29 April 2019

2019 – Good start, uncertain continuation

In the first two months of 2019, the growth rates of the most important sectors of the Hungarian economy accelerated compared to last year. However, domestic economic expectations reached their two-year low in April. The EU's economic sentiment index fell to its level measured three years ago, whereas the German business confidence index dropped to its level registered two and a half years ago. Various international growth forecasts suggest that the EU is slowing down in 2019. The German growth rate is expected to be only 0.5-1 per cent in 2019, and this is bad news for Hungarian exports. The expansion of investments and consumption in Hungary will also slow down even though their growth rates remain high, thus the growth rate of GDP is expected to decrease markedly, from 4,9 per cent in 2018 to around 3,5 per cent in 2019. Inflation is accelerating, the forint is weak, and interest rates on government securities meant to be sold to households are already rising.

The government expects 3.9 per cent GDP growth rate in 2019, the National Bank of Hungary 3.8 per cent, and the market consensus is 3.6 per cent. In the first two months of 2019, industrial production increased by 5.2 per cent (by 3.6 per cent in 2018 on a yearly average), retail sales by 6.9 per cent (by 6 per cent last year), and construction output by a spectacular 39 per cent (by 22 per cent last year). Export growth accelerated and the import-export gap in terms of different growth rates narrowed by 1.4 percentage points. These are much better figures than those expected for the whole year. Although EU transfers are likely to continue to grow in 2019, they will only generate an investment growth of around 7 per cent. Deceleration is indicated by the fact that the construction contract portfolio at the end of February was only 2.6 per cent higher than a year before. In addition, the prospects of agriculture are quite poor due to the drought this year.

The growth rate of gross earnings was slowly but steadily decreasing in 2018, in accordance with inflationary trends. As a result, real earnings slowed down to around 8 per cent from a rate of above 10 per cent in 2017. The rate can be expected to total some 5.5-6 per cent in 2019. In the autumn, about 0.5 per cent increase in pensions can be expected due to faster inflation than projected by the government. In addition to sharp wage growth, the rise in consumption is boosted by strong consumer confidence and the expansion of lending. However, last year's 4.6 per cent expansion in consumption may slow down to around 4 per cent this year.

At the beginning of the year, the number of workers in the primary (domestic) labour market increased by 80 thousand compared to last year, the number of those participating in public workfare schemes decreased by about 40 thousand, and the number of those working abroad went up by 15 thousand. The 3.6 per cent unemployment rate is slightly more favourable than a year ago, and it is lower than the EU average even if the rate includes those involved in public workfare schemes. However, it has stagnated for about three quarters.

Hungary's inflation rate is one of the highest in the EU (similarly to Romania, where wages also rose spectacularly) and the rate of core inflation reached 3.8 per cent in March. GKI considers the tightening of domestic monetary conditions unavoidable in 2019. As a first step, the National Bank of Hungary raised its overnight deposit rate by 10 basis points at the end of March. However, it stressed that its monetary policy remains basically unchanged. As a result, the forint weakened significantly. However, the Government Debt Management Agency is issuing government securities with higher interest rate, which implies monetary tightening. In the case of accelerating inflation and further weakening of the forint, the National Bank of Hungary may also implement a base rate increase during the year. The base rate could rise to 1-1.15 per cent at the end of 2019.

Data on the external equilibrium of the Hungarian economy were significantly corrected by the National Bank of Hungary. The current account surplus declined to 0.5 per cent of GDP in 2018 due to strong domestic demand. Such a low level has been unprecedented since 2011. As trends remain unchanged, the surplus may run out this year, and even a deficit may emerge. At the same time, the amount of incoming EU transfers may increase.

FORECAST OF GKI FOR 2019

	Description	2016	2017	2018	2019	
					01-02	forecast
1	GDP (%)	102.3	104.1	**104.9**	**-**	**103.5**
2	Industrial production (%)	100.9	104.8	**103.6**	**105.2**	**103.2**
3	Investments (%)	88.3	118.2	**116.5**	**-**	**107**
4	Construction services (%)	81.2	129.6	**122.3**	**139.0**	**109**
5	Retail trade turnover (%)	104.7	104.9	**106.0**	**106.9**	**104**
6	Exports (current prices in euro, %)	103.4	108.2	**104.2**	**106.7**	**104**
7	Imports (current prices in euro, %)	102.3	111.1	**107.3**	**108.4**	**106**
8	Foreign trade balance (EUR billion)	9.7	8.1	**5.6**	**1.3**	**4**
9	Balance of the current and capital account (EUR billion)	7.0	4.9	**3**	**-**	**4.5**
10	Average exchange rate of euro (in HUF)	311.5	309.2	**318.9**	**318.0****	**320**
11	General government deficit* (HUF billion)	-848.3	-1974	**-1445.1**	**-141.9****	**-1000**
12	Index of average gross earnings	106.1	112.9	**111.3**	**110.6**	**109**
13	Consumer price index	100.4	102.4	**102.8**	**103.2****	**103.2**
14	Consumer price index at the end of the period (corresponding month of the previous year=100)	101.8	102.1	**102.7**	**103.7****	**103.5**
15	Rate of unemployment (at the end of the period, %)	4.4	3.8	**3.6**	**3.6*****	**3.6**

** Cash flow basis, without local governments*
*** January-March 2019*
**** December 2018 – February 2019*

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