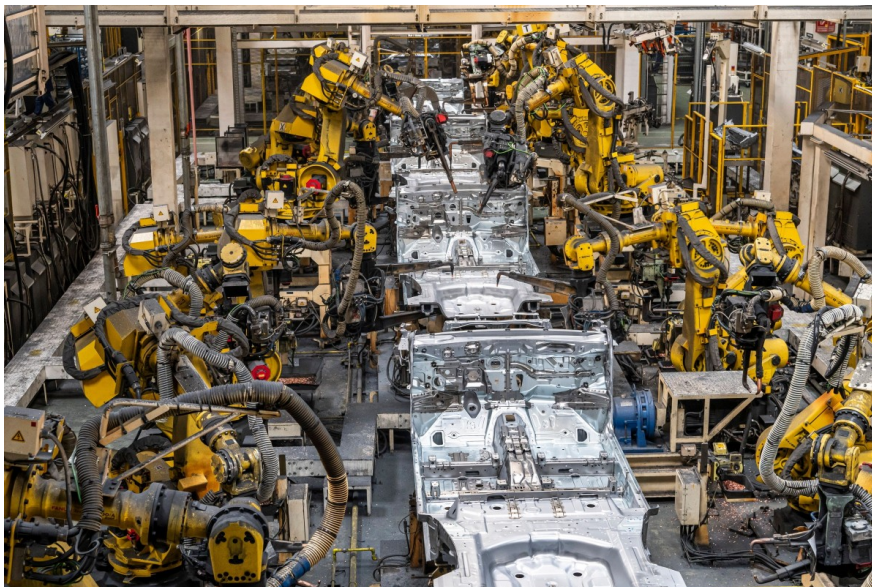


Hungarian industry still limited by domestic demand

There still seems to be some kind of glass ceiling in industrial production. After a positive surprise in July, there was a sharp correction in August. However, this could be enough to lift Hungary out of a technical recession



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

-6.1%

Industrial production (YoY, wda)

ING estimate: -1.9% / Previous: -2.6%

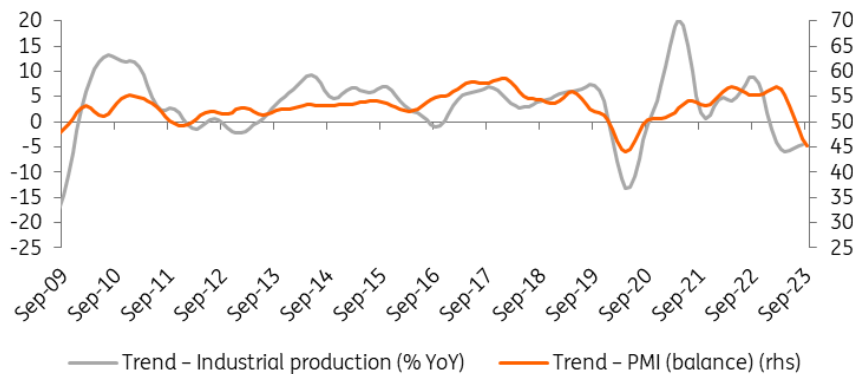
Worse than expected

Industrial activity was very weak in August. The Hungarian Central Statistical Office (HCSO) reported a month-on-month decline that was much worse than expected. Compared with July, industrial production (seasonally and working day adjusted) fell by 2.4%. This effectively wiped out July's surprising industrial growth. It is also important to note that production volumes have been fluctuating around a level that is 20% higher than the level recorded in 2015, thus it seems that

production levels are unlikely to increase further in the current economic environment. It is like hitting some kind of glass ceiling.

Industrial production fell by 6.1% year-on-year in working day adjusted terms. Given that the so-called soft indicators based on surveys (PMIs, industrial confidence indices) have remained in contractionary territory recently, they still suggested some improvement last month. Looking at the hard data for August, it can be said that the predictive power of these indicators is still limited.

