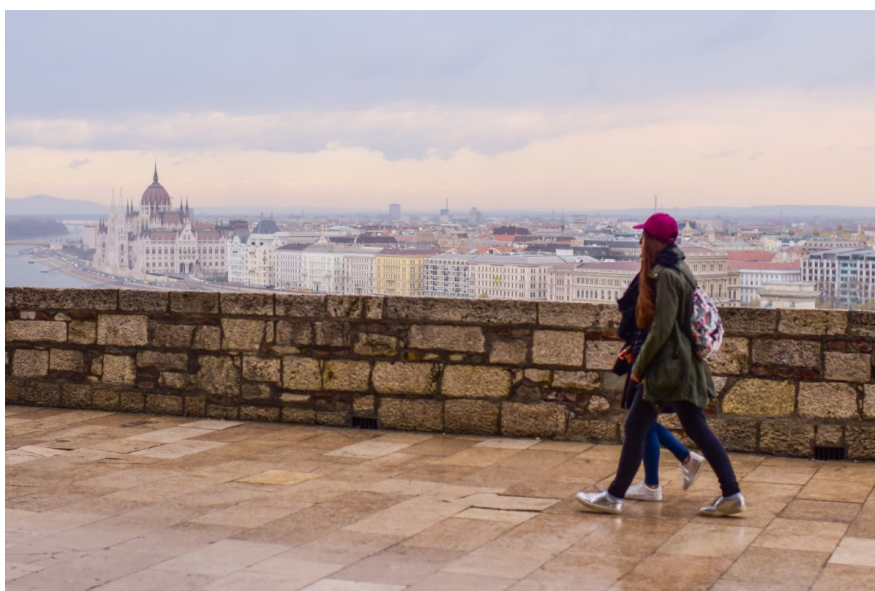


Hungary's mixed outlook offers a few glimmers of hope

Industrial and retail data for February upheld the mixed picture we've been seeing lately for Hungary. With no signs of an imminent turnaround for industry, we think it'll prove a drag on the country's economy as a whole this year. On a more positive note, we're retaining some hope for retail sales to make a solid recovery



February's data wasn't too encouraging, but we think retail sales could still pull through this year

The Hungarian Central Statistical Office (HCSO) has released retail sales and industrial production figures for February. The retail data showed a disappointing decline after the rebound in January, suggesting that this was due to one-off factors rather than a real turnaround. However, we still expect retail sales to perform better this year than in previous years. Still, industry remains a drag, with neither global nor domestic trends showing a positive outlook and the expected start-up of new export capacity continuing to be delayed.

-8.0%

Industrial production (YoY, wda)

ING estimate: -6.6% / Previous: -3.9%

Lower than expected

Industry remains a drag on the Hungarian economy

We saw some growth in industrial production in January, but we pointed out at the time that the recovery from the slowdown at the start of the year tends to be more dynamic than this. And this weak momentum was reflected in February's industrial production data. On a monthly basis (seasonally and working day adjusted), the volume of production fell by 1.3%. This completely wiped out the improvement seen in January, so the overall picture remains rather gloomy. This is all the more true given that we had the gloomiest forecast in the market and industrial production in February was lower than even we had predicted. Compared with the average monthly output in 2021, industrial production volumes are now 7.1% behind. The last time industrial production was this low was in 2020 due to Covid closures.

