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I. The World Economy

The **global growth** rate reached 3.1% in 2023 and might be slightly lower in the coming two years. Global growth will be hampered mainly by a slowdown in China but some deceleration will occur in the US as well, although the American economy proved to be more resilient than expected before. At the same time, the economic performance in the euro area will remain sluggish in 2023, following last year's decline, mainly due to the weakness of the German economy. Various regional conflicts cause downward risks as the outcome of both the events in the Gaza Strip and the Russia-Ukraine conflict is unclear – one can only assume that they remain easily escalating crisis hotspots for a considerable time. Partly due to regional conflicts, transport costs have started to rise sharply, particularly for maritime transport, which is holding back the expansion of world trade. Inflation is moderating worldwide, but commodity markets remain unsettled and further price increases cannot be ruled out. Monetary policy easing can be expected this year, but the uncertainties concerning the pace of disinflation make it uncertain how quickly monetary adjustments will take place. Fiscal policy is unlikely to provide growth stimulus this year: most countries have accumulated debts during the pandemic that will need to be addressed: tax adjustments and expenditure cuts will be attempted, which will tend to hamper growth.

The IMF has revised downwards its **world trade** forecast for this year, as well as for 2025. The slowdown in economic growth, particularly in China, is responsible for this downward adjustment. The world economy has not yet returned to a stable growth trajectory – it suffers from overproduction of some products and shortages in others. China is trying to get rid of its stocks at depressed prices, which causes disruption in the developed economies. The situation has also been made worse by events in the Gulf of Aden: container ships bypass the African continent around the Cape of Good Hope in South Africa, which means at least two weeks of additional transport time, extra costs and — last but not least — air pollution for European shipping companies. So, after an expansion rate of 0.3 to 0.4% last year, world trade is expected to grow by about 3.0% this year and will accelerate only modestly (to 3.3%) next year.

According to the World Bank, the **energy commodity index** rose in March to 104.3 from 102.2 in February. The non-energy commodity index rose from 106.8 to 109.2 (2010=100), while the global commodity index climbed from 103.7 to 105.9. A clear upward trend has thus emerged over the past month.

The **price of Brent crude oil** was around $85 per barrel in mid-March, and by the beginning of April, it had jumped to over $90, well above last year's annual average level of $82. Since mid-February, the oil price has been on a slightly upward trend and futures prices have also crept higher. There have been large swings in the market, reflecting the growing uncertainty. Various geopolitical tensions, Ukrainian attacks on Russian energy facilities, and increasing risks to maritime deliveries have heightened fears surrounding supply uncertainties. Global oil demand is expected to expand at a slower pace this year than last year, driven by cyclical trends as well as the push for various energy efficiency measures. Chinese demand will continue to take up the bulk of the increase, but the

slowdown in Chinese growth will lead to a more moderate pace of demand expansion. The global crude oil supply may expand by as much as 1.5 million barrels per day, despite the latest decision to keep the OPEC+ production curbs in place until the end of June 2024. Russia announced last month that it would cut oil production by a further 471,000 barrels in the second half of the year. Even if it would be logical, based on economic trends, to expect oil prices to fall, the various supply and delivery uncertainties are increasing the volatility in the market, which is reflected in a temporary rise in prices. It is also not known whether or not the OPEC+ will decide to maintain the production curbs longer than originally planned. Thus, we expect extreme price volatility, and our forecast moves between $83 to 88 dollar per barrel this year with downside and upside risks simultaneously.

There is also a lot of uncertainty in the European **gas market**. Despite full gas storages and the mildest winter in decades, fears of supply uncertainties pushed gas prices up, too, in the first half of March. Later in March, gas prices moderated somewhat, due to the abundant European reserves, together with a favorable supply outlook and continued favourable weather forecasts. But overall, there was a clear upward trend in March.

As to **non-energy commodity prices**, the price indices appear stable, but some products are becoming almost inexplicably more expensive. The price of gold is breaking historic records as investors turn to precious metals for protection from global uncertainty. The growing protectionist fears are not entirely unfounded, which is affecting investment and consumption plans and, indirectly, the prices of raw materials as well.

The latest **inflation data** point to a further moderation in the pace of price increases. At the same time, inflation is still above the central bank's targets, and several factors could add to inflationary pressures, including the impact of geopolitical conflicts on energy prices, risks from extreme weather, significant wage pressures in many sectors and countries and the consequences of unexpected events due to general political uncertainty. As a result, it is not yet clear to what extent the disinflationary trends will be sustained, which in turn will continue to force central banks to remain cautious. The Fed will begin a period of interest rate cuts later this year, but given the robust US economy, it is unlikely that a rapid pace of rate cuts will occur. The ECB is expected to adjust interest rates for the first time in June, but here too there is talk of cautious moves, despite the weak economic outlook in Europe and inflation already hovering around the central bank's target.

The economic trends **outside the European Union** show a mixed picture. In the **US**, economic growth last year was more robust than expected, with GDP growing by 2.5% in 2023. This year's data suggest a slowdown in growth for the time being. Private consumption expanded only moderately in the first months of the year, retail sales fell sharply in January, and industrial production also showed a slowing trend. While residential construction continues to expand, business investment in construction appears to be slowing, reflecting the phasing out of government support programs that

were still in place last year. However, overall construction investment will continue to support growth this year, as major public investments started in recent years are still ongoing. As for machinery and equipment investment outlays by companies, On the other hand, the impact of restrictive monetary policy already weighed down heavily on machinery and equipment investment outlays in 2023 and will continue to do so this year.

Japan's economic output fell in the second half of 2023, but due to the strong growth rates in the first half of the year, GDP grew by 1.9-2% annually last year. Overall, growth is expected to be around 1% this year, with only a modest acceleration next year. The slowdown is mainly due to a moderation in investment, but private consumption is also expanding at a slower pace than in 2023. Net exports will support growth this year, mainly because sluggish domestic demand weighs on imports growth. Business investment is stagnating this year and residential construction is falling; only public investment will increase. Next year, business investment will pick up somewhat, but residential construction will continue to fall.

In the **United Kingdom**, growth is expected to remain sluggish over the coming two years. According to the data currently available, the UK economy was in recession in the second half of the last year and GDP growth reached only 0.3% in 2023. For this year, too, only a modest acceleration is expected, with UK GDP estimated to expand by 0.9%, and by around 1% next year, even if the data at the beginning of the year were better than expected. Private households' disposable incomes are rising but are still below pre-pandemic levels. Consumer confidence indices tend to point downwards, and even this low growth forecast comes with several downside risks.

Both domestic official sources and experts from international organisations are forecasting a slight slowdown in **China**'s GDP growth from 5.2% last year to about 4.7% in 2024. Nevertheless, China will remain one of the countries in the world economy with the fastest growth rates. However, an increasingly large government stimulus is needed to achieve the official growth target. Efforts to restore confidence in the real estate sector are the most important, but there is also a strong need to shore up confidence among foreign investors as well. In international fora, the Chinese leadership is encouraging foreign companies to relocate some of their R&D centers to China, to conduct joint research with Chinese experts. This is a sign that, as in the earlier stages of the country's industrialization, the Chinese leadership still deems it important to attract FDI.

Despite the apparent slowdown of Chinese economic growth, **Asia** has retained its role as the engine of the world economy. It is expected to account for 60 percent of world GDP growth in 2024, the same as last year and a much larger share than before the pandemic. The biggest credit for this goes to **India**, which has been the fastest-growing country with significant economic potential for years, with GDP growth of 6.7% last year and 6.5% this year and next. Benefiting from US and European protectionist measures against China, Southeast Asian countries have gained strong positions in many areas amid efforts to diversify value chains, particularly in the so-called green technologies. The reshaping of value chains, the so-called nearshoring, is also having an impact in Latin America. In particular, Mexico, Panama and Costa Rica can benefit from the development of supplier relationships due to their proximity to the US market. According

to several forecasts, Africa will be the second fastest-growing region in the world in 2024, with an average GDP growth of 3.2%.

In the second half of last year, the **GDP of the euro area** stagnated, with a fall of 0.2% in the third quarter and zero growth in the fourth. Both private consumption and investment activity performed weakly, and net exports provided only marginal support to growth, as exports slowed less than imports. After last year's moderate GDP expansion of 0.4%, we expect only a marginally faster growth rate of 0.7% this year, and the pace of growth is expected to remain below 2% in 2025 as well, despite the expected moderate upturn. This is mainly due to the continued weak investment performance and uncertainties about export developments. Private consumption is expected to expand by around 1% this year, with investment stagnating at best and public consumption posting a growth of about 0.9%. Exports will expand minimally, while net exports will tend to pull back growth this year as imports expand at a rate above 1%. Private consumption will pick up over the forecast period as inflation falls and real wages rise. The various economic indicators point to a slight recovery but do not indicate an excessive recovery. The latest data on manufacturing production also point downwards. There are significant differences in growth rates between countries. The main drag on Euro Area growth is the weakness of the **German economy**. Europe's largest economy has stagnated since mid-2022. Industry is the weakest link, but private consumption remains sluggish as well and uncertainty is keeping savings high. Last year, the German GDP contracted by 0.3%, but the outlook for this year is not rosy either: the economy will remain virtually stagnant, with an expected growth rate of 0.1%, accelerating to 1.2% next year. The IFO business barometer, which had been trending downwards since November last year, showed some improvement in February-March, mainly driven by the services sector, as manufacturing companies are still rather pessimistic and the German manufacturing output in March continued to decline year-on-year, while on a month-on-month basis, it already showed some growth.

Inflation has started to slow in all eurozone countries, from 8.4% in 2022 to 5.4% in 2023 for the euro area as a whole, and all but Slovakia have seen single-digit inflation rates. Inflation is expected to be around 2% this year, and the indices of 2.6% in February and 2.4% in March (year/year) are already encouraging. Core inflation has also started to fall. However, there are large differences between the different Euro Area countries, and some experienced some reacceleration of inflation in recent months. As indicated earlier, the ECB's main concern is wage inflation, as tight labor markets have led to rising wage claims in most sectors and countries. Increased wage pressures could slow the pace of inflation moderation.

The *trends* are similar in the **EU-27**: last year's GDP growth of 0.4% could accelerate to 0.9% this year at most, in line with the more dynamic growth of 2.7% in the EU13. *the* moderate GDP growth rate of 1.7% expected for 2025 also indicates that the problems are not well addressed, and the downside risks are high.

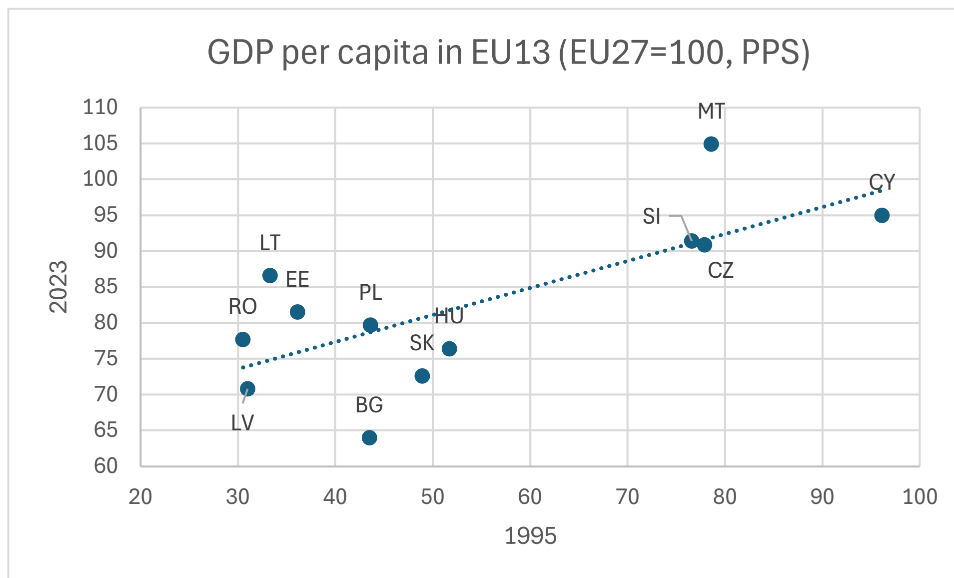
II. The EU13 Countries

In the fourth quarter of 2023, growth in the EU13 Member States was only 1.2% year-on-year. The annual expansion rate was as low as 0.5% in 2023, which is just 0.1 percentage points "swifter" than the EU15 average. Only two new member states were in recession in the last quarter, Estonia (-2.5%) and Latvia (-0.2%). Estonia has been in an economic downturn for two years and is expected to turn into growth this year. The Baltic state was able to recover quickly from the pandemic, but the Russian-Ukrainian war caused significant damage. Estonia was one of the most exposed EU member states to Russian energy, so the dramatic increase in gas prices hit households hard. The government has cut off energy ties with Russia firmly, in one stroke. At the same time, compared to the majority of the member states, Estonia was less reticent to allow household energy prices to be affected by the energy price hike and the additional cost of alternatives, typically Scandinavian energy. The rational adaptation of the population was to reduce private consumption, as well as increase savings. The consequences of the war for Estonian companies were not only higher energy prices but also the almost complete collapse of value chains. The Russian export market has contracted significantly, while demand from the Nordic countries has also become subdued. Both government and companies sought to retain their workforce to avoid a wave of emigration like Latvia's during the 2008 global economic crisis. As a result of the jobs preserved with heavy state subsidies, productivity began to decline, the country's competitiveness also began to erode, while unemployment barely worsened. The Estonian central bank is optimistic that the economy will grow as early as this year, but for this to be more than just the result of base effects, household confidence needs to rebound, a necessary condition for the revival of private consumption. Also, companies need to restructure their value chains and export markets. Unfortunately, the global economic conditions are not favorable at the moment, but the fall in energy prices could help a lot this year.

Growth in the CEE region continued to be led by Poland (1.7%) and Romania (1.1%) in the fourth quarter. Croatia, despite its small economy, made the third largest contribution to growth, with an expansion of 4.3% (it was 6.3% in 2022!), making it the largest GDP growth together with Malta. Croatia stands out by far not only from the EU13 but also from the old Member States. In the last quarter, private consumption boosted the economy, partly because households were making up for previously postponed consumption; on the other hand, the summer tourist season also brought significant income to the country. EU funds also support growth, but it should not be forgotten that the country will hold parliamentary elections in the summer of 2024, so the government has also pursued a looser fiscal policy. Croatia is also becoming increasingly popular among investors by adopting the euro and joining the Schengen area. In the first three quarters of 2023, around €600 million of FDI arrived in the country, far more than the total since 2016. Growth is robust, but its sustainability is questionable as it is in great part due to one-off factors. According to the European Commission's calculations, the gap of potential output was around 2 percentage points in 2023, meaning that Croatia is expected to show a decelerating trend until 2025.

There have been significant changes in Member States' GDP per capita figures. Romania overtook Hungary in terms of GDP per capita (in PPS terms), while Poland moved further ahead of Hungary. However, the big question remains how much progress Croatia has

made (data for Croatia is not yet available at the time of writing). In 2022, Croatian GDP per capita was 72.8% of the EU average, while in 2023 the Hungarian figure was 76.4%. As mentioned above, Croatia achieved the fastest growth last year, while Hungary was in recession, and record-level inflation dampened the domestic purchasing power, while inflation in Croatia hit a relatively more moderate level of 8.4% (compared to 17% in Hungary). Although it is unlikely that Croatia overtook Hungary, there is a good chance that it has caught up with it to a large extent, and will probably overtake Hungary next year. If so, Hungary will become the 10th most developed country in the EU13 and the 25th most developed in the EU27 in 2024. If we compare the performance of the new Member States to 1995, it is starting to break away from the regional trend, and there are only three Member States together with Hungary that are steadily lagging behind: Bulgaria and Slovakia. All this does not mean a stalling of convergence processes, but only a slowdown in the speed of convergence, which leads to the widening of the gap among the more developed Eastern European countries.



Last year, high inflation was the biggest problem in the region. The inflation rate averaged 10.7%, although an outlier, the 17% rate in Hungary, played some role in this. However, even without Hungary, the region's inflation rate was still around 10%. In the first three months of the year, the regional inflation rate moderated to 4.1%, a significant slowdown, but still at least 1-1.5 percentage points higher than in the previous years. It should be noted, however, that the deceleration is more due to a decline in energy prices, with core inflation standing at 5.9%, suggesting that the inflationary pressure remains significant across the new member states. In Romania, for example, core inflation stood at 10.1% in March, the highest figure among the EU13 countries. Although an energy price shock is not expected in the short term, wage settlements are now starting in Member States based on last year. Also, most annual household utility contracts will be repriced at the beginning of the year, which will have a negative impact on the price index. Wage negotiations typically end with real wage increases, putting additional pressure on monetary policy. In the absence of a negative turnaround, we expect disinflationary developments to continue; the regional price index is expected to hit 4% this year and 3.5% next year in the new member states.

As for GDP growth, we expect the regional-level growth rate to accelerate to 2.7% this year, with a further increase to just over 3% next year. The risks are tilted to the downside, partly due to the unpredictability of Russian aggression and partly depending on the outcome of the US presidential election. Therefore, external conditions are far from ideal, but the resumption of economic activity and a revival in consumption can give a recovery impulse to the region.

Table 2/1.

