

3 SEPTEMBER 2018

GROWTH FASTER THAN EXPECTED BUT SLOWING DOWN

Although the Hungarian economy grew faster than expected and most EU member states in the second quarter of 2018, its growth rate calculated by the EU methodology has been slowing down for six months. According to market forecasts, GDP growth will exceed 4 per cent in 2018 (GKI upgraded its forecast to 4.2 per cent). It will fall to nearly 3 per cent next year, which would be among the lowest in the CEE region where the decline will be more moderate. 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. There is growing uncertainty and slowdown in the EU, due to, for example, the Turkish and the Italian situation, the threat of a trade war and the Fed's interest rate rises.

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. Industry is also expected to slow down compared to last year, even if there will be some improvement in the second half of 2018; mainly due to the transformation in the vehicle industry and market uncertainty. However, it is a positive sign that the problems in Audi's production in Hungary are probably over. Market services, especially trade and tourism are expanding rapidly. The expansion of investments accelerated in the second quarter. As a result, GKI raised the forecast growth rate of fixed capital formation to 12 per cent. However, in the second half of the year, only a minimal increase can be projected due to the very high investment level last year.

The growth rate of gross earnings is decreasing slowly. Inflation is accelerating, thus the growth rate of real earnings is expected to be slightly lower than last year's double-digit rate; however, it remains very high (7-8 per cent). 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 anticipated to decline compared to the end of 2017, although the number of those involved in public workfare schemes is decreasing, which is favourable. The official unemployment rate is the third lowest in the EU, after the Czech Republic and Germany. The number of those involved in public workfare schemes is almost the same as the number of unemployed, and counted both together, the Hungarian unemployment rate would be around the EU average. Inflation had accelerated for the fifth month in July, reaching 3.4 per cent. This is the third highest in the EU after Romania and Bulgaria. There may be some further increases during the year, due to the weak forint, and an average annual rate of around 3 per cent is likely.

The cash-flow deficit of the general government was close to HUF1,500bn in the first seven months of 2018, almost 10 per cent higher than foreseen for the whole year. As tax revenues were favourable, the main reasons for this include the budgetary advance payments of EU transfers and other budget expenditures (e.g., Modern Cities Programme), which are not independent of the upcoming local government elections. The general government deficit according to the EU methodology, which does not take into account the advance payments of EU transfers, is likely to be somewhat 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 less than expected by the EU and remains above 73 per cent.

FORECAST OF GKI FOR 2018

Description	2015	2016	2017	2018	
				Q1-Q2	forecast
1 GDP (%)	103.4	102.2	104.0	104.5	104.2
2 Industrial production (%)	107.5	100.9	104.8	103.5	104
3 Investments (gross fixed capital formation, %)	107.1	85.1	116.7	117.1**	112
4 Construction services (%)	103.0	81.2	129.6	119.1	114
5 Retail trade turnover (%)	105.8	104.7	104.9	106.9	106
6 Exports (current prices in euro, %)	107.0	103.4	108.2	104.8	105
7 Imports (current prices in euro, %)	104.6	102.3	111.1	106.2	106.5
8 Foreign trade balance (EUR billion)	8.6	9.7	8.1	4.2	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	315.6***	319
11 General government deficit* (HUF billion)	1218.6	848.3	1974	1491***	1500
12 Index of average gross earnings	104.2	106.1	112.9	111.9	110
13 Consumer price index	99.9	100.4	102.4	102.5***	103
14 Consumer price index at the end of the period (corresponding month of the previous year=100)	100.9	101.8	102.1	103.4***	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-July 2018

**** May-July 2018

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