remains industrial exports. Recession in domestic demand will come to an end; however, no substantial recovery can be expected in 2011. Reaching the sixth consecutive years of decline, construction may slightly recover in the second half of 2011. Following the stagnation in the first months, a slight expansion of retail trade is likely, mainly in the sale of vehicles and consumer durables. Services are developing only very modestly.

Domestic investment and consumer demand is increasing very modestly. Overall, the tax changes will raise costs for companies, whereas the purchasing power of consumers in the lower and middle classes will hardly increase. In many cases it will decrease. The HUF250bn freezing in general government expenditures will also reduce domestic demand. Credit supply is also tightening. The slow start of the new Széchenyi Plan, as well as the slow restart of the disbursement and the allocation of EU funds limit investment demand. The continuous deterioration of predictability and transparency as well as anti-foreign bias of government communication inhibit new foreign capital investments. For all these reasons investments are only growing slightly. Apart from some big automotive manufacturing projects, a downturn will be typical.

Real wages will increase by around 2 per cent (by 2.5 per cent in the private sector and about 1 per cent in the public sphere). The expansion of the grey economy is bolstered by the elimination of the so called expected wage category, the increase in the costs of low wage employees and the nationalization of the assets of private pension funds. As the combined consequence of these factors, the real income of households (after the disbursement of the real yields of private pension funds to their members) will increase by about 2 per cent. Income differentiation will intensify. Final household consumption will grow only by 1.5 per cent. This is because burdens associated with the amortization of bank loans are very high and the uncertain future encourages the formation of reserves, too. Furthermore, borrowing intentions and options are also limited.

The deficit calculated by the ESA methodology will differ from the 2.94 per cent deficit target included in the budget act, because the assets of private pension funds should be entirely recorded as capital income in 2011. However, the planned debt consolidation of Hungarian State Railway Company (MÁV) and Budapest Transport Company (BKV), the buyout of certain PPP facilities and the possible takeover of some local government debt by the central government will worsen the balance. As a result a surplus of around 2 per cent of GDP can be expected in 2011. The effects of one-off spending at the expense of private pension fund assets are demonstrated by the fact that the general government deficit would correspond to 7 per cent of GDP without it. During the excessive deficit procedure and the European Economic Semester in spring mainly the structural deficit will be assessed excluding one-off revenues, which would rise in 2011 according to official calculations

The Kalman Szell Plan and the convergence programme contain important steps into the right direction, and the government deficit target for 2012 will likely be met. However, owing to the lack of detailed programs and the uncertain social acceptance of the plan, the measures for implementing the plan may change significantly, and structural changes are expected to play a much smaller role than declared previously. Therefore, the foreign assessment of Hungary, together with the exchange rate of the forint, may fluctuate during the year.

The forecast of GKI Economic Research Co.: the Hungarian economy in 2011

		2008	2009	2010	February 2011	2011 (forecast)
1.	Volume of GDP (previous year=100)	100.8	93.3	101.2	-	102.5
2.	Industrial production (constant prices, previous year=100)	98.9	82.3	110.5	113.8	109
3.	Investments in the national economy (constant prices, previous year=100)	100.4	93.5	94.4	-	101
4.	Construction (constant prices, previous year=100)	94.9	95.7	89.9	96.1	97
5.	Retail trade (volume index, previous year=100)	98.2	94.8	97.7	100.1	101.3
6.	Exports (current prices in euro, previous year=100)	106.3	80.6	121.4	126.5	117
7.	Imports (current prices in euro, previous year=100)	106.6	75.2	119.4	125.0	118
8.	Trade balance (EUR billion)	-0.3	3.7	5.5	0.8	6
9.	Balance of the current and capital account (EUR billion)	-6.8	0.8	3.8	-	4.5
10.	Average exchange rate of euro (in HUF)	251.2	280.6	275.4	272.4*	272
11.	Deficit of the general government (cash flow basis, without local governments; HUF billion)	909	918.6	870	742.1*	690
12.	Index of average gross earnings	107.5	100.5	101.4	103.1	103.5
13.	Consumer price index	106.1	104.2	104.9	104.2*	104.2
14.	Consumer price index at the end of the period (corresponding month of the previous year=100)	103.5	105.6	104.7	104.5*	104
15.	Rate of unemployment (at the end of the period, per cent)	8.0	10.5	10.8	11.6*	10.7

* January-March 2011
Sources of actual data: HCSO, NBH, MoF