Economic Growth in the EU Member States

(Percentage change of real GDP over the previous year)

	Weights	2018	2019	2020	2021	2022	2023	2024*	2025*
Germany	24.3	1.0	1.1	-3.8	3.2	1.8	-0.3	0.1	1.2
France	16.5	1.9	1.8	-7.5	6.4	2.5	0.7	0.6	1.1
Italy	12.3	0.9	0.5	-9.0	8.3	4.0	0.9	0.5	1.1
Netherlands	6.1	2.4	2.0	-3.9	6.2	4.3	0.1	0.7	1.5
Belgium	3.4	1.8	2.2	-5.3	6.9	3.0	1.3	1.3	1.2
Luxembourg	0.5	1.2	2.9	-0.9	7.2	1.4	-1.1	1.0	2.8
Ireland	3.0	8.5	5.3	6.6	15.1	9.4	-3.2	1.9	4.5
Greece	1.3	1.7	1.9	-9.3	8.4	5.6	2.0	2.0	2.0
Spain	8.6	2.3	2.0	-11.2	6.4	5.8	2.5	1.7	1.8
Portugal	1.6	2.8	2.7	-8.3	5.7	6.8	2.3	1.4	1.7
Austria	2.8	2.4	1.5	-6.6	4.2	4.8	-0.8	0.2	1.8
Finland	1.6	1.1	1.2	-2.4	2.8	1.3	-1.0	0.1	1.9
Estonia	0.2	3.8	4.0	-1.0	7.2	-0.5	-3.0	1.2	3.1
Slovakia	0.7	4.0	2.5	-3.3	4.8	1.8	1.1	2.2	2.4
Slovenia	0.4	4.5	3.5	-4.2	8.2	2.5	1.6	2.4	2.5
Cyprus	0.2	5.6	5.5	-3.4	9.9	5.1	2.5	2.5	2.4
Malta	0.1	7.4	7.1	-8.2	12.5	8.1	5.6	4.0	4.5
Latvia	0.2	4.0	0.6	-3.5	6.7	3.0	-0.3	2.0	3.0
Lithuania	0.4	4.0	4.7	0.0	6.3	2.4	-0.3	2.3	3.3
Croatia	0.4	2.8	3.4	-8.6	13.8	6.3	2.8	2.8	3.0
Euro Area	**84.7**	**1.8**	**1.6**	**-6.1**	**5.9**	**3.4**	**0.4**	**0.7**	**1.5**
Denmark	2.2	2.0	1.5	-2.4	6.8	2.7	1.8	0.4	1.6
Sweden	3.2	2.0	2.0	-2.2	6.1	2.7	-0.2	0.1	1.8
Hungary	1.2	**5.4**	**4.9**	**-4.5**	**7.1**	**4.6**	**-0.9**	**2.5**	**3.2**
Czech Republic	1.8	3.2	3.0	-5.5	3.6	2.4	-0.5	1.3	2.5
Poland	4.4	5.9	4.4	-2.0	6.9	5.3	0.2	3.3	3.5
Romania	1.9	6.0	3.9	-3.7	5.7	4.1	2.1	3.0	3.5
Bulgaria	0.6	2.7	4.0	-4.0	7.7	3.9	1.8	2.1	3.0
EU14	**87.5**	**1.6**	**-5.8**	**5.3**	**3.5**	**1.8**	**0.4**	**0.6**	**1.5**
New EU13	**12.5**	**4.9**	**4.0**	**-3.5**	**6.3**	**4.1**	**0.5**	**2.7**	**3.2**
EU27	**100**	**2.1**	**1.8**	**-5.6**	**6.0**	**3.4**	**0.4**	**0.9**	**1.7**
Memorandum items									
USA		2.9	2.3	-2.2	5.8	1.9	2.5	2.1	1.7
Japan		0.6	-0.4	-4.3	2.1	0.9	2.0	0.7	1.2
United Kingdom		1.3	1.6	-11.0	8.7	4.3	0.3	0.9	1.2
China		6.8	6.0	2.2	8.1	3.0	5.2	4.7	4.2
Russia		2.8	2.0	-3.0	5.6	-1.2	3.6	2.2	0.8
South-Eastern Europe									
Serbia		4.5	4.3	-0.9	7.7	2.5	2.5	3.1	3.7
Turkey		3.0	0.8	1.9	11.4	5.5	3.5	3.8	4.0

* Kopint-Tárki forecast
EU-14 = Countries that joined the European Union before 2004
Új EU-13 = Countries that joined the European Union in 2004, 2007 and 2013
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)

	Weights	2018	2019	2020	2021	2022	2023	2024*	2025*
Germany	23.5	1.9	1.4	0.4	3.2	8.7	6.0	2.1	1.5
France	16.7	2.1	1.3	0.5	2.1	5.9	5.7	2.7	2.0
Italy	14.2	1.2	0.6	-0.1	1.9	8.7	5.9	1.9	2.1
Netherlands	5.1	1.6	2.7	1.1	2.8	11.6	4.1	1.2	1.8
Belgium	3.4	2.3	1.2	0.4	3.2	10.3	2.3	1.3	1.9
Luxembourg	0.3	2.0	1.6	0.0	3.5	8.2	2.9	2.5	2.2
Ireland	1.6	0.7	0.9	-0.5	2.4	8.1	5.2	2.4	1.8
Greece	1.7	0.8	0.5	-1.3	0.6	9.3	4.2	2.3	1.8
Spain	9.2	1.7	0.8	-0.3	3.0	8.3	3.4	2.1	1.9
Portugal	1.9	1.2	0.3	-0.1	0.9	8.1	5.3	1.9	1.9
Austria	2.7	2.1	1.5	1.4	2.8	8.6	7.7	3.8	2.7
Finland	1.6	1.2	1.1	0.4	2.1	7.2	4.3	1.3	1.9
Estonia	0.2	3.4	2.3	-0.6	4.5	19.4	9.1	3.5	3.0
Slovakia	0.8	2.5	2.8	2.0	2.8	12.1	11.0	3.5	3.3
Slovenia	0.4	1.9	1.7	-0.3	2.0	9.3	7.2	2.6	2.6
Cyprus	0.2	0.8	0.5	-1.1	2.3	8.1	3.9	2.1	1.9
Malta	0.1	1.7	1.5	0.8	0.7	6.1	5.6	3.3	3.0
Latvia	0.3	2.6	2.7	0.1	3.2	17.2	9.1	2.0	2.5
Lithuania	0.5	2.5	2.2	1.1	4.6	18.9	8.7	2.0	2.5
Croatia	0.5	1.6	0.8	0.0	2.7	10.7	8.4	3.3	3.0
Euro Area	**84.4**	**1.8**	**1.2**	**0.3**	**2.6**	**8.4**	**5.4**	**2.2**	**1.9**
Denmark	1.9	0.7	0.7	0.3	1.9	8.5	3.4	0.9	1.5
Sweden	2.7	2.0	1.7	0.7	2.7	8.1	5.9	2.5	2.2
Hungary	**1.1**	**2.9**	**3.4**	**3.4**	**5.2**	**15.3**	**17.6**	**4.3**	**3.5**
Czech Republic	1.6	2.0	2.6	3.3	3.3	14.8	12.0	2.2	2.2
Poland	4.9	1.2	2.1	3.7	5.2	13.2	10.9	4.8	3.7
Romania	2.3	4.1	3.9	2.3	4.1	12.0	9.7	5.7	4.0
Bulgaria	0.6	2.6	2.5	1.2	2.8	13.0	8.6	3.3	2.9
EU14	**86.5**	**1.9**	**1.3**	**0.4**	**2.6**	**7.8**	**5.3**	**2.1**	**1.9**
New EU13	**13.5**	**2.3**	**2.7**	**2.7**	**4.4**	**13.9**	**11.4**	**4.1**	**3.3**
EU27	**100.0**	**1.8**	**1.4**	**0.7**	**2.9**	**9.2**	**6.4**	**2.4**	**2.1**
Memorandum items[a]									
USA		2.4	1.8	1.4	4.7	8.0	4.1	2.7	1.9
Japan		0.5	0.5	0.0	-0.2	2.5	3.2	2.1	1.8
United Kingdom		2.5	1.8	0.8	2.6	9.1	7.2	3.6	2.9
China		2.0	2.9	2.5	0.8	1.9	0.4	1.0	1.5
Russia [b]		2.9	4.5	2.6	5.9	13.8	5.9	7.2	6.0
South-Eastern Europe									
Serbia		2.0	1.9	1.8	4.0	11.7	12.1	5.6	3.7
Turkey		16.3	15.2	12.3	19.6	72.3	54.0	53.6	22.9

a Non-harmonized price indexes
b December/December
* Kopint-Tárki forecast
EU-14 = Countries that joined the European Union before 2004
EU-13 = Countries that joined the European Union in 2004, 2007 and 2013
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)

	Weights	2018	2019	2020	2021	2022	2023	2024*	2025*
Germany	20.1	3.4	3.1	3.6	3.6	2.7	2.9	3.0	2.9
France	14.2	9.0	8.4	8.0	7.9	7.3	7.3	7.2	7.1
Italy	11.7	10.6	10.0	9.6	9.6	8.2	7.7	7.4	7.0
Netherlands	4.5	3.8	3.4	3.3	4.2	3.4	3.5	3.3	3.2
Belgium	2.4	6.0	5.4	6.4	6.3	5.6	5.6	5.5	5.3
Luxembourg	0.2	5.6	5.6	5.8	5.5	4.7	5.0	5.2	5.0
Ireland	1.1	5.8	5.0	6.7	6.3	4.8	4.1	4.3	4.1
Greece	2.1	19.3	17.3	15.3	14.8	12.5	11.0	10.0	9.8
Spain	11.0	15.3	14.1	15.2	14.8	13.1	12.0	11.6	10.5
Portugal	2.4	7.1	6.5	6.7	6.6	5.9	6.5	6.3	6.1
Austria	2.2	4.9	4.5	6.4	6.2	4.6	6.4	6.7	6.5
Finland	1.3	7.4	6.4	7.7	7.7	6.7	7.0	7.3	7.1
Estonia	0.3	5.4	4.4	6.8	6.2	6.1	7.0	6.9	6.8
Slovakia	1.3	6.5	5.8	6.8	6.8	6.3	5.7	5.4	5.2
Slovenia	0.5	5.1	4.5	4.6	4.8	4.1	3.6	3.7	3.6
Cyprus	0.2	8.4	7.1	7.5	7.5	7.2	6.4	6.1	5.9
Malta	0.1	3.7	3.6	4.0	3.5	3.2	2.7	2.7	2.7
Latvia	0.5	7.4	6.3	7.3	7.6	7.1	6.8	6.6	6.5
Lithuania	0.7	6.2	6.3	7.1	7.1	6.0	6.8	6.7	6.5
Croatia	0.9	8.5	6.6	6.7	7.7	6.3	6.5	6.2	5.8
Euro Area	**77.7**	**8.2**	**7.6**	**8.0**	**7.7**	**6.7**	**6.5**	**6.4**	**6.1**
Denmark	1.4	5.1	5.0	5.3	5.1	4.2	4.8	4.7	4.6
Sweden	2.6	6.4	6.8	8.9	8.8	7.4	7.4	7.2	7.3
Hungary	**2.3**	**3.6**	**3.3**	**4.1**	**4.1**	**3.7**	**4.1**	**4.3**	**3.7**
Czech Republic	2.5	2.2	2.0	2.7	2.8	2.7	2.4	2.5	2.5
Poland	8.0	3.9	3.3	3.3	3.4	2.7	3.0	2.8	2.7
Romania	3.9	4.2	3.9	5.0	5.6	5.4	5.4	5.2	5.3
Bulgaria	1.6	5.2	4.2	5.1	5.3	5.2	4.2	4.2	4.2
EU14	**77.2**	**7.5**	**7.1**	**7.9**	**7.8**	**6.7**	**6.6**	**6.4**	**6.1**
New EU13	**22.8**	**4.5**	**4.1**	**4.4**	**4.6**	**4.1**	**4.1**	**4.0**	**3.9**
EU27	**100.0**	**7.4**	**6.8**	**7.2**	**7.1**	**6.1**	**6.0**	**5.9**	**5.6**
Memorandum items [a]									
USA		3.9	3.7	8.1	5.4	3.6	3.6	3.7	4.0
Japan		2.8	2.4	2.8	2.8	2.7	3.0	2.8	2.7
United Kingdom		4.1	3.8	4.5	4.6	3.7	4.0	3.8	3.6
China[b]		4.0	3.8	3.6	4.0	4.2	4.2	4.0	4.0
Russia[c]		5.4	4.6	6.0	5.9	3.9	4.5	4.3	4.1
South-Eastern Europe									
Serbia[d]		12.7	10.4	9.0	10.7	9.2	8.7	8.3	7.9
Turkey		10.9	13.7	13.2	12.8	12.9	10.1	10.3	9.9

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
EU14 = Countries that joined the European Union before 2004
EU13 = Countries that joined the European Union in 2004, 2007 and 2013
Source: Eurostat, national statistical offices, ILO, OECD

Macroeconomic indicators for Hungary and Kopint-Tárki forecast

(year-on-year change, percentage)

	Data							Forecast		
			2023				2024	2024		2025
	2022	2023	Q1	Q2	Q3	Q4	Q1	2024 Jan.	2024 Apr.	2024 Apr.
GDP aggregates, real growth										
GDP total	4.6	-0.9	*-0.9*	*-2.4*	*-0.4*	*0.0*		2.7	**2.5**	**3.2**
Domestic Demand	4.1	-5.6	*-4.4*	*-8.1*	*-5.1*	*-6.1*		2.7	**2.7**	**3.1**
Private Consumption	6.8	-1.0	*-2.9*	*-1.7*	*-1.2*	*1.0*		2.8	**2.8**	**3.2**
Public Consumption	0.8	-1.5	*-5.1*	*1.0*	*4.5*	*-3.8*		0.5	**0.5**	**0.5**
Gross Fixed Capital Formation	1.4	-7.4	*-3.6*	*-13.4*	*-12.3*	*-3.0*		3.2	**2.2**	**4.5**
Gross Capital Formation	0.3	-14.9	*-4.9*	*-22.1*	*-14.8*	*-13.0*		3.2	**3.6**	**4.0**
Export	11.4	0.9	*6.6*	*1.1*	*-3.1*	*-4.7*		3.0	**0.9**	**4.3**
Import	10.8	-4.3	*2.4*	*-5.3*	*-8.1*	*-9.0*		2.9	**1.1**	**4.2**
Industrial production	6.1	-5.5	*-3.4*	*-6.2*	*-5.2*	*-7.3*	*-0.9* [e]	5.0	**1.7**	**5.3**
Consumer Price Index	14.5	17.6	*25.4*	*21.9*	*15.4*	*7.8*	*3.7*	3.5	**4.3**	**3.5**
Employment, earnings										
Number of Employed, growth [a]	1.3	0.6	*0.5*	*0.7*	*0.5*	*0.8*	*0.6*	0.7	**0.4**	**0.5**
Unemployment Rate [a]	3.6	4.1	*4.1*	*3.9*	*4.1*	*4.4*	*4.6*	3.4	**4.3**	**3.7**
Unit Labor Costs, in EUR [b]	1.3	26.1	*16.0*	*33.1*	*24.8*	*26.1*		4.1		
Gross Nominal Wages [c]	17.4	14.2	*10.8*	*16.5*	*14.8*	*14.9*	*14.3* [e]	8.0	**13.5**	**8.0**
Net Real Wages [c]	2.5	-2.9	*-11.6*	*-4.4*	*-0.5*	*6.6*	*10.2* [e]	4.3	**8.8**	**4.3**
Savings Rate, % of GDP [d]	4.0	6.7	*4.7*	*5.7*	*6.2*	*6.7*		6.0	**6.6**	**5.9**
Current and Capital Accounts Balance, % of GDP	-6.4	1.2	*-1.4* [f]	*3.5* [f]	*1.8* [f]	*0.5* [f]		1.9	**2.0**	**3.0**
General government Fiscal Balance, ESA-2010, % of GDP	-6.2	-6.7	*-9.5*	*-3.0*	*-3.7*	*-10.6*		-3.5	**-5.5**	**-5.0**
Gross Government Debt, % of GDP	74.0	73.5	*75.5*	*75.2*	*75.0*	*73.5*		70.0	**73.2**	**72.5**
Short-term Government Yields (3M), eop	12.32	6.23	*14.48*	*10.03*	*8.17*	*6.23*	*6.59*	5.0	**5.5**	**4.5**
Long-term Government Yields (10Y), eop	8.98	5.86	*8.44*	*6.98*	*7.40*	*5.86*	*6.74*	5.0	**6.0**	**5.5**
External assumptions										
Internat. Trade in Goods and Services [d]	5.4	0.4							**3.3**	**3.6**
Brent Oil Price ($/bbl, p. avg.)	100.9	82.5	*81.2*	*78.3*	*86.7*	*83.7*	*83.0*	84.0	**86.0**	**88.0**
GDP Real Growth, Eurozone	3.4	0.4	*1.6*	*0.4*	*-0.2*	*0.0*		1.4	**0.7**	**1.5**
GDP Real Growth, New EU Members	4.0							3.7	**2.7**	**3.2**
EUR-HUF, period average	391	382	*389*	*373*	*384*	*382*	*388*	385	**390**	**390**
EUR-USD, period average	1.05	1.08	*1.07*	*1.09*	*1.09*	*1.08*	*1.09*	1.08	**1.08**	**1.08**

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 All employers
d Net lending of households, financial accounts statistics, percentage of GDP, four-quarter cumulative data
e January-February
f Seasonally adjusted data by the MNB

III. The Hungarian Economy

The overall economic activity declined by 0.9% on an annual basis in 2023 – or by 0.7%, if the seasonally and calendar-adjusted GDP is considered. The rate of decline exceeded the expectations of most analysts, due to the disappointing stagnation of GDP in the fourth quarter, on a quarterly and annual basis alike.

During the year, domestic demand was the primary drag on economic growth. Amid the skyrocketing inflation and the resulting fall in real wages, *private consumption* decreased. But the domestic sales of industry plummeted as well, especially in industrial subsections that mostly produce intermediate inputs. In addition, in the second half of the year – when real wages first stopped falling and later started to rise – merchandise import fell steeply. The willingness of domestic-oriented firms declined severely, due to the adverse demand conditions.

While real wages rose considerably in the fourth quarter, private consumption expenditures stagnated. The fall in investments decelerated sharply. This is primarily the result of a temporary investment surge in the budgetary sector, but investment activity also improved in some of the domestic-oriented economic industries. At the same time, the downward pull of **inventory reduction** became drastic in the last quarter.

Regarding wages and consumption, it is important to keep in mind that **total household incomes** might have even increased in 2023, despite the fall in real wages, due to the jump in mixed and property income. This growth, however, probably did not happen before the second half of the year, when labor incomes stopped falling as well. In any case, the household segment that has sizeable financial assets may have had a good year overall, which may have been an additional factor behind the steep rise in financial savings in the last year.

As opposed to domestic demand, net export contributed positively to economic growth in every quarter of the year. But this happened in the context of worsening export performance – merchandise export started to decrease in the second half of the year – which means that the net position was positive due to the even steeper fall in imports. This might be connected to the negative turn in manufacturing investments in the fourth quarter which interrupted a continuous growth spell lasting for several years.

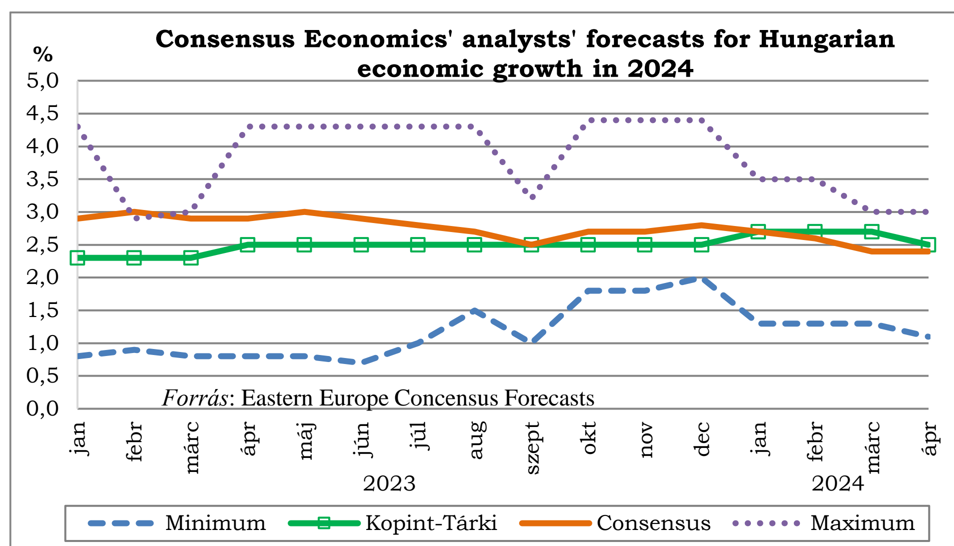
We expect modest GDP growth in 2024. This growth will be supported primarily by the strong *real wage growth*. Still, the pattern seen in the fourth quarter of 2024 – stagnating consumption expenditures amid rising real wages – and the relatively disappointing evolution of retail trade turnover in the first two months of this year is a warning sign that households are likely to remain cautious regarding their consumption decisions. As a result, consumption growth will probably fall way short of what the ongoing jump in real wages would suggest. At present, we expect the growth rate of private consumption to remain slightly below 3% in 2024.

The investments of domestic-oriented firms may also start expanding, together with consumption, but the drop in manufacturing investments in the fourth quarter of 2023 is also likely to prove temporary. But the pace of growth is expected to remain modest and the same is true of the housing investments by households, even if the upward impact of the newly introduced credit support scheme and the housing renovation aid which is to be introduced around mid-year.

