Hungary: Warning on growth

The advance GDP growth estimate remained unchanged at 4.5% year-on-year in the fourth quarter, with domestic demand rising and net exports plunging. Still, the coronavirus outbreak means that the risks are clearly and significantly tilted to the downside

Source: Shutterstock

4.5%

GDP growth (YoY)

Consensus 4.5% / Previous 5.0%

As expected

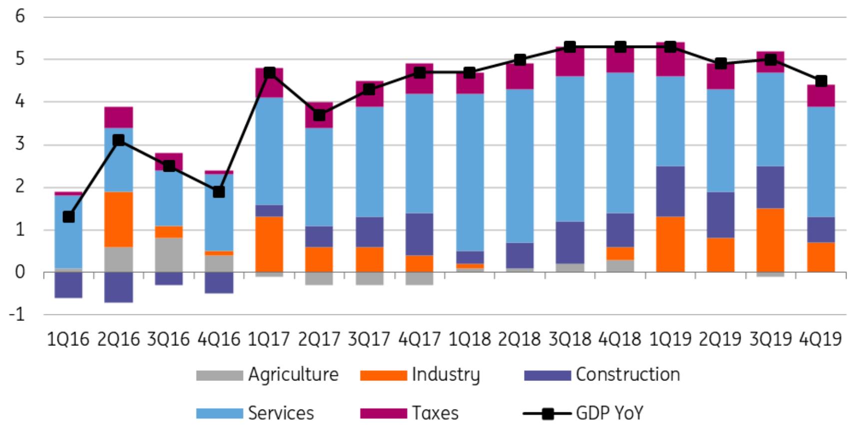
Services rule on the production side

The first estimate made by the Hungarian Central Statistical Office (HCSO) remained unchanged at 4.5% YoY. This is a continuation of the mild slowdown that started in mid-2018 but remains a robust figure in every respect.

On the production side, the value added of services increased at the fastest pace since end-2018, rising 4.6% YoY. The uptick was expected on the back of the strong labour market metrics and the high frequency data seen in retail sales. In line with this, services provided 2.6 percentage points to GDP growth in the fourth quarter, remaining the single most important sector. The fourth quarter GDP data came in above expectations, with the surprise factor coming from industry and construction. Value added growth in industry slowed, but less than expected, up 3.2% YoY. The slowdown was caused mainly by a drop in demand related to the car industry.

Construction was expected to show a weaker performance, yet it was still stronger than we anticipated on the monthly output data. The 11.3% YoY increase in the fourth quarter is the lowest since 2016, as huge EU-funded projects are running out and the majority of capacity enhancements in industry have ended. Industry and construction helped GDP growth by 0.7 and 0.6ppt, respectively. The balance of taxes and subsidies remained in positive territory (0.5ppt) due to better economic activity and the retreat of the shadow economy. The only sector without a positive contribution in the fourth quarter was agriculture.

Contributions to GDP growth – production side (% YoY)



Source: HCSO, ING

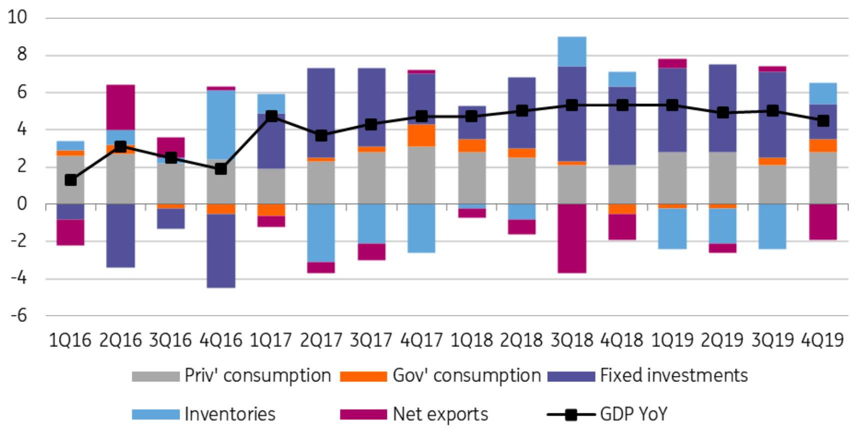
Net exports are huge drag on the expenditure side

On the expenditure side, the main driver behind GDP growth remained domestic use (actual final consumption and gross capital formation), which added 6.5ppt to economic activity. It is a significant increase from a quarter ago, and it is mainly due to consumption. Social transfers rose significantly on a yearly basis while household consumption also accelerated by 0.4ppt to 5.4% YoY. Actual final government consumption increased by 7% YoY, matching the highest reading in two years. Against this backdrop, it hardly comes as a surprise that the contribution of actual final consumption (including private and government) added a 3.5ppt impetus to GDP growth in the fourth quarter.

Inventories added 1.1ppt to economic activity. This is partly a usual year-end top-up and a reaction to the expected supply chain disruptions. Such a jump used to mean that a drop was in the making in the coming quarters, and with the Covid-19 effect, it could be an even bigger drag on growth. Gross fixed capital formation increased by 7.0% YoY, the lowest since 2016. A high base, the end of EU-financed projects and the end of capacity enhancements all affected this figure. The contribution to GDP growth dropped to 1.9ppt.

A still-strong increase in consumption and investment activity, and the increase in inventories pushed imports higher. Still, export activity was disrupted by easing external demand. Against this backdrop, the difference in the trade balance was remarkable, translating into a 1.9ppt drag from net exports in the fourth quarter.

Contributions to GDP growth – expenditure side (% YoY)



Source: HCSO, ING

We issue a growth warning

While it was interesting to see which factors were behind the surprising fourth quarter GDP growth, unusually, none of these will matter going forward. The coronavirus outbreak may have caused significant disruption to global supply chains, affecting local industry. We haven't seen any sign in the soft or hard indicators yet that Covid-19 has affected the real economy. Moreover, as Hungary has yet to report any cases, the "fear factor" (impact on services) might be lower than other countries like Italy. However, without any data, we refrain – for now – from any downgrade to domestic GDP growth. It would be ill-advised to change the outlook blindfolded.

Instead, we maintain our 3.8% YoY GDP growth forecast while issuing a growth warning. The risks are clearly and significantly tilted to the downside, especially in the first half of 2020. The growth impact will depend on the severity of the supply chain disruption, as well as the number of reported cases and the existence (or non-existence) of quarantine measures. We will closely monitor the situation and if any of these happen, we'll update our economic outlook.

Author

Peter Virovacz
Senior Economist, Hungary
peter.virovacz@ing.com

Disclaimer