

Hungarian industry and retail sector diverge

In contrast to the trends seen last month, industrial production surprised to the upside in February, while retail sales surprised to the downside. In light of these monthly reversals, it's hard to argue that a clear trend has begun, and divergence remains an issue



Any expected improvement at the end of the year will not be enough to salvage the situation for Hungarian industry, which could prove significant drag on GDP growth in 2024

The Hungarian Central Statistical Office (HCSO) has released the industrial and retail sales figures for February. Contrary to last month's dynamics, industrial production rose on a monthly basis, while retail sales fell. Going forward, however, as domestic demand recovers, we expect a gradual convergence between the performance of these two sectors, putting economic activity on an improving path.

1.4%

Industrial production (YoY, wda)

ING estimate: -3.4% / Previous: -4.0%

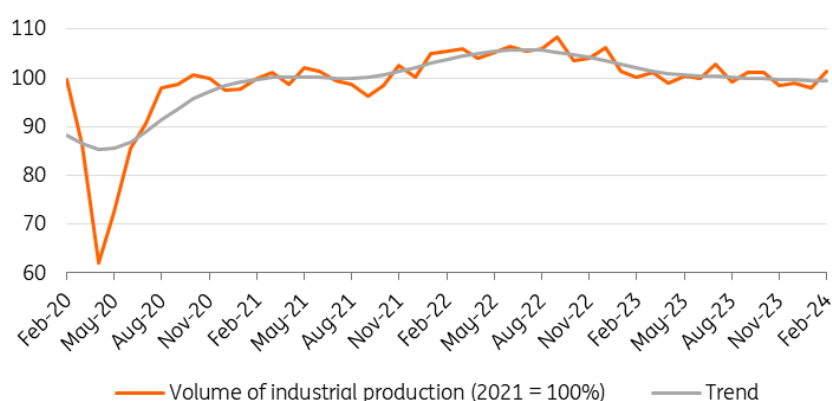
Better than expected

Industry surprise might be only a one-off

After a prolonged period, we can finally report a positive surprise regarding the performance of the industrial sector. In February 2024, production increased by a remarkable 3.5% on a monthly basis, surpassing market consensus expectations. In light of the February trade balance data, this strong performance from the sector was somewhat anticipated.

On an annual basis, production exceeded the level observed a year earlier by 1.4%, adjusted for working days. The last time the industrial sector witnessed a positive year-on-year index was in the final month of 2022. Nevertheless, despite the encouraging February correction, the overall volume of industrial output remains well below the peaks witnessed in 2022.

Volume of industrial production

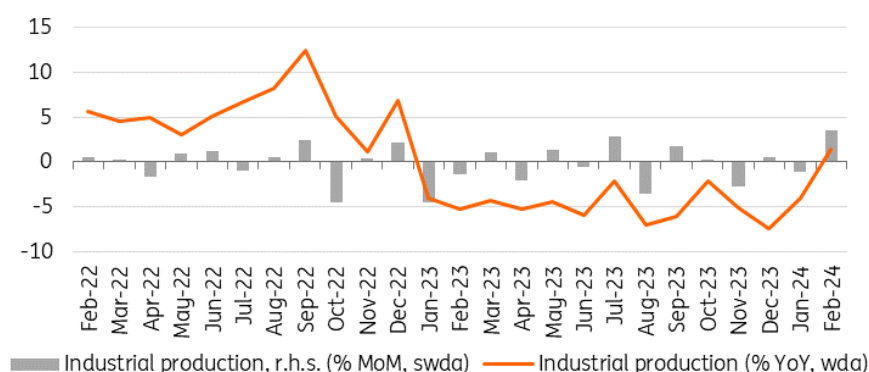


Source: HCSO, ING

While we must await the detailed data, the preliminary release from the HCSO outlined a generally improving trend. The expansion in production was supported by the majority of sub-sectors. However, such a substantial monthly change is unlikely without robust performance from the high-weight industries.

In this regard, the automotive sector may have been the driving force, alongside the food industry's strong performance. Conversely, electrical equipment manufacturing continues to face challenges, as production declined on an annual basis. A similar trend was observed in the electronics industry, although this may be less surprising.

Performance of Hungarian industry

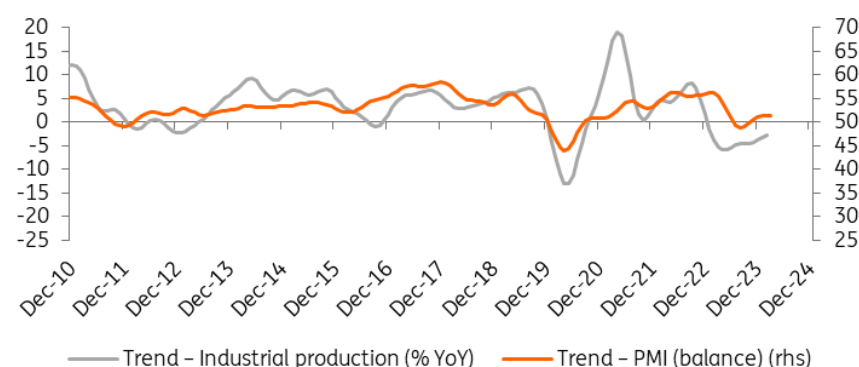


Source: HCSO, ING

As the proverb states, "One swallow does not make a summer." Therefore, the February rebound should be taken with a pinch of salt. It is entirely possible that this is not a trend reversal but merely a one-time surge in production levels. There are several reasons to interpret the data with caution, not least because the industrial climate in Europe and Asia remains weak. Demand for industrial products is low, inventory levels are fully stocked, and order books are shrinking.