In sum, the revival of domestic demand can be taken for granted – unless some unexpected shock occurs – even if question marks remain regarding the timing and degree of this revival. We expect *final domestic use* to expand by 2.5-3% this year. The prospects are much murkier in the case of *export* demand: the international news does not unequivocally point to an economic upturn, especially not in the case of Germany. Based on the preliminary external trade data, export might have stopped contracting in February, but it is too early to say whether this is a harbinger of a trend change or just a one-off bounce. The same can be said about the moderately encouraging industrial performance in February. The stock of manufacturing export orders is still declining, and the share of industrial firms struggling with overcapacity is still high, even though the firms' expectations regarding the future have somewhat improved.

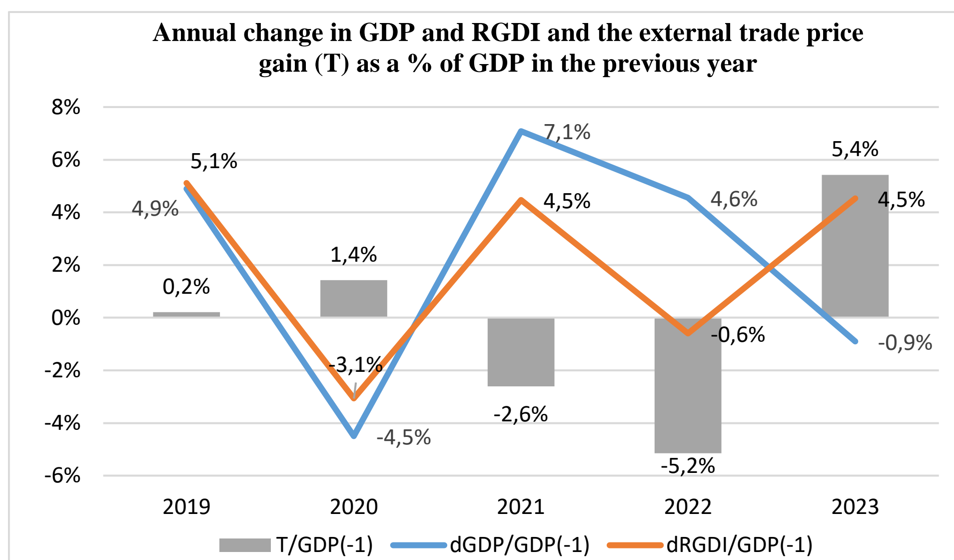
Due to the year-end drop in export volumes, the outlook regarding the net export position is gloomier now than three months earlier. Even if it can be hoped that the annual average export volume will grow in 2024, the pace of growth will be very modest, and will most probably trail import growth, since the latter will get a boost from the rebound of domestic demand.

Since net export is likely to weigh down on GDP growth, the overall rate of GDP expansion will be lower than the approximately 3% growth in domestic demand. We expect a GDP growth rate of about 2.5% in 2024 – this prediction is somewhat above the average expectation among the participants of the Consensus Economics poll.



The impact of the terms-of-trade shifts on real gross domestic income between 2021 and 2023

The changes in the terms of trade (the ratio between the export and import price indices) affect the balance of external trade and, as a result, the balance of payments as well. (The latter is discussed in the section on the balance of payments.) From a macroeconomic view, another effect is just as important: the terms-of-trade changes cause a divergence between the trajectory of real GDP and real gross domestic income (RGDI). The latter shows the evolution of the *real disposable income incurred by domestic sectors*. The RGDI is calculated as the GDP at prices the previous year multiplied by the term-of-trade index. As the graph below shows, the RGDI lagged far behind real GDP in 2021 and 2022. The terms-of-trade loss was 2.6% in 2022 and 5.2% in 2023 – as a result, the loss netted out more than half of the GDP growth in 2021, while in 2022 it caused a 0.6% decrease in RGDI, despite the GDP growth rate of 4.6%.



Source: own calculation based on CSO data.

Note: We use the formula recommended by the ESA 2010 to calculate the trading gain/loss (T):

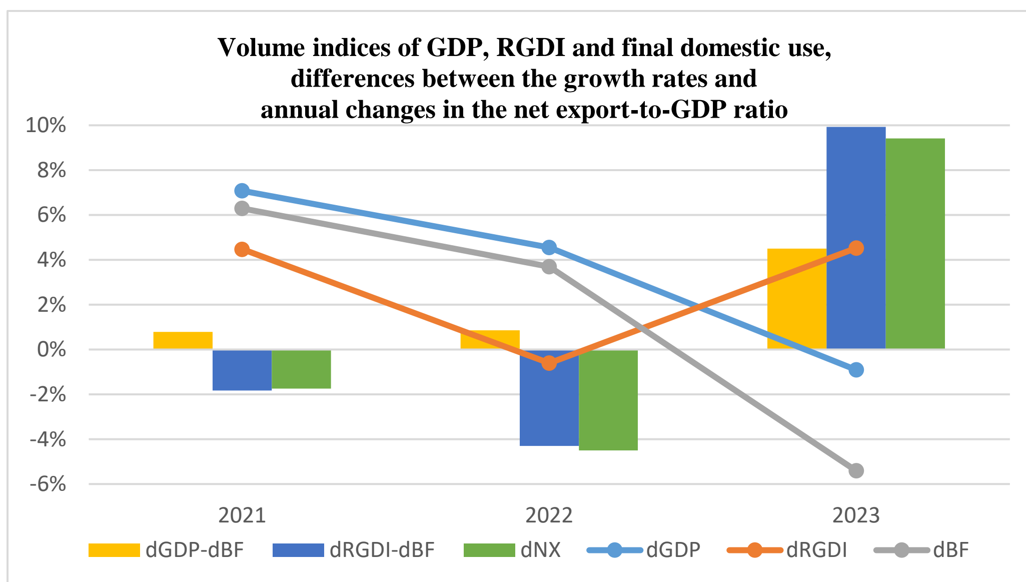
$$T = \underbrace{\frac{X_1 - M_1}{P_{xm}} - \left(\frac{X_1}{Px} - \frac{M1}{Pm}\right)}_{Terms-of-trade\ effect}$$

Where *X* and *M* denote the exports and imports, respectively, *0* and *1* denote the base period and reference period, respectively, *Px* and *Pm* denote the export and import price indices and *Pxm* denotes the average of the export and import price indices.

As can be seen from the graph, the relationships changed profoundly in 2023: while real GDP contracted by 0.9%, the RGDI expanded by 4.5%, due to the terms-of-trade gain amounting to 5.4 percentage points.

Why is it important to keep track of the RGDI in times of substantial terms-of-trade changes? Because it provides a key to understanding the change in the external balance position. In such times, the relationship between the changes in real GDP and real final domestic use is not suitable to correctly interpret the changes in external balances. To do this, it is necessary to compare to changes in RGDI with the changes in final domestic use.

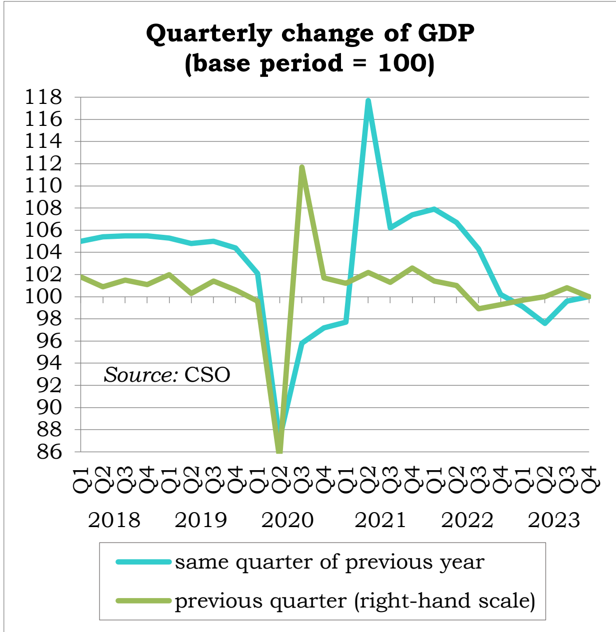
The graph below demonstrates that in cases of substantial trade-of-terms changes the divergence between RGDI and domestic final use shapes the external balance (as a percentage of GDP), instead of the divergence between GDP and domestic use. It can be also seen from the graph that the sizeable income transfer in 2023 only restored the balance that had been upset during the preceding years.

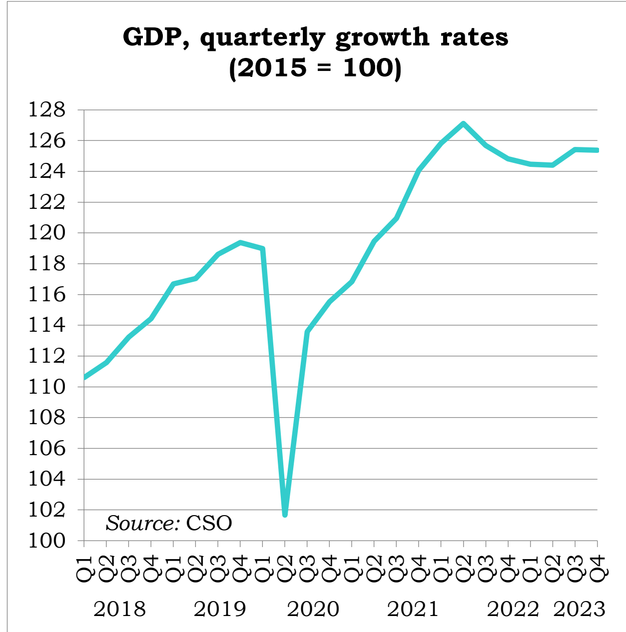


Source: own calculation based on CSO data

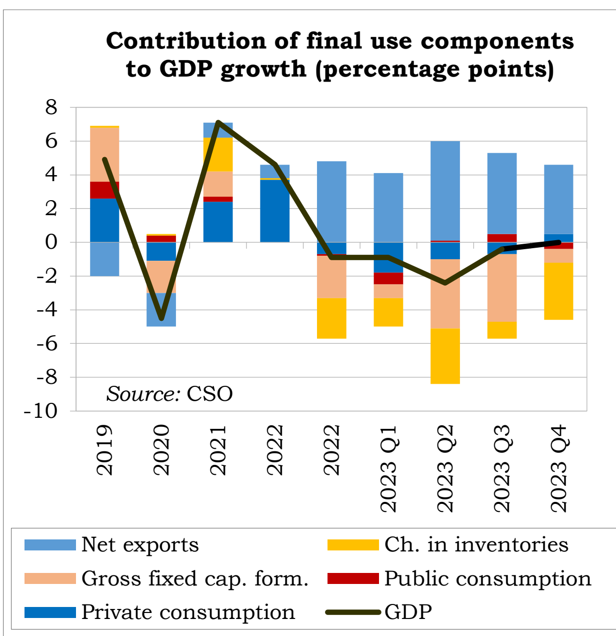
3.1. The GDP and its components

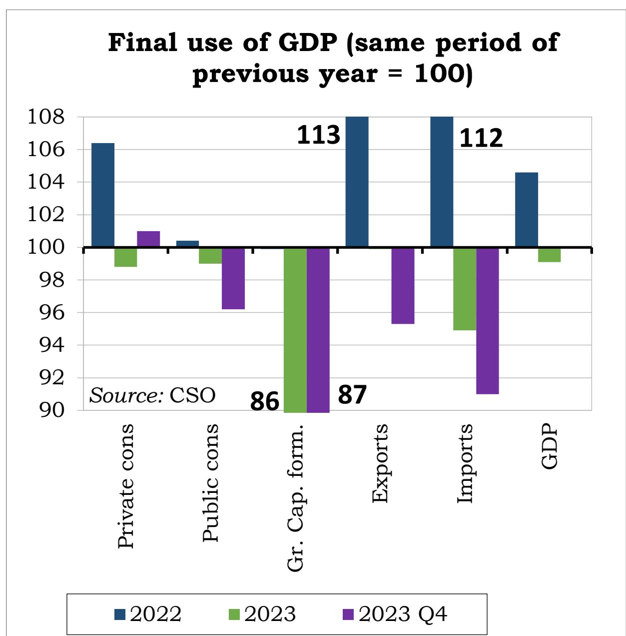
After three consecutive quarters of year-on-year contraction, the GDP stagnated in the last quarter of 2023 on an annual basis. Actually, this outcome was disappointing because the analysts expected some degree of positive growth. (The *seasonally and calendar-adjusted GDP* grew indeed, by 0.5%, on an annual basis.) Compared to the previous quarter, GDP stagnated as well, another negative surprise after the upturn in the third quarter. In 2023 as a whole, GDP fell by 0.9%.





Besides the decrease in domestic demand, external conditions also deteriorated toward the end of the year. But during most of 2023, domestic demand was the primary culprit. On the **expenditure side**, total ***domestic use*** was down 5.4% annually, and it kept falling by 4.1% in the fourth quarter as well. The factors behind decreasing domestic demand were changing during the year, however. In the case of the largest component – *private consumption expenditures* – the pace of fall was not especially drastic even at the





start of the year, amid peak inflation. And consumption expenditures basically stagnated in the fourth quarter which saw an acceleration of disinflation and a nearly 7% rise in real wages. This means that households remained cautious even amid expanding real incomes. On an annual average, the consumption expenditures of households contracted by 2.5% in 2023 while net financial savings steadily increased over the year. *Household investments*, on the other hand, fell significantly.

The volume of government transfers to households grew considerably, due to which the ***total consumption of households*** was up 1% in the last quarter and decreased only by 1.2% annually in 2023. This means that at the end of the year, gross fixed capital formation, and especially the *changes in inventories* were the main culprits behind the decrease in domestic demand. Fixed capital formation dropped by only 3% in the last quarter – a deceleration compared to the second and third quarters – despite the fact that *manufacturing* investments started to decrease, a new development which reflects the worsening outlook among exporting firms. At the same time, government investments grew spectacularly, which was mainly responsible for the overall moderation in the pace of investment fall in the last quarter.

In the meanwhile, the ***net export of goods and services*** contributed positively to GDP growth in the fourth quarter, just as during the previous quarters. But from the middle of the year, this positive contribution was not due to export growth, but only to the fact that the fall in import was much more drastic than the decline in exports. Merchandise import decreased by more than 10% in the last quarter (the fastest rate in 2023), even though consumption stopped falling by then, which suggests that the year-end drop in imports was mainly a reflection of the inventory reduction by the increasingly pessimistic industrial firms.

On the ***production side***, agriculture was the only economic industry that posted positive growth in 2023 (due to the favorable weather following the drought in 2022). Construction suffered from the lack of domestic demand – especially state demand – declined by 6% in 2023, with a year-on-year drop of more than 7% in the fourth quarter. Industrial activity continuously underperformed in the last year, and the fourth-quarter decline of industrial value added exceeded 7%. During most of the year, the lack of domestic demand was the main driver of industrial weakness but in the second half of the year – due to the high statistical base – industrial export sales also fell by more than 6%. While some of the engineering-related economic sections posted growth in 2023, the last quarter saw a decrease even in the electrical equipment industry and in the manufacturing of transport equipment.

In 2023, the value added of *services* was down 1.6% annually, with a decrease of 1% in the fourth quarter. Market services fell more substantially while the overall growth in services got a boost from the dramatic expansion in the state-dominated healthcare sector. Among market services, wholesale and retail *trade* fell the most steeply, but the output of transport and storage decreased substantially as well.

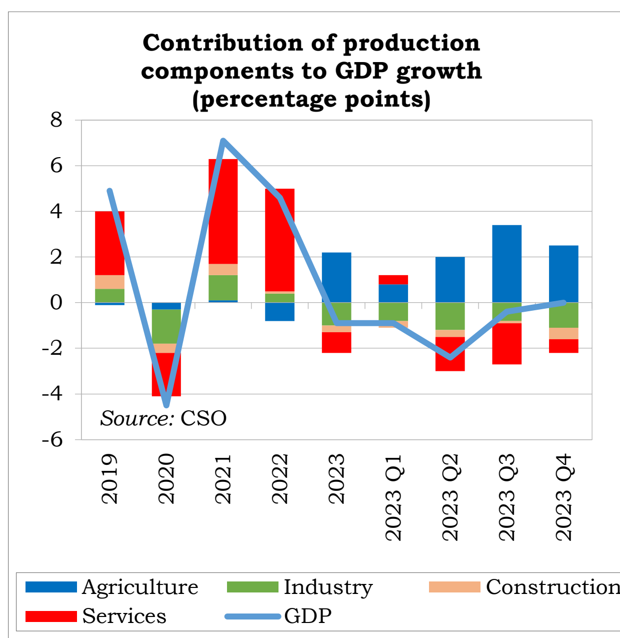
The prospects for ***this year*** are contradictory. On the one hand, real wages will without doubt grow substantially in 2024, which will lead to an increase in *household consumption demand*. However, the degree of this increase seems uncertain in light of the fact that consumption expenditures failed to grow in the fourth quarter of 2023 even though real wages were already rising at that time. Another warning sign is that retail trade remained relatively weak in January-February. (Much of the observed growth in

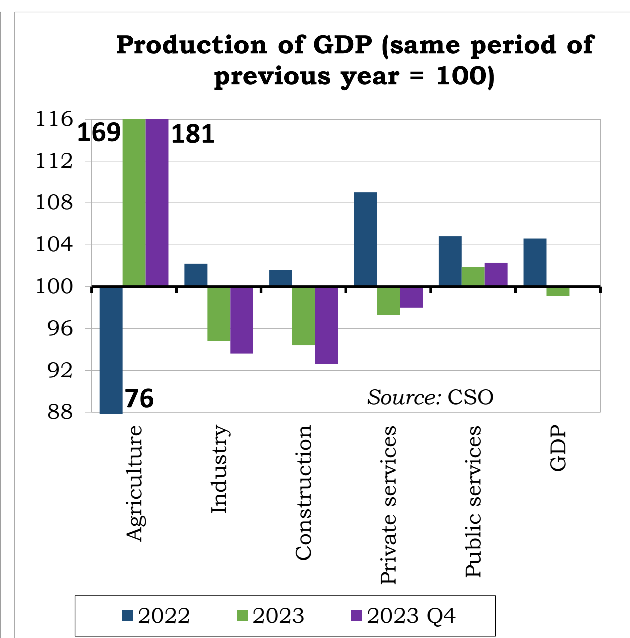
February was due to the calendar effect coming from the leap day in February 2024.) On an annual average, we expect household consumption to grow by ***2.5-3% in 2024***. The question is the degree to which growing consumption can boost business investments and generate a reversal in the inventory cycle. It is important to keep in mind that the *external demand* conditions are still quite gloomy. This may have a restraining effect on the investments of export-oriented firms. As of now, only the (moderate) revival of domestic demand and the lowering of interest rates can be considered as business investment incentives. The further inflow of EU funds is still uncertain. By now, it is clear that government investments will be lower than in 2023, due to a decision to postpone several investment projects amounting to HUF 675 billion, due to the fiscal difficulties. Household investments may expand amid a broad-based growth in real incomes, lower interest rates, and the moderate stimulating effect of the CSOK Plusz scheme and the new housing renovation support scheme, announced in April. In sum, overall fixed investments may expand by **2-2.5% in 2023**.

The export dynamism will improve at a slow pace at best – this improvement is unlikely to offset the gradual acceleration of imports, a result of the strengthening of domestic demand. (The export of goods decreased on an annual basis in January, but possibly turned into positive growth in February, which may well prove temporary.) In sum, we expect the annual growth contribution of net exports to be slightly *negative* this year.

On the *production side*, the broad-based household income growth is likely to give a boost to the services sector, even if the annual growth rate of services is unlikely to substantially surpass 3% in 2024. Housing construction and renovation will be reinvigorated somewhat as well, even if in the case of construction much of the improvement will probably take place only in the next year. While domestic demand will strengthen domestic industrial sales, the still weak export outlook makes it uncertain whether industry can post any positive growth at all. For now, we expect a modest industrial growth rate of 1.5-2% but the negative risks are substantial.

