Economic Trends in

Eastern Europe

Vol. 30. No. 2 (2020)

KOPINT-TÁRKI
Konjunktúrakutató Intézet Zrt.

KOPINT-TÁRKI

Economic Research Limited

Budapest

Economic Trends in Eastern Europe

Economic Trends in Eastern Europe is an insightful publication providing subscribers with a comprehensive picture of Eastern European economic developments.

Economic Trends in Eastern Europe is written by the research team of the Kopint-Tárki Economic Research Institute – the same group that has authored the previous 24 volumes of this publication. Each issue provides an analysis of the current economic situation as well as of the specific problems of economic growth and institutional changes in Eastern Europe.

2020 No. 2 August

Published by KOPINT-TÁRKI Economic Research Institute Limited

Responsible Publisher:
Éva Palócz

Authors:

Chapter 1: International Environment
Katalin Nagy

Chapter 2: Central and Eastern Europe
Katalin Nagy, Péter Vakhal

Chapter 3: The Hungarian Economy
Zoltán Matheika, Éva Palócz, Péter Vakhal

Edited by Éva Palócz

Closed on August 2020.

Subscription Information

Annual subscription rate 2020
EUR 600.00 (one year - 3 issues), single issue price: EUR 200.00 including carriage charges.

H-1112 Budapest XI., Budaörsi út 45.
Published and distributed in Hungary
by KOPINT-TÁRKI Economic Research Institute Limited
Phone: (36-1) 309-2695
Fax: (36-1) 309-2647

Orders should be addressed to KOPINT-TÁRKI Economic Research Institute.

This publication may not be reproduced without the permission of KOPINT-TÁRKI Economic Research Institute.

Printed in Hungary by KOPINT-TÁRKI Economic Research Company Limited

Technical editor: Erika Rózsás
HU ISSN: 1216-1829 ©
Kopint-Tárki Budapest
info@kopint-tarki.hu

Economic Trends in Eastern Europe

No. 2. 2020

Budapest, August 2020

1. The global economy

The consequences of the coronavirus pandemic profoundly reshaped **global economic conditions**. The fast – in some regions even dramatic – spread of the epidemic has brought about a double whammy of demand and supply-side shocks. The abrupt economic contraction has somewhat eased after the first weeks and many governments strive to restart the economy through various fiscal stimulus measures. But the level of uncertainty is still very high, not least because the easing of restrictions resulted in another rise in the number of new cases in many places – even though sometimes these flare-ups remain local. But in many developing countries the epidemic is still on its upward phase, reaching frightening proportions, with potentially more devastating consequences than in the developed countries. With no vaccine in sight yet, the world needs to learn to live with the virus, which means the in some areas (tourism, for example) the restart of economic activity will be very slow. According to the latest report of the OECD (in June) – global economic growth will be minus 6 percent in 2020, provided that the recovery begins in the second half of the year – otherwise, the economic contraction may reach 7 percent. At the same time, the IMF projects a fall of global GDP by 5 percent. The global economy may have contracted by about 10 percent in the first half of 2020, and the recovery is to be slow and protracted even in the best of cases. Due to faltering demand, inflation remains moderate, but unemployment is bound to rise substantially, resulting in a deterioration of household incomes.

The pandemic reached the **developing countries** relatively late but with great ferocity – its economic consequences are still hard to assess. The income sources on which these countries are dependent took a hard hit. Most low and middle-income countries face severe fiscal crisis since they are forced to increase their health spending – and expenditures aimed at keeping the citizens and enterprises that lost their income source above water – amid a harsh fall of fiscal revenues. These countries face deteriorating lending conditions and suffer from a fall of FDI inflow, and their growing need for external help is met by a reduced capacity of international aid organizations to help.

While merchandise trade flows were/are hampered by movement restrictions, they still could grow on a year-on-year basis, due to the emerging economies. The flow of services trade, on the other hand, virtually stopped, and – at least in the case of international tourism – no recovery is expected by the end of this year. As a result, the volume of **international trade of goods and services** will decline by more than 10 percent in 2020. A rebound is expected in the next year, but even this expectation is not without downward risks.

Commodity market trends clearly reflect the elevated risk aversion among investors that led to a rise in the price of gold almost to the level of palladium price. The gradual restart of the Chinese economy stopped the decline of industrial commodities, but they remained below the level seen one year earlier by 10-20 percent. The prices of these commodities are unlikely to reach 2019 levels by the end of the year, or even in 2021.

In the second quarter of 2020, the **crude oil price** reached historical lows: it fell below 10 USD/barrel in April. According to expectations, global oil demand may decrease by 9 million barrels per day this year. The plunge of oil prices prompted not just the major OPEC members but also Norway, Canada, and Russia to restrict their production volumes. Extraction is restricted in the US as well. According to the June OPEC decision, the agreement regarding output reduction will remain in effect at least until the end of

July, and some restriction may remain even in August-September. The agreement helped the oil price to partially recover to around USD 40/barrel. According to the IEA, oil demand will remain subdued until as late as 2022, mostly due to the fall in aviation. Chinese and Indian oil demand rebounded strongly in March-April but oil reserves in the OECD countries are at a high level, which lowers demand. Hence we expect the annual average oil price to remain around USD 40/barrel that may rise to USD 45/barrel in 2021. Volatility is high: every piece of news causes substantial movements on the oil market.

Due to the coronavirus crisis, the **monetary** easing that began in the last year has continued. The fall of economic activity – more severe than in 2008/2009 – forced central banks to resort to radical expansionary measures. The *FED* lowered the policy rate by 150 basis points in 2020, and no upward correction is on the horizon. The *ECB* expanded its asset purchase program – originally introduced in March – to EUR 1,350 billion and prolonged the time horizon of purchases to June 2021. The reference rate is to remain at 0 percent as long as the eurozone inflation does not approach 2 percent. Considering that at present the inflation rate was 0.3 percent in June, this may take some time. The *Bank of England* reduced the policy rate to around 0 percent and raised the fund allocated to quantitative easing from GBP 645 billion to GBP 745 billion. The *Japanese central bank* has also expanded its asset purchase program and it also buys stocks in large quantities. In June the *Russian* central bank lowered the reference rate the third time in 2020, to a record low of 4.5 percent, and it also indicated the possibility of further rate cuts in the coming months.

It is becoming clear that monetary policy options are being exhausted, massive **fiscal measures** are needed to counter the fall of economic activity. This is why the European Commission approved the suspension of the Maastricht limit of state debt. The various national rescue programs revved up fiscal spending. Abundant liquidity and cheap credit make government spending easier right now but after the crisis dealing with the ballooned state debt may become a problem. The fiscal debt-to-GDP ratio is well above 100 percent in the US, Japan, France, Italy, Spain, Greece and Portugal, but it is also near 100 in the UK.

Economic recession is virtually universal outside the European Union. The **US economy** shrank at a rate of 5 percent and we expect an annual fall of 7.8 percent in 2020. Both private consumption and gross fixed capital formation are to decrease by 7-8 percent this year, while export may fall by as much as 10 percent. The fact that the epidemic is not easing in the US makes the 2021 prospects hard to assess as well. Unemployment was 11.1 percent in June but employment rose by nearly 5 million compared to the previous month. The annual unemployment rate may hit 11-12 percent in 2020, while sluggish demand and low energy prices keep inflation down. For now, we expect a V-shape recovery but it can easily evolve into a U-shaped or even L-shaped trajectory. Due to the large-scale monetary and fiscal easing state debt jumped by 20 percent and the debt-to-GDP ratio may reach 133 percent, which can become a problem in the future.

In **Japan,** the present recession surpasses everything that happened earlier in the postwar history of the country. We expect a GDP fall of 5.8 percent in 2020 and only a growth of 2 percent in the next year, provided that the fiscal stimulus measures remain in effect in 2021. Export will contract by more than 10 percent while consumption is likely to drop by about 9 percent. Investment is likely to decrease at a less drastic rate, but only because it was rather

low, to begin with. The government tries to stimulate the economy with a fiscal package amounting to 5.8 percent of GDP, with direct transfers to households, tax allowances, business subsidies, bank and loan guarantees, etc.

Chinese GDP was down 6.8 percent in the first quarter of 2020, a less sharp decline than previously expected. Preliminary data suggest that economic growth restarted in the second quarter, and China may post positive growth – of about 1.5 percent – in 2020 as a whole, as opposed to almost every other country of the world. What is more, Chinese growth is expected to return to its usual pace in 2021. Government consumption and public investments will drive the recovery. Beside healthcare R+D investments and infrastructure investments (roads and public utility infrastructure, a nationwide extension of the 5G network), defense industry investments are also gaining prominence. China arms itself at a considerable pace.

According to our downwardly revised forecast, the GDP of the **euro area** may drop by 10.2 percent in 2020, and this – despite the stimulus packages – is an optimistic scenario. While the acute crisis is already easing, the recovery will be very slow, the downsizings of workforce and capacities are still ongoing. Every GDP component but government consumption will contract this year. While government consumption may climb 2.5 percent, private consumption is expected to fall by 8-9 percent, fixed capital formation by 10 percent, and the export of goods and services by 11 percent. The latter will be offset by the fall of import. A rebound of GDP is expected in the next year, with a growth rate of about 6.5 percent – provided that there is not another economic stoppage due to a second wave of the pandemic – but this is not enough to get close to the GDP level seen in 2019.

The epidemic put the worries about Brexit out of the limelight, but actually nothing is solved on that front. The UK did not ask for an extension but there is no progress in agreeing upon the terms of the exit, which is a source of uncertainty for European and British firms.

In the **EU27**, we expect an average GDP decline of 9.4 percent, followed by a moderate 6.1 percent growth in 2021. In the "new member states" – EU13 – GDP is to contract by 4.9 percent, with – assuming a positive scenario – a rebound of 4.3 percent in the next year.

Inflation is likely to remain below 1 percent this year. Decreasing demand and especially subdued commodity prices push overall inflation downward. In the eurozone, the inflation of 0.7 percent in 2020 may give way to a higher rate of 2.1 percent in the next year, while in EU27 the expected rates are 0.9 and 2.1 percent, respectively. The crisis has destabilized the labor markets, the number of unemployed is on the rise, even if the available data do not yet clearly reflect this rising trend. The unemployment rate has been recently fluctuating around 7.3 but will rise in the coming months, due to downsizings in a number of economic areas. By the end of the year, the unemployment rate may rise above 9 percent in the eurozone and to 8.7 percent in the EU27 as a whole.

The EUR/USD exchange rate, after hovering for a while around 1.12, began climbing in July, well above the average level in the first half of the year (1.10). Some of the experts expect this strengthening of the euro to last through the second half of the year, but this depends – among other factors – on the overall economic performance of the eurozone

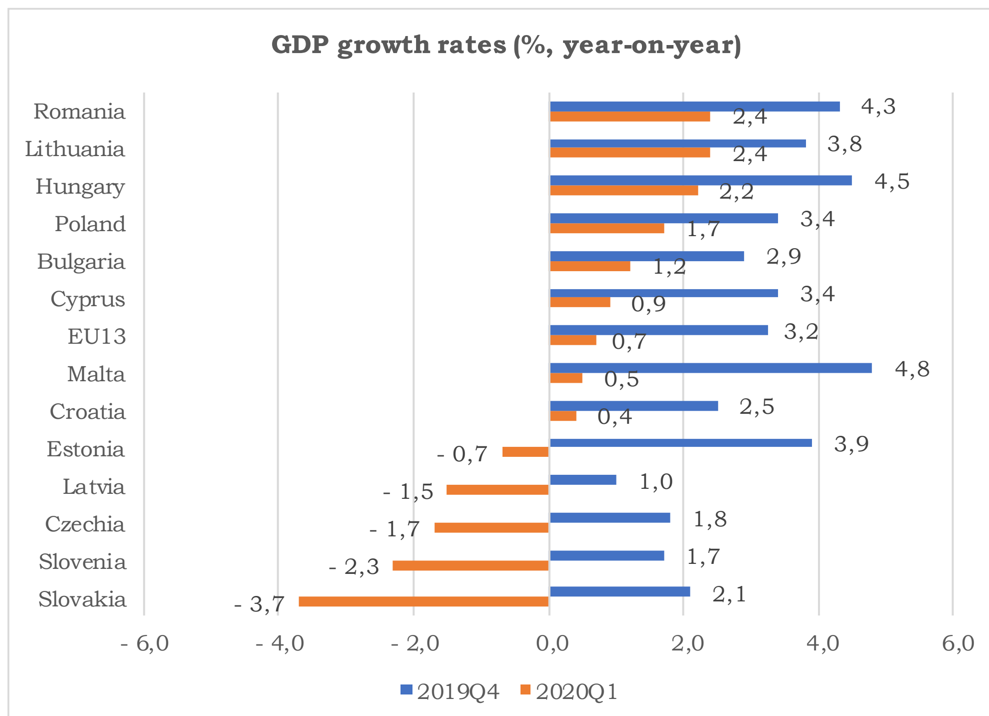
during the rest of the year. The annual average exchange rate may be 1.12 EUR/USD in both 2020 and 2021.

In **Germany**, the coronavirus recession peaked in April that was followed by an upturn, due to the end of temporary closures and the stimulus measures. But the output losses will not go away any soon. The IFO barometer has not fallen to such a degree since 1991 as it did in this March. The May reading indicates a turnaround but the index is still very low. Recovery is hampered by the fact that the most important trade partners of GDP were hit by the crisis even more drastically – as a result, German export may drop 12-13 percent this year. Due to the temporary shut-downs, the fall of GDP may be 7.2 percent in 2020, as opposed to the 4.5 percent decrease predicted in our previous report. Investments and private consumption are about to contract by 7 percent, but consumption may rebound faster than investments since the uncertainties regarding demand prospects discourage firms from launching new investment projects.

In the **United Kingdom**, GDP is likely to drop by about 10 percent, but in the case of a second wave of the epidemic, the economic contraction may reach 14 percent. Investments may fall by as much as 20 percent, while private consumption and export may decrease by 15 percent. Investor sentiment is hurt not just by the COVID epidemic but also by the ever-growing risk of a no-deal Brexit.

2. New EU member states

Due to the epidemic-related restrictions in March, all EU-countries took a brutal hit. The new member states were no exception even if the shock was only partially reflected in their first-quarter GDP numbers – in any case, those numbers remained below their pre-epidemic baseline trajectories. Out of the 13 member states, GDP declined in 5 (Estonia, Slovakia, Slovenia, Latvia and Czechia) in the first quarter, but the regional average was still positive, 0.7 percent, on a year-on-year basis. Slovakia suffered the hardest GDP fall 3.7 percent. Due to the transformation of the European auto industry, Slovakian economic growth already slowed down considerably in 2019, with a deep fall in the domestic trade, transport and tourism sectors. The restrictions introduced in March lead to an almost complete closure of services: the value-added of the financial sector dropped by 42 percent in the first quarter, while construction value-added decreased by 25 percent. The 3 percent fall of the transport vehicle industry is comparatively mild. On the whole, in Slovakia the restrictions hit an economy already in a fragile state, and among the new member states, the recession may be the deepest here.



The situation is somewhat similar in Slovenia, where GDP decreased by 2.3 percent in the first quarter. Being adjacent to Italy and Austria, the Slovenian tourism sector stopped entirely the Slovenian guest workers working in the said countries returned as unemployed. The 1 percent growth of industrial value-added could not offset the 5 percent fall in services. Croatia, due to its economic structure similar to Slovenia, also faces significant recession, although here the strong seasonality of inbound tourism (unlike in Slovenia, winter tourism is not prominent here) may help: the inflow of tourists in the summer may cushion of the negative shock in the spring.

Besides tourism, retail trade usually took the heaviest hit in the region, although here the picture is varied, due to differences in consumption patterns and the severity of restrictions. In most new member states the volume of retail trade turnover fell by about 20 percent between March and May, but in a few countries (Hungary, Poland) the fall was only half as severe.

To alleviate the fallout in consumption and employment, the governments made several steps. For example, various types of wage tax allowances have been introduced that benefit both employers and employees. In almost every country a credit moratorium has been put into effect for either households or firms, or both – although their duration varies widely. Also, fiscal stimulus packages have appeared that aim certain economic areas (primarily firms in the hotel and restaurant sector), in the form of tax holidays, investment subsidies or loan guarantees.