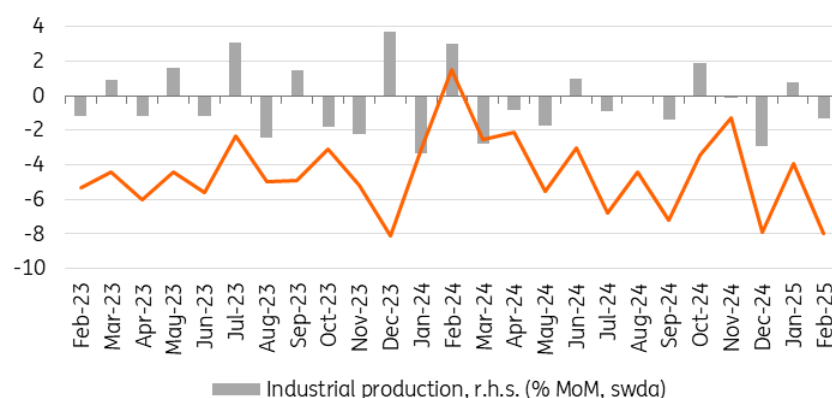
Volume of industrial production



Source: HCSO, ING

The detailed data is yet to be seen, but the preliminary data published by the HSCO illustrates perfectly that the Hungarian industry can only show a positive performance these days if there is a one-off positive surge in the smaller sectors. The most important sectors, such as transport and electrical equipment manufacturing, are still in the doldrums. However, not only here but in all manufacturing sub-sectors, production volumes fell in February this year compared to the previous month.

Performance of Hungarian industry



Source: HCSO, ING

With a significant proportion of manufacturers continuing to hoard labour, a series of weak industrial performance is bringing us closer to the breaking point – where companies will decide that it is simply no longer worthwhile and too costly to hoard labour. After two years of downturn, 2025 does not yet look like the year when Hungarian industry will emerge from the doldrums. We'd argue that it doesn't even look as though the bottom has been reached.

The Trump-induced change in the world trade regime also creates further major uncertainties. Unsurprisingly, the employment outlook component of the industrial confidence index has been in negative territory for three months now, meaning that more and more companies may be considering layoffs.

Perceptions of order books are also deteriorating. Unsurprisingly, in the latest (January) release of detailed industrial data, the HCSO indicated that total order books had fallen by 13.6% on an annual basis, again showing a downward trend. This reality continues to be completely contradicted by the latest Hungarian manufacturing PMI, which remains in expansionary territory above 50. The reliability of this indicator remains highly questionable; it could also be said that it has no meaningful significance.

Looking ahead, it is difficult to see a turnaround in industry. Even before the tariff war, industrial production was not picking up enough to replenish stocks and avoid tariffs. This highlights the weakness in global demand for industrial goods. The inventory cycle has yet to turn, and tariffs may delay it further.

All in all, the outlook for export-oriented sectors has deteriorated recently, and if the tariff war really does intensify – which is the direction things seem to be heading – this could ultimately have a negative impact on global trade. Of course, the start-up of new export capacity in Hungary for cars and electric vehicle (EV) batteries will be a one-off effect, but it is very likely that the external environment will push back the start-up of this productive capacity from this year to 2026.

The domestic industrial sectors can hope that consumption growth will be maintained and that this will bring some trend expansion, although the trend in domestic order books doesn't look encouraging. But even if there is some recovery here, the dominance of the export sector will

make it a mere drop in the 'industrial' ocean, and overall, industry could drag down the performance of the Hungarian economy in 2025.

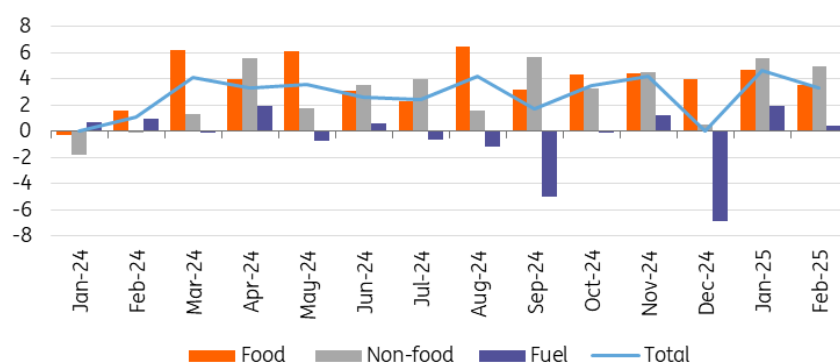
3.3% Volume of retail sales (YoY, wda)
ING estimate: 3.9% / Previous: 4.7%

Hungary's retail sales correct after surge at the start of the year

After a strong rebound in January, retail sales were again somewhat disappointing. According to HCSO data, the sector contracted by 0.6% month-on-month in February. This was accompanied by a significant decline in the year-on-year index, on top of last year's relatively high base. Accordingly, the (adjusted) index for February is 3.3%. This means that the correction was stronger than the market consensus, i.e., a negative surprise.