On the whole, we predict a **2.5% growth of GDP** in 2024. This projection, however, is marred by negative risks. The pace of economic growth may accelerate in the next year





but much of this acceleration hinges on whether the eurozone gains enough momentum in 2025 to support Hungarian exports, or the post-Covid (and post-energy price shock) struggling continues.

3.2. Production of GDP

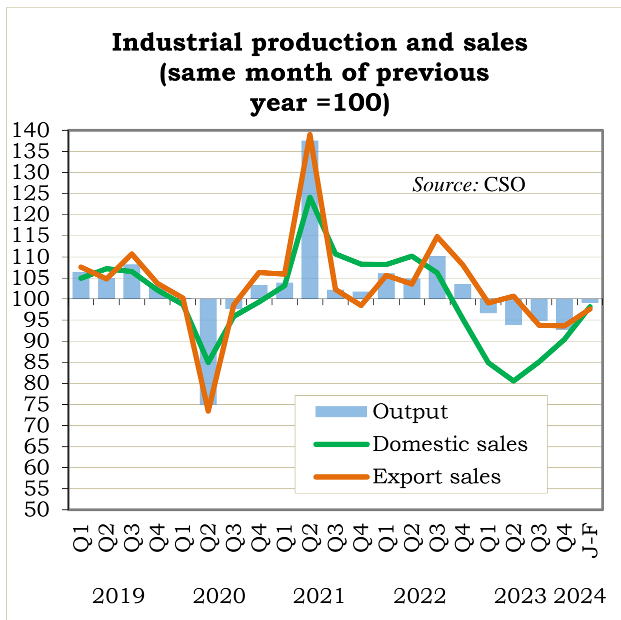
3.2.1. Industry

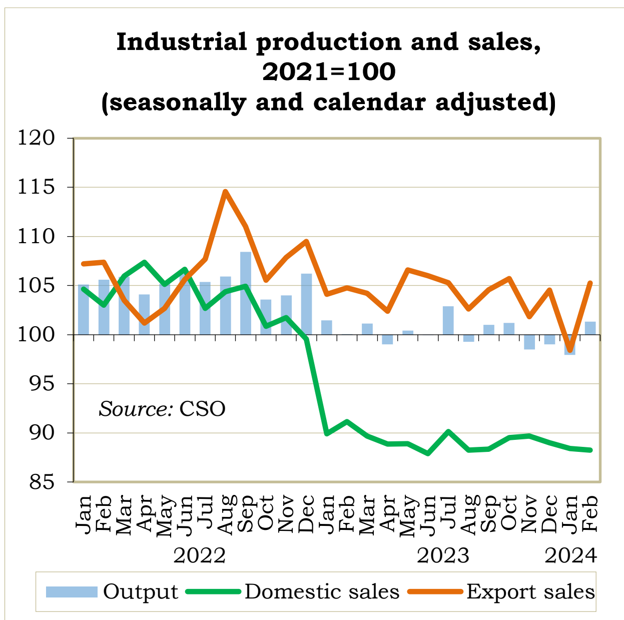
While industrial growth remained relatively dynamic in 2022 despite the war, the next year saw a dramatic negative turn: industrial output dropped by 5.5% in 2023. On a year-on-year basis, output decreased in all four quarters and the pace of the fall was the largest (-7.3%) in the very last quarter. The steep fall in domestic demand was the main culprit behind the industrial contraction but in the second half of the year, export sales fell by more than 6% as well. After that, in January 2024 the decrease in production decelerated and February saw a modest growth, due to an upturn in export sales. But this may be a temporary upsurge because the solid basis for steady export growth does not seem to be present yet.

The seasonally adjusted fixed-based monthly data confirms that industrial domestic sales plummeted at the beginning of 2023 and have largely remained at this lower level since then – which means that the deceleration of the decrease in year-on-year domestic sales from late 2023 was a result of the statistical base effect. Notably the fall in domestic *energy* sales played a nontrivial role in the sudden plunge of domestic sales: manufacturing domestic sales displayed a downward trend as well, but in the case of manufacturing, there was no sudden drop. An improvement is expected from the spring onwards even if there was no sign of an upturn up until February.

The decline affected most of the manufacturing subsections in 2023, not to mention the mining and energy sectors. The steep decline in food industry output (partly a consequence of the catastrophic agricultural yields in 2022) continued until the very end of 2023 but turned into growth in January-February. The former main growth drivers, the automotive industry and the electrical equipment industry (which includes battery production) expanded in 2023 as a whole but contracted in the last quarter and in January 2024.

The electrical industry was badly hit by falling domestic sales but export sales also started declining from November. Within manufacturing, the rubber, plastic and

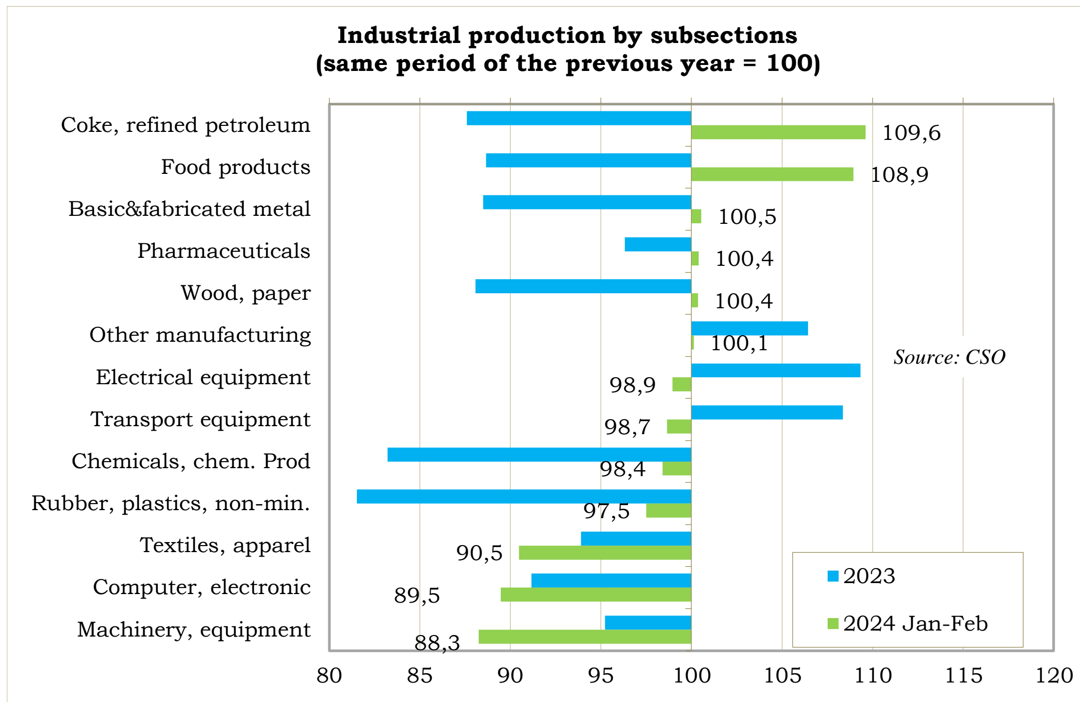




construction material industry suffered the biggest drop, with no real trend change in sight at the beginning of this year. The electronic industry declined at an accelerating pace in 2023 but some green shots seem to appear in early 2024.

This year will be characterized by a revival of domestic demand on the one hand – even if there are no clear signs of such a revival in the domestic sales data up to February – and deep uncertainty regarding the export outlook on the other. Based on the recent trends, only the food industry seems to have relatively bright prospects for this year. Even if the domestic demand recovers, more or less, from the slump in 2023, we cannot be sure that this will be enough to produce general growth in the predominantly export-oriented industrial sector. Up to February, the evolution of the stock of orders does not suggest an upturn in short order.

At present, we expect a very modest industrial **growth rate of 1.5-2% for 2024** but – depending on the evolution of external conditions – a pessimistic scenario with annual stagnation is also possible. The pace of growth is expected to gain steam in 2025 but this projection may also prove overly optimistic, due to the chronic structural problems that the German economy struggles with.



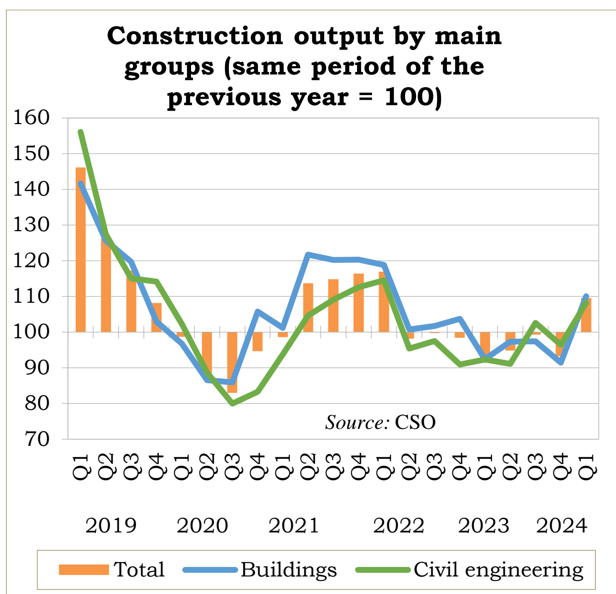
3.2.2. Construction

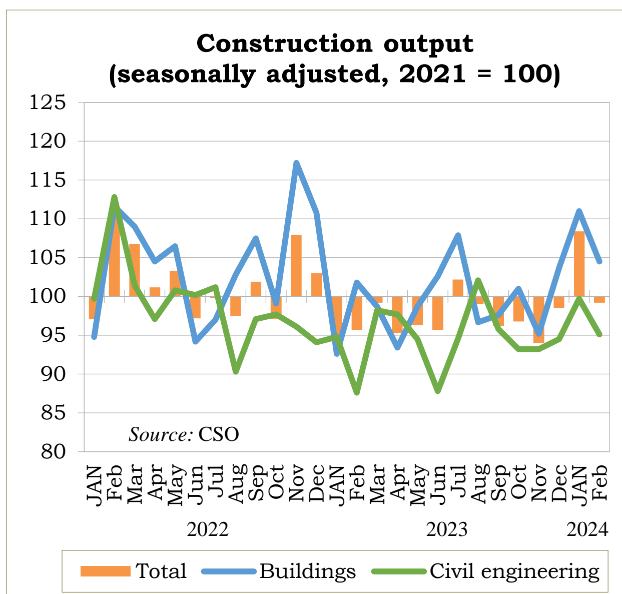
Construction output steadily declined on an annual basis in 2023: on average, the rate of fall was 5%, while in the fourth quarter alone the output was down 6.8%. There was no dramatic difference between the main groups, but the rate of decrease in the construction of buildings (5.6%) somewhat exceeded the analogous rate in civil engineering (3.8%). The difference was bigger in the fourth quarter (at the expense of building construction) but this was mostly a result of a statistical base effect. The seasonally adjusted monthly data shows a more or less directionless fluctuation in both main groups, within fluctuation bands that were for the most part below the average seen in 2022. The level of output *jumped* in January 2024, but a partial correction promptly followed in February. It is unclear whether the relatively strong year start is a harbinger of a positive trend reversal.

For construction firms, the main impediment to growth is insufficient demand. The volume of orders was 8% lower in February than one year ago, although this is an improvement compared to the previous months. In civil engineering, the dearth of ***state investments*** is clearly the cause of the insufficient demand. The fiscal constraints also have some effects on housing investments, through the expiration of various earlier support schemes (or the narrowing of the target population in the case of existing ones).

According to the *iBuild* database, the value and volume of the *newly initiated* construction projects continued to decline in the fourth quarter. On average, the volume of activity starts dropped by 34% in building construction and 50% in civil engineering in 2023. Within the construction of buildings, non-housing projects declined especially steeply while within civil engineering road and railroad projects suffered the biggest drop.

The steep fall in activity start is another sign that makes the future outlook less than encouraging and makes it uncertain whether construction output will grow or keep declining in 2024. For now, we expect an **increase of a few percent** but a real upturn – even in the best of scenarios – is unlikely to occur before 2025. The newly introduced CSOK Plusz housing support program and the housing renovation support program (expected to start in June) may help to generate modest growth in the construction sector.



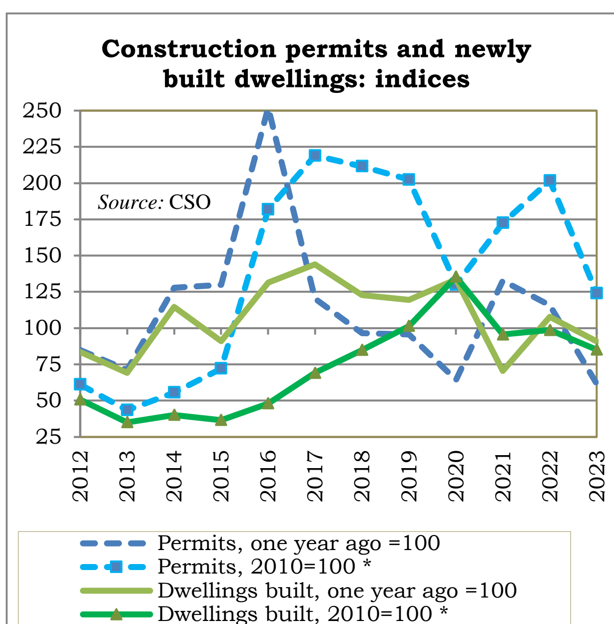


3.2.3. Housing construction

After four consecutive quarters of year-on-year decline, the number of dwellings built *increased* by 13% in the fourth quarter of the last year. The increase is entirely due to the projects completed by business organizations. Still, on average, the annual number of dwellings built dropped by 9% in 2023. The number of *permit applications/notifications*, on the other hand, continued to decrease in the fourth quarter – the annual average rate of decline was 39% in the last year.

The data provided by the iBuild database paints a mixed picture about the future outlook: the volume of the newly started multi-dwelling construction projects kept decreasing in the fourth quarter, but the volume of projects *completed* increased in 2023 and it may remain high in 2024 as well.

The housing construction activity suffers primarily from weak demand, and the financing conditions were unfavorable during much of the last year. In 2024, the value of housing support transfers is likely to decrease. The newly introduced CSOK Plusz credit scheme generated significant interest and will contribute to the upturn in housing market turnover, but it is unclear to what degree, and when, it will generate demand for housing *construction*.



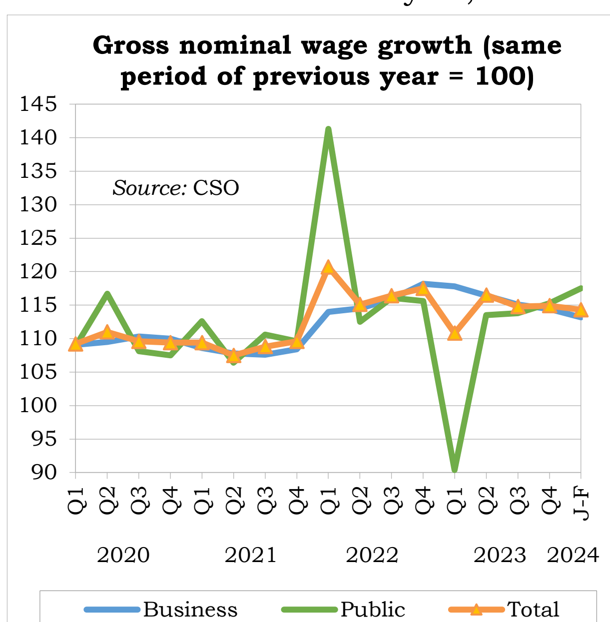
The question is basically the same regarding housing lending: the downward trend in lending rates facilitated the revival of lending activity, but it is uncertain how it will affect construction activity. For now, we expect a very modest growth in the number of dwellings completed in 2024, but this expectation may prove overly optimistic.

3.3. The final use of GDP

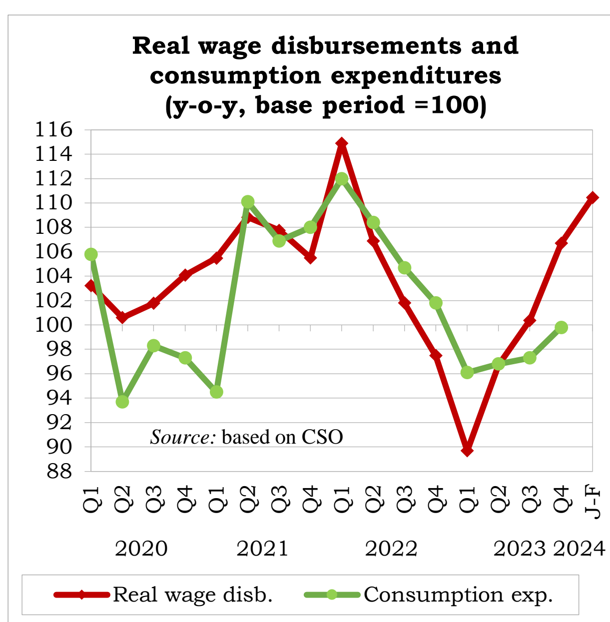
3.3.1. Household income, consumption and saving

In 2023, **nominal wages** climbed 14.2%, falling short of the annual inflation rate of 17.6%. As a result, real wages were down 2.9% in the last year. Real m*edian wages* declined at a slower pace (since the statistical base level was much less distorted by the large-scale one-off premium paid to the members of armed bodies in February 2022 than in the case of average wages). As the number of employees continued to grow minimally amid the recession, the decrease in ***net real wage disbursements*** was only 0.7% in 2023.

Since inflation steadily decelerated during the year, the pace of real wage decrease moderated from quarter to quarter, and real wages *rose* by 6.6% in the fourth quarter. These gyrations were accompanied by a relatively muted response of ***household consumption expenditures*** in both directions. In the first half of the year, the fall in consumption expenditures was relatively mild, while the return to real wage growth at the end of the year was almost accompanied by a stagnation in consumption expenditures. This suggests that households remain – at least at a macro level – distinctly **cautious** following the end of the three-quarter real wage drop. On average, private consumption expenditures were down 2.5% in 2023, while *total actual private consumption* decreased by a mere 1.2% compared to 2022, due to an upturn in the transfers in kind received from the government.