Thanks to these measures, unemployment rates climbed only moderately, by 1 percentage point at most, until May. This is still a negative turn compared to the former trend, but nothing compared to the giant jump in unemployment levels seen in the US. To keep the employment situation manageable, however, the governments needed to deploy enormous resources, which will backfire in fiscal deficit numbers in the short run and government debt levels in the longer run.

The rise of prices decelerated discernibly in the region, but inflation turned into deflation only in a handful of countries (Estonia and Latvia, for example). In some countries (e.g. Czech Republic, Poland) inflation trends even remained unaffected by the pandemic, but considering the universal factors of the shocks, the deceleration of inflation is expected to become more uniform among the new member states, even if no substantial deflation is likely anywhere. The exception is Croatia where the downward price shock may prove more drastic, due to the prominence of the tourism industry. In the non-eurozone countries, interest rates were reduced to help to keep the economy afloat. At the moment, low interest rates do not pose any inflationary pressure, due to the losses in overall demand; later this is bound to change, but it is hard to tell, especially regarding the individual countries, that how much later and to what degree this will happen.

On the whole, the Eastern European member states have been hit less drastically hit by the pandemic so far than the more developed member states. One of the reasons is that here the spread of the epidemic remained moderate. On the other hand, while the region is highly exposed to value chain turbulences, the local links of the value chains produce less-value added than the Western European locations, hence the losses are smaller than in Germany, France or even the US. Among the affected industries, the auto industry is in the most difficult situation because here the slowdown was visible even before the pandemic. The Eastern European automotive value chain may take even heavier losses than it took so far, irrespectively of the restart of the economy. The future challenges are manyfold. On the one hand, member states have to prepare themselves for the further spread of the virus and remain cautious while restarting their economies. On the other hand, the states – and the firms as well – will need to find a way to manage the mountain of debt generated during the crisis and the accompanying stimulus measures.

Table 2/1.

Economic Growth in the EU Member States

(Percentage change of real GDP over the previous year)

	Weight	2014	2015	2016	2017	2018	2019	2020*	2021*
Germany	20.9	2.2	1.7	2.2	2.5	1.5	0.6	-7.2	5.7
France	14.7	1.0	1.1	1.1	2.3	1.7	1.3	-12.0	7.1
Italy	10.9	0.1	0.9	1.1	1.7	0.9	0.3	-12.0	6.8
Netherlands	4.9	1.4	2.0	2.2	2.9	2.6	1.7	-4.0	3.0
Belgium	2.9	1.3	1.7	1.5	1.7	1.4	1.4	-7.0	5.3
Luxembourg	0.4	4.3	3.9	2.4	1.5	2.6	2.3	-4.4	4.0
Ireland	2.1	8.6	25.2	3.7	8.1	8.2	5.5	-6.7	4.7
Greece	1.1	0.7	-0.4	-0.2	1.5	1.9	1.9	-6.8	5.2
Spain	7.6	1.4	3.8	3.0	2.9	2.4	2.0	-12.2	6.3
Portugal	1.3	0.9	1.8	1.9	2.8	2.1	2.2	-6.3	5.9
Austria	2.4	0.7	1.0	2.1	2.5	2.4	1.6	-7.0	4.5
Finland	1.5	-0.6	0.5	2.8	3.0	1.7	1.0	-9.0	2.5
Estonia	0.2	2.9	1.9	3.5	4.9	3.9	4.3	-4.5	3.6
Slovakia	0.6	2.8	4.2	3.1	3.2	4.1	2.3	-5.8	5.5
Slovenia	0.3	3.0	2.3	3.1	4.9	4.5	2.4	-7.0	5.0
Cyprus	0.1	-1.3	2.0	4.8	4.5	3.9	3.2	-7.0	6.5
Malta	0.1	8.2	10.8	5.6	6.8	6.7	4.4	-5.0	5.0
Latvia	0.2	1.9	3.0	2.1	4.6	4.8	2.2	-5.9	5.5
Lithuania	0.3	3.5	2.0	2.4	4.1	3.5	3.9	-5.0	4.7
Euro Area	**72.4**	**1.4**	**2.1**	**1.9**	**2.5**	**1.9**	**1.2**	**-10.2**	**6.5**
United Kingdom	15.3	2.9	2.3	1.8	1.8	1.4	1.4	-10.1	6.3
Denmark	1.9	1.6	2.3	2.4	2.3	1.5	2.2	-5.2	4.0
Sweden	2.9	2.7	4.4	2.4	2.4	2.3	1.2	-4.0	4.1
Hungary	**0.9**	**4.2**	**3.5**	**2.3**	**4.1**	**4.9**	**4.9**	**-5.0**	**3.5**
Czech Republic	1.3	2.7	5.3	2.5	4.4	2.9	2.4	-5.9	4.4
Poland	3.2	3.3	3.8	3.1	4.8	5.1	4.1	-4.0	4.0
Romania	1.4	3.4	3.9	4.8	7	4.1	4.1	-4.6	3.8
Bulgaria	0.4	1.3	3.5	3.9	3.8	3.1	3.4	-5.0	4.8
Croatia	0.3	-0.1	2.4	3.5	2.9	2.6	2.9	-7.0	5.5
EU-15	**90.8**	**1.3**	**2.4**	**1.9**	**2.3**	**1.8**	***1.3***	***-9.9***	***6.3***
New EU-13	**9.2**	**2.7**	**3.8**	**3.2**	**4.8**	**4.3**	***3.6***	***-4.9***	***4.3***
EU-28	**100**	**1.8**	**2.3**	**2.0**	**2.6**	**2.0**	***1.5***	***-9.5***	***6.1***
BREXIT	**84.7**			**2.0**	**2.7**	**2.1**	***1.5***	***-9.4***	***6.1***
Memorandum items									
USA		1.8	2.5	2.9	1.6	2.2	2.3	-7.8	4.0
Japan		2.0	0.3	1.1	1.0	1.9	0.7	-5.8	2.4
China		7.7	7.3	7.0	6.7	6.8	6.1	-2.6	6.8
Russia		1.3	0.7	-2.8	-0.2	2.2	1.3	1.5	4.0
South-Eastern Europe									
Serbia		-1.8	1.7	3.3	2.1	4.3	3.2	-4.0	6.1
Turkey		5.2	6.1	3.2	7.4	2.5	-2.3	-5.4	4.4

* Kopint-Tárki forecast

EU-15 = Countries that joined the European Union before 2004 (“Old EU Member States”)
New EU-13 = Countries that joined the European Union in 2004, 2007 and 2013 (“New EU Member States”)
Source: Eurostat, national statistical offices, OECD

Table 2/2.

Inflation in the EU Member States

(Harmonized consumer price indices, percentage change over the previous year)

	Weight	2014	2015	2016	2017	2018	2019	2020*	2021*
Germany	19.8	0.8	0.1	0.4	1.7	1.9	1.4	0.3	2.9
France	14.2	0.6	0.1	0.3	1.2	2.1	1.3	0.9	2.0
Italy	12.1	0.2	0.1	-0.1	1.3	1.2	0.6	0.8	1.4
Netherlands	4.0	0.3	0.2	0.1	1.3	1.6	2.7	1.5	2.5
Belgium	2.7	0.5	0.6	1.8	2.2	2.3	1.2	0.8	1.6
Luxembourg	0.2	0.7	0.1	0.0	2.1	2.0	1.6	1.0	2.0
Ireland	1.2	0.3	0.0	-0.2	0.3	0.7	0.9	0.9	1.5
Greece	1.4	-1.4	-1.1	0.0	1.1	0.8	0.5	0.6	1.4
Spain	8.0	-0.2	-0.6	-0.3	2.0	1.7	0.8	0.3	1.4
Portugal	1.5	-0.2	0.5	0.6	1.6	1.5	0.3	0.3	1.4
Austria	2.2	1.5	0.8	1.0	2.2	2.1	1.5	0.6	0.9
Finland	1.4	1.2	-0.2	0.4	0.8	1.2	1.1	0.7	1.8
Estonia	0.2	0.4	0.1	0.8	3.7	3.4	2.3	0.5	2.0
Slovakia	0.6	-0.1	-0.3	-0.5	1.3	2.5	2.8	2.2	1.5
Slovenia	0.3	0.4	-0.8	-0.2	1.6	1.9	1.7	0.0	1.7
Cyprus	0.2	-0.2	-1.6	-1.2	1.0	0.8	0.5	-0.5	0.9
Malta	0.1	0.7	1.2	0.9	1.3	1.7	1.5	0.9	1.5
Latvia	0.2	0.7	0.2	0.1	2.9	2.6	2.7	0.7	1.0
Lithuania	0.3	0.3	-0.7	0.7	3.8	2.5	2.2	1.3	1.0
Euro Area	**70.4**	**0.4**	**0.0**	**0.2**	**1.5**	**1.8**	**1.3**	**0.7**	**2.1**
United Kingdom	18.0	1.5	0.0	0.7	2.7	2.5	1.8	1.2	2.2
Denmark	1.6	0.4	0.2	0.0	1.1	0.7	0.7	0.4	1.0
Sweden	2.3	0.2	0.7	1.1	1.9	2.0	1.7	1.2	1.7
Hungary	**0.8**	**0.0**	**0.1**	**0.4**	**2.4**	**2.9**	**3.4**	**3.2**	**3.4**
Czech Republic	1.2	0.5	0.2	0.7	2.3	2.0	2.6	3.5	3.0
Poland	3.4	0.1	-0.7	-0.2	1.6	1.2	2.1	3.0	2.8
Romania	1.6	1.4	-0.4	-1.1	1.0	4.1	3.9	2.7	2.5
Bulgaria	0.4	-1.6	-1.1	-1.3	1.0	2.6	2.5	2.0	1.7
Croatia	0.3	0.3	-0.3	-0.6	1.3	1.6	0.8	0.0	0.5
EU-15	**90.6**	**0.6**	**0.1**	**0.4**	**1.7**	**1.9**	***1.4***	***0.8***	***2.1***
New EU-13	**9.4**	**0.3**	**-0.4**	**-0.2**	**1.7**	**2.2**	***2.6***	***2.5***	***2.4***
EU-28	**100.0**	**0.5**	**0.0**	**0.3**	**1.7**	**1.9**	***1.5***	***0.9***	***2.1***
BREXIT	**82.0**			**0.2**	**1.6**	**1.8**	**1.4**	**0.9**	**2.1**
Memorandum items[a]									
USA		2.1	1.5	1.6	0.1	1.3	1.8	1.2	1.1
Japan		0.0	0.4	2.7	0.8	0.5	0.8	-0.3	0.9
China		2.6	2.6	2.0	1.4	2.0	2.2	3.8	1.9
Russia[b]		6.8	7.8	15.5	7.0	2.9	4.5	3.7	4.2
Délkelet-Európa									
Serbia		1.5	2.3	1.1	3.1	2.0	2.5	0.8	1.9
Turkey		7.8	8.9	7.7	11.0	16.7	13.3	11.4	11.7

a Non-harmonized consumer price indices
b December/December
* Kopint-Tárki forecast
EU-15 = Countries that joined the European Union before 2004 (“Old EU Member States”)
New EU-13 = Countries that joined the European Union in 2004, 2007 and 2013 (“New EU Member States”)
Source: Eurostat, national statistical offices, OECD

Table 2/3.

Harmonized Unemployment rates in the EU Member States

(Unemployed as a percentage of the labor force aged 15-74, ILO-Eurostat)

	Weight	2014	2015	2016	2017	2018	2019	2020*	2021*
Germany	17.5	5.0	4.6	4.1	3.8	3.4	3.2	4.8	4.9
France	12.2	10.3	10.4	10.1	9.4	9.1	8.5	11.0	10.5
Italy	10.5	12.7	11.9	11.7	11.2	10.6	10.4	10.9	11.9
Netherlands	3.7	7.4	6.9	6.0	4.9	3.8	3.4	4.8	4.5
Belgium	2.1	8.5	8.5	7.8	7.1	5.9	5.6	7.0	7.8
Luxembourg	0.1	6.0	6.5	6.3	5.6	5.3	5.3	6.5	5.6
Ireland	1.0	11.9	10	8.4	6.7	5.8	5.1	5.8	6.0
Greece	1.9	26.5	24.9	23.6	21.5	19.3	17.8	18.1	16.0
Spain	9.4	24.5	22.1	19.6	17.2	15.3	14.0	15.8	16.8
Portugal	2.1	14.1	12.6	11.2	9.0	7.0	6.4	7.0	6.9
Austria	1.8	5.6	5.7	6.0	5.5	4.9	4.7	5.5	5.2
Finland	1.1	8.7	9.4	8.8	8.6	7.4	6.8	7.5	7.2
Estonia	0.3	7.4	6.2	6.8	5.8	5.7	5.5	9.0	6.0
Slovakia	1.1	13.2	11.5	9.7	8.1	6.9	5.8	9.0	7.0
Slovenia	0.4	9.7	9	8.0	6.6	5.6	4.2	7.0	5.0
Cyprus	0.2	16.1	15	13	11.1	8.2	6.5	8.0	7.0
Malta	0.1	5.8	5.4	4.7	4.0	3.9	3.5	6.0	4.0
Latvia	0.4	10.8	9.9	9.6	8.7	7.3	6.5	8.0	7.5
Lithuania	0.6	10.7	9.1	7.9	7.1	6.5	6.1	10.0	8.0
Euro Area	**66.4**	**11.6**	**10.9**	**10**	**9.1**	**8.2**	***7.6***	***9.2***	***9.3***
United Kingdom	13.5	6.1	5.3	4.8	4.4	4.0	3.8	9.2	7.8
Denmark	1.2	6.6	6.2	6.2	5.7	5.0	4.9	6.0	5.4
Sweden	2.2	7.9	7.4	6.9	6.7	6.3	6.8	8.5	8.0
Hungary	**1.9**	**7.7**	**6.8**	**5.1**	**4.2**	**3.7**	**3.4**	**5.5**	**4.3**
Czech Republic	2.2	6.1	5.1	4.0	2.9	2.4	2.3	5.0	4.0
Poland	7.0	9.0	7.5	6.2	4.9	3.3	3.8	7.0	5.0
Romania	3.6	6.8	6.8	5.9	4.9	4.3	4.2	7.0	5.0
Bulgaria	1.3	11.4	9.2	7.6	6.2	6.0	4.0	7.0	6.0
Croatia	0.7	17.2	16.1	13.4	11.1	9.1	6.0	10.0	7.0
EU-15	**80.2**	**10.5**	**9.9**	**9.2**	**8.4**	**7.5**	**7.1**	**9.2**	**9.1**
New EU-13	**19.8**	**10.4**	**7.9**	**6.6**	**5.5**	**4.5**	**4.1**	**7.0**	**5.2**
EU-28	**100.0**	**10.2**	**9.4**	**8.6**	**7.6**	**6.8**	**6.4**	**8.7**	**8.3**
BREXIT	**86.5**			**9.2**	**8.2**	**7.3**	**6.7**	**8.7**	**8.4**
Memorandum items [a]									
USA		7.4	6.2	5.3	4.9	4.3	3.7	11.8	11.0
Japan		4.0	3.6	3.4	3.1	2.8	2.4	3.7	3.9
China[b]		4.6	4.7	4.1	4.0	4.0	3.8	5.4	5.4
Russia[c]		5.5	5.1	5.6	5.7	5.4	5.2	7.3	7.5
South-Eastern Europe									
Serbia[d]		22.1	19.2	15.3	13.5	12.7	11.0	12.0	10.0
Turkey		9.0	9.9	10.9	10.9	11.0	14.0	17.0	17.0

a Non-harmonized unemployment rates
b Urban unemployment
c OECD statistics, unemployment rates for the age group 15-64
d National statistics, unemployment rates for the age group 15-64
* Kopint-Tárki forecast

EU-15 = Countries that joined the European Union before 2004 ("Old EU Member States")
New EU-13 = Countries that joined the European Union in 2004, 2007 and 2013 ("New EU Member States")

Source: Eurostat, national statistical offices, OECD

Macroeconomic indicators for Hungary and Kopint-Tárki forecast

(year-on-year change, percentage)