It's still difficult to draw meaningful conclusions from one or two months of data, but for the time being, it seems that the sector's ongoing growth trend is likely to remain fairly moderate, even after the jump seen in January. The fixed index has deteriorated in line with the monthly performance, meaning that sales volumes are now only 1.3% above the monthly average for 2021, essentially reflecting the sales volumes that were typical towards the end of 2022.

Breakdown of retail sales (% YoY, wda)



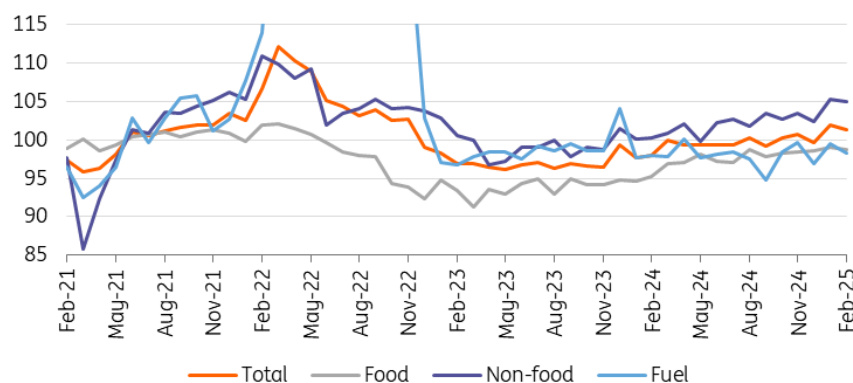
Source: HCSO, ING

Looking at the details, one or two small things are worth pointing out. Food sales fell in February compared with January, which could well be the result of much higher food prices. In addition, non-food retail sales show a minimal month-on-month decline after a surge in January. The one-off payments (such as coupon payments from retail bonds) to which households continued to have access in February (e.g., more payments) seem to no longer have affected this retail segment.

On a month-on-month basis, only pharmaceuticals and cosmetics recorded a significant increase in turnover, which may be mainly related to the strong flu season. Furniture and electrical goods,

textiles, and industrial goods stores recorded more serious declines. In other words, it really does seem that the big jump in January was triggered by the redemption and coupon payment of retail government bonds rather than a sustained turnaround in consumer spending. And given the general rise in fuel prices in February, it is hardly surprising that there was a correction in fuel sales, which fell by more than 1% month-on-month.

Retail sales volume in detail (2021 = 100%)



Source: HCSO, ING

What seems certain for the time being is that January's strong figure was due to one-off factors rather than a lasting turnaround. Nevertheless, the overall performance in the first quarter could still be positive, so consumption is likely to make a positive contribution to Hungary's economic performance. This is more than can be said for industry, which will clearly be a drag on growth. In the next month or two, we may see a more pronounced expansion in retail sales, as government bond payments may provide a further boost. Price curbs on some basic food items from the second half of March to the end of May alone could also boost retail sales as people try to stock up on cheaper food.

We could see this momentum could fade by the middle of the year, however, especially if real wage growth is significantly lower than expected. While January's data was encouraging, we are likely to see a further erosion of purchasing power in the coming months. This is partly due to high inflation and a slowdown in wage outflows. However, government measures coming into force towards the end of the year (changes to PIT for mothers, increase in family tax allowance, etc.) could provide a further boost to the sector. In the light of the past two years, we can therefore expect a much more positive year for retail in 2025. We still expect average annual growth of around 4-5%.

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