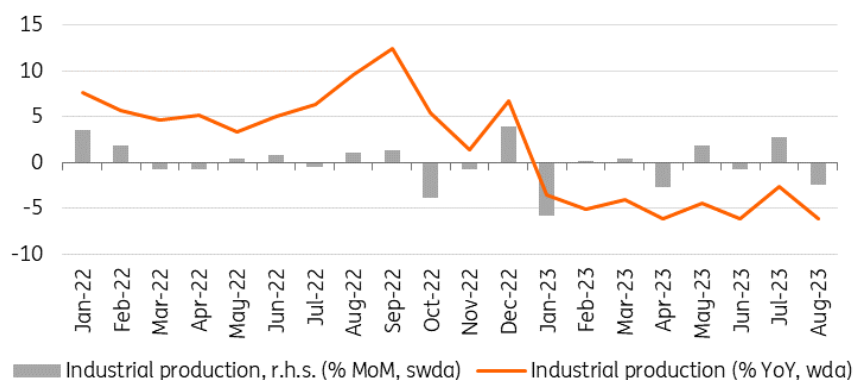
Manufacturing PMI and industrial production trends



Source: HALPIM, HCSO, ING

Detailed data are yet to be released, but according to preliminary data from the HCSO, there were no significant changes in the structure of industrial production. While most sub-sectors contributed to the decline in output, the exceptions remain the manufacture of electrical equipment (battery production) and car manufacturing. Given the renewed sharp contraction, it is likely that the effects of the summer shutdowns in August may have been felt in sectors producing for export, while a further decline in domestic demand is weighing on the performance of sectors producing for the domestic market. It therefore appears that, in the absence of a sustained change in the economic environment, industrial production will hover around the production levels observed since the beginning of the year. This also means that industrial production is expected to contract by around 5-6% for the year as a whole.

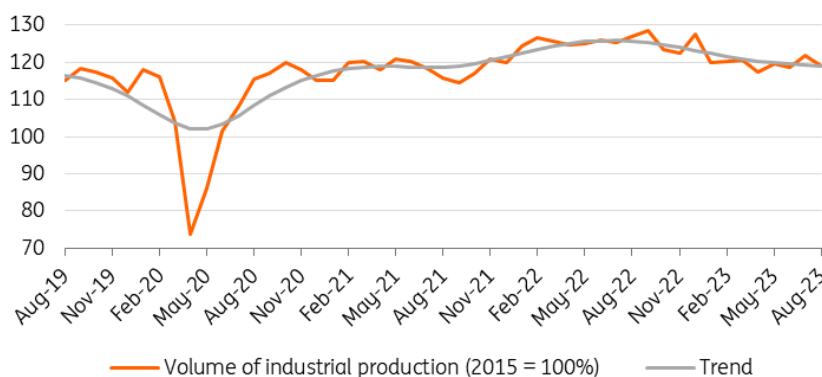
Performance of Hungarian industry



Source: HCSO, ING

Regarding the risks surrounding the industrial outlook, clouds are already gathering on the external demand side, i.e. the export-producing sectors, as European industrial performance remains sluggish while Chinese growth is more inward-looking, hardly conducive to a recovery in global trade. In addition, the one-day loss of production caused by a technical fault at the Volkswagen Group, which also forced the closure of the Audi plant in Hungary, is likely to weaken the September figure.

Volume of industrial production



Source: HCSO, ING

Turning to domestic developments, there are currently no signs of an imminent pick-up in output growth in sectors producing for the domestic market in the short term. However, what supports a somewhat improving outlook towards the end of the year is that industrial companies may be able to renegotiate their energy contracts at a much more favourable market price. This could result in a significant reduction in their costs, leading to a pick-up in output in sectors that are now underperforming due to cost constraints.

Moreover, as inflation moderates and purchasing power in the domestic economy recovers towards the end of the year, industrial sectors producing for the domestic market may receive some positive impetus not only from the supply side but also from the demand side. This may offset a possible slowdown in industrial exports. Finally, we conclude on a positive note. Despite the correction in August, the expected industrial performance in the third quarter should be significantly better than in the second quarter. Thus, barring an ugly surprise in September, quarter-on-quarter industrial production growth will remain in positive territory. In other words, industry, together with agriculture, could help the Hungarian economy emerge from a technical recession in the third quarter of 2023.

Author

Peter Virovacz

Senior Economist, Hungary

peter.virovacz@ing.com

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