	Data				Forecast		
	2018	2019	2020		2020		2021
			Q1	Apr-May	2020 Apr.	2020 July	2020 July
GDP aggregates, real growth							
GDP total	5.1	4.9	*2.2*		-5.5	**-5.0**	**3.5**
Domestic Demand	7.3	5.6	*4.0*		-4.4	**-2.1**	**3.1**
Private Consumption	4.0	4.4	*4.3*		-3.8	**-2.1**	**3.0**
Public Consumption	2.0	2.0	*2.4*		0.6	**1.0**	**0.0**
Gross Fixed Capital Formation	17.1	15.3	*-2.6*		-7.8	**-5.6**	**4.5**
Gross Capital Formation	18.3	9.5	*4.3*		-7.8	**-3.1**	**4.5**
Export	4.3	6.0	*-0.5*		-8.8	**-10.1**	**5.8**
Import	6.8	6.9	*1.3*		-7.5	**-6.8**	**5.1**
Industrial production	3.4	5.3	*0.4*	*33.7*	-10.0	**-10.0**	**5.0**
Consumer Price Index	2.8	3.4	*4.3*	*2.5* [e]	3.8	**3.2**	**3.4**
Employment, earnings							
Number of Employed, growth [a]	1.1	1.0	*-0.7*	*-2.3* [e]	-8.0	**-2.3**	**1.8**
Employment rate [a]	60.4	60.8	*60.3*	*59.5* [e]	56.1	**59.5**	**60.1**
Unemployment Rate [b]	3.7	3.4	*3.7*	*4.6* [e]	7.5	**5.0**	**4.3**
Unit Labor Costs, in EUR[c]	9.0	4.8	*-2.1*		-2.2	**2.9**	**4.1**
Gross Nominal Wages	11.3	11.4	*9.1*	*8.6*	6.0	**7.0**	**7.0**
Net Real Wages	8.3	7.7	*4.6*	*6.2*	2.1	**3.7**	**3.5**
Savings Rate, % of GDP [d]	6.2	5.0	*5.2*		5.0	**5.8**	**5.3**
Current and Capital Accounts Balance, % of GDP	2.2	1.0	*1.7*		0.8	**0.4**	**1.0**
General government							
Fiscal Balance, ESA-2010, % of GDP	-2.1	-2.0	*-1.5*		-4.0	**-5.2**	**-3.8**
Gross Government Debt % of GDP	70.2	66.3	*66.8*		73.9	**74.6**	**72.5**
Short-term Government Yields (3M), eop	0.00	-0.01	*0.77*	*0.18* [e]	1.0	**0.8**	**1.0**
Long-term Government Yields (10Y), eop	3.01	2.01	*2.65*	*2.15* [e]	3.0	**3.0**	**3.0**
External assumptions							
Internat. Trade in Goods and Services [d]	4.0	4.0			-3.9	**-11.9**	**8.0**
Brent Oil Price ($/bbl, p. avg.)	71.3	64.4	*50.4*	*23.9*	45.0	**40.0**	**45.0**
GDP Real Growth, Eurozone	1.9	1.3	*-3.0*		-5.2	**-10.2**	**6.5**
GDP Real Growth, New EU Members	4.3	3.6	*0.7*		-3.9	**-4.9**	**4.3**
EUR-HUF, period average	319	325	*339*	*352* [e]	360	**347**	**350**
EUR-USD, period average	1.18	1.12	*1.10*	*1.10* [e]	1.10	**1.12**	**1.12**

a ILO methodology, period averages, aged 15-74, public workers are counted as employed
b Manufacturing, based on gross value added and the monthly average compensation of employees in euro, cumulated from the beginning of the year
c Net lending of households according to the financial accounts statistics, percentage of GDP, four-quarter cumulative data
d Trade of goods and services, data based on IMF World Economic Outlook
e Second quarter

3. Hungarian Economy

Introduction

Three months have passed since our previous report in late April, and now we have much more information about the trajectory and the economic consequences of the pandemic. Yet, it is cannot be stated with certainty that the picture is much clearer now than it was in April – uncertainties still abound.

In April we based our forecast on the assumption that the epidemic would peter out by the end of summer and the last third of the year would be characterized by economic normalization. Now we know that the phase of mass infections has never arrived in Hungary. The whole trajectory of the epidemic was milder than originally thought. But a new outbreak is still in the cards, especially considering the rapid pace of the global spread of the virus and the worrying developments in several Eastern European countries in the wake of the opening of the economies and the borders.

The fact that the acute phase of the epidemic was shorter in Hungary than previously thought is the primary reason behind the upward revision of our growth forecast: now we expect the GDP to fall by 5 percent in 2020, as opposed to the 5.5 percent projection given in our April report.

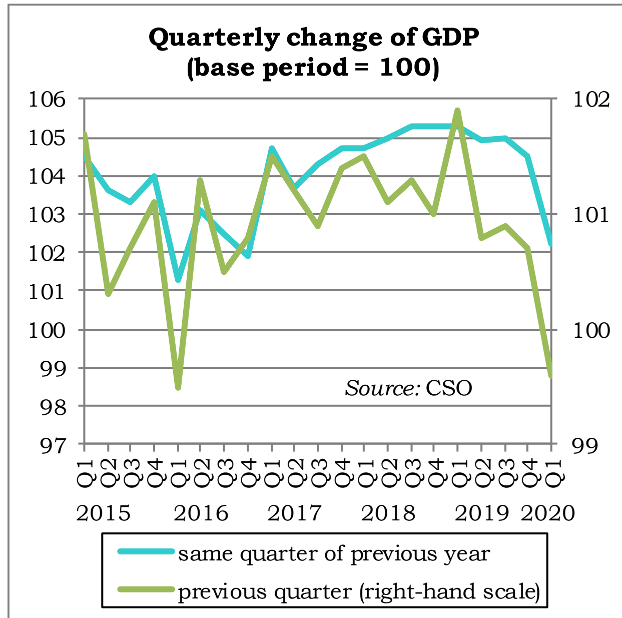
Regarding the economic reverberations of the epidemic, the data of the recent months paint a mixed picture. In some of the components of the production side of GDP (industry, tourism) the situation is even worse than what we expected in April. On the other hand, the retail trade numbers are better than previously expected. As a result, on the expenditure side, the consumption outlook is now less gloomy than in April, but the merchandize trade prospects have deteriorated. The latter is mostly the result of the unfavorable industrial output numbers.

In the second quarter, retail turnover – which makes up more than half of consumer spending – only decreased by roughly 5 percent, despite the much deeper fall in April. As for fixed investments – the other major component of final domestic use – the information is too sporadic to make a reliable assessment. There are reports about deferred investments, but on the other hand, the government is trying to rev up state investments. It is not yet clear how much of the almost unlimited and cheap credit funding provided by the central bank is spent on business investments, as opposed to replacing existing debt with new, cheaper ones. At present, amid uncertainties regarding both domestic and external demand prospects, it is not easy for firms to decide upon investment projects.

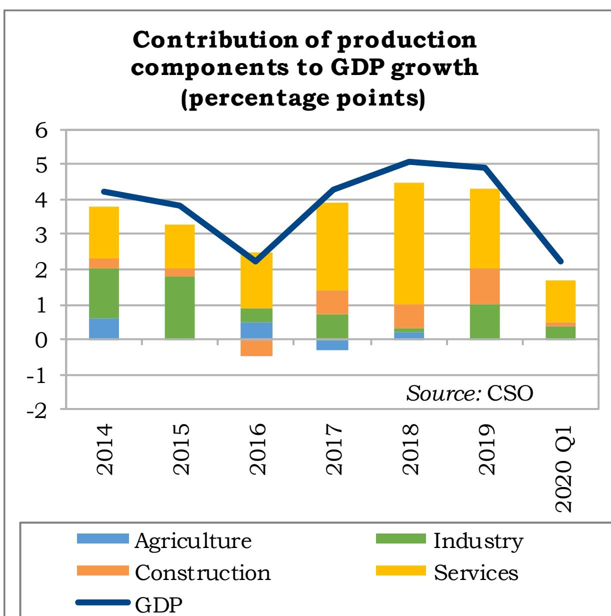
All in all, the pace of future recovery is still hard to predict. What is certain is that there are hard times ahead for the two most vulnerable sectors, that is, industry (more specifically: automotive and machinery industry) and tourism. Demand for auto vehicles is unlikely to entirely rebound within 1-2-3 years, and the pre-crisis international tourism patters will not return soon, either. Domestic tourism will not be able to offset the steep fall of inbound tourism. This is why we only expect consolidation – and not s strong rebound of economic activity for 2021.

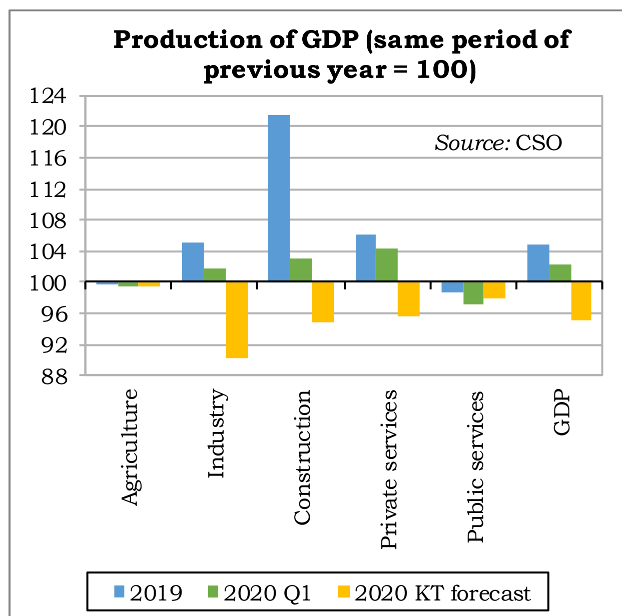
GDP and its components

In the first quarter of 2020 Hungarian GDP climbed 2.2 percent year-on-year, which is better than expected and also way better than the EU average. Still, even this meant a sharp deceleration compared to the growth rates seen in the past two years. The seasonally and working day adjusted growth rate was slightly lower, 2 percent, while the quarter-on-quarter rate was negative (-0.4 percent), the first time since early 2016. It should be noted that the better-than-average first-quarter Hungarian growth performance was mostly a result of the time factor: the pandemic appeared in the country later than in many other European countries, and as a result, the restrictive measures also were introduced only around mid-March.



On the ***production side***, the growth of *services* decelerated roughly as expected – from 4.2 percent in 2019 to 2.4 percent. Within market services, retail trade, tourism, accommodation and restaurant services as a whole expanded at a good pace of 5 percent. This, however, was purely a result of galloping retail trade growth: the tourism accommodation and restaurant sectors imploded in March and – as a result – decreased in the first quarter as a whole. In the meanwhile, growth rates in *industry* and *construction* slowed down spectacularly but – somewhat surprisingly – remained positive. That is why overall GDP growth did not dip below 2 percent, defying expectations. The crisis-generated plunge only occurred in April in industry and in May in the construction sector.



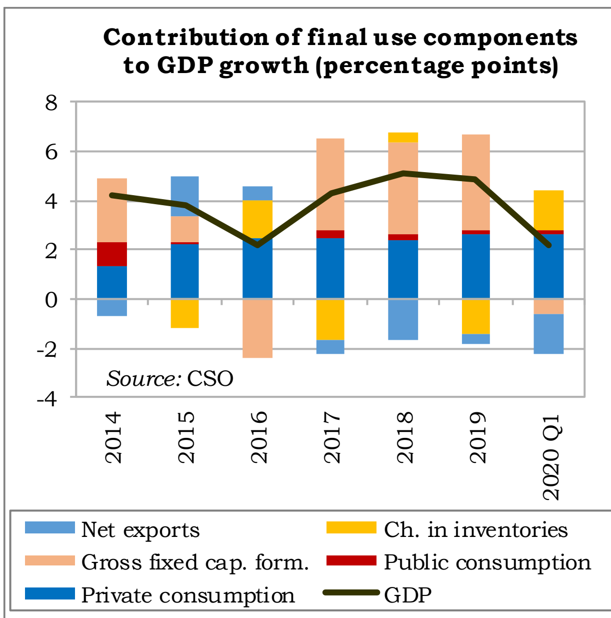


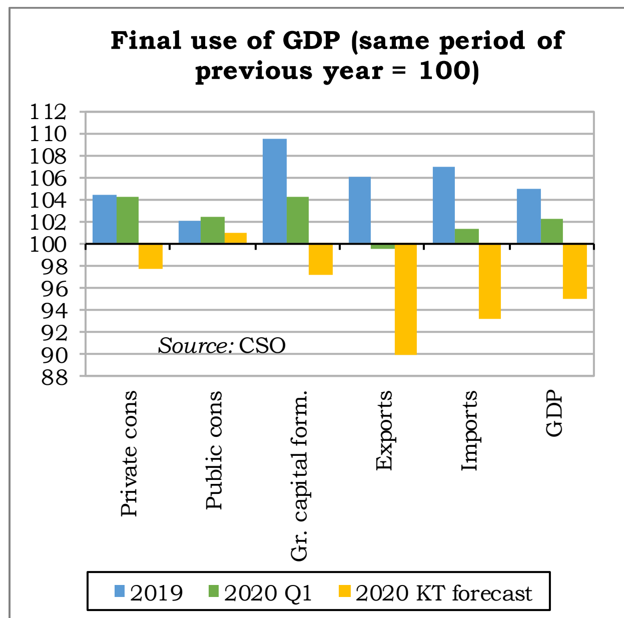
On the ***expenditure side***, primarily *consumption* helped to keep up economic growth at a perceptible level: private consumption was up 4.3 percent almost the same as the annual average in 2019, a result of an outstanding January and February and, in the case of *some* product categories, still respectable growth in March. Besides, *gross fixed capital formation* contracted only at a modest pace, by 2.6 percent: while government (and government-linked corporate) investments fell, private business investments still kept growing in the first quarter. Due to the changes in inventories, overall capital formation expanded, resulting in a growth of ***final domestic use*** by 4 percent, which indicates that overall domestic demand was only mildly affected by the pandemic in the first quarter of the year. It should be noted, however, that the "favorable" change in inventories is at least partly a result of the accumulation of unsold output stock, a consequence of the coronavirus crisis.

The still positive trend in domestic use was in great part offset by the substantial deterioration of the ***net export position***. In March the volume of merchandise export already fell (but did not yet plummet like in April) while the export of services began to plunge (because inbound tourism virtually ceased to exist) from the second half of March. Hence, not just the net export of services but the gross export of services contributed negatively to economic growth, something unprecedented since 2012.

On the whole – as already indicated in our previous report – the first-quarter figures are a combined result of a reasonably strong January and February and a partially crisis-affected March. The second quarter, by contrast, began by a dramatic plunge in April and – based on less than comprehensive data – only a partial normalization has taken place by the end of June. The trends in the third quarter are still uncertain but apparently, parts of domestic demand are recovering much faster than the external trade flows. We expect the GDP to fall at a double-digit pace in the second quarter, with an easing of decline in the subsequent quarters.

The most dramatic fall occurred in *industry* where gross output was down 34 percent (and the transport vehicle sector contracted by 66 percent) in April-May on an annual basis. The future recovery of the largely export-oriented industrial sector heavily depends on external (European) developments, hence the fact that the majority of German firms expect normalization only in 2021 is not a good sign.





The *construction sector* may weather the year with a substantial but not drastic contraction – even though April saw a double-digit fall, and the pandemic resulted in a sudden decline in newly started construction projects. *Services* as a whole may also avoid dramatic decline, mostly due to the fast recovery of retail turnover, although the crisis will be severe and protracted in certain areas, like tourism and events-festivals-conferences. Retail trade has likely benefited from the fact that the fall of employment has been less severe than previously feared, partially thanks to the radical expansion of the originally rather ungenerous wage subsidy program.

The external trade of goods and services, on the other hand, are expected to suffer during most of the year. Fixed capital formation will probably fall at a double-digit pace in the second quarter as many firms deferred or even reconsidered their previous investment plans, due to the new financial and demand outlook. The government will strive to rev up both government investments and – through newly introduced investment subsidy tools – business investments. It is uncertain, however, to what extent these efforts will affect investment activities this year and to what extent we will see a delayed effect in 2021. At present, we expect a moderate decline of roughly 5 percent in fixed capital formation in 2020.