Although various industrial surveys and confidence indicators suggest the beginnings of improvement, a sustained performance upturn in Hungary may still be some way off. The HCSO will release detailed data on fresh order books later, but the January figure, with its nearly 17% annual decline, hardly suggests that the February performance improvement is the first step in a lasting recovery.

Manufacturing PMI and industrial production trends



Source: HCSO, HALPIM, ING

The industrial sector's economic performance in the first two months of this year undoubtedly paints a more favourable picture and may even contribute positively to first-quarter GDP growth. However, a meaningful trend reversal – in light of global developments – is still expected only in the second half of the year. By then, bloated inventories may have been depleted, and external demand could improve somewhat.

The gradual recovery of sectors serving the domestic market in the first half of the year is unlikely to be sufficient for a strong performance; better industrial output is anticipated in the second half. The current rebound is more likely attributable to exports rather than domestic demand, as evidenced by the disappointing recent retail sales data. Overall, industrial performance for the full year is likely to be slightly negative, thus weighing on 2024 GDP growth.

1.1% Volume of retail sales (YoY, wda)

ING estimate: 2.6% / Previous: 0.6%

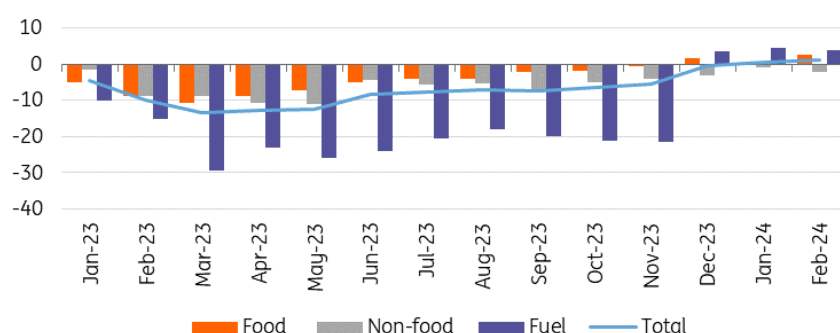
Worse than expected

Consumption-led recovery stalls temporarily

The latest Hungarian retail sales data for February 2024 has brought some disappointing news, especially when compared to the positive surprises seen in the industrial sector. After stagnating in the previous month, the volume of retail sales – adjusted for seasonal and calendar effects – contracted by 0.6% on a monthly basis. However, due to the low base effect from the previous year (caused by the fuel price effect), the year-on-year index managed to improve, registering a 1.1% growth in the sector.

A closer look at the details reveals that the most significant surprise came from the non-food retail stores, which experienced a 1.1% decline on a monthly basis. Sales in furniture and electronics stores, books, newspapers, and stationery shops, as well as cosmetics shops, saw a sharp decline. This segment had seen a substantial positive surprise in the previous month, suggesting that February's figures were a correction. Surprisingly, mail order and internet retailing decreased by nearly 3%, indicating that January's growth of around 3% might have been a one-off effect.

Breakdown of retail sales (% YoY, wda)

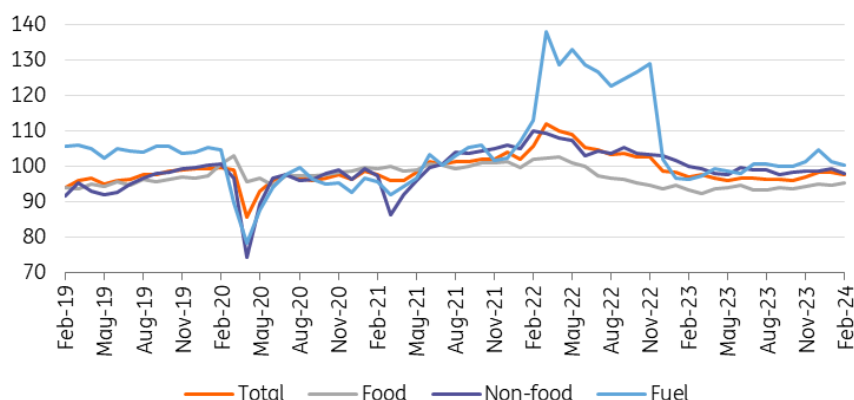


Source: HCSO, ING

What makes the latest data particularly concerning is that, similar to January, there were significant coupon payments related to retail government bonds in February. This was specifically highlighted in the February budget data. It appears that these coupon payments did not translate into increased retail sales. However, it is possible that this effect may have manifested in the service sector, which will only be confirmed once the first quarter GDP data is released.

Food store sales volume increased by 0.3% on a monthly basis in February, with a more significant improvement seen on an annual basis due to the low base effect. Nevertheless, sales indicators at the beginning of 2024 still correspond to the levels seen at the end of 2018 and early 2019, indicating that the food retail sector still has room for improvement. Lastly, fuel sales continued to show negative changes. After the frontloading of fuel purchases in December due to the excise tax increase, January was weak, and February did not bring a rebound. In fact, further rising prices led to even more restrained consumption, with fuel station sales decreasing by another 0.9% on a monthly basis.

Retail sales volume in detail (2015 = 100%)



Source: HCSO, ING

Overall, the February retail performance can be characterised as structurally weaker. Historically, the overall retail sales volume still remains at the levels seen at the end of 2020 and early 2021, which is not a particularly encouraging picture. This is precisely why we have previously indicated that it is premature to speak of a trend-like and dynamic recovery, a concern that has unfortunately been confirmed.

Nevertheless, in the coming months, the low base effect, normalising inflation, and strong real wage growth may provide support to the retail sector. March also sees significant coupon payments in terms of retail government bonds, which could potentially give some impetus to the sector, although the expected similar effect in February failed to materialise. This further indicates that consumer confidence needs to improve further, and the precautionary savings need to ease, which will take time. However, we are already seeing some encouraging signs in this regard.

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