Monthly flash report for top executives

(November 2019)

In the first half of 2019, the over 5 per cent **growth rate of Hungary**'s GDP was faster than in the past or in the other EU countries. Based on the data to date, the rate of growth in the third quarter could not be much lower than in the previous quarters; however, a slowdown can be expected this year and especially in the next one due to the deterioration in the external environment and the reduction in the growth promoting impact of EU transfers. **GKI predicts a faster-than-previously-expected GDP growth of 4.7 per cent in 2019 and around 3 per cent in 2020**. The Hungarian economy, at least until now, has resisted to the global economic slowdown, thus the **European Commission** also raised its growth projections for 2019 (from 4.4 to 4.6 per cent). According to the Commission, this trend will slow down significantly as soon as the effects of its supporting internal factors run out. As the main export markets remain weak, a GDP growth rate of 2.8 per cent is likely in 2020.

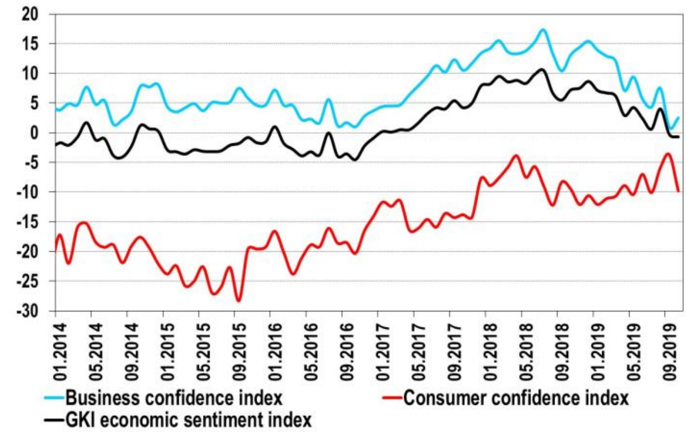
Summary figures, 2018-2020

	2018	Q1–Q2, 2019	2019	2020
GDP (previous year = 100)	104.9	105.1	104.7	103
Gross fixed capital formation (preceding year = 100)	116.5	119.1	113	102
Consumption (previous year = 100)	104.6	104.5	104.5	103.5
Current account balance (EUR billion)	-0.7	-0.1	-1	-2
Current account and capital account/GDP (per cent)	2.0	2.6	1.4	1.0

Source: HCSO, NBH. 2019-2020: GKI

The greater-than-expected slowdown in the Chinese economy poses a permanent risk to the **world economy**. However, the US-China economic war might ease somewhat as Trump held out the prospect of abolishing the penalty tariffs on Chinese goods. The further postponement of Brexit and the early elections in the UK prolong uncertainty. The approval of the EU budget between 2021-2027 is delayed, thus the already significantly decreasing amount of EU transfers to Hungary are going to be very modest in 2021 and 2022.

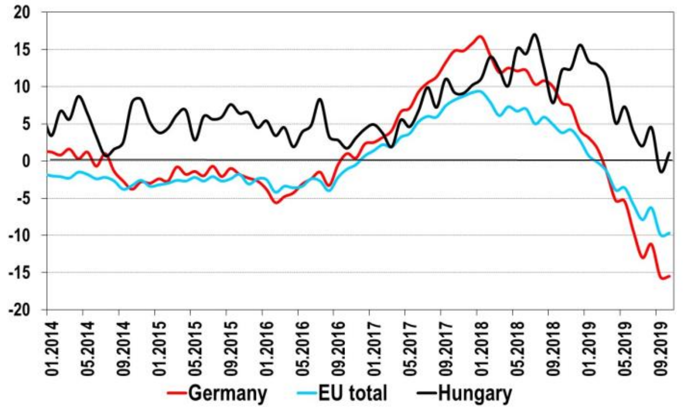
GKI business confidence index, 2014-2019



Source: surveys of GKI

Since the EU must also face several possible economic shocks in the near future, the **most recent prognosis of the European Commission does not expect acceleration in 2020**, the growth rate of the EU's aggregate GDP might be 1.4 per cent both in 2019 and 2020. Pessimism seems to be long-lasting in the European Union, the slow erosion of the economic outlook continued in October, although the **EU's economic sentiment index** fell only within the statistical margin of error this month. This indicator is nearing to its six-year low. The trade and services confidence indexes declined noticeably on a monthly basis, the industrial one remained essentially unchanged and the construction one increased slightly. Consumer expectations decreased within the statistical margin of error. After its decline in September, the **German industrial confidence index**, which is important for Hungarian exports outlook, stabilized in October.

Industrial confidence indices in Hungary and the EU, 2014-2019



Source: EU, surveys of GKI

GKI's economic sentiment index decreased within the statistical margin of error and reached its almost three-year low. Business expectations rose slightly compared to their three-year low. Following its increase of two months, the **consumer confidence index** fell close to its July level in October. Households assessed their financial situation, the possibility of buying high-value durables, and especially their saving capacity much worse than a month ago.

Trends in the real economy, 2018-2020

(Volume, the same period of the previous year = 100)

	2018	01-09, 2019	2019	2020
Industrial production	103.6	106.3	105.5	104
Construction	122.3	129.6*	121	102
Exports of goods	104.2	103.7*	103	102
Imports of goods	106.3	105.4*	105	103.5
Retail sales	106.0	105.8	106	104

Source: HCSO, 2019-2020: GKI *January–August 2019

After its halt in August, **industrial** output rose by 9 per cent in September, resulting in an increase of 6.3 per cent in the first three quarters of 2019. It is also favourable that the industrial sentiment index adjusted positively in October. Owing to the deterioration in the external environment, the growth rate of industry is expected to decline in the coming months. GKI predicts the annual rate of gross industrial growth to be over 5 per cent in 2019 and only 4 per cent in 2020.