As for the trajectory of the pandemic, the first wave subsided even earlier than we previously thought, by early summer. On a less positive note, we can be less optimistic about the possible re-ignition of the epidemic, due to the continuing rise of daily cases in many parts of the world, including some European countries. A very partial reintroduction of restrictions has already begun, and while a general closure (like in the spring) is unlikely, the epidemic situation may continue to hinder normalization in the course of the year.

To sum up, **we predict the GDP to decrease by 5 percent in 2020, with a moderate recovery in 2021**. This forecast, however, is not without downward risks. While the normalization of the financial standing of firms has begun in some areas, many firms are still very vulnerable. A secondary wave of corporate bankruptcies and layoffs is still in the cards, and such a development would seriously hinder macro level stabilization.

3.1. The production of GDP

3.1.1. Industry

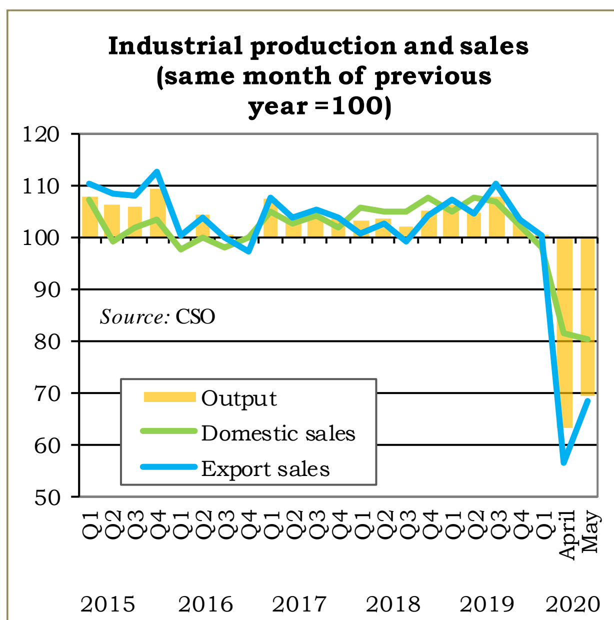
In the first five months of 2020 industrial production fell by 13.8 percent compared to the same period of the previous year. The modest growth in the first two months was followed by a decrease in March and a freefall in April and May. The large auto manufacturers halted production in the second half of March and restarted only toward the end of April, but they operated at a very reduced capacity. This is reflected by the fact that the output of the transport vehicle industry was still down 53 percent in May, after a drop of 79 percent in April.

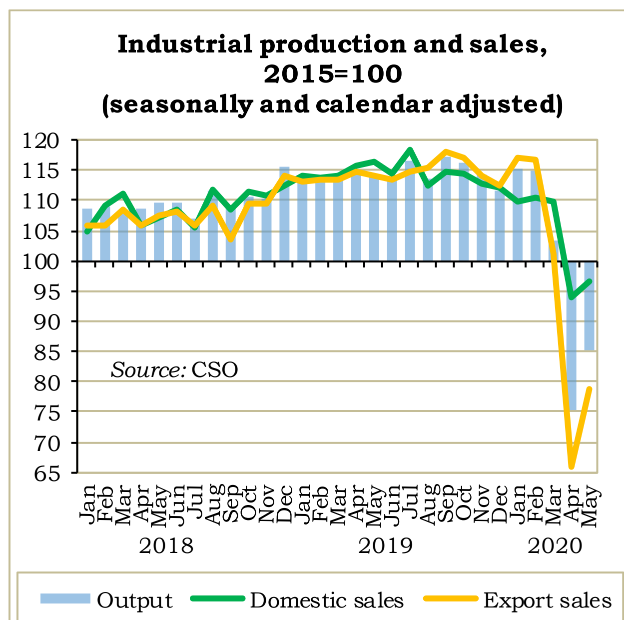
But while the automotive sector was the epicenter of the industrial crisis, the decline encompassed almost every industrial branch in April and was universal in May. Save the wood, paper and printing industry, and the pharmaceutical industry, every manufacturing industry underwent a shock during the March-May period, according to the seasonally adjusted production data. While obviously the auto industry took the biggest hit, the other manufacturing branches suffered a double-digit deterioration of year-on-year growth rates from Q1 to April-May as well, with the exception of the two industries mentioned above.

This means that even with a reasonably significant rebound in June, the second-quarter industrial growth rate is likely to be catastrophic, around a level of minus 25 percent.

Since the Hungarian industrial downturn is largely the consequence of a European and global crisis, industrial export sales fell at a steeper pace than domestic sales: in April-May, export and domestic sales dropped by 38 and 19 percent, respectively. While firms' assessment of perspectives was gradually improving since the April nadir in Germany and the euro area, the recovery will be protracted, and temporary setbacks are possible.

For 2020 **we predict a 10 percent drop in industrial output**. This also means the industry is expected to be an economic area that will prominently hold back overall economic normalization.



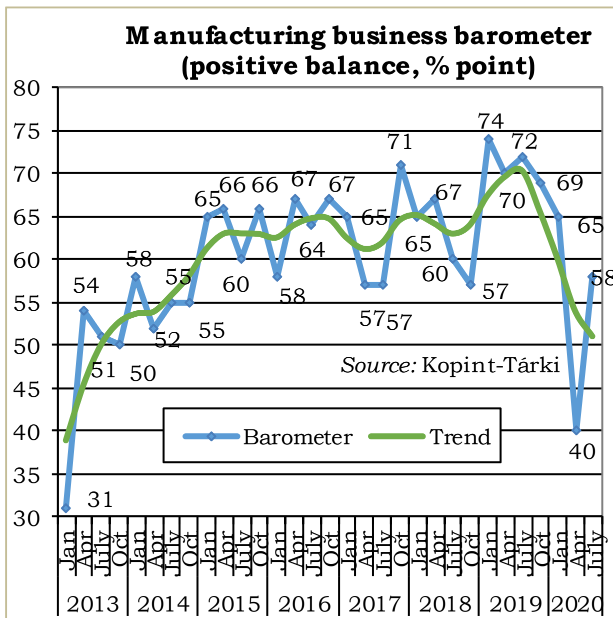


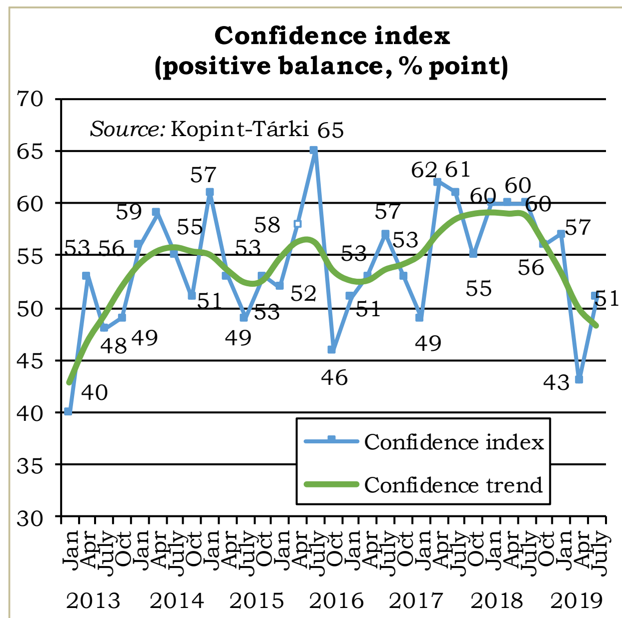
Manufacturing confidence survey

While our previous survey in the spring painted a disheartening picture about the manufacturing sector – the confidence index at historical lows, firms struggling with severe supply problems and precipitous fall in demand – the most recent survey indicates a significant improvement. According to the respondents, the situation is better now, and the perceived outlook bounced back too, which means that the majority seem to believe that their output may return to 2019 levels by the end of the year. 75 percent of the respondents have not applied for state support and also 75 percent weathered the emergency period without structural adjustment. (13 percent was forced to reduce its workforce.)

According to the survey, capacity utilization stands at 66 percent, 14 percentage points lower than in January and 6 percentage points lower than three months ago. The stock of orders is usually still lower than in January but substantially higher than in March. Output inventory levels somewhat improved but in any case, they are at a medium level, meaning that there was no drastic year-on-year change in output inventory during the period of restrictions.

The respondents still deem the economic situation unfavorable, but they have positive expectations regarding the future; the same is true for their production projections, that is, the firms do not expect a lasting severe production loss. They expect positive profits – or at least no losses – for 2021. As a result, the business barometer stands at 58 while the confidence index at 51 points. Micro and small enterprises tend to be in worse shape, and they have been more prone to apply for state support.





Construction

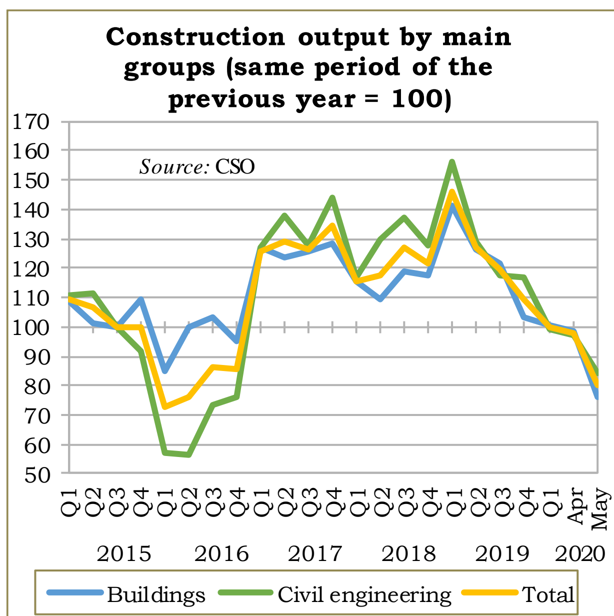
In the first five months of 2020, construction output fell by 5.6 percent on an annual basis. This is a result of the state of near-stagnation in the first quarter, a relatively mild decrease in April, and a sudden, precipitous fall in May.

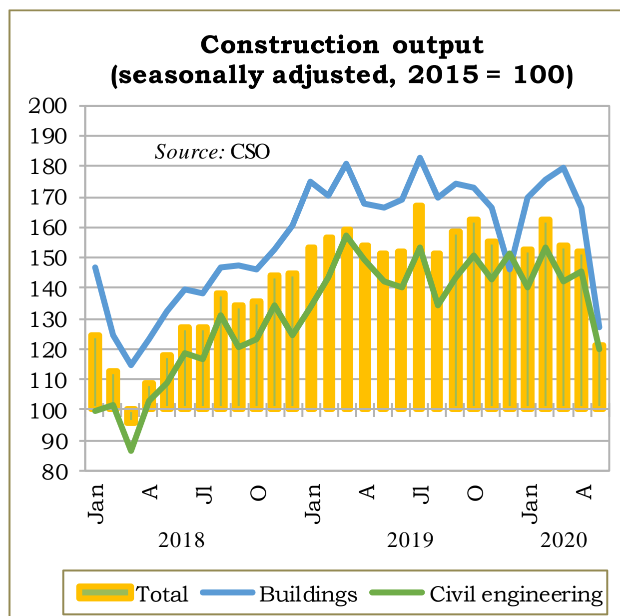
Even the stagnation in the first months was a harsh, although not unexpected, change after years of double-digit growth. The fall in May, on the other hand, is largely the result of the coronavirus crisis. In other economic areas the impact of the crisis kicked in already in March or April, but in construction overall output was only mildly affected until May, even though the volume of *newly started* construction projects fell sharply from the second half of March – that is, from the moment the pandemic-related restrictions were introduced.

The cumulative five-month fall of output was not much different in the two main groups of construction – with negative growth rates of -5.3 and -5.7 percent, respectively, in the construction of buildings and civil engineering. But the coronavirus shock is apparently more drastic in the case of the construction of buildings: in May, output in this main group dropped by 24 percent, while the fall in civil engineering was less dramatic, 15,6 percent. Even the start of two large-scale projects – the renovation of the stations of one of the Budapest underground lines, and the construction of a new Samsung plant – could not save the construction of buildings from dropping like a stone, that sharp was the stoppage of other new projects.

This may change, however, in the coming months, considering that most restrictions were abolished during May. Hence the pace of output decline is likely to moderate during the summer, as demand from private customers somewhat bounces back. Such an easing of decline is expected in civil engineering as well, although this area has a deeper underlying problem, namely the phase-out of many large-scale infrastructure projects, co-funded by the EU. A complete recovery and a return to growth, however, is unlikely.

On the whole, we expect a yearly decline of **5-7 percent in construction output** in 2020.

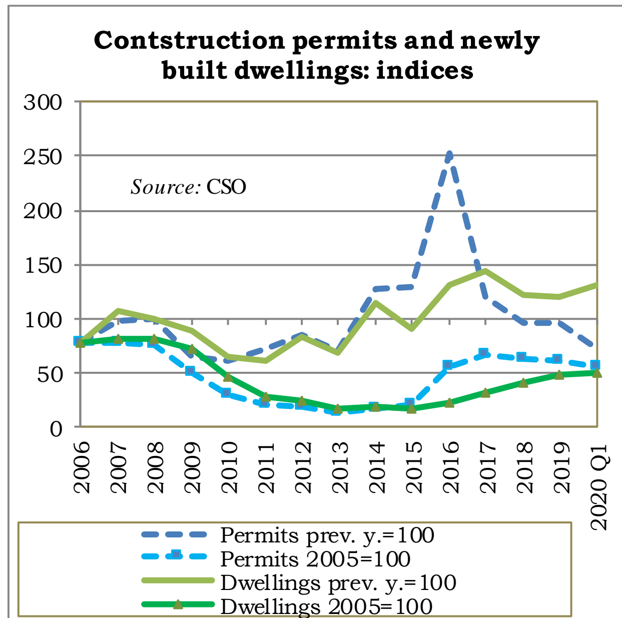




Housing construction

The wave of housing completions continued in the first quarter of 2020: the number of dwellings built climbed 30.4 percent on an annual basis. This is impressive even if we take into account the fact that the number of housing construction projects ***started*** – based on data on multihousehold housing construction projects – continued to decline compared to the same period of the previous year. The number of building permits and notifications issued was 27 percent lower in the first quarter than one year earlier.

The phasing out of preferential VAT rate on housing construction had the expected effect on housing construction activity, but now this is compounded by the bleaker income and employment outlook, caused by the coronavirus pandemic. As a result, the demand for new dwellings is impaired further, inevitably deepening the downward effect on housing construction. We expect, despite the strong year start, a sizable **annual drop in the number of dwellings built in 2020**.



The fall in the number of projects started means a muted construction activity in the coming years as well. The new government support scheme for building dwellings in designated “rust belts” will not have any upward effect before 2021 since the first round of designating eligible areas will only take place in September.

3.2. The final use of GDP

3.2.1. Household income, consumption and savings

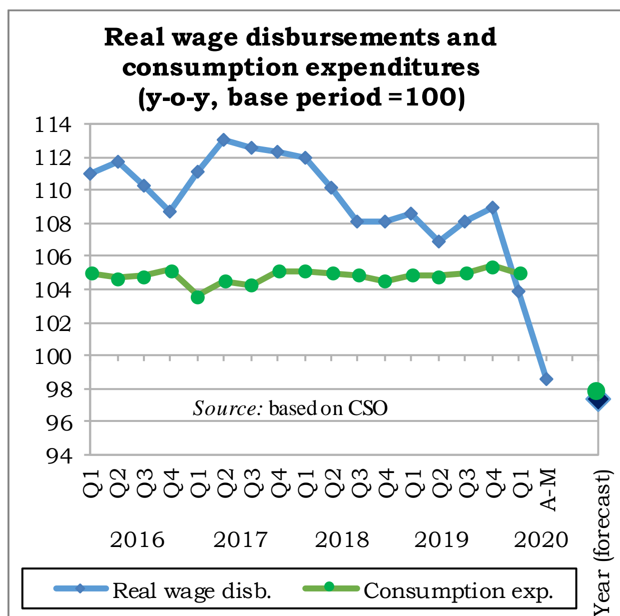
In the first five months of 2020, nominal wages grew by 8.5 percent, *not including public workers*. This is a lower rate than in 2019, by about 2 percentage points, but still substantial. Business sector wages rose somewhat faster while public sector wages at a slower pace – the latter is due to the deceleration of the rise of public administration wages and despite the acceleration in healthcare and social worker wages.

