Keeping the wrong direction

According to the forecast of GKI Economic Research Co., in Hungary recession is continuing in the rest of the year. In spite of surging exports by Mercedes, Hungary's total exports are hardly accelerating and no improvement is expected in demand. The strength of the forint attributed to the relatively favourable atmosphere prevailing during the summer in international money and capital markets and due to the news on the start of Hungary's negotiations with the IMF proved to be temporary. Since the government does not want to introduce changes in its economic policy, the conclusion of the agreement with the IMF is not possible, and thus investors' confidence necessary to trigger investments that are indispensable to kick-start GDP growth will not be established.

Hungary's GDP contracted by 1 per cent in the first quarter of 2012. This rate was much higher than the 0.2 per cent average of the EU. In the CEE region only the Czech and the Slovenian GDP decreased, that of the other countries including Romania that had concluded an agreement with the IMF increased. Although the recession of the EU is only slightly more pronounced than projected formerly, the deterioration of the perspectives is worrying. Hungary's industrial production fell by 0.4 per cent in the first half of 2012. Domestic sales were down by 1.7 per cent, and exports grew by a mere 1 per cent. Exports in the motor industry surged by more than 11 per cent. The start of the production by Mercedes could not counterweight falling external demand for the rest of Hungary's exports. The other exception is the food industry whose production mounted by nearly 10 per cent in the first half of 2012 thanks to the good harvest of last year and the improvement of export possibilities due to the weak forint. Nevertheless, because of the drought the harvest of this year will be much smaller particularly in the case of maize and staples than last year. In the first half of 2012, the performance of construction fell by more than 10 per cent, that of home building by 20 per cent. Retail trade turnover declined by 1.1 per cent in the first half and 2.3 per cent in the second quarter of 2012 but in the second half it is likely to fall by 2.5-3 per cent.

Although employment increased slightly in statistical terms, this was to a large extent the result of expanding workfare programs. In addition, grey employment must have increased as well. In the first half of 2012 employment went back by 2.4 per cent year-on-year in the public sector excluding workfare programs and by 1.8 per cent in the competitive sector employing more than five persons. In July 2012 the rate of unemployment was lower than one year earlier for the first time. The number of unemployed decreased by 4400 persons. The number of those involved in workfare programs increased at a significantly higher rate.

Excluding the workfare programs, real earnings are likely to contract by 2-2.5 per cent in 2012 in the economy, and by 1.5 per cent in the competitive sphere. The rate of inflation totalled 5.8 per cent in July 2012 month-on-month, and a similar rate is expected year-on-year. The forint was relatively strong during the summer, but following the reduction of the reference rate by the National Bank of Hungary by 25 bps it set to weaken. Hungary's rate of inflation is outstandingly high by EU standards. The reference rate was reduced in spite of the high inflation rate and the uncertain state of the general government in both 2012 and 2013. This measure indicates the increasing activity of the external members of the Monetary Council and erodes the confidence in the National Bank of Hungary

The government strives to reach an agreement quickly with the IMF and the EU in words but its actual measures do not support this. Since the beginning of summer the propensity of the government to spend without appropriate revenues has intensified again. This policy serves short term populist objectives but it is problematic in terms of economic growth and macroeconomic equilibria. There are no sings indicating that the government would like to introduce changes in its failed economic policy that produced the lowest rate of GDP growth and the highest rate of inflation in the CEE region this year. Due to the particularly high risk premium of financing the government debt it can manage the balance of the general government only by additional austerity measures. Further corrections will be necessary to reach the deficit target of this year and particularly of the next one.

The forecast of GKI Economic Research Co. on the Hungarian economy in 2012

		2010	2011	H1 2012	2012
1.	Volume of GDP (previous year=100)	101.3	101.6	99.0*	98.5
2.	Industrial production (constant prices, previous year=100)	110.5	105.4	99.6	101
3.	Investments in the national economy (constant prices, previous year=100)	94.4	95.5	92.9	96
4.	Construction (constant prices, previous year=100)	89.9	92.2	89.9	93
5.	Retail trade (volume index, previous year=100)	97.7	100.2	98.9	98
6.	Exports (current prices in euro, previous year=100)	121.4	112.0	100.5	102
7.	Imports (current prices in euro, previous year=100)	119.4	110.6	101.1	101.5
8.	Trade balance (EUR billion)	5.5	7.1	3.7	7.5
9.	Balance of the current and capital account (EUR billion)	2.8	3.6	0.7**	3.5
10.	Average exchange rate of euro (in HUF)	275.4	279.2	294.2***	295
11.	Deficit of the general government (cash flow basis, without local governments; HUF billion)	870	1734.4	437.5***	700
12.	Index of average gross earnings	101.4	105.2	104.4	104.5
13.	Consumer price index	104.9	103.9	105.6***	105.7
14.	Consumer price index at the end of the period (corresponding month of the previous year=100)	104.7	104.1	105.8***	105.5
15.	Rate of unemployment (at the end of the period, per cent)	10.8	10.7	10.5****	10.8

* Seasonally and calendar-effect adjusted: 98,9%.
** First quarter of 2012
*** January – July 2012
**** May - July 2012
Sources of actual data: CSO, NBH, NGM