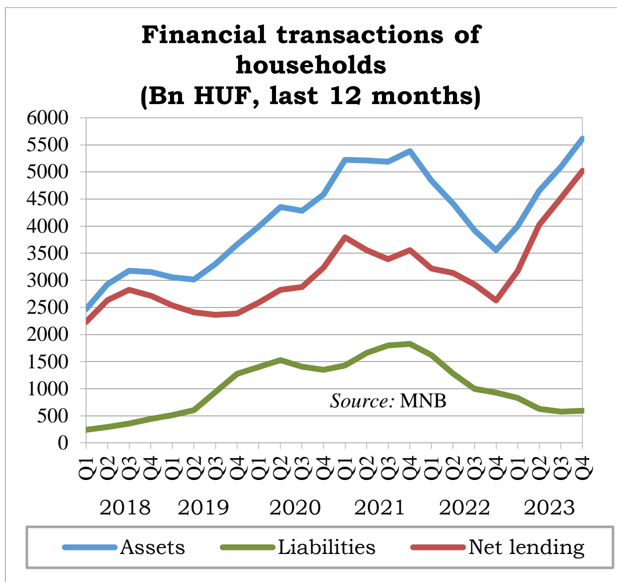


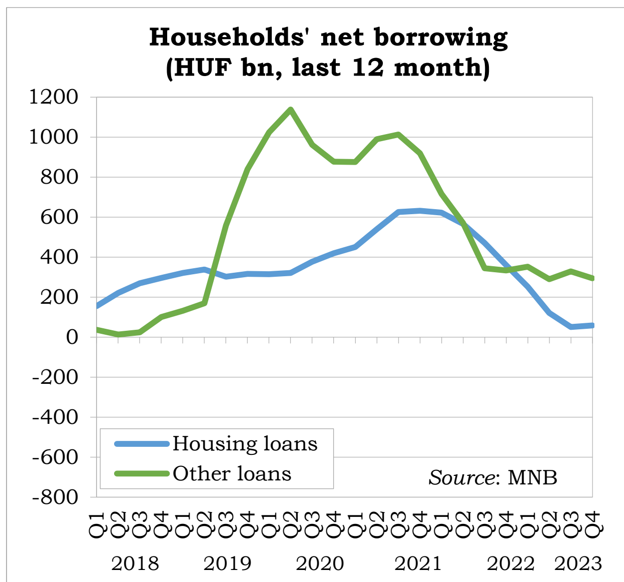
The cautiousness is also reflected by the ***steady and strong rise in the net financial savings of households*** during 2023. In addition to the year-on-year growth in gross savings, net borrowing declined in the first three quarters of the last year and stagnated in the fourth quarter. This means that in the first quarter, the fall in real wages prompted households to cut back their spending, but this reticence continued in the second half as well, even after real wages started to grow. (It is worth noting that – in light of the nominal data on sector accounts – the ***mixed and property incomes of households*** grew considerably in 2023.) The volume of *investment* spending of households dropped as well in the last



year. Within net borrowing, the balance of housing borrowing contracted markedly while other borrowing almost stagnated on an annual average, but in the fourth quarter housing borrowing also grew somewhat. The *four-quarter cumulated* savings rate – as a percentage of GDP – rose from 4% in 2022 to 6.7% in 2023.

The consumption outlook for this year is positive but not especially sanguine since the cautiousness of households will only gradually ease, especially in light of the recent loosening of the labor market. Still, household consumption is supported by strong wage growth: in January-February, real wages were up 10.1% on average. Apparently, the 15% hike in nominal minimum wages is generating a significant overspilling effect, even though the 'guaranteed wage minimum' – that is, the wage minimum for qualified workers – was only raised by 10%. The annual real wage growth may well **surpass 8%** in 2024. Still, we expect the growth in household consumption to remain tentative, with a growth rate **slightly below 3%** in 2024.

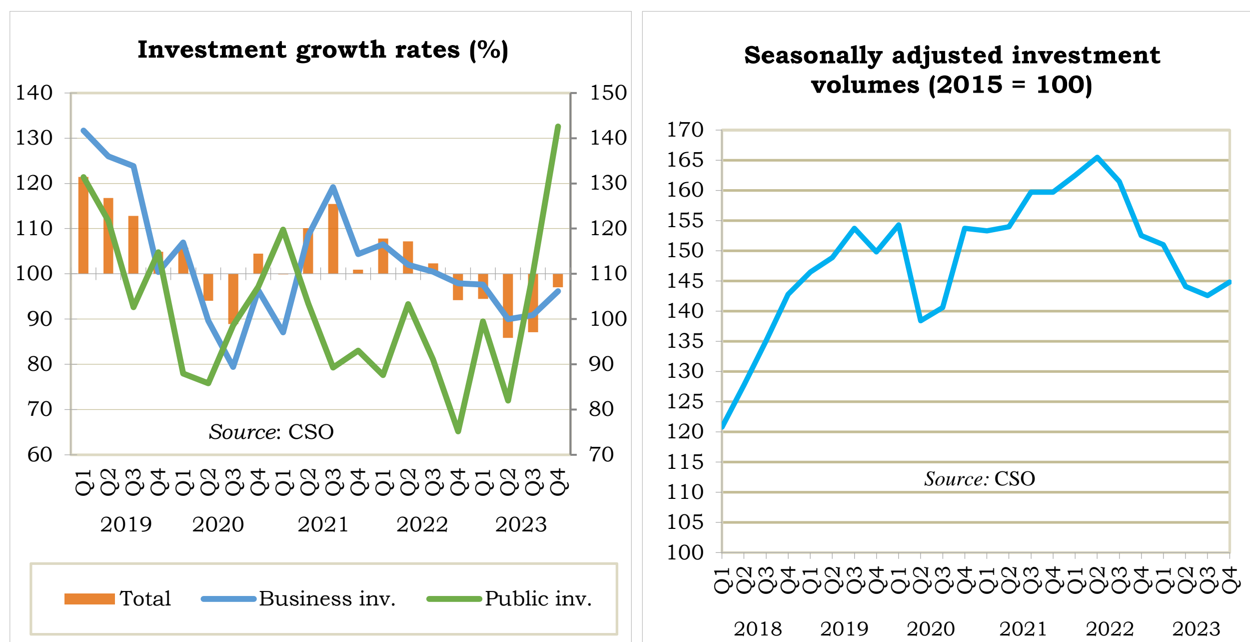




3.3.2. Investments

In the fourth quarter of 2023, the volume of investments decreased by 3% on an annual basis. This constituted a significant improvement compared to the two-digit rates of decrease in the second and third quarters. Compared to the *previous quarter*, investments increased by 1.5%, after five consecutive quarters of decline.

According to the CSO, much of the improvement can be attributed to the *budgetary sector* which saw a year-on-year increase of almost 43% in the fourth quarter. On the other hand, business investments continued to fall, even though the pace of decrease moderated. This is good news, but it is worth noting that the improvement was not reflected in every economic section. Notably, while *manufacturing* investments continued to expand previous three quarters, they started to decline in the fourth quarter, primarily because of the fall in the battery sector which served as a growth driver throughout the past couple of years. By contrast, some (but not all) of the domestic-oriented sectors saw some improvement in investment growth rates in the fourth quarter.

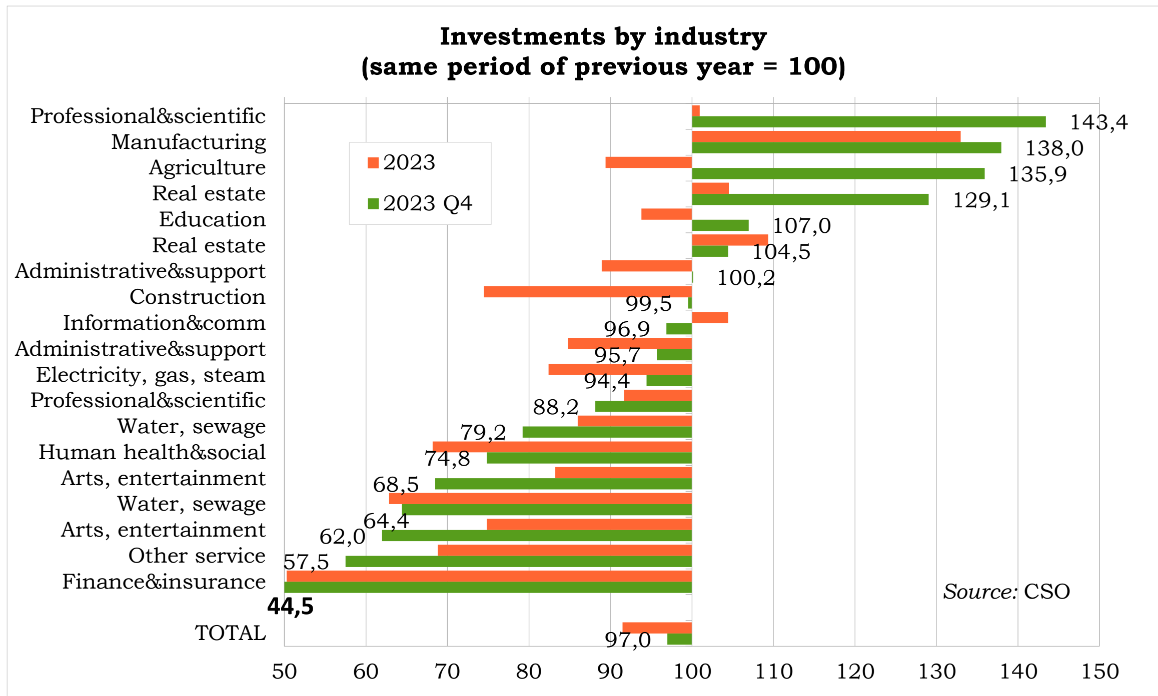


In sum, the number of economic sectors where investments fell in the last quarter was four fewer than the average number seen in the first three quarters. Manufacturing was the only sector where positive investment growth turned into negative in the very last quarter. Beyond that, however, the picture is still mixed. Numerous economic areas saw a worsening of investment dynamism – an acceleration of decline or deceleration of growth compared to the first three quarters of 2023 – although the number of improving sectors was somewhat bigger. But the largest improvement was registered in the three state-dominated areas: public administration, education and healthcare.

On average, the volume of investments dropped 8.5% in 2023 compared to the previous year.

Investments will probably **start growing in 2024** but the growth rate is unlikely to reach **2.5%** amid the unfavorable external conditions and the pressing fiscal constraints. The unlocking of a part of the frozen EU funds can prompt an acceleration of the pre-financing of the relevant development projects. On the other hand, in 2024 it will be no

longer possible to spend sources allocated to the budgeting period of 2013-2020, while in 2023 the use of such sources still supported investment activity.



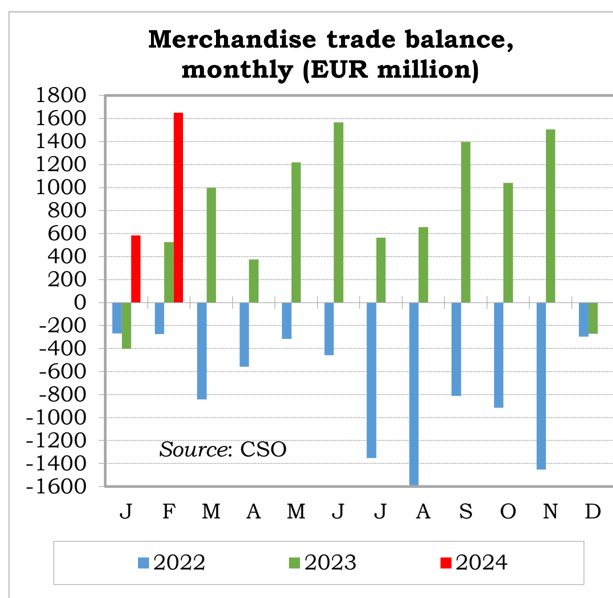
3.3.3. External trade

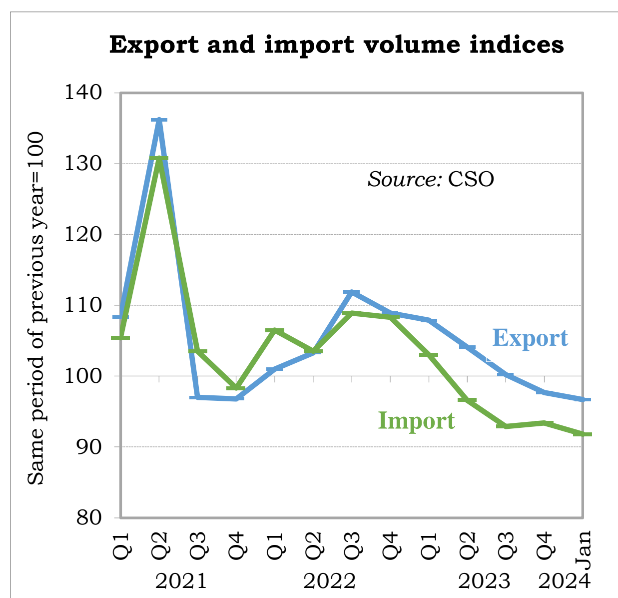
After a precipitous deterioration in 2022, the external trade balance improved steadily and just as sharply in 2023. Amid the steep fall in domestic demand, a wide gap opened between the respective export and import volume indices – to the expense of the latter – even if export growth continuously weakened and eventually, in the last quarter, turned into a decrease.

While export growth was driven by machinery and transport equipment in the first half of the year, the same group of commodities suffered the steepest decline during the fourth quarter. At the same time, food exports started to expand, primarily due to the good agricultural yields in 2023. On an annual basis, the volume of import started to contract from the second quarter, due to falling domestic demand, and all groups of commodities were involved in the decrease save one: fuels and energy. In sum, the annual volume index of import was 6 percentage points below the volume index of export.

The contribution of the sharp *terms-of-trade* improvement (by nearly 7% annually, according to the external trade statistics) to the improving external balances was approximately as great as that of volume changes. As a combined effect, the annual trade *surplus* amounted to EUR 9.2 billion (the second highest level, surpassed only by the absolute record in 2016), as opposed to the trade *deficit* of similar magnitude in 2022.

During the first two months of 2024, the external trade balance still continued to improve on a year-on-year basis. In January, the volume of import fell more drastically than export, and this was compounded by the still ongoing – even if weakening – terms-of-trade improvement. It is somewhat encouraging that export grew in all commodity groups, *except for* the most important (machinery and transport vehicles). The preliminary nominal data suggests that export may have turned into growth in *February*, but this upturn may well prove temporary. Imports will gain some momentum during the year while the same cannot be said with confidence about exports, due to the uncertainties regarding the global and European growth prospects. We expect the annual trade surplus to decrease to a level of around EUR 7 billion in 2024.



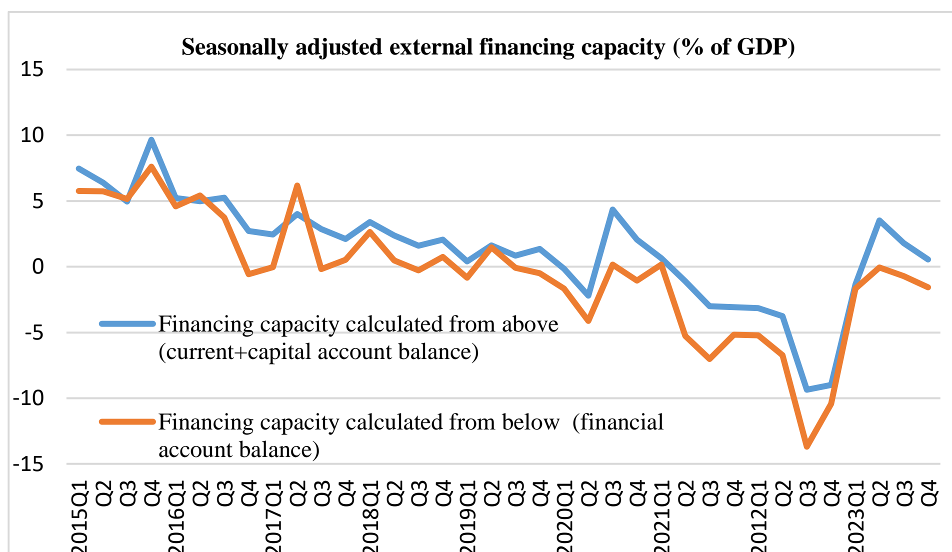


3.3.4. Balance of payments and the net external liabilities in 2023

The evolution of the balance of payments was shaped by two profound factors in 2023: the substantial fall in final domestic use (by 5.4%) and the sharp improvement in the terms of trade (by 6.2%, according to the GDP statistics). The former gave a boost through the decrease in import volumes while the latter exerted a positive impact through the trading gain. As a combined result, the balance of the external trade of goods and services turned from a deficit amounting to 4.4% of GDP in 2022 to a surplus amounting to 5.1% in 2023. Such an improvement (by 9.5 percentage points) is without precedent in Hungary over the 28 years since 1995 (the period for which methodically consistent, comparable data is available), but it is also outstanding if compared to the external balance corrections among other EU member states in 2023. This substantial "positive" shift, however, also means that in 2023 the final domestic use as a percentage of GDP dropped nowhere in the EU as sharply as in Hungary. Accordingly, the improvement in the Hungarian external trade balance was entirely based on the fall in imports (by 9.5% in nominal terms and 5.1% in real terms) – exports basically played no part in it. The changes in the other items within the current account had also a relatively marginal effect on the GDP ratios of the important consolidated balances compared to the shift in net export: the 1 percentage point deterioration in net income and the capital account is negligible in comparison with the turn registered in the trade balance. The GDP ratio of the current account changed from -8.3 in 2022 to 0.2% in 2023, the net financing capacity calculated "from above" (that is, the combined balance of current and capital accounts) turned from -6.3% to 1.2%, the net financing capacity calculated "from below" (that is, the financial account balance) went from -9.1% to -1%. The stock of external liabilities as a percentage of GDP climbed 1 percentage point to 47%, with a small decrease in net FDI and a mild increase in the net external debt.

Annual changes in the components of the balance of payments

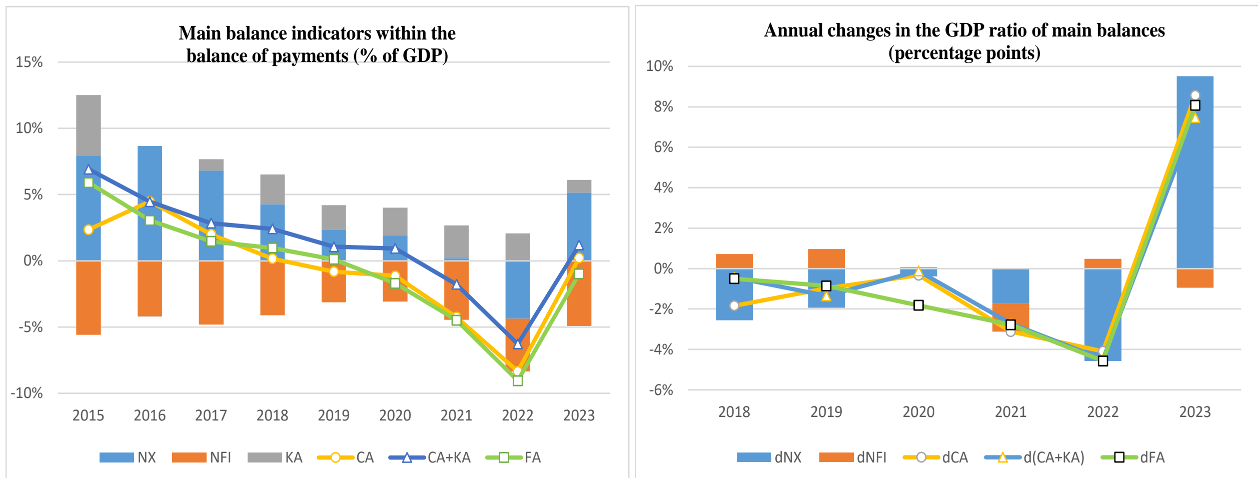
According to the seasonally adjusted data, the two complementary balances of the balance of payments – combined current and capital balance (net financing capacity "from above") and the financial account balance which records the financial flows (net financing capacity "from below") started to improve from the third quarter of 2022. The upward trend halted (if not reversed) toward the end of 2023.



Source: MNB

Hereinafter we will concentrate on annual comparisons, but the chart above amply illustrates that the economic processes tend to disregard the periodizations based on calendar years.