It is surprising that in April – the month of the most severe stoppage of the economy – wage growth only slowed down very moderately and reaccelerated in May. The slowdown was severe in heavily affected areas: manufacturing, tourism accommodation and food service, and especially the arts-entertainment sector. Apparently – at least on a macro level – wages are less affected by the crisis than we previously expected.

A qualification is due, however: the composition effect due to the growing share of part-time workers pushes wage growth numbers upwards. While many employees were put into part-time status and faced a decrease of wage income to various degrees, the wage data only covers full-time wages, therefore these wage cuts are not reflected in the statistical numbers. With the inclusion of this composition effect, the actual rate of wage growth may have been 1-1.5 percentage points lower in April and May than what the numbers show.

With *public workers included*, overall gross wages were up 8.8 percent in January-May. **Real wages** grew by 5.1 percent, while ***net real wage disbursements*** – due to an accelerating pace of decrease in personnel – only climbed 1.2 percent. In April and May, real wage disbursements already decreased – by about 1.5 percent – as the pace of the fall in the number of employees accelerated to 7.6 percent in May.

The **outlook** for the rest of the year is mixed. On the one hand, the absence of sharp decline in wage dynamism in April-May and the abatement of the epidemic by the middle of June suggest the continuation of relatively dynamic wage growth. On the other hand, many companies may find themselves at the end of their rope financially during the coming months, especially in areas where the recovery is more protracted than, say, in retail trade. In the second half of the year, a part of companies may be forced to reconsider their wage agreements and – if they hire again after layoffs – they may pay lower wages to the new employees than they did to their ex-employees before the layoffs.



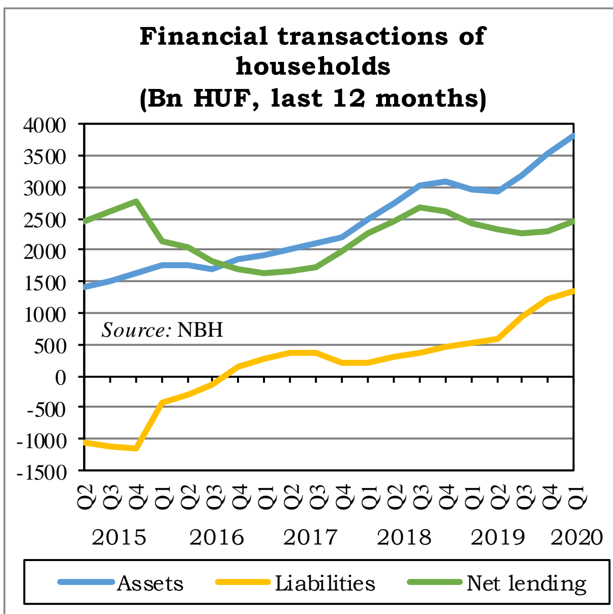
As a result, we still expect a deceleration of wage growth for the rest of the year, with **annual average wage growth of 7 percent** in 2020. **Net real wages** are to grow by 3.7 percent while net real wage disbursements are likely to decrease. The abovementioned fact that wage data covers only the wages of full-time employees, the real decline of

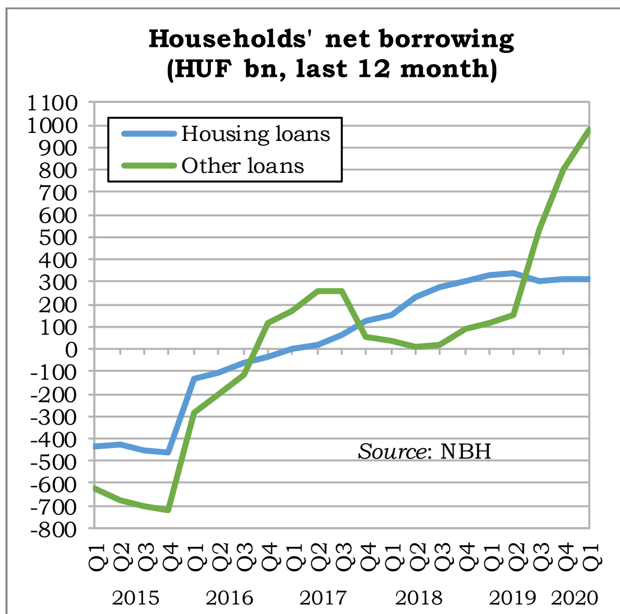
real wage disbursements is likely to be more substantial than what the official numbers show.

Households' consumption expenditures expanded at a very dynamic pace, by 5 percent, in the first quarter. From April on, however, consumption decreases on a year-on-year basis: retail sales fell by 10 percent, not to speak about car sales and spending on food services. What is remarkable, however, is the fast deceleration of decrease in May and June: in June, the volume of retail trade turnover only decreased by 1 percent year-on-year, although the recovery is very far from being universal across the various retail segments and car sales and food services continued to contract sharply.

While slightly diminishing real incomes point toward the continuing decrease of overall household consumption, the pace of the decrease may close to zero by the end of the year. Negative risks exist, however, due to the possibility of further layoffs and the uncertainties regarding those employees who – after the three-month deadline – fall out of the wage support scheme. **Still, the decline of annual household consumption will be much less drastic in 2020 than previously expected, it may not exceed 2 percent**.

Households' ***net financing capacity*** mildly rose further in the first quarter of 2020 as *gross savings* continued to rise steeply while the upward curve of *net borrowing* flattened somewhat. The said flattening is primarily linked to *consumption loans*: the pace of growth of the latter decelerated in the first quarter, even if remained significant, as opposed to the ongoing stagnation of housing loans. (The picture is complicated by the fact that the so-called "baby loan" is tagged consumption loan even though the borrowers





tend to use a substantial part of the loan for housing purposes.) During the rest of the year, **we expect the continuing rise of the savings-to-GDP ratio**. Due to the higher level of uncertainty, households will increase their savings – at least those who can afford it. This seems to be corroborated by the sharp rise in outstanding household deposits in April and May, although some of this may reflect an accumulation of temporarily deferred consumption. At the same time, both housing and consumption borrowing may decrease, even though in the balance of borrowing this may be partially offset by the impact of the loan repayment moratorium.

3.2.2. Investments

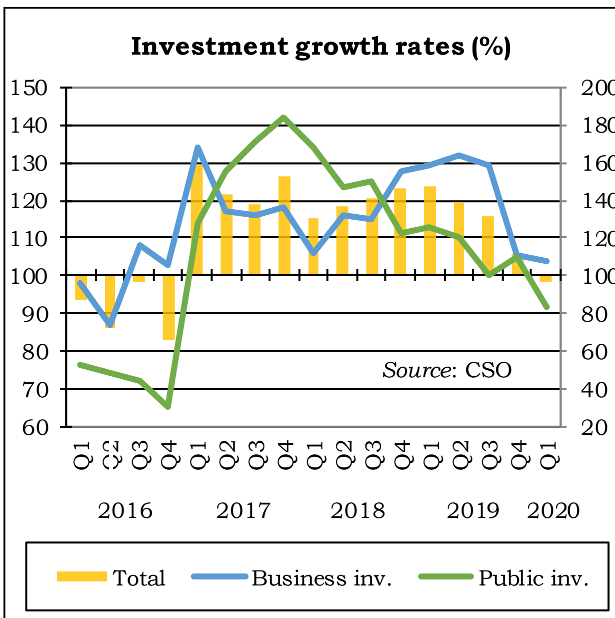
In the first quarter investments decreased by 1.8 percent on an annual basis, the first negative growth since late 2016. A 7 percent fall of machinery investments were accompanied by a 2.8 percent growth of building investments.

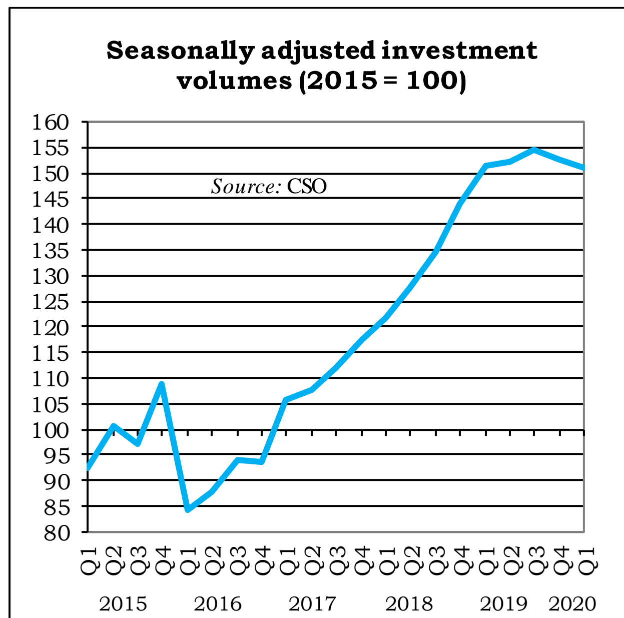
In sectoral breakdown, the decline is basically due to the fall in *public sector investments* (by 13 percent), especially in public administration and defense. This decrease has less to do with the coronavirus crisis – yet – rather it is a result of the completion of many significant development projects co-funded by the EU. Within public investments, however, healthcare investments grew spectacularly, which can be attributed to the pandemic.

By contrast, the sector of *medium and large firms* increased its investment activity, by a year-on-year rate of 4 percent. Since the investments of the government-linked firms (the so-called quasi-fiscal sector) decreased, according to the NBH, the growth of private firm investments probably was more buoyant. (The same NBH data suggests, on the other hand, that the investments of micro- and small enterprises probably did not do so well.)

Still, the 4 percent growth is a sharp deceleration compared to the last year, although only a moderate slowdown compared to the fourth quarter of the last year. It is important to note that the rise in corporate investments is only reflected in a handful of economic branches, while in the majority of branches the volume of investments decreased. Investments minimally expanded in the *manufacturing*, the economic area with the largest share, and real estate investments grew significantly, mostly due to the still strong housing construction activity. Also, investments rose precipitously in agriculture and information-communication. It is worth noting that manufacturing investments *outside the automotive sector* grew significantly, while the auto industry investments decreased, which was probably an early consequence of the coronavirus crisis, at least in part.

With the arrival of the pandemic, capacity utilization decreased sharply in the majority of economic areas, which may decrease the incentive to invest. On the other hand, the pandemic gave a push to digitalization and – most probably – to automatization projects. The problem is that many companies faced a deterioration of financial standing,



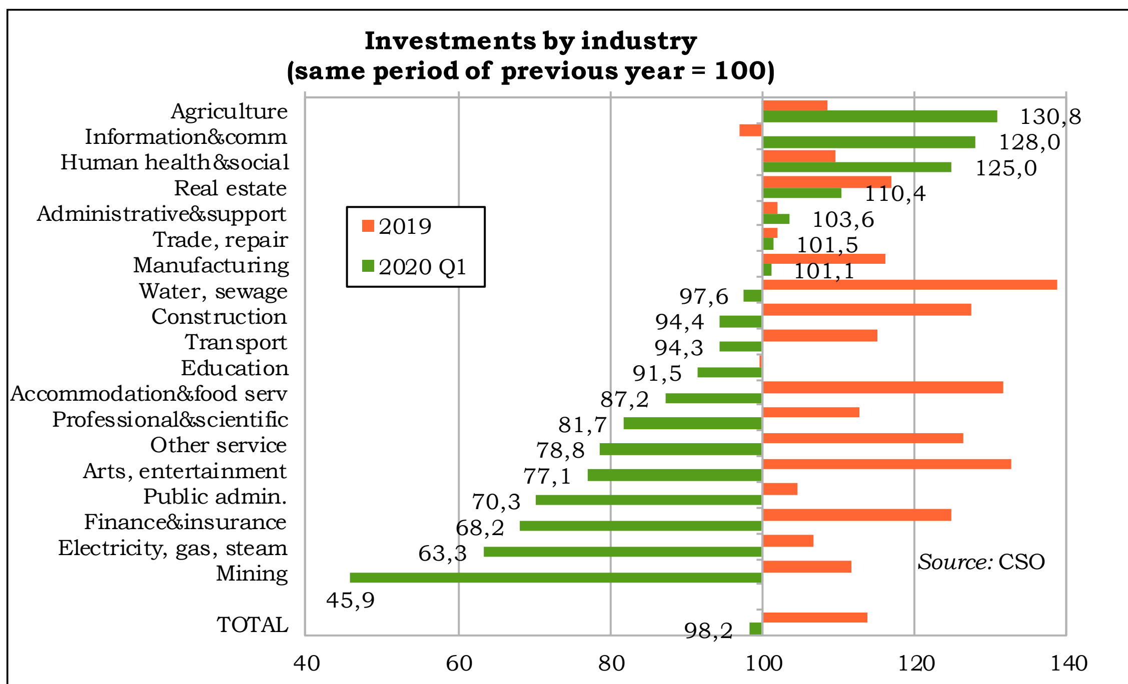


restricting the firms' potential to invest, and prompting them to reconsider earlier investment plans.

The government is intent to rev up public investments but whether these efforts will be sufficient to offset the decline of EU-funded investments is uncertain. Local governments are forced to delay many of their investment plans because their revenues are decimated by both the pandemic and several government decisions about the centralization of tax incomes.

The government has also introduced several investment subsidy schemes for the business sector – one of them is the so-called competitiveness-enhancing support program for larger enterprises. Also, the central bank introduced a generous loan support package for smaller firms („Funding for Growth Go") but the extent to which these loans are used for actual investments varies. On the whole, we expect, despite the stimulus efforts, a decline of both business and public investments.

At present, our prediction is a **5.5 percent decrease in investments in 2020**.



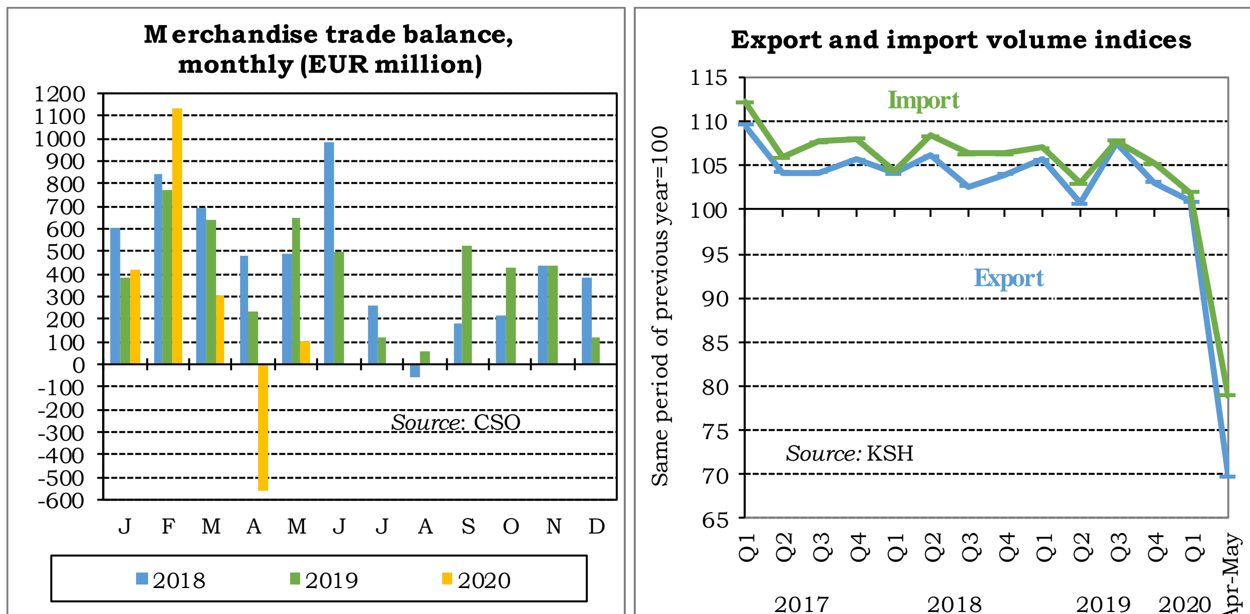
External trade

After some moderate growth in the first two months of the year, both export and import began to decrease in March, and it plunged in April and May. Export was hit the harder, especially in April. In April-May, export dropped by 30 percent on average, while import declined by about 21 percent. The negative gap between export and import change became enormous in April, resulting in a sizeable external trade *deficit* – a first since January 2009. Fortunately, the gap decreased in May and the positive monthly trade balance returned, albeit it was only a fraction of the surplus in the same month of 2019. The euro-denominated cumulative trade surplus was 48 percent lower in January-May than in the same period of the previous year.