After a strong July, the rate of increase in **construction** output dropped to around 6 per cent in August. However, total production surged by almost 30 per cent in the first eight months. **Housing construction** went up only symbolically in the first three quarters of 2019, merely by 1 per cent. Most of the projects are well behind schedule, thus even if the fourth quarter will be very strong, fewer-than-previously-thought new homes will be built in 2019 (about 20 thousand). Of course, this will reduce the negative impact of the increase of the preferential VAT rate on new homes in 2020 (16-18 thousand homes are expected to be built in 2020). The volume of the **stock of contracts** in construction was 12 per cent lower at the end of August than a year earlier. The construction confidence index decreased slightly in October, and essentially returned to its August level. The growth rate of production is expected to jump by slightly more than 20 per cent this year; however, it may decelerate close to 2 per cent in 2020.

Retail trade performed well in September as well, the volume of its turnover grew by 5.8 per cent on an annual basis. Thus, its performance was up by 5.8 per cent in the first nine months y-o-y. In October, the trade confidence index overadjusted its September drop. **GKI** raised slightly its forecast for 2019, expecting retail sales to grow by 6 per cent in 2019 and by around 4 per cent in 2020. In **foreign trade of goods** August proved to be a quiet month (the volume of exports mounted by 3.3 per cent and that of imports by 2.9 per cent). Thus, the total volume of imports grew almost 2 percentage points faster than that of exports in the first eight months. The **terms of trade** remained unchanged. In September, exports in euro terms increased by almost 4.5 percentage points faster than imports, thus the surplus of foreign trade in goods increased by EUR0.6bn. **GKI** expects an annual surplus larger than previously in 2019. The **services** confidence index changed within the statistical margin of error in October, and it remained low.

Labour market trends, 2018-2020

	2018	01-08 2019	2019	2020
Unemployment rate (average)	3.7	3.5*	3.5	3.4
Gross earnings**	111.3	110.7	110.5	108
Real earning **	108.2	107.0	107	104.5

Source: HCSO, 2018-2020: **GKI** */ July–September 2019,
**/ The same period of the previous year = 100

Consumer price inflation slowed down slightly in September, and it accelerated only minimally in October. As a result, **GKI** decreased its 2019 forecast somewhat (from 3.5 per cent to 3.3 per cent).

The **number of employees** increased by 0.7 per cent on an annual basis in the first eight months of 2019. The **unemployment rate** was 3.5 per cent between July and September, representing a 0.3 percentage point contraction on an annual basis, whereas it was 0.2 percentage points higher than in the previous quarter. **Willingness to employ** weakened in industry, strengthened in retail trade and services, and remained unchanged in construction. Households' fear of unemployment, albeit from very low levels, has been increasing for the second month. The number of employees may increase by slightly less than 1 per cent this year, and by less than 0.5 per cent next year. **Gross earnings** mounted by 11.5 per cent in the first eight months of this year (the negative "record holder" was education with a growth rate of only 3.6 per cent). The decrease in the number and share of low-paid workers involved in public workfare schemes contributes statistically to the increase of gross earnings. **Real wages** rose by 7.1 per cent over the same period. **GKI** expects real incomes to **grow** by 7 per cent in 2019 and by 4.5 per cent in 2020.

Interest rates, 2018-2020
(per cent, at the end of the period)

	2018	10, 2019	2019	2020
NBH reference rate	0.90	0.90	0.90	0.90
Fed reference rate	2.50	1.75	1.75	1.5
ECB reference rate	-0.4	-0.5	-0.5	-0.5
Reference yield of one-year government securities	0.39	-0.03	0.02	0.1

Source: NBH, 2019-2020: **GKI**

After September, the **Fed** cut its reference rate by 0.25 percentage points in October as well, to the range of 1.5-1.75 per cent. (The stock market welcomed the reductions once again and indexes jumped to new historical highs.) According to the announcement of the Fed, no further cuts can be expected in the near future. In addition, as the third-quarter GDP data was better than expected, there is no need for this. However, next year's US presidential election may have an impact on interest rates. The **ECB** did not change its base rate in October either. According to its September decision, the ECB's asset purchase programme will restart with a monthly amount of EUR20bn from the 1st of November. The programme will continue as long as it can boost economic growth. The **National Bank of Hungary** is not expected to change its benchmark interest rate next year, thus low domestic interest rates will persist for a long time. The **reference yield of Hungarian government securities** with a maturity of 1 year fell to historic lows in October (-0.03), whereas the exchange rate against the euro is also close to its historic low.

Financial indicators, 2018-2020

	2018	01-10,2019	2019	2020
Consumer price index	102.8	103.3	103.3	103.3
EUR/HUF exchange rate	318.9	324.0	325	335
Foreign trade balance (EUR billion)	5.5	3.9*	4.5	2.5
General government balance (cash flow, without local governments, HUF billion)	-1445	-575.4	-1000	-500

Source: HCSO, NBH, MoF, 2019-2020: **GKI.** */January–September 2019

According to **GKI**, owing to favourable growth performance and high tax revenues, the target **budget deficit** of 1.8 per cent of GDP can be reached this year, with a deficit slightly higher than the target one of 1 per cent next year (1.3 per cent). The European Commission predicts that the government targets could be achieved in both years. The **government debt relative to GDP** may fall to close to 68-69 per cent by the end of 2019 and to around 67 per cent in 2020.