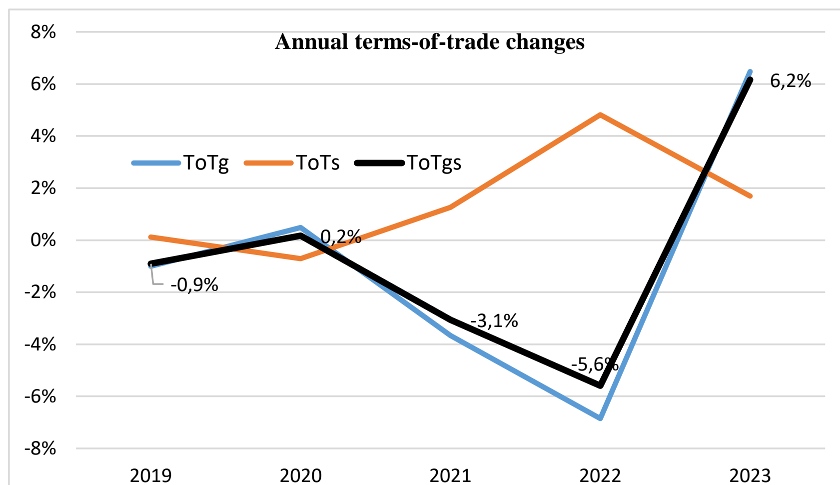
The two charts below show the magnitudes of – and the yearly changes in – the main balance of payment indicators as a percentage of GDP.



Codes: NX: net export; NFI: net (primary and secondary) income; KA: capital account; CA: current account (NX+NFI); FA: financial account; *d:* annual change in the GDP-ratio of the indicator

Source: MNB, CSO, own calculation

As the left-side graph shows, the external balance indicators were deteriorating from 2016 almost without interruption, which was in great part due to the decrease in the trade surplus that in 2022 turned into a substantial deficit, only to reverse back to substantial surplus in 2023. In the last year, the usual deficit in net incomes (primary plus secondary) increased slightly, to 5% of GDP, while the usual capital account surplus decreased (to 1% of GDP: this item includes the transfers from the EU for development purposes). But all these negative shifts were dwarfed by the massive improvement in the trade balance (see the right-hand chart).

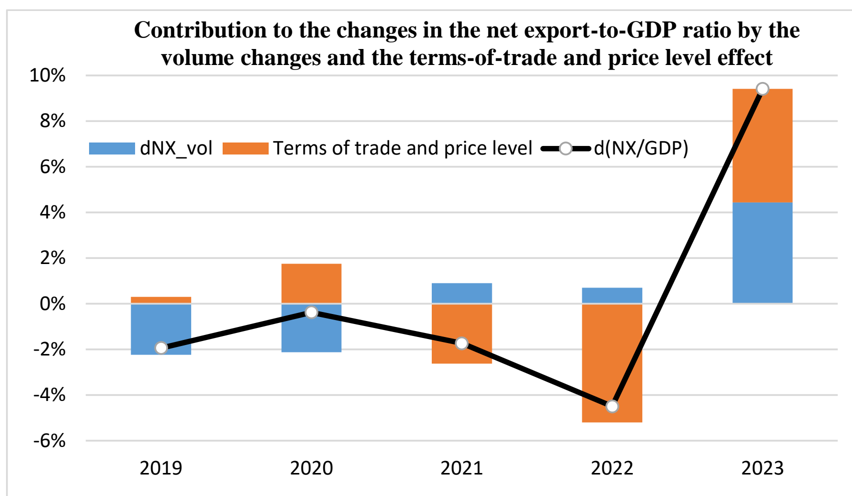


Source: own calculation based on Eurostat data

Codes: ToTg, ToTs, Totgs: terms of trade in the trade of goods, services and total trade, respectively

While the worsening of the trade balance in 2021-2022 had much to do with the terms-of-trade deterioration, the positive turn of the trade balance in 2023 was in great part a result of the terms-of-trade improvement. The chart below shows the yearly terms-of-trade changes between 2019 and 2023. Interestingly, the terms of trade in the trade of services moved in the opposite direction compared to the terms of trade in merchandise trade every year, but the total changes in the terms of trade are dominated by the trade of goods, due to the much greater weight of the latter. And the merchandise trade balance, in turn, is greatly shaped by the price developments regarding energy imports.

The terms of trade started deteriorating in 2021, and the deterioration steeply accelerated in 2022 but took a sharp turn in 2023. The question is: to what degree the relative price movements contributed to the yearly changes in the external trade balance, compared to the trade volume changes? The next chart shows the relative importance of these two factors in the changes in the trade balance as a percentage of GDP.[1]

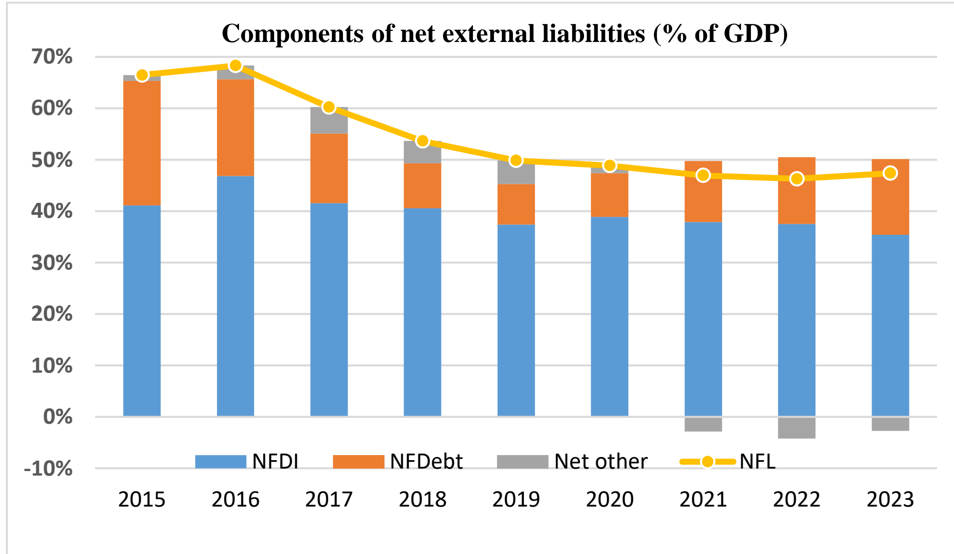


Source: calculation based on CSO data

As can be seen from the chart above, the trade balance deterioration in 2021-22 was primarily driven by the trade-of-terms loss, the impact of which was only marginally cushioned by the opposite volume effect. By contrast, the reversal in 2023, amounting to 9.5% of GDP, was shaped by the relative price and volume effect to an almost identical degree. But the positive volume effect, far from reflecting an improvement in the macroeconomic performance or a strengthening of external trade flows, rather reflects that the volume of import adapted to the steep fall in domestic demand while the volume of export stayed virtually level.

[1] $(X_1 - M_1) - (X_0 - M_0) = \underbrace{[(X_1 - M_1) - \frac{X_1 - M_1}{P_{xm}}]}_{Árszinthatás} + \underbrace{[\left(\frac{X_1}{Px} - \frac{M1}{Pm}\right) - (X_0 - M_0)]}_{Volumenhatás} + \underbrace{[\frac{X_1 - M_1}{P_{xm}} - \left(\frac{X_1}{Px} - \frac{M1}{Pm}\right)]}_{Cserearányhatás}$
where the first member is the price level effect, the second member is the volume effect, and the third member is the term-of-trade effect. *X* denotes exports, *M* denotes imports, the base and reference periods are denoted by *0* and *1*, respectively. The export and import price indices are denoted by *Px* and *Pm*, respectively, while *Pxm* denotes the average of the two price indices.

As regards total *net foreign liabilities* (NFL), there was hardly any change in 2023, but – as the chart below shows – net FDI slightly decreased while net foreign debt (NFdebt) mildly increased, basically offsetting each other.



Source: calculation based on MNB data

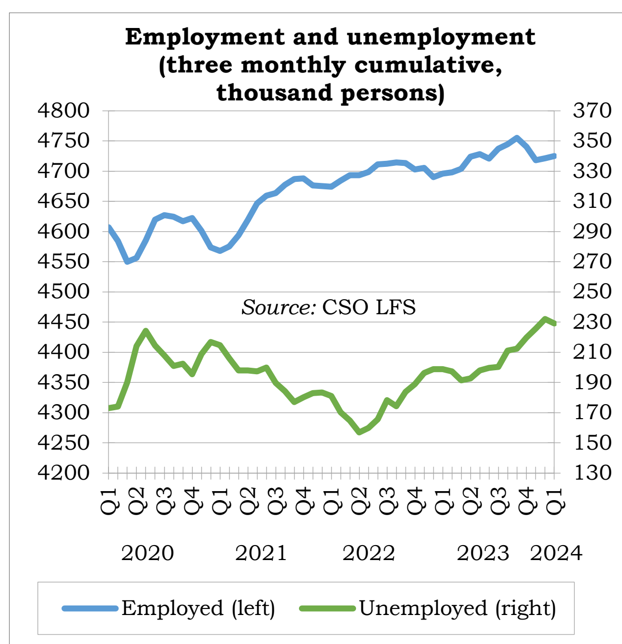
3.4. Employment, unemployment

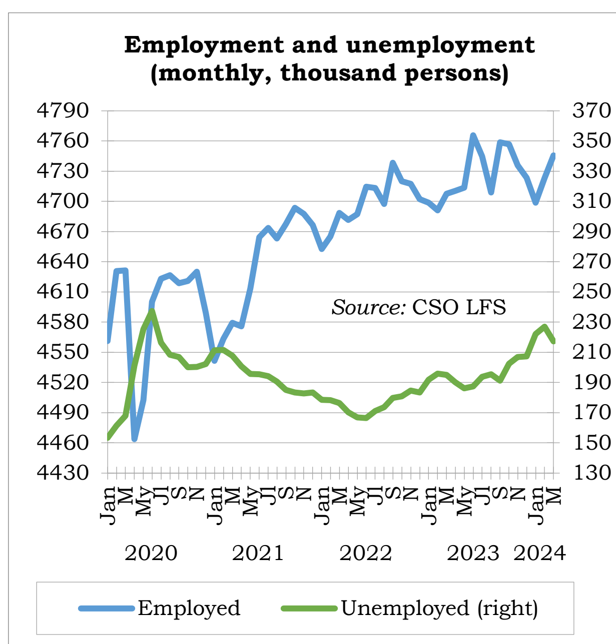
According to the labor force survey (LFS), the employment situation kept improving somewhat in 2023 and at the start of 2024, even though in an increasingly contradictory way. The *number of employed* is still rising: in the last quarter of 2023 and the first quarter of 2024, the respective growth rates were 0.8% and 0.6%. Amid a continuing decline in the number of public workers and a steady rise in the number of those employed abroad, the number of employed on the domestic *primary* labour market is still growing, at a slow pace.

Other indicators, however, suggest that the recession in 2023 has an adverse , even if delayed, impact on the labor market situation. The three-month average *unemployment rate*, after fluctuating between 3.9% and 4.1% for three quarters, started to rise after the third quarter of 2023 and – after peaking at 4.7% in December-February – stood at 4.6% in the first quarter of 2024. The *absolute number* of unemployed has been rising on an annual basis since the second quarter of 2023, with no sign of change. The number of *job vacancies* is slowly decreasing, along with the ratio of vacancies a percentage of the number of unemployed.

At the same time, the number of people in the labor force keeps rising at a good pace, which means that the inflow from inactivity to activity continues. But in 2023 – as opposed to 2022 – the number of economically active rose in greater numbers than the number of employed, that is, the capacity of labor market to absorb the new entrants is on a decrease. This leads to an expansion in the potential labor reserve. It also means that most of the growth in unemployment is still due to the inflow into the labor force, rather than a rise in job losses.

These mixed trends are likely to continue during much of 2024. The number of employed may grow further, but the growth rate will be way below the 0.6% recorded in 2023. The unemployment rate will probably decrease amid the coming revival of economic growth, but the annual average rate will exceed the 2023 level (4.1%).





3.5. Fiscal, monetary and financial developments

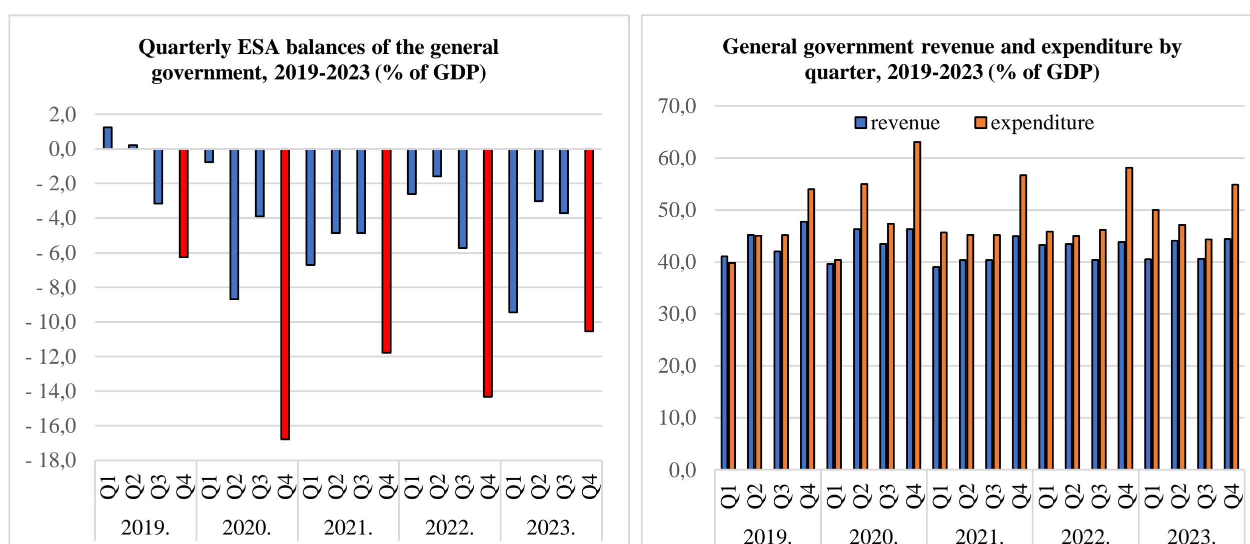
3.5.1. Fiscal developments

Fiscal performance in 2023

The 2023 fiscal budget law, adopted back in June 2022, set the general government deficit target at 3.6% of GDP. During the last year, this deficit target was amended several times, rose to 5.2% by early December 2023, and finally, in a document published on December 30 under the title “Macroeconomic and fiscal projections, 2023-2027”, was set at 5.9%, based on the admission that, as opposed to the earlier growth expectations, the annual GDP growth rate was likely to be minus 0.4%. The actual growth outcome was -0.9% and the ESA deficit amounted to as much as 6.7% of GDP. The central subsystem of the general government closed the year with a cash-flow deficit of HUF 4,593.4 billion, as opposed to the originally envisaged HUF 2,352 billion.

It is true that part of the reason for the deficit reaching almost twice the target was that the (mis-)planned GDP growth did not materialize. The budgetary act was based on the projected GDP growth of 4.1%, an assumption which was already unrealistic in July 2022. On the other hand, it is also true that at the time the target was set the GDP fall of 0.9% was not yet predictable. This **highlights the problem of adopting the budgetary act too early, at a time when the necessary information was still unavailable.**

As the chart below shows, all of the past couple of years saw a massive jump in expenditures in the fourth quarter: the last-quarter deficits have always exceeded 10% of GDP since 2020. In 2023, the fourth-quarter deficit was 10.4%, due to a rise in expenditures to 56% of the fourth-quarter GDP, as opposed to approximately 50% in the previous three quarters. The right-hand chart demonstrates that the elevated deficit was almost exclusively a result of the jump in expenditures in the fourth quarters of the respective years.



Source: CSO, balance of the general government sector, 2023

According to the report of the Ministry of Finance, the budget was burdened with numerous one-off expenditures in 2023, such as the acquisitions of state ownership in

Vodafone Limited, the Hungarian Post Insurance Limited and the Hungarian Post Life Insurance Limited.

The 2024 budget: budgetary plan and forecast

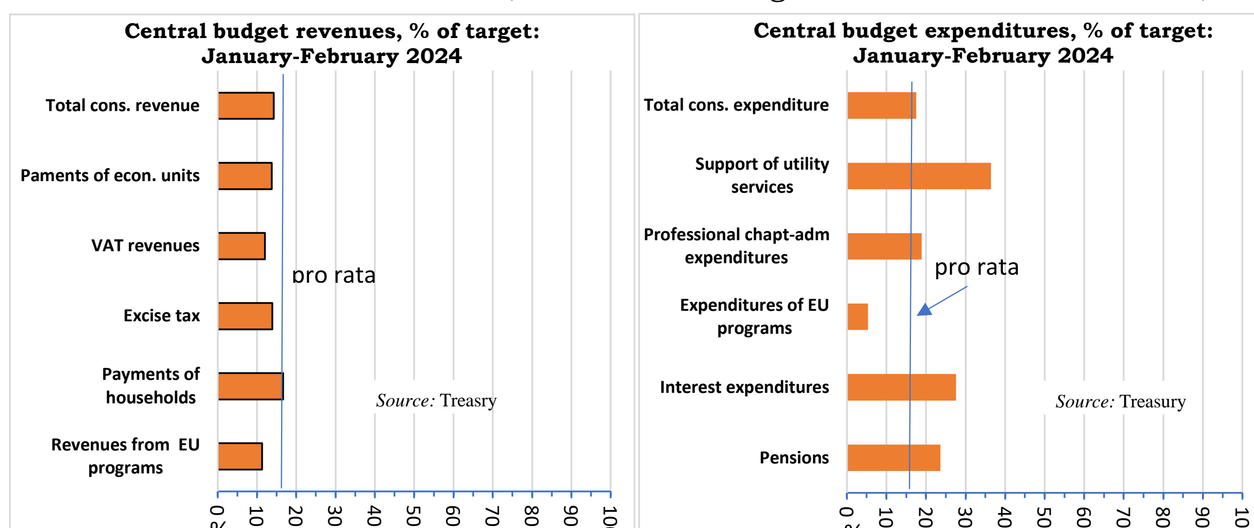
The 2024 budget law, adopted in the summer of 2023, set the deficit target at HUF 2,514 billion, 3.1% of GDP, while the primary deficit target was 0%, with the assumption of an annual GDP growth rate of 4%. But it is known from the announcement by the minister for national economy in March that by now even the government expects only an annual growth rate of 2-3%, as independent forecasters have been predicting for several months, instead of the originally set growth target of 4%.

The cumulative cash-flow deficit in the first two months amounted to HUF 1,704 billion, which is 68% of the annual deficit target. The Ministry of Finance responded to this development by raising the deficit target to **4.5% of GDP** in its February report. If we assume that the nominal GDP projection of the ministry (HUF 81 thousand billion) is correct, this new target implies a deficit of about HUF 4,000 billion. The debt management agency, after adopting this new nominal deficit target, raised its financing plan by about HUF 1,450 billion.

According to the latest report, the cash-flow deficit was HUF 618 billion in March – as a result, the cumulative three-month deficit amounted to HUF 2,321 billion, getting close to the original deficit target for the whole year. Compared to the raised deficit target, the first-quarter deficit reached only 58% of the annual target, but even this interim outcome raises serious doubt about whether the revised deficit target is within reach.

As for the deficit in the first two months, it is outstanding due to one-off – but not unexpected – factors, such as the payment of the 13th-month pension (approx. HUF 500 billion) and the large interest payments in February (HUF 855.4 billion). Neither of these expenditure items could be anticipated, even though not in the summer of 2023, at the time of the original budget plan. Following a multi-year series of prediction fiascos, the government decided not to submit the 2025 budget bill before November 2024, to base the targets on better macroeconomic projections and achieve better revenue and expenditure planning.

The February report by the ministry of finance attributes a part of the very high deficit to the fluctuation of the VAT revenues, saying that a significant VAT inflow was recorded in March. That is true but even so, it is disconcerting that in the first two months, the



nominal VAT revenues were even smaller than in the same period of the previous year, despite the higher price level. As for March, the monthly VAT revenue amounted to a relatively healthy level of HUF 618 billion, which makes the HUF 617 billion monthly deficit hard to explain. The 2024 budget envisaged a 23% (!) rise in VAT revenues, which was implausible to begin with and was inconsistent with the GDP and consumption growth projections (even if assuming a GDP growth of 4%). In the first two months of 2024 excise tax revenues trailed expectations as well, despite the substantial raise in the excise tax on fuels.