These developments, along with plummeting industrial export sales and the relatively quick recovery of retail turnover, show that the crisis hit the export performance of Hungary much more drastically than the domestic market. This is far from universal in the EU: in April, the year-on-year fall of export was among the most severe in Hungary compared to the other member states while retail trade was much less affected in Hungary than in many other member states.

The plunge of export in April and May was primarily due to machinery and transport vehicles – especially transport vehicles. The export of manufactured products also fell sharply while the decrease in food export remained mild. In the case of import, the contraction was more evenly distributed – save manufactured goods, a two-digit decrease was registered in every main product group.

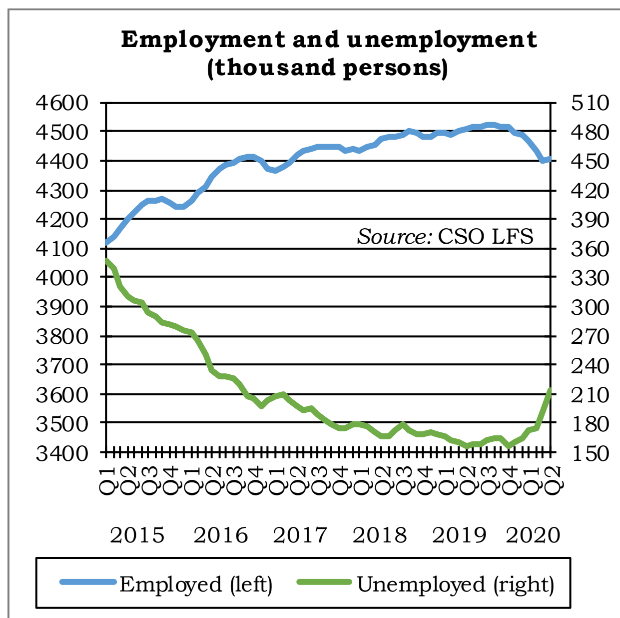
While a gradual recovery of both export and import is expected in the coming quarters, import is likely to get close to normal sooner than export. Hence the annual trade surplus is expected to decrease dramatically in 2020 as a whole.



3.3. Employment, unemployment

According to the LFS data, the number of employed only decreased by 0.7 percent in the first quarter but dropped by 2.3 percent in the second. Still, this is a milder fall in employment than previously expected, and it would have been even milder, 1.9 percent, without the steep fall in the number of employed abroad. During May and June, the number of employed already rose compared to the previous month. The *unemployment rate* increased from 3.7 percent in the first quarter to 4.6 percent in the second, but in June alone it was higher, 5.1 percent. This is still an underestimation of the actual number of people who have lost their jobs: In June, the number of registered jobseekers constituted more than 8 percent of the active population, which is far higher than the official unemployment rate. This is mostly due to the fact that much of the laid-off first became inactive according to the LFS statistical classification, because of the epidemic-related restrictions of movement. From May, a growing number of jobless is officially labeled as unemployed, hence the unemployment rate may grow further in the coming months, even as the employment situation begins to slowly improve.

While the wage subsidy program aiming at preserving jobs arrived relatively late and became comprehensive enough even later, eventually it was apparently quite effective in keeping job losses under check. By the middle of July, about 200 thousand employees were involved in the support scheme. Some of this success may be temporary: in various areas, the financial standing of enterprises may remain problematic, and even the wage costs reduced by the support program may become too high, which could potentially lead to further layoffs.



This, and the possible further reverberations of the crisis, means that a fast recovery of employment is not very likely. Still, in the light of the recent data, our earlier expectations about the very harsh drop in employment proved to be exaggerated. At present, we expect a 2-2.5 percent decrease in the number of employed. The annual unemployment rate may reach 5 percent in 2020, but this partly depends on how much of the jobless will be relabeled from inactive to unemployed during the rest of the year.

3.4. Fiscal, monetary and financial developments

3.4.1. Fiscal trends and outlook

The 2020 budget

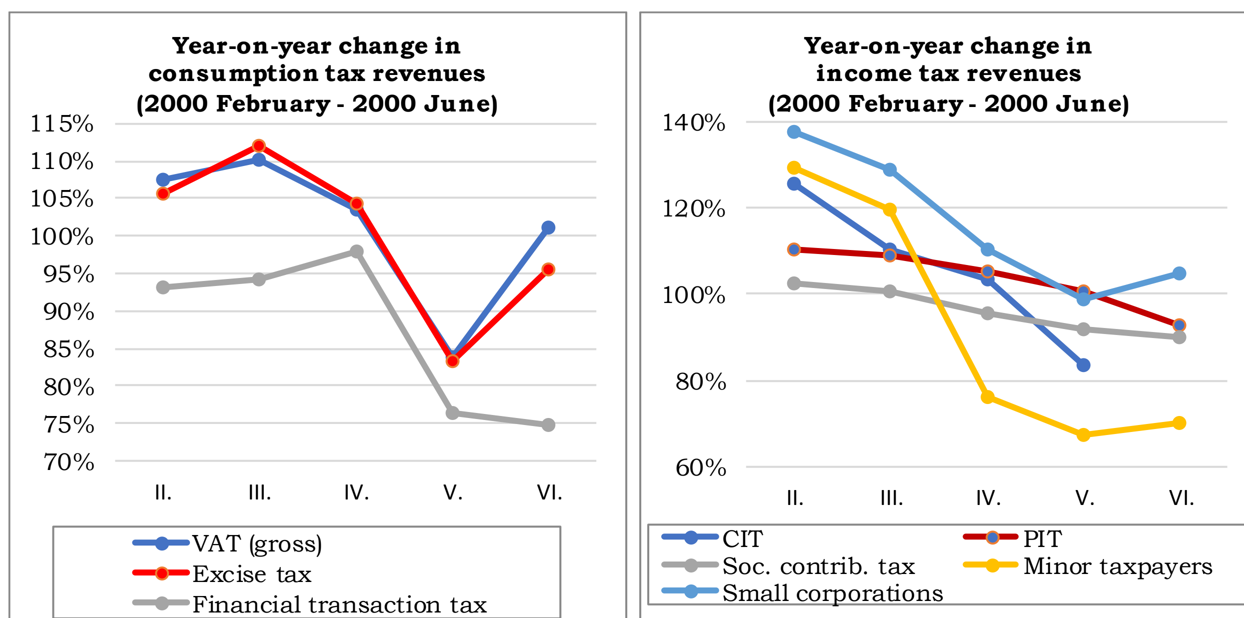
The outbreak of the Coronavirus epidemic, the epidemic-related restrictions of movement, and the fiscal stimulus measures profoundly reshaped the 2020 budget. The cash-flow deficit of the central subsystem (general government minus local governments) reached HUF 1,837 billion, five times the originally planned annual deficit.

Regarding tax revenues, it should be noted that the latest monthly data (for June) reflects economic developments in the previous months (May). This is why central budget tax revenues dropped by about 7 percent in May, while the overall decrease eased in June (to 2 percent). Clearly, taxes on consumption suffered the largest loss among the major revenue categories, with a decrease of VAT inflow by 70 percent and a 17 percent fall of excise tax revenues in May. June, on the other hand, saw a degree of recovery: VAT revenues decreased only by 11 percent on a year-on-year basis.

In the case of wage-related revenues, the impact of the crisis was somewhat delayed: In May, nominal personal tax income still minimally grew but it dropped by 7 percent in June. Firms initially tend to try to retain much of their workforce in crisis. On the other hand, the effect of the crisis on personal tax incomes is likely to be more protracted than the impact on consumption-related taxes. Revenues from social contributions by employees and employers dropped 8 percent in May-June. Revenues from taxes on economic units dropped at a similar rate in April-May.

By the end of May, the estimated revenue impact of the epidemic is about HUF 300-400 billion. Out of this sum, a few ten billion forints can be attributed to various stimulus measures (allowance on social security contributions, suspension of the obligation to pay the itemized tax on minor taxpayers).

The latest fiscal data corroborates our earlier expectations about the significant worsening of the fiscal outcome. Hence, **we predict the annual fiscal deficit to reach**



5.2 percent of GDP, as opposed to the 1 percent stipulated in the budget law. It should be noted that the risk connected to this forecast is outstanding not just in terms of magnitude but also in terms of complexity. Besides the risks related to the pace of recovery, there are risks related to the second wave of the epidemic and the fiscal performance of local governments, of which there is no interim data available.

Several factors contributed to the deterioration of fiscal balance, first of all the recession itself. The budget plan envisioned a GDP growth of 4 percent, while now the most likely outcome – according to our estimate – is a fall of 5 percent. This in itself worsens the deficit by 3.1 percentage points. Roughly half of this comes from the diminished revenues from income taxes and social security contributions, a result of the layoffs and deferred wage increases. Most of the rest comes from decreased revenues from taxes on corporations and on consumption.

The defense against the epidemic and stimulus measures to counter the economic crisis together generate additional expenditures to the magnitude of 2.3 percent of GDP. According to the information provided by the Ministry of Finance, the larger part of this sum is linked to healthcare investments, for example, equipment purchases. The actual fiscal stimulus amounts to 1.2 percent of GDP – this is the part of the newly decided expenditures whose source is not the reallocation of formerly existing funds. Within the stimulus spending the largest segment is the wage subsidy paid to employees put into the short-time working scheme, the one-off wage supplement paid to auxiliary health-care personnel, the wage subsidy scheme for job-creating enterprises and the lost revenue from the partial exemption from the payment of social security contributions. A number of other measures (temporary exemption from the payment of the itemized tax on minor taxpayers, the contribution of tourism development, and the tax on tourism), while helping certain economic sectors, have an only minimal fiscal effect. On the other hand, a countervailing fiscal effect – amounting to 0.2 percent of GDP – comes from the raise of retail and banking sector taxes.

Two other factors may ease the adverse effect of the abovementioned fiscal measures. First, to support the fight against the epidemic and the economic downturn, the EU provides financing that amounts to 0.8 percent of GDP. Second, the magnitude of reserves in the 2020 budget significantly exceeds the usual magnitude – out of this surplus, the part that can be spent discretionally – thus can be used to cushion the increase of deficit – amounts to 0.3 percent of GDP, according to our estimate.

State debt

The gross government debt stood at 66.6 percent of GDP at the end of the first quarter, including the debt of Eximbank (1.6 percent of GDP). Compared to the previous quarter, transactions reduced but revaluations raised the amount of debt. Net government debt amounted to 52.4 percent of GDP.

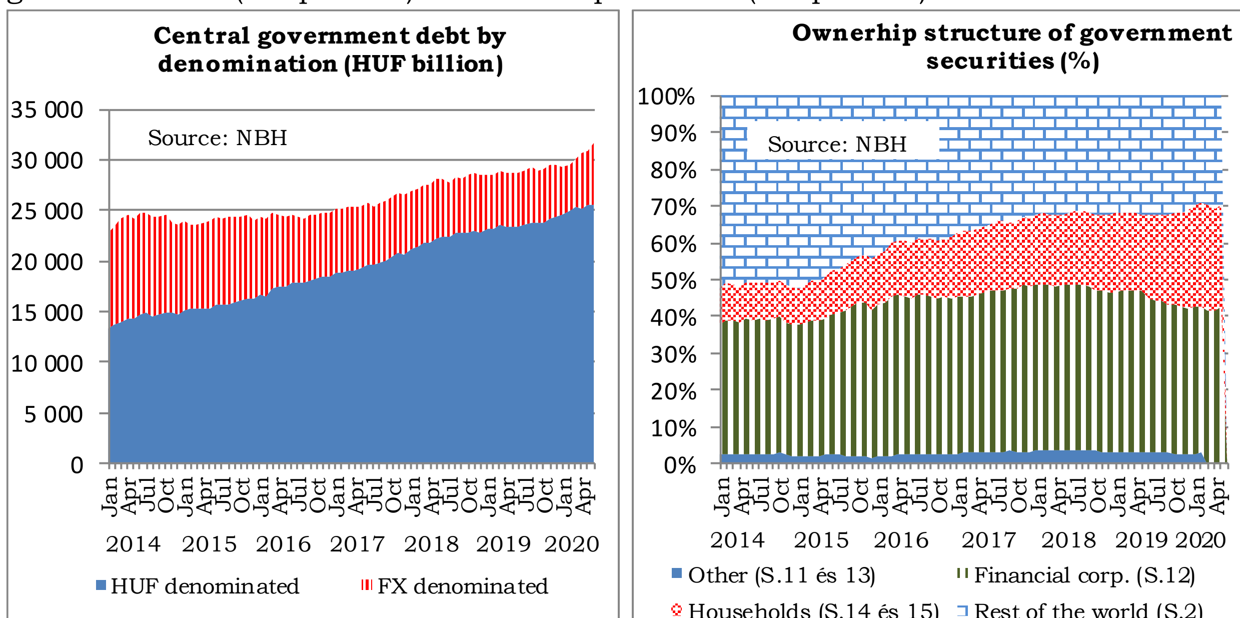
The rise in the share of households in the ownership of government securities has halted for now: after a peak of 28.2 percent in February, it dipped below 27 percent in April and May. At the same time, the share of financial enterprises rose somewhat – to 41.5 percent – while the share of foreign owners is relatively stable, below 30 percent. The decrease of households' share can be attributed to negative levels of net borrowing during March and April, but the balance of borrowing became positive again in June.

By the end of June, the share of FX debt within total debt rose to 19.1 percent (from the 15.4 percent in February), due to the issuance of FX-denominated government bonds in April and an epidemic-related weakening of the forint. Since the forint lost 5-6 percent of its pre-crisis value by the end of June, the weakening in itself raises the debt-to-GDP ratio by 0.6-0.7 percentage point. Due to the 5.2 percent deficit and 5 percent GDP fall expected for 2020, **the debt ratio is likely to rise to 74.6 percent by the end of this year, probably followed by a downward correction to 72.5 percent by the end of 2021**.

The 2021 budget

While the majority of the EU member states prepare their budgets in the fall, the Hungarian government, just as in the previous years, introduced its budget plan in May. Since at present even the short-term projections are marred with uncertainties, the introduction of the 2021 budget at such an early date is especially risky. The detailed assessment of the next year's budget is also hindered by the fact that the plan does not even provide a comprehensive picture of the government's expectations about *this* year. In the assessment given by the Fiscal Council, however, there are some figures presented about the expected revenue from some key taxes in 2020.

According to the budget bill, the government assumes that the fiscal deficit will amount to 2.9 percent of GDP in 2021. **The Kopint-Tárki expects a much higher deficit amounting to 3.8 percent.** Half of the difference comes from the fact that we expect a much higher deficit than the government for this year to begin with; the other part is due to the fact that the government expects a substantially higher rate of economic growth in 2021 (4.8 percent) than the Kopint-Tárki (3.5 percent).



Our forecast rests on the assumption that even if another wave of the epidemic reaches Hungary, its duration will be shorter and its economic effects less debilitating than what occurred in the spring, hence much of the one-off expenditures of this year will not happen again in 2021. If our assumptions turn out to be overly optimistic, the fiscal outcome will be worse. The downward risk is compounded by the reduction of the fiscal reserve from 1 percent of GDP in 2020 to 0.6 percent in the next year's budget.

There are relatively few novel measures in the 2021 budget, but they unanimously point toward fiscal easing. The first step of the reintroduction of the 13th-month pension – by the inclusion of an additional quarter of the monthly pension into the budget – will increase expenditures by HUF 78 billion, while the reduction of the rate of tax on small corporations by another percentage point (to 11 percent) will reduce revenues by HUF 5 billion. According to our calculation, total consolidated expenditures will decrease to 44.8 percent of GDP (from 48.8 percent in 2020) while total revenue decreases to 41.9 percent (from 43.3 percent in 2020).

