Hungarian industry in freefall

What February brought, March took away. The last month of the first quarter was a very weak one for Hungarian industry. The outlook is anything but rosy, with capacity utilisation at levels lower level than during the Covid

A factory in Gyor, Hungary

-2.8%

Industrial production (YoY, wda)

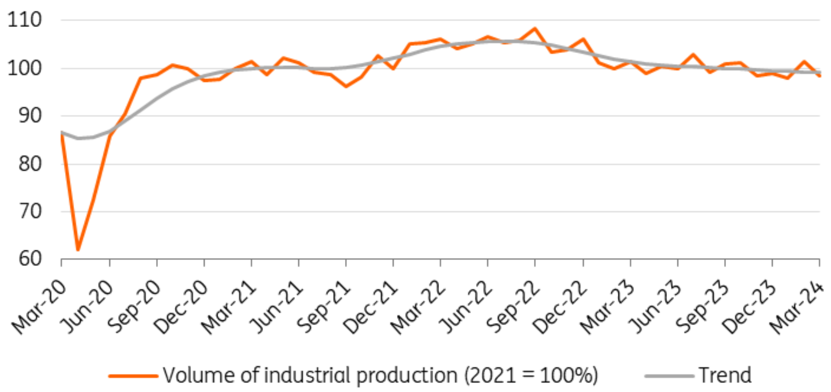
ING estimate: -2.2% / Previous: 1.8%

Worse than expected

The negative pattern continued: same month and one positive surprise, plus one negative surprise. After the surprisingly strong March retail sales data and the Q1 GDP flash estimate, the writing was on the wall. It was almost inevitable that industry would suffer a sharp contraction in March. However, industrial production fell by 3% month-on-month, below all expectations. This effectively wiped out February's rebound.

The double-digit year-on-year decline is mainly due to three fewer working days. If we remove this working day effect from the data, we see a decline of just 2.8% over the same period of the previous year. Overall, it is a generally bleak performance and a continuation of a downtrend, with total industrial production volume falling below the monthly average in 2021.

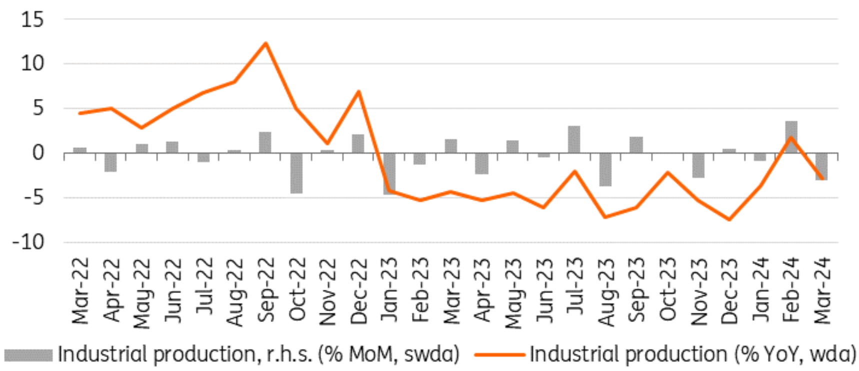
Volume of industrial production



Source: HCSO, ING

We're still waiting for more detailed data, but the preliminary figures released by the Hungarian Central Statistical Office (HCSO) show a generally worsening trend. It is telling that the flash report did not name a single sub-sector with a meaningful positive performance. The most positive news was that the food industry declined less sharply. In addition, the most important sub-sectors, transport and electrical equipment manufacturing, are in a slump. This is hardly surprising, given the state of the global economic cycle, the lack of demand for industrial products due to record-high inventories and the fact that order books are down by around 20% on a yearly basis.