At the same time, interest expenditures also exceeded the plan: they amounted to HUF 855 billion in the first two months. In the EDP report, the new gross interest payment projection is HUF 3,951 billion – much higher than the originally envisaged HUF 3,100 billion – which amounts to 4.8% percent of the expected GDP. The net interest cost is expected to reach 4.1% of GDP, as indicated by the debt management agency.

The expenditures on professional chapter-administered appropriations amounted to HUF 730.5 billion in January-February, a 50% growth compared to the same period of 2023. The non-refundable grants paid from the tourism target appropriation were **HUF 72 billion** – this is more than the sum paid in the whole year of 2023, which indicates the revival of free tourism subsidies. Before 2023, the yearly amount exceeded HUF 100 billion.

During the remaining 9 months of the year, the cumulated deficit should not exceed HUF 1,700 billion to meet the yearly HUF 4,000 billion target, even though the first-quarter deficit alone reached HUF 2,300 billion. At the moment, neither one-off revenue items nor an expected downward turn in expenditure items guarantee makes such a feat realistic. The yearly VAT revenues will fall HUF 1,000 billion short of the implausibly bloated target even if household consumption gains momentum during the rest of the year, due to the rise in real wages (which cannot be taken for granted, based on the January-February retail data). This, and the HUF 800 billion rise in interest expenditures point toward **a fiscal deficit of 5.5-6%**, even if this time the government abstains from the year-end binge-spending seen regularly in recent years. But if spending gets out of control again toward the end of the year, the annual deficit can easily exceed 6% of GDP, as was the case in 2023.

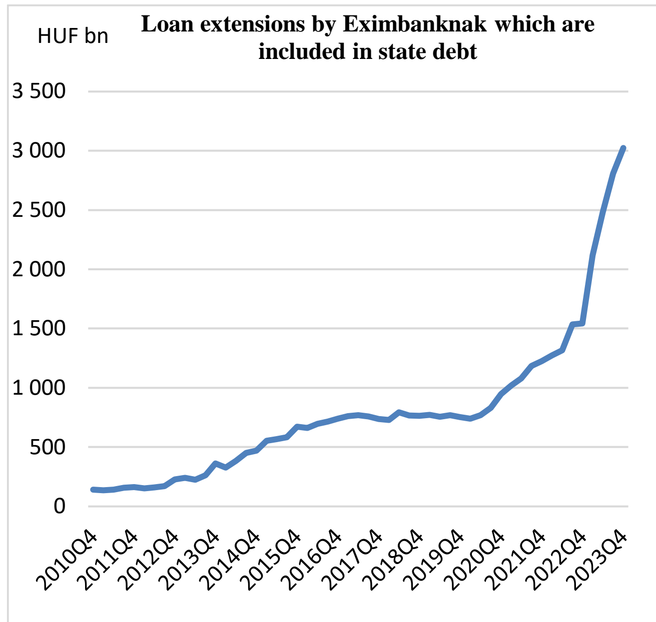
Fiscal debt

The **gross debt of the general government** (including the Eximbank) rose by HUF 6,300 billion in 2023 and exceeded HUF 55 thousand billion, according to the MNB. The GDP ratio of the fiscal debt eased to 73.5% by the end of the year.

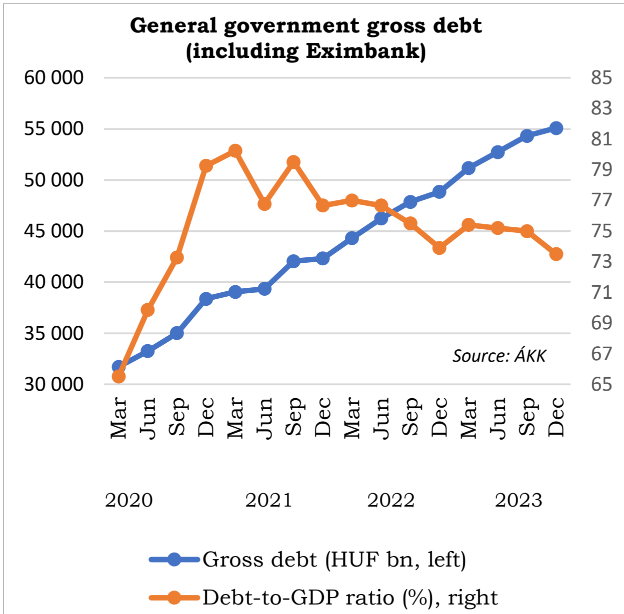
If calculated without the Eximbank, the debt amounted to HUF 52.1 thousand billion. The gap between the two data series has been growing for years but 2023 saw a particularly sharp increase in debt incurred by the Eximbank. The Eximbank debt became a part of the overall fiscal debt in 2018 since according to the Eurostat assessment, the state-owned Eximbank conducts lending activities on behalf of the Hungarian state.

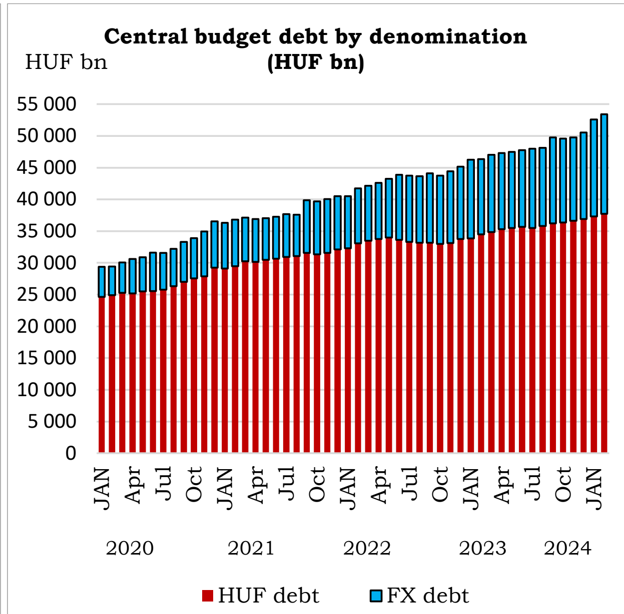
Our calculations based on MNB data suggest that the stock of outstanding loans by the Eximbank surged from HUF 1,500 billion at the end of 2022 above HUF 3 thousand billion, reaching 4% of GDP, by the end of 2023.

By the end of February 2024, nominal debt exceeded HUF 53.7 thousand billion, (without Eximbank), a year-on-year increase of HUF 7,000 billion. To this increase, the appreciation of the outstanding FX debt, due to the weakening of the forint, contributed by HUF 450 billion.



The share of FX-denominated debt within the overall debt rose to 29.2% by the end of February, getting very close to the ceiling that was raised to 30% in 2023 by the debt management agency (ÁKK). The ÁKK indicated that it has no intention to raise the ceiling further – instead, it wants to meet the increased financing needs by rebalancing the individual currency denominations and various types of securities. By the end of 2024, the government plans to reduce the debt-to-GDP ratio minimally to 73.2% of GDP. But even this marginal reduction is at risk, primarily because the growth in nominal debt may well exceed the projection, but the growth in nominal GDP may also fall short of expectations.





3.5.2. Inflation

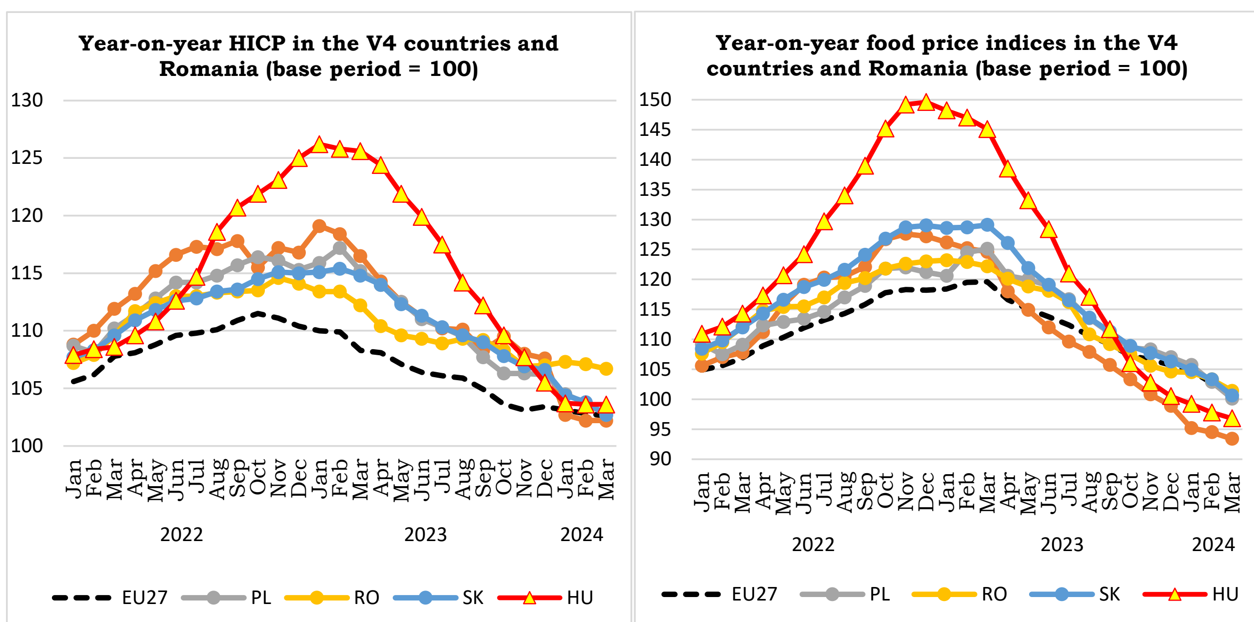
Consumer prices grew by 17.6% in 2023 on an annual basis. The monthly year-on-year inflation rates steadily decelerated over the year, from 26% in January to just 5.5% in December.

Food prices were up 25.9%, household energy prices climbed 22.1%, while the prices of other goods and motor fuels rose by 18.6% in 2023. The annual average price hike was 15.4% for alcoholic and tobacco products and 13.2% for services, but the price index was lower in the case of clothing (8.3%) and consumer durables (5.6%).

With such indexes, the Hungarian inflation rate was high above the other EU member states and substantially exceeded the inflation rates recorded in the other CEEs as well. On average, the annual price level was up 6.4% in the EU, 10-12% in the other Visegrad countries and below 10% in Romania.

But toward the end of the year, the gap between the year-on-year price index of Hungary and the other V4 countries closed, due to the continuing disinflation – in the first months of 2024, the monthly Hungarian year-on-year inflation rates even dipped below the levels seen in some Visegrad countries. This is especially true of food prices, where the Hungarian price index was lower than in most V4 countries, and even dipped below the EU average, from November 2023.

It is important to note, however, that while the year-on-year price indices are now lower than in many other countries, that does not compensate for the consequences of the skyrocketing price indices in the preceding period. The low price indices seen recently are added to the high indices recorded previously. The outstanding inflation rates during 2022-2023 elevated the majority of the Hungarian consumer prices above the levels seen in the other countries of the region, and this relative position will not change easily, even if the price of some consumer goods is slightly decreasing now. To return to the relative price levels seen before the inflationary wave, prices should fall to such a degree which is simply not in the cards. As a result, the Hungarian price level is now well above the level that would be warranted based on our level of economic development, which may



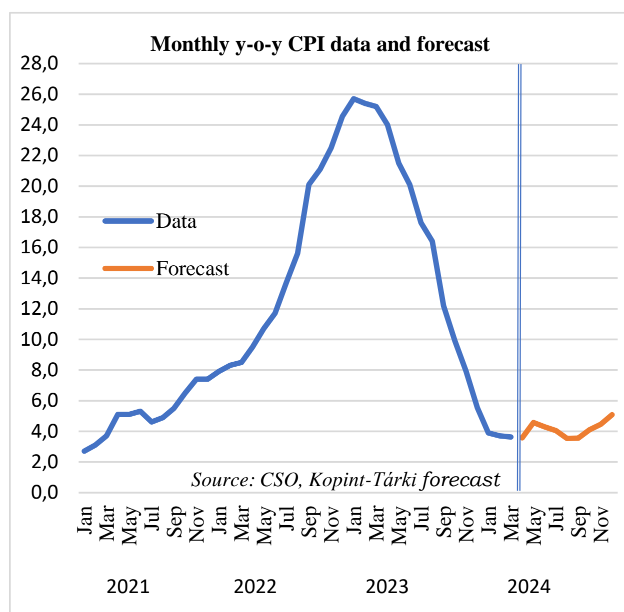
even reduce our purchasing power parity denominated per-capita GDP, although the latter is affected by the GDP deflator and the exchange rate developments as well.

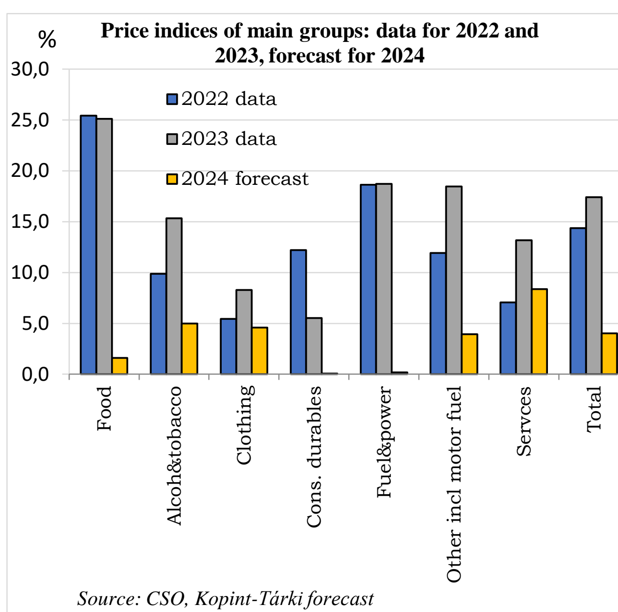
In the first months of 2024, the annual price index dropped from 5.5% last December to 3.8% in January, 3.7% in February and 3.6% in March. Food prices rose at an even slower pace (by an average of 2.2% in January-March), and the prices of many food products even decreased – both on an annual and monthly basis – especially the ones that underwent the steepest price hikes during 2022 and 2023 (dairy products, egg, certain meat products).

At the same time, the price index of services remained high (in March, 9.9% year-on-year and 1.8% month-on-month). It is likely to remain above the average inflation rate during the year since services are the area where the impact of wage growth is the most pronounced. Besides, the services sector is especially characterized by oligopolistic structures that make it possible for the service providers to raise prices.

We expect an annual **inflation of 1-1.5%** for 2024, provided that there will be no such fiscal stabilization measures that could cause a rise in prices, directly or indirectly. Even if some raises in the regulated prices – or some other state measures that may have price-increasing effects – are possible, they are likely to happen in the second half of the year, thus the bulk of their price effects will be felt in 2025, rather than in 2024.

The inflation trajectory probably will not be linear within the year. The year-on-year index may drop to near 3% in mid-year, but it may rise again to levels around 5% by the end of the year, mostly due to the statistical base effect.





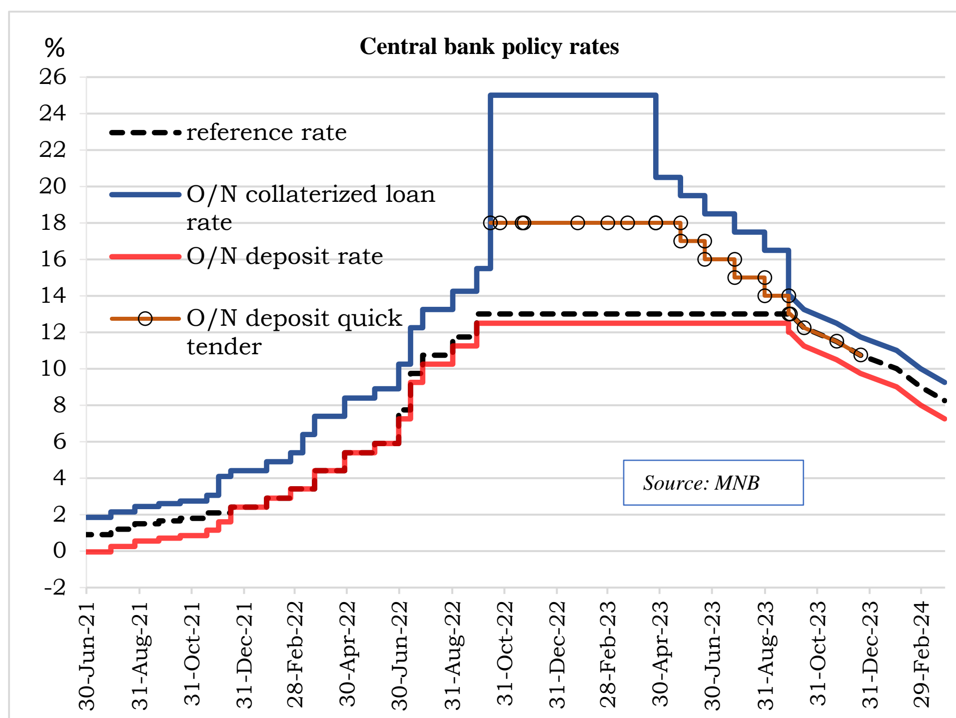
3.5.3. Financial and capital markets

Central bank interest rates and exchange rate developments

As inflation began to gradually decrease, the **central bank** also started reducing the **effective policy rate** (the overnight deposit quick tender rate) in May 2023 from 18%, a record level reached after the last rate hike in October 2022. With monthly rate cuts by 100 basis points, the O/N deposit quick tender rate reached the level of the official reference rate (13%) in September 2023, and from then, the reference rate regained its key instrument status. From then, the reduction of the reference rate began, with monthly cuts of 75-100 basis points. The reference rate dropped to 8.25% by March 2024, after which a smaller cut of 50 basis points – to 7.75% – was implemented in April. The interest rate related to required reserves has remained aligned with the reference rate.

The reduction of the O/N deposit rate and the rate on the O/N loan kept pace with the reference rate cuts. The interest rate corridor remains relatively narrow (± 100 bps) and symmetric.

