30 JULY 2018

HUNGARIAN ECONOMIC GROWTH PROBABLY REACHED ITS APEX

The Hungarian economy grew by 4.4 per cent in both the last quarter of 2017 and the first quarter of 2018. A growth rate faster than this was registered only once in the past decade. This is the fourth or fifth highest rate in the CEE region, and Hungary is likely to be at the peak of its current business cycle. The rate of increase in investments financed by EU transfers and in household consumption, boosted by the elections as well, is expected to slow down during the rest of the year. In addition, external demand is expected to deteriorate rather than grow further.

The era of trends in the world economy particularly favourable for Hungary with low energy prices and interest rates has been over, and the European recovery that started six years ago is likely to be over its zenith. The currencies of emerging countries are being devalued, especially in the case of countries with extreme affinity for loose monetary policy. Apart from the unpredictability of the American president, the threat of a commercial war and the deterioration of the US-EU relations, a significant risk is the effect of a very predictable raise of interest rates by the Fed. In addition to the actual implementation of Brexit, from the point of view of the future of the EU further uncertainties arise from the fact that its unity weakens, including the Visegrad country group as well (for example, regarding their relationship with Russia).

In 2018, construction, agriculture, info-communications and trade are expected to expand fastest in Hungary, though the increase in construction will be lower than last year due to its high statistical base. Although industrial expectations are favourable, changes in the automotive industry that is the driving force of the Hungarian industry, exacerbated by the risk of a customs war between the EU and the US, may cause serious concerns. The investment rate may rise to 22.5 per cent in 2018, reaching its pre-crisis levels. This will be mainly due to development projects in the public sector, largely based on EU transfers, whereas business investments are more restrained. For example, in the spring of 2018, German companies considered the Hungarian investment environment least attractive among the four Visegrad countries.

The growth rate of gross earnings will slow down from 13 per cent in 2017 to 10 per cent in 2018, entailing a very fast growth rate of real earnings of about 7 per cent (less than its two-digit increase last year). Although the minimum wage will go up “only” by 8 per cent in 2018 after 15 per cent last year, exerting a smaller impact on earnings in 2018, labour shortages and the election year will still have significant effects on them. Consumption has been expanding for the sixth consecutive year and it is expected to reach its peak in 2018 by 4.5 per cent, and final household consumption will grow even faster, by 5.5 per cent. Unemployment is hardly expected to decline compared to the end of 2017, although the number of those involved in workfare programs is decreasing. Together with those involved in workfare programs, the Hungarian unemployment rate is around the EU average. Inflation accelerated to 3.1 per cent in June, which is the third highest in the EU and a further rise is likely during the year, due to, among other things, the weak forint.

Taking into account the EU’s warning regarding the high cash-flow deficit due to the budgetary advance payment of EU transfers, there will be no major spending in December 2018, although this will be countered by the 2019 EU parliamentary and local municipal elections. The general government deficit according to the EU methodology is expected to be slightly smaller than planned (but above its 2017 level): around 2.2 per cent of GDP. As a result of the high cash-flow deficit, the government debt relative to GDP is expected to decline only slightly. As the budget for 2019 is based on overoptimistic assumptions, during the year some modifications and a somewhat higher than projected, albeit lower than in 2018, general government deficit can be expected (around 2 per cent).

Forecast of GKI for 2018

	Description	2015	2016	2017	01-05	
					2018	forecast
1	GDP (%)	103.4	102.2	**104.0**	**104.4****	**104**
2	Industrial production (%)	107.5	100.9	**104.8**	**103.1**	**104**
3	Investments (%)	107.1	85.1	**116.7**	**117.1**	**109**
4	Construction services (%)	103.0	81.2	**129.6**	**116.9**	**110**
5	Retail trade turnover (%)	105.8	104.7	**104.9**	**107.1**	**106**
6	Exports (current prices in euro, %)	107.0	103.4	**108.2**	**104.0**	**106**
7	Imports (current prices in euro, %)	104.6	102.3	**111.1**	**105.9**	**107.5**
8	Foreign trade balance (EUR billion)	8.6	9.7	**8.1**	**3.2**	**7**
9	Balance of the current and capital account (EUR billion)	8.9	7.0	**5.1**	**2.1****	**7**
10	Average exchange rate of euro (in HUF)	309.9	311.5	**309.2**	**314.0********	**319**
11	General government deficit* (HUF billion)	1218.6	848.3	1974	**1420********	**1500**
12	Index of average gross earnings	104.2	106.1	**112.9**	**112.1**	**110**
13	Consumer price index	99.9	100.4	**102.4**	**102.3********	**103**
14	Consumer price index at the end of the period (corresponding month of the previous year=100)	100.9	101.8	**102.1**	**103.1********	**103.5**
15	Rate of unemployment (at the end of the period, %)	6.2	4.4	**3.8**	**3.6**********	**3.8**

** Cash flow basis, without local governments*
*** First quarter of 2018*
**** January-April 2018*
***** First half of 2018*
****** Second quarter of 2018*

GKI Economic Research Co.

1092 Budapest, Ráday u. 42-44.

Phone: +36 1 318 1284 E-mail: gki@gki.hu

For more information: Andras Vertes, Laszlo Akar, Gabor Karsai