As for compliance with the fiscal rules, the 2021 budget presents a mixed picture. The debt-to-GDP ratio is expected to decrease by more than 2 percentage points in 2021, which is in accordance with the Hungarian and EU-level fiscal rules. But the deficit will substantially surpass 1 percent – the medium-term target for the structural deficit, although the Hungarian set of rules approaches this rule with considerable flexibility, and there is no direct consequence of missing this target in the EU legislation. What can cause a problem, however, is the 3 percent deficit rule (the "Maastricht deficit rule") – it is no accident that the budget presents a deficit target just below this threshold. But we predict a higher deficit-to-GDP ratio for 2021. While the EU Commission and the council of economic and finance ministers agreed to waive the deficit rule for this year, there is no sign so far of doing the same for the next year. If that is the case, however, a deficit higher than 3 percent may have serious consequences – even a new Excessive Deficit Procedure may be launched against Hungary.

3.4.2. Inflation

In the first six months of 2020 consumer prices rose, according to the CSO data, by 3.4 percent. The monthly (year-on-year) indexes were on an almost monotone decreasing trend, from 4.7 percent in January to 2.2 percent in May and 2.9 percent in June. The overall decreasing trend was expected since the high inflation rates in the first quarter were a result of the statistical base effect. But the degree of the decrease – the 2.2 percent in May – was a surprise.

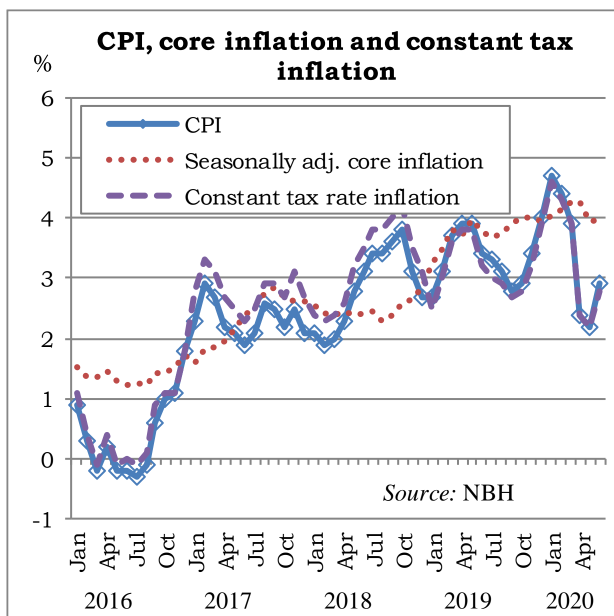
In May the monthly price index is usually quite high, primarily due to the high price of early-season vegetables. Fruit and vegetable prices did jump in this May – by 11.6 percent from the previous month and 39 percent compared to the same month of 2019. With meat and fish prices also climbing at a steep pace, overall food prices grew by more than 9 percent in May. This – and the 8.8 percent growth of food prices in January-May – actually exceeded our previous expectations, even if we predicted an above-average growth of food prices in our spring report.

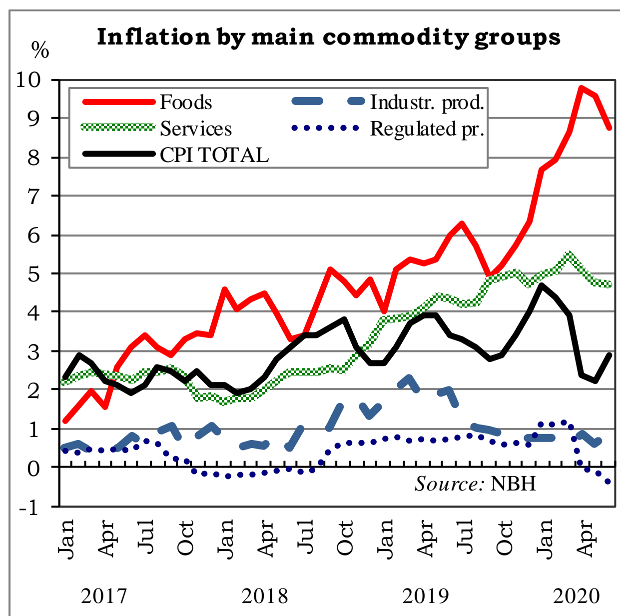
Yet, prices of other groups of products and services stalled this year, mostly because the epidemic hit consumer demand hard.

Due to the multiple and contradictory factors, it is still hard to give a forecast about this year's inflation. It is uncertain how the COVID-19 crisis will reshape demand and supply for the year as a whole.

1. We expect the fast growth of food prices to continue in the coming month. The fact that food products are the very product group where any drastic fall of demand is unlikely also corroborates this assumption.

2. On the other hand, international commodity prices – due to the high volatility – are typically on a downward trend. Since the low point at USD 10/barrel in April, oil prices rebounded to about USD 40 in June and USD 43 in July, due to some consolidation of oil demand and the agreement between oil producers. But oil price prospects are still highly uncertain. Beyond the direct effect on fuel and chemical





prices, the global oil price has an impact on a wide array of products, mostly through transport costs.

3. Third, domestic inflation is influenced by the decidedly disinflationary environment outside Hungary. The ECB predicts a 0.2-0.4 percent inflation rate in 2020 for the eurozone.

4. While gradually improving in the course of the year, domestic demand will show fast the jump in the number of jobless in the spring will be countered by rebounding employment during the second half of the year. There is also the question of whether households react to the elevated risk of unemployment by raising consumption or raising their savings. Past experience suggests that typically the cautionary motive gains the upper hand in similar situations.

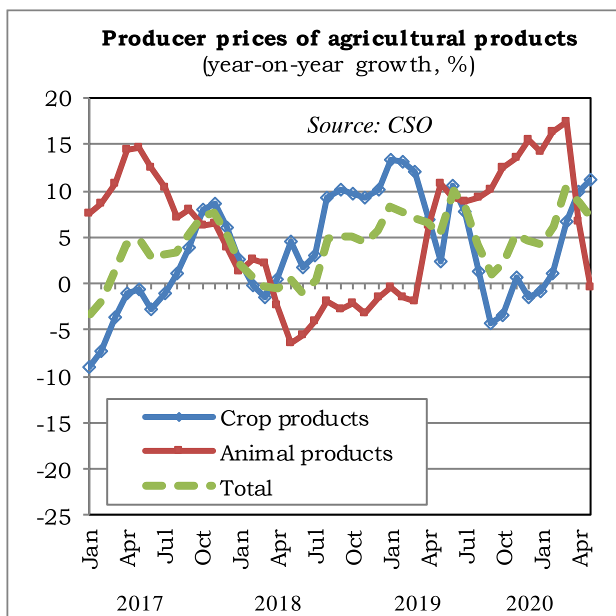
5. Uncertain exchange rate outlook: since the drastic weakening of April (above EUR/HUF 360) the forint has recovered to a degree: it stood near 345 at the end of July. But the future exchange rate movements are hard to predict, due to the volatile global financial market sentiment and because the NBH may cause further surprises during the rest of the year.

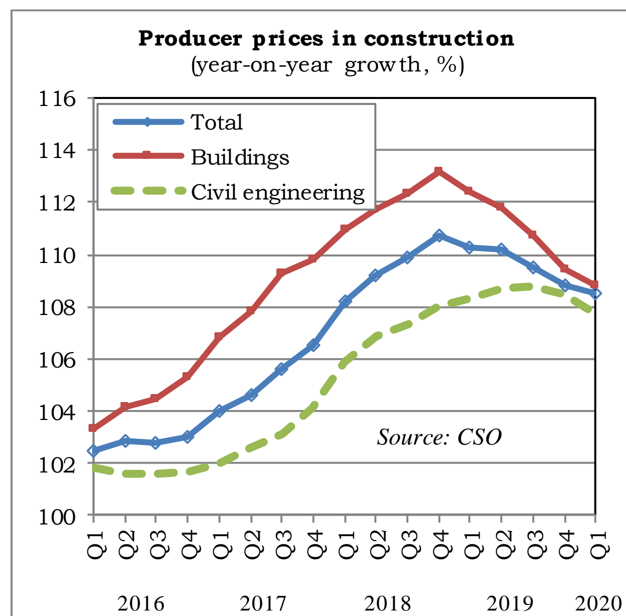
6. The seasonally adjusted core inflation rate steadily surpassed the headline rates, which suggests the presence of some upward inflationary pressure.

After taking into account every tendency and uncertainty, we surmise that the disinflationary factors will narrowly dominate the ones that point toward higher inflation. Hence, we revised our 2020 **forecast to 3.2** percent from the 3.4 percent in our previous report. Still, a higher annual inflation rate is still in the cards if, for example, the forint weakens again strongly or in case of a jump in oil prices.

The evolution of producer prices in construction contributes to the disinflationary trend since the construction price index has been on the decline since its peak in mid-2019. Agricultural prices on the whole point to the opposite direction, but this was already taken into account in our forecast.

.-.-.-.-.

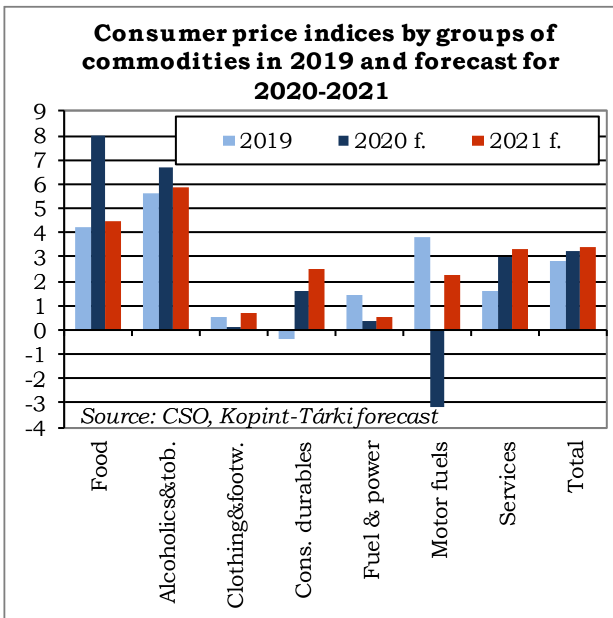


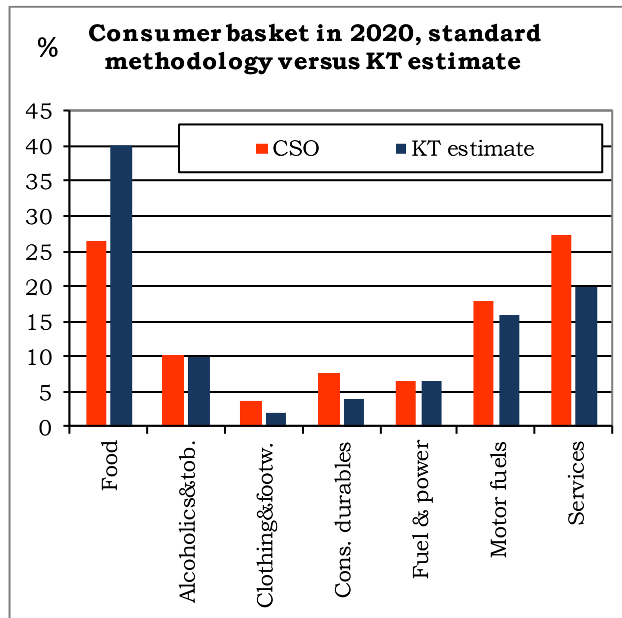


There is an important caveat, however. Our 3.2 percent prediction for 2020 is based on the internationally accepted methodology, that is, the calculation is based on the basket of goods in 2018. Usually, the use of the consumer basket of a year from the recent past does not cause any problems, because the change in the composition of the basket is usually slow.

This year, however, will see a sudden and drastic change in the composition of goods and services purchased by the population, due to decreasing households' income and also because the reduced mobility of the households and the movement restrictions caused a shift in the structure of everyday needs. We already highlighted this anomaly in our previous report. Due to decreasing real incomes, a bigger part of the income is spent on food, while many other categories of goods and services will lose prominence. Moreover, many types of services became temporarily unavailable for a period of time. (actually, a few limitations, for example regarding events that involve large-scale gatherings, are still in effect) which obviously reduces their weight in household consumption.

If we attempt to make an estimate for this sudden change in the composition of consumption (shown on the left-hand chart) the overall inflation rate may reach about 4-4.5 percent in 2020 (precisely 4.4 percent, if calculated with the weights used in the chart below). The higher inflation rate reflects the fact that food products – the price index of which will be very high in 2020 – will be unusually prominent in this year's private consumption. For 2021 predict an annual inflation rate of 3.4 percent.





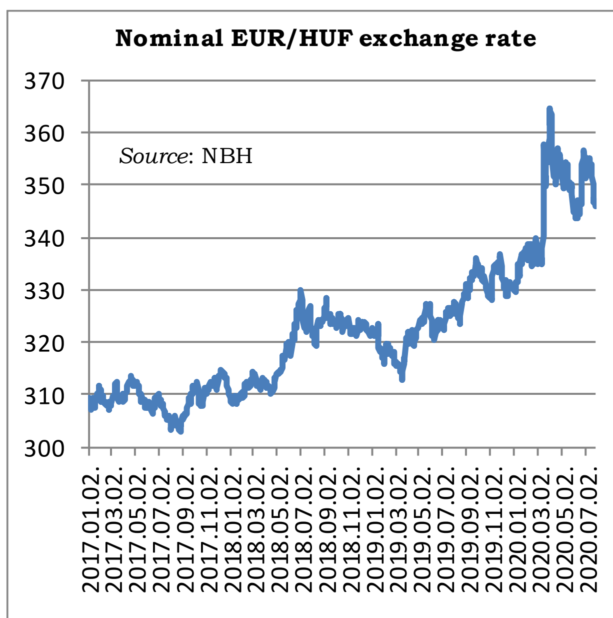
3.4.3. Financial and capital markets

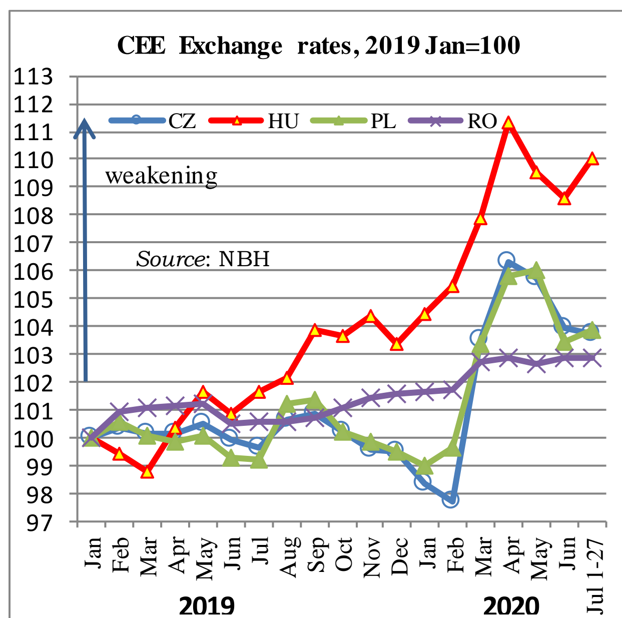
Exchange rate

The coronavirus outbreak brought about a sharp depreciation of the forint, and its exchange rate has remained extremely volatile since then. Before the crisis, expansive monetary policy and deteriorating external trade balance caused a weakening trend; the pandemic and the movement restrictions exerted further pressure on the Hungarian currency. As a result of the initial weakening spell, the EUR/HUF exchange rate skyrocketed from about 335 in early March to almost 365 in early April.

This elicited an important decision from the NBH. Although the Monetary Council kept the policy rate unchanged, it raised the rate of the O/N and the one-week collateralized credit instrument from 0.9 to 1.85 percent. Besides, while the one-week deposit rate remained, in principle, at 0.9 percent, the rate became variable within an interest rate corridor, and the momentary actual rate is set at the weekly tenders by the NBH. In addition to this *de facto* rate hike, the government decided to issue FX bonds to a total of EUR 2 billion. Partly due to these measures, the period of fast weakening ended, and the EUR/HUF exchange rate dipped below 345 by mid-June.

The next weakening phase was brought about by an unexpected rate cut in June and July, from 0.9 percent (stable for many years) to 0.6 percent in two steps. The new deputy governor emphasized that this is not the beginning of a new cycle of rate cuts. Partly due to the monetary easing, the forint weakened again – to 355 HUF/EUR by the end of June – but this was followed by another correction, to around 345 by the end of July.