Performance of Hungarian industry



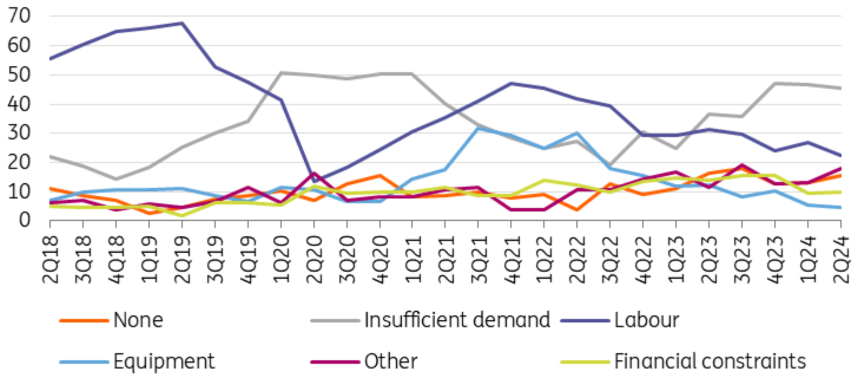
Source: HCSO, ING

As we pointed out in our February commentary, '*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.*" Unfortunately, we were right: we saw no turnaround, just a one-off bounce in production levels, followed by a similar correction in March.

Although various business surveys and confidence indicators are already pointing to some improvement, their reliability remains highly questionable. The manufacturing PMI has been above the 50 mark for six months, indicating expansion, while actual industrial production has not picked up at all. The GKI business confidence index also points to an improving trend, although here we can at least bet that the services sector is pulling the confidence index upwards.

Industry's economic performance in the first quarter of this year is not egregious, thanks to the jump in February, but we can already say that there are negative developments in terms of value added. The sector's negative impact on GDP is no accident. Against this background, the huge foreign trade surplus in March is even more puzzling. In our view, the main explanation is that the country's declining energy demand and weak consumption and investment are reducing import demand. Meanwhile, export sales from inventories (presumably mainly in agriculture) are able to keep foreign trade in such a surplus.

Factors limiting the production (%)

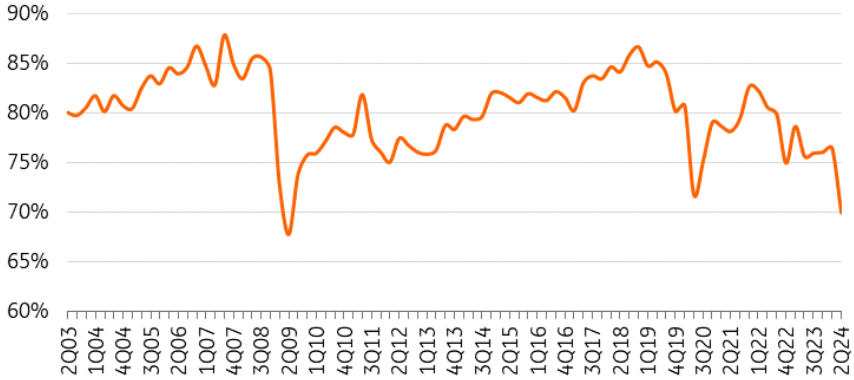


Source: Eurostat, ING

As far as the industrial outlook is concerned, we continue to expect a cloudy future in the short term. Based on the Eurostat survey measuring factors limiting production, around 50% of manufacturers complain about insufficient demand. This is in line with the latest survey by the German-Hungarian Chamber of Industry and Commerce (DUIHK). According to the report, weak demand tops the list of biggest risks for companies.

Even more worrying is the current level of capacity utilisation. Survey respondents reported capacity utilisation of only 70%, which is lower than the low point of the Covid-crisis. This hardly paints a rosy picture for the future.

Current level of capacity utilisation in Hungarian industry



Source: Eurostat, ING

On the contrary, we continue to believe in a sustainable turnaround in the second half of the year, given the expected global developments. By then, the record high level of inventories will have been worked down, and some improvement in external demand will be seen on the back of rising global demand for industrial products. A slow recovery in domestic manufacturing in the first half of the year will not be enough to sustain a good performance. Here, too, we expect industrial data to improve in the second half of the year as consumption and investment pick up. All in all, the industrial performance for the year as a whole is still likely to be slightly negative, thus holding back GDP growth in 2024.

Authors

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

Dávid Szőnyi
Research Trainee
david.szonyi@ing.com