Based on our inflation forecast – an annual rate of 4-5% in 2024 – the 7.75% reference rate is still high enough to provide a high real interest rate, therefore further rate cuts are likely during the rest of the year. The central bank indicated in March that a new phase of the rate cut cycle was to begin in April. We expect the continuation of monthly rate cuts of 50-75 basis points in the second quarter, which may be replaced from July by a regime of monthly rate cuts of only 20-75 basis points. As a result, the reference rate may drop to 6.5-7% by the middle of the year and **5.5%** (± 0.5%) **by the end of 2024**. Based on our prediction of about a 5% rate of inflation in December 2024, even this year-end reference rate ensures some degree of real yield. Considering the forward-looking inflation rates, the real interest rate will be higher because the annual inflation

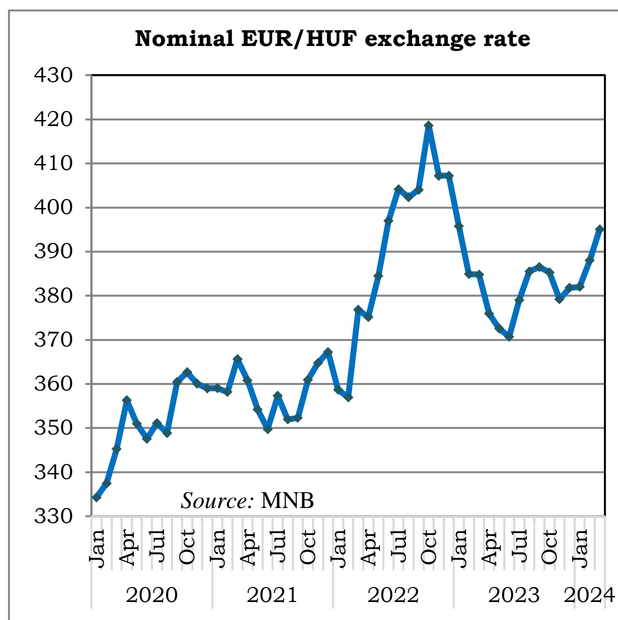


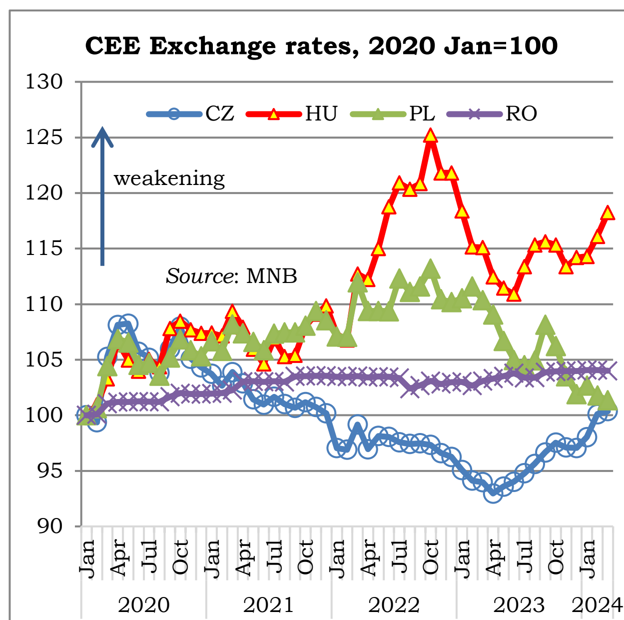
rate is expected to drop near 3% during the first half of 2025. This will provide some room for some further rate cuts in 2025.

The **exchange rate** of the forint was relatively stable during most of the last year – the forint even appreciated somewhat against the euro. At the end of 2023, the bilateral exchange rate stood at 382.78 EUR/HUF, as opposed to the 400 EUR/HUF at the end of 2022. The exchange rate mostly remained within the 370-390 band. This means that the rate cut cycle did not precipitate such a flight of speculative capital that could noticeably weaken the forint.

Still, the longer-term exchange rate trend remained less favorable in Hungary than in the surrounding countries. The exchange rate trajectories differed considerably in the past year within the region. The Polish zloty showed a strengthening tendency in 2023 – although interspersed by interruptions, and its exchange rate in March 2024 was almost identical to the level seen in January 2020. The Czech koruna weakened in the past year but even after this weakening, the koruna exchange rate was close to its January 2020 level – that is, the pre-COVID level – due to the preceding period of appreciation during 2021-2022. The stability of the Romanian leu was ensured by the continuous central bank interventions, enabled by the high level of central bank reserves. Only the Hungarian forint remained much weaker than at the beginning of 2020. What is more, the bilateral exchange rate has tended to weaken again since July 2023.

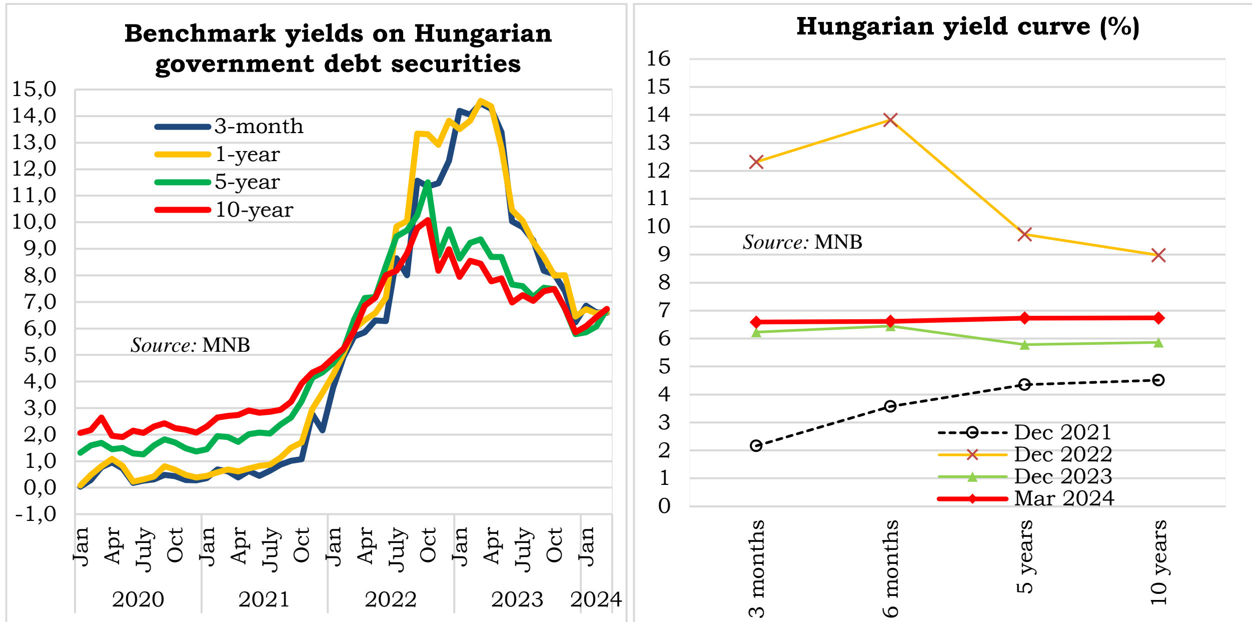
The first three months of 2024 were characterized by a weakening trend, amid hectic daily and weekly gyrations. By early April, the exchange rate got close to 400 EUR/HUF but has not crossed that psychological line. But eventually, it will happen during this year, which also follows from the fact that the drastic difference between the Hungarian and the other regional inflation rates – to the expense of Hungary – resulted in a substantial relative strengthening of the real exchange rate of the forint that undermines the price competitiveness of Hungarian exporting firms.





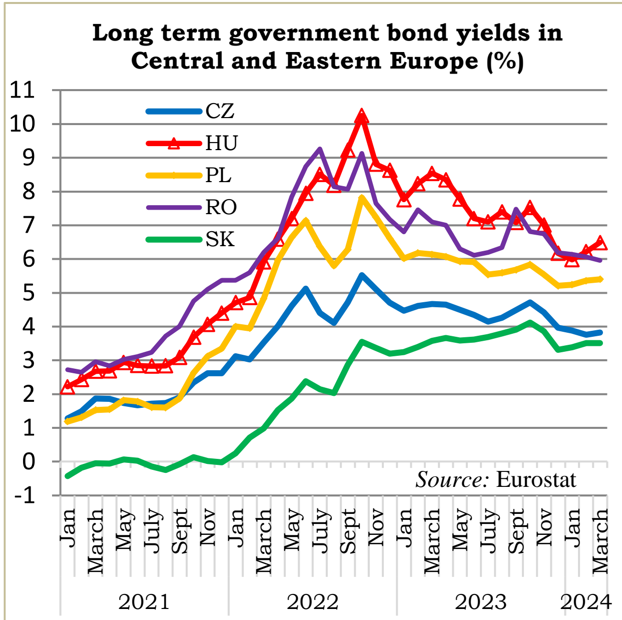
Government security yields and lending rates

After a period of steep rise between October 2022 and March 2023, government **benchmark yields** started to decrease on every maturity. The preceding rise was especially steep in the case of shorter maturities but after that, short yields dropped at a faster rate as well. This conforms with the typical pattern of *yield curve shift* during the descending phase of an inflationary wave.



It is noteworthy that by the end of 2023, the difference between the yields on various maturities became negligible: on every maturity, the yield was close to 6%. In the first three months of 2024, yields slightly rose again, and the yield curve became even flatter: the yields on various maturities were within the very narrow band of 6.59% (3-month yield) and 6.79% (3-year yield), an extremely rare phenomenon.

In regional comparison, the yield ranking has changed only slightly during the last year. In the past couple of years, the Hungarian and Romanian long yields were taking turns to have the dubious distinction of having the highest long yield within the region. In the first two months of this year, the two countries were head-to-head with their very high 10-year yields (above 6%), going through almost identical. In March, on the other hand, the Hungarian rate rose, breaking away from the Romanian rate. The Polish, Czech and Slovakian yields have also followed the general (downward) trend, and the 10-year yields of the latter two countries have dipped below 4%.



Corporate and household interest rates

The ongoing reduction in the central bank reference rate and the decrease in the benchmark rates had only a limited impact on the **interest rates of forint-denominated corporate and household loans**.

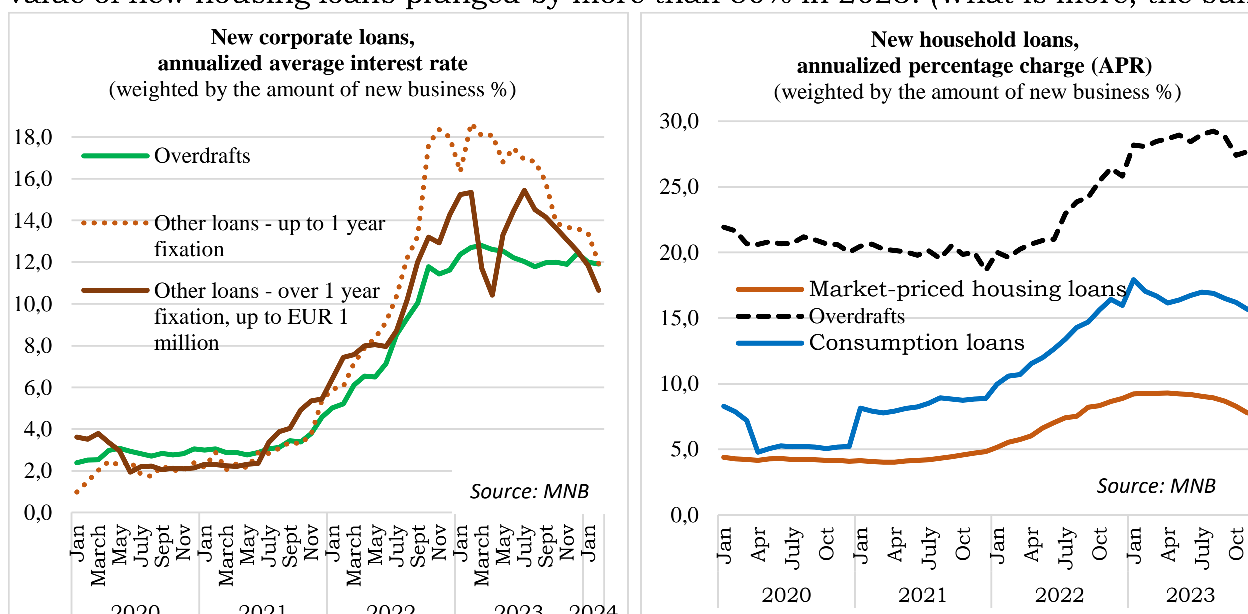
Business lending rates peaked in early 2023 and have gradually moderated afterwards. The interest rate of corporate *overdraft loans*, the most important interest rate regarding working capital financing, did not decrease during 2023, however: it hovered around 12% and even in early 2024, it remained just barely below the expected interest rate ceiling (12% for working capital loans). The voluntary interest rate ceiling was introduced by the banks on the 9th of October 2023 for corporate working capital loans and the new housing loans. Under the agreement, overdraft loan rates should have dropped below 10% from January 1 2024, but this drop has not materialized.

The interest rate of the *other business loans* was more volatile. The rate of loans with up to 1 year fixation was above 18% during 2023 but dropped below 12% by February 2024. Within that category, the interest rate of the loans under EUR 1 million has moderated to a level near 10%.

The APR of *consumption loans* to **households** has been on a decrease from early 2023, with minor interruptions, and dipped to 15% by January-February 2024. The APR of household *overdrafts* almost reached 30% in 2023 and it stood at 25% even in February 2024.

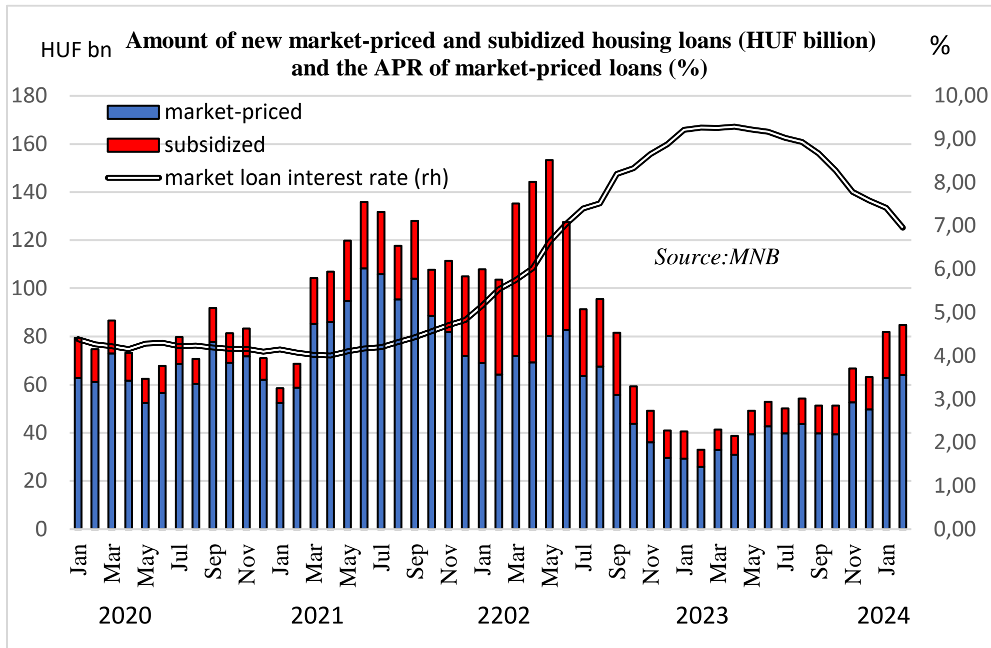
The APR of non-subsidized (market-priced) *housing loans* declined from 9.22% in January 2023 to 6.96% in February 2024. This means that in the case of new housing loans, the voluntary pledge of the banks not to let the APR increase above 8.5% – and from January 1- 2024, above 7.3% – was observed. At the same time, the APR of subsidized housing loans decreased as well from 15% in early 2023 to 10.66% in February 2024 – here, the bulk of the interest costs is borne by the state.

The government and the banks hope that the moderation of housing lending rates will lead to a surge in housing borrowing. The high APR of housing loans (nearly 10% in much of the last year) led to a drop in the demand for housing loans and the nominal value of new housing loans plunged by more than 50% in 2023. (What is more, the sum



of new housing loans provided for building or renovating purposes was barely above 20% of its 2022 level in the last year.)

Housing borrowing gained momentum in the first months of 2024. But even in February, 70% of these new loans still financed purchases of used dwellings. (True, this rate was as high as 76% at the end of 2023.) Still, the elevated demand for housing loans suggests that 2024 will be a better year than the previous one.



Economic Indicators 2016-2023, forecast 2024-2025 (percentage change)

	2016	2017	2018	2019	2020	2021	2022	2023	2024*	2025*
GDP AGGREGATES, ANNUAL REAL GROWTH										
GDP total	2.2	4.3	5.4	4.9	-4.5	7.1	4.6	-0.9	2.5	3.2
Domestic Demand	1.8	5.7	7.1	7.1	-2.6	6.3	4.1	-5.6	2.7	3.1
Private Consumption	4.1	4.5	4.1	4.5	-1.8	4.0	6.8	-1.0	2.8	3.2
Public Consumption	0.5	3.8	4.3	9.5	4.2	2.5	0.8	-1.5	0.5	0.5
Gross Capital Formation	-3.5	10.1	15.9	12.0	-6.8	12.9	0.3	-14.9	3.6	4.0
of which: Fixed Capital Formation	-10.6	19.7	16.3	12.8	-7.1	5.7	1.4	-7.4	2.2	4.5
Export	3.8	6.5	5.0	5.4	-6.1	8.3	11.4	0.9	0.9	4.3
Import	3.5	8.4	7.0	8.2	-3.9	7.3	10.8	-4.3	1.1	4.2
PRODUCTION INDICES										
Agricultural Production (gross)	9.4	-4.1	2.6	-0.1	-2.4	-1.1	-16.5	25.2	0.0	0.0
Industrial Production	0.9	4.6	3.5	5.6	-6.0	9.5	6.1	-5.5	1.7	5.3
Retail Trade Volume	4.8	5.6	6.7	6.3	-0.1	3.7	5.0	-7.8	2.6	3.0
EMPLOYMENT, EARNINGS										
Number of Employed	3.4	1.5	1.3	0.8	-0.9	0.7	1.3	0.6	0.4	0.5
Unemployment Rate	5.0	4.0	3.6	3.3	4.1	4.1	3.6	4.1	4.3	3.7
Gross Nominal Wages [a]	6.1	12.9	11.3	11.3	9.8	8.9	17.4	14.2	13.5	8.0
Net Real Wages [a]	7.4	10.3	8.3	7.6	6.3	3.6	2.5	-2.9	8.8	4.3
PRICES, EXCHANGE RATES										
Consumer Price Index	0.4	2.4	2.8	3.4	3.3	5.1	14.5	17.6	4.3	3.5
EUR/HUF Exchange Rate (annual average)	311	309	319	325	351	359	391	382	390	390
EUR/USD Exchange Rate (annual average)	1.11	1.13	1.18	1.12	1.14	1.18	1.05	1.08	1.08	1.08
Short-term Interest Rates (3M), eop	0.06	-0.01	0.00	-0.01	0.28	2.16	12.32	6.2	5.5	4.5
Long-term Interest Rates (10Y), eop	3.16	2.02	3.01	2.01	2.08	4.51	8.98	7.0	6.0	5.5
BALANCE OF PAYMENTS										
Current and Capital Accounts, % of GDP	4.5	2.8	2.4	1.1	0.9	-1.8	-6.4	1.2	1.9	1.9
GOVERNMENT BUDGET										
General Government Balance, ESA-95, % of GDP	-1.8	-2.5	-2.1	-2.0	-7.6	-7.2	-6.2	-6.7	-5.5	-5.0
Gross Government Debt, % of GDP [b]	74.9	72.1	69.1	65.3	79.3	76.7	74.1	73.5	73.2	72.5

a As of 2019, the data encompass all employers; as for the preceding years, only the enterprises employing at least 5 persons, budgetary institutions and the non-profit organizations that are significant in terms of employment are included.

b Including the balance sheet of Eximbank

* Kopint-Tárki forecast

Source: CSO, MNB

Contents

I. The World Economy 5
II. The EU13 Countries 9
III. The Hungarian Economy 16
The impact of the terms-of-trade shifts on real gross domestic income between 2021 and 2023 18
3.1. The GDP and its components 20
3.2. Production of GDP 24
3.2.1. Industry 24
3.2.2. Construction 26
3.2.3. Housing construction 27
3.3. The final use of GDP 28
3.3.1. Household income, consumption and saving 28
3.3.2. Investments 30
3.3.3. External trade 32
3.3.4. Balance of payments and the net external liabilities in 2023 33
3.4. Employment, unemployment 36
3.5. Fiscal, monetary and financial developments 38
3.5.1. Fiscal developments 38
3.5.2. Inflation 42
3.5.3. Financial and capital markets 44
Central bank interest rates and exchange rate developments 44
Government security yields and lending rates 46
Corporate and household interest rates 47