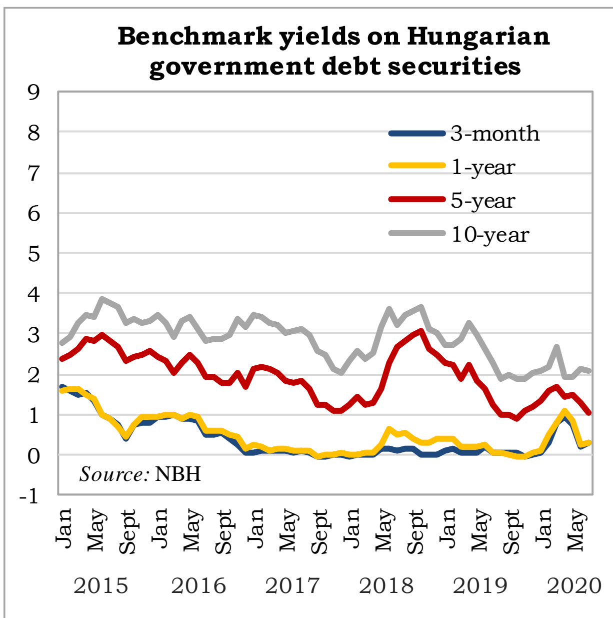
Government yields

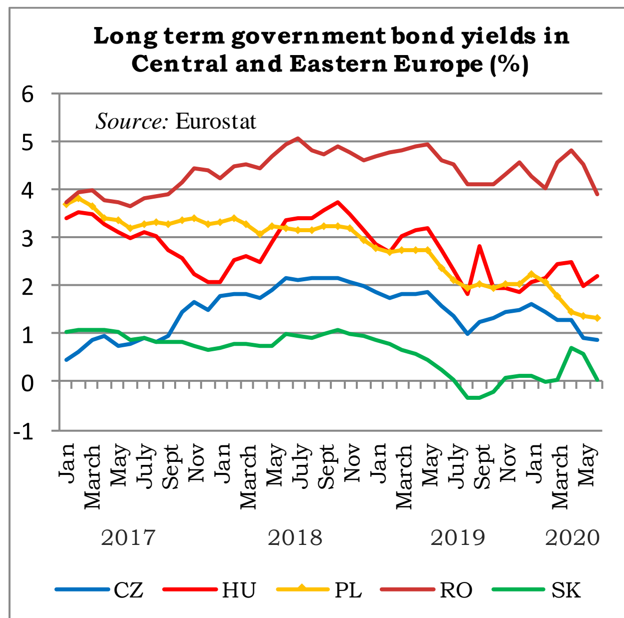
The epidemic brought about spectacular movements in government yields. 3-month and 1-year yields, after being stable around 0 percent for months, rose to 1 percent in April but then gradually returned to a level somewhat above 0 percent by the end of June. In the case of long yields, a rising trend began in late 2019 and – due to the

pandemic-related fears – surged in March. Since early April, however, a correction has taken place. By the end of July, the 5-year yield decreased to 1.25 percent (from 1.69 at the end of March) while 10-year yield quickly dipped below 2 percent by the end of April but hovering slightly 2 percent in June and July.

The April bounce of short yields was arguably a result of the de facto monetary tightening in early April, while short rates did not really budge in the wake of the two-step rate cut in June and July. The decision of the NBH to launch a government securities purchase program also helped stabilize the bond market. Regarding this program, the NBH says it will concentrate on forint denominated securities with maturity of at least 3 years. Also, the NBH will limit its purchases – in accordance with the ECB policy – to a maximum of 33 percent of the outstanding stock of the securities involved. In addition to the above, government financing was helped by the issue of euro-denominated government bonds with 6-year and 12-year maturity to a total of EUR 2 billion, and later – in June – the issue of green bonds, to a total of HUF 1.5 billion, with a 15-year maturity.

Outside Hungary, Romania and Slovakia were affected by rising long yields within the region, but that was followed by a correction in afterward. As for the respective levels of long yields, Romania has the highest yields for years now, around 4-5 percent. The Hungarian long yield is near 2 percent but the Polish yield, after a period of moving together with the Hungarian yield, in now approaching the 1 percent threshold. In Slovakia and – recently – Chechia, the long yield is below 1 percent.





3.4.4. Corporate and retail lending

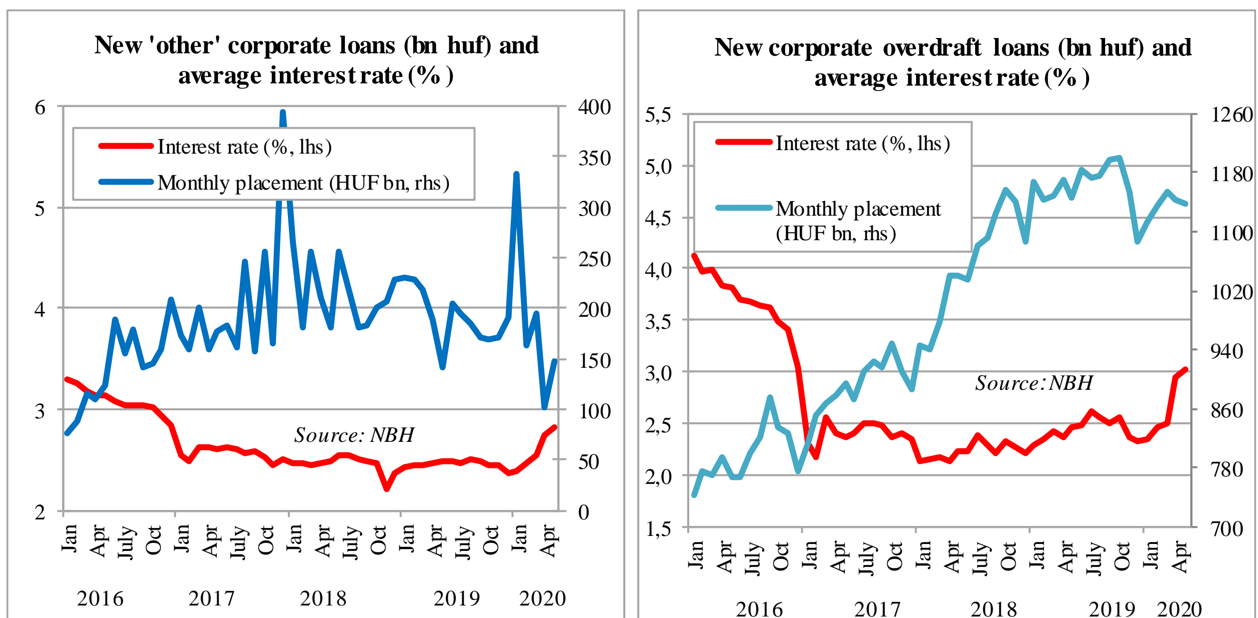
Corporate lending

Epidemic-related restrictions heavily affected lending trends. According to a survey, conducted by the NBH, some two-third of the originally planned corporate investments were in danger of being delayed or canceled. But various lending segments differed widely in terms of the impact of the epidemic. While overdraft lending largely remained stable during March-May, the monthly amount of other corporate loans fell sharply in April and May compared to February and March. According to the NBH data, loans over EUR 1 billion with floating rates were affected the most.

The interest rate of overdraft loans left the 2-2.5 percent band within which it was fluctuating during most of the past years and reached 3 percent in May, which is unprecedented since early 2017. The average interest rate of other loans has also risen above its former fluctuation band 2.8 percent, primarily due to the rise in the interest rate of short-term loans.

During recent months several measures aimed at stimulating the demand side of lending. One of these was the introduction of debt service moratorium (in effect until the end of the year) that specifies that the amount of monthly debt service cannot be raised even after the end of the moratorium. According to an NBH estimate, this policy measure may generate additional liquidity of HUF 2500-3000 for the firm sector.

In April 2020 the central bank launched the “Funding for Growth Go!” scheme that provides loans of HUF 20 billion or less, with a maximum maturity of 20 years, at a maximum interest rate of 2.5 percent for small and medium-sized enterprises, to a total of HUF 1500 billion. Until the end of July more than 2.2 thousand contracts were signed, to a total magnitude of HUF 123 billion. In addition to the above, the Hungarian Development Bank launched a lending, guarantee and capital program for firms of all sizes, to a total of HUF 1500.



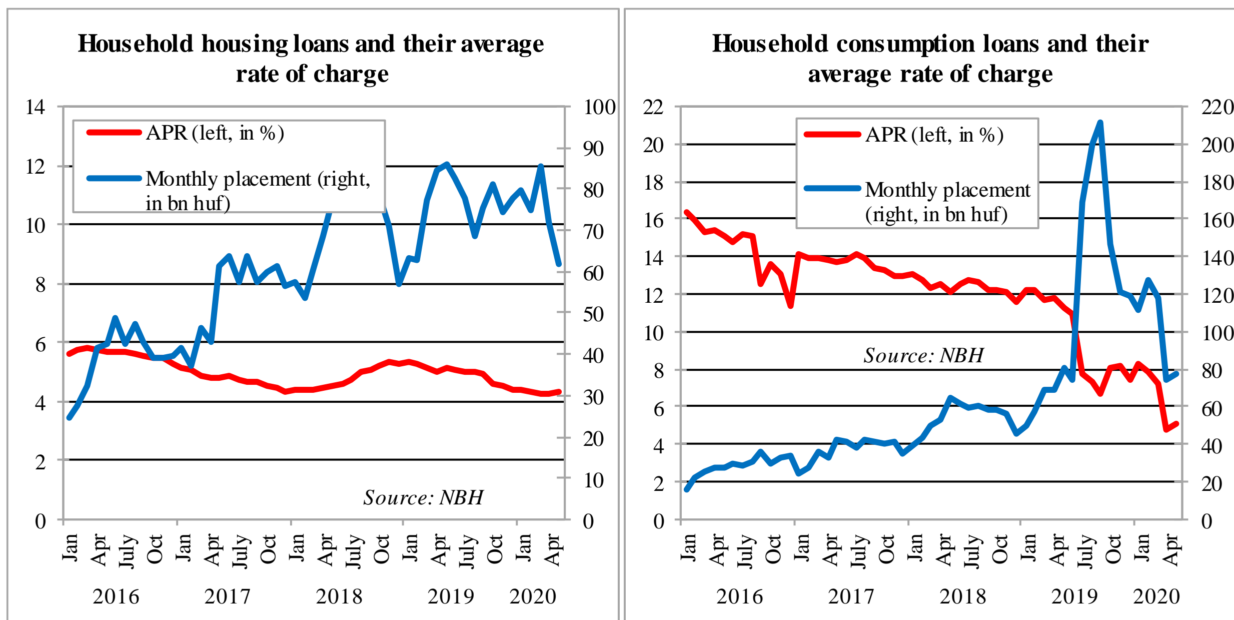
Retail lending

While in March the monthly amount of new forint denominated housing loans rose above HUF 85 billion, near the record level of the past decade, it dropped sharply afterward. In May, the amount was only HUF 62 billion. The fall was even more spectacular in the case of consumption loans, from HUF 119 billion in the first quarter it dropped to 76 billion in April-May.

The APR of housing loans remained mostly stable in April and May, but the APR of consumption loans plunged from an average of 7.8 percent in the first quarter to only 4.9 percent in April-May. (A previous fall of similar proportions happened after June 2019, due to the introduction of the so-called baby loan.)

In the case of consumption loans, a key factor behind the decreasing monthly payments and especially the drop of interest rates was the fact that in mid-March the government temporarily maximized the APR of consumption loans at 5 percentage points above the policy rate. This preferential APR does not apply to the whole duration of the loan, only until the end of this year. This implies that those who took a loan in the recent months may face a rate hike from January 2021.

As in the case of corporate loans, a repayment moratorium was introduced for retail loans as well, and – according to the NBH survey conducted in April – some 50-70 percent of debtor households were to make use of the moratorium. The MNB found that, in terms of the number of loan contracts, 33 percent of loans belonged to debtors who worked in economic areas heavily affected by the pandemic (for example, tourism).



Economic Indicators 2012-2019 Forecast 2020-2021 (percentage change)

	2012	2013	2014	2015	2016	2017	2018	2019	2020*	2021*
GDP AGGREGATES, ANNUAL REAL GROWTH										
GDP total	-1.5	2.0	4.2	3.8	2.2	4.3	5.1	4.9	-5.0	3.5
Domestic Demand	-3.0	2.0	5.3	2.4	1.7	5.2	7.3	5.6	-2.1	3.1
Private Consumption	-2.5	0.1	2.1	3.7	4.2	4.2	4.0	4.4	-2.1	3.0
Public Consumption	0.0	6.0	9.8	1.1	0.3	3.2	2.0	2.0	1.0	0.0
Gross Capital Formation	-6.0	6.1	12.8	-0.2	-4.1	9.0	18.3	9.5	-3.1	4.5
of which: Fixed Capital Formation	-3.0	9.8	12.3	4.8	-10.6	18.7	17.1	15.3	-5.6	4.5
Export	-1.7	4.1	9.2	7.4	3.8	6.9	4.3	6.0	-10.1	5.8
Import	-3.5	4.3	11.0	6.0	3.4	8.2	6.8	6.9	--6.8	5.1
PRODUCTION INDICES										
Agricultural Production (gross)	-10.0	12.5	11.4	-2.4	9.3	-4.1	2.7	-0.3	-0.5	0.0
Industrial Production	-1.1	1.0	7.9	7.8	1.3	4.4	3.4	5.3	-10.0	5.0
Retail Trade Volume	-2.2	1.8	5.2	5.8	4.8	5.6	6.7	6.1	0.0	3.0
EMPLOYMENT, EARNINGS										
Number of Employed	1.8	1.7	5.3	2.7	3.4	1.6	1.1	1.0	-2.3	1.8
Unemployment Rate	11.0	10.2	7.7	6.8	5.1	4.2	3.7	3.4	5.0	4.3
Gross Nominal Wages	4.6	3.4	3.0	4.3	6.1	12.8	11.3	11.4	7.0	7.0
Net Real Wages[a]	-3.4	3.1	3.2	4.4	7.4	10.3	8.3	7.7	3.7	3.5
PRICES, EXCHANGE RATES										
Consumer Price Index	5.7	1.7	-0.2	-0.1	0.4	2.4	2.8	3.4	3.2	3.4
EUR/HUF Exchange Rate (annual average)	289	297	309	310	311	309	319	325	347	350
EUR/ USD Exchange Rate (annual average)	1.28	1.33	1.33	1.11	1.11	1.13	1.18	1.12	1.10	1.11
Short-term Interest Rates (3M), eop	5.33	2.86	1.43	0.80	0.06	-0.01	0.00	-0.01	0.8	1.0
Long-term Interest Rates (10Y), eop	6.11	5.61	3.60	3.33	3.16	2.02	3.01	2.01	3.0	3.0
BALANCE OF PAYMENTS										
Current and Capital Accounts, % of GDP	4.1	7.3	4.9	7.0	4.5	3.2	2.2	1.0	0.4	1.0
GOVERNMENT BUDGET										
General Government Balance, ESA-95, % of GDP	-2.3	-2.6	-2.7	-2.0	-1.8	-2.5	-2.1	-2.0	-5.2	-3.8
Gross Government Debt, % of GDP [b]	78.6	77.4	76.8	76.2	75.5	72.9	70.2	66.3	74.6	72.5

a A GDP-statisztika szerinti áru- és szolgáltatásexport és -import
b Nem veszi számításba a gyermekek utáni adókedvezmény hatását.
c Az államháztartás az Eximbankkal együtt
* A Kopint-Tárki előrejelzése
Forrás: KSH, MNB

CONTENTS

1. The global economy 1
2. New EU member states 5
3. Hungarian Economy 11
Introduction 11
GDP and its components 12
3.1. The production of GDP 15
3.2. The final use of GDP 19
3.3. Employment, unemployment 24
3.4. Fiscal, monetary and financial developments 25
3.4.1. Fiscal trends and outlook 25
3.4.2. Inflation 29
3.4.3. Financial and capital markets 32
3.4.4. Corporate and retail lending 34