Hungary's retail sales and industrial output continue to tumble

The rapid deterioration in domestic demand is bad news for both the retail sector and industry, as they continue to struggle. With the latest set of data showing continued weakness, we expect the economy to remain in a technical recession in the first quarter

Shoppers in Budapest

Sky-high inflation has been suffocating economic activity in Hungary, which is reflected in the latest set of data released by the Hungarian Central Statistical Office (HCSO). Year-on-year (YoY) performances seem very bleak, as the volume of retail sales dropped by 13.1%, while industry registered a 4% plunge in the volume of production (both working-day adjusted data). As we foreshadowed in our latest Monitoring Hungary, the drop in real wages has been constraining both household consumption and domestic demand towards goods. With such dynamics in play, we pencil in another yearly-based drop in real GDP in the first quarter of 2023, as we expect the Hungarian economy to remain in a technical recession.

Struggling retail sector points towards fall in consumption

-13.1%

Volume of retail sales (YoY, wda)

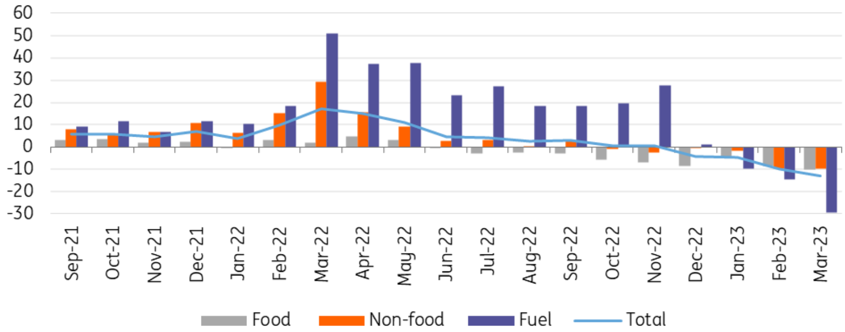
ING estimate: -14.8% / Previous: -10.1%

Better than expected

After three consecutive months of both yearly and monthly drops in the volume of retail sales, a year-on-year drop in March was registered once again. The 13.1% fall, adjusted for calendar effects was the result of a 0.8% MoM increase in sales volume. Therefore, for the time being, the monthly-based trend has been broken, but judging by the detailed breakdown there is little reason for joy.

Looking under the microscope, on a monthly basis the volume of retail sales only increased due to a rise in fuel retailing - a sub-component which grew by 1.9% MoM. This increase comes as no surprise, given that retail fuel prices fell in March, which consequently sparked demand, hence the growth in fuel retailing. However, if we exclude fuel sales, then the volume of retail sales posted a 0.9% MoM decline. This marks the sixth month in a row, where retail sales ex-fuel sales have declined.

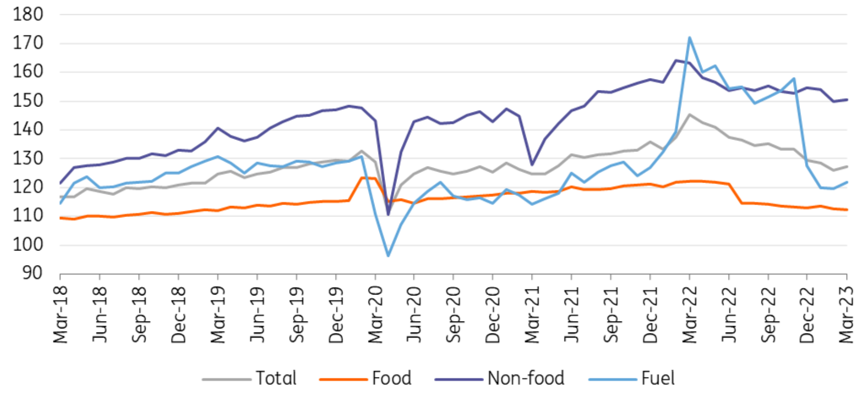
Breakdown of retail sales (% YoY, wda)



Source: HCSO, ING

The other two sub-components, namely food and non-food retailing, have posted similarly sharp year-on-year contractions, but their monthly dynamics differ. Amid sky-high inflation, the volume of food sales dropped by 0.4% MoM, while for non-food retailing it increased by 0.3%. Under the hood, there are segments in non-food shops where significant growth can be observed (books, newspapers), but other segments saw drastic declines, such as cosmetics shops or furniture and electrical goods retailers. Therefore, it seems like households are drastically cutting back on spending on items that are more expensive or can be considered luxurious. This tendency is not surprising given the marked fall in the purchasing power of households, which has been continuing for the sixth month in a row.

Retail sales volume in detail (2015 = 100%)



Source: HCSO, ING

Looking at the first quarter as a whole, the performance of the retail sector declined sharply. On an annual basis, the fall is more than 8%, while on a quarterly basis the decline is close to 4%, which suggests that consumption in the first quarter may have been weak. Of course, it is important to point out that the retail data release does not consider the performance of the services sector. However, based on the latest data on domestic tourism, it is clear that households are likewise cutting back spending on services. In our view, this broad-based weakness in consumption will have a marked drag on real GDP, therefore we expect a contraction in the first quarter of 2023.

Going forward, we believe that the retail sector will continue to suffer due to households' deteriorating purchasing power. Even though the inflation peak is behind us we believe that a turnaround in real wages will happen only in the fourth quarter of this year. Until then, we expect continued weakness regarding the volume of retail sales.

Industry struggles to rebound as domestic demand further deteriorates

-4.0%

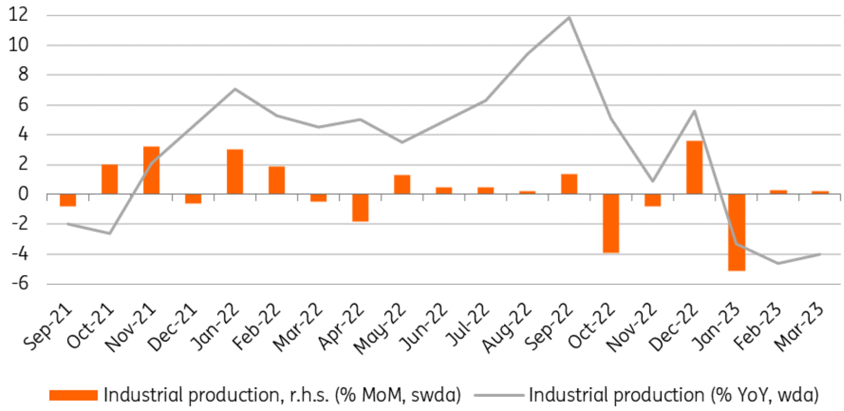
Industrial production (YoY, wda)

ING estimate: -3.0% / Previous: -4.6%

Worse than expected

Hungary's industry continued to underperform in March, as the volume of industrial production fell by 4% YoY, after adjusting for calendar effects. The yearly-based drop is the result of a 0.2% MoM increase in the volume of industrial production, after adjusting for seasonal and calendar effects. Despite the monthly based increase in March, industrial output has been practically stagnating since the start of the year.

Performance of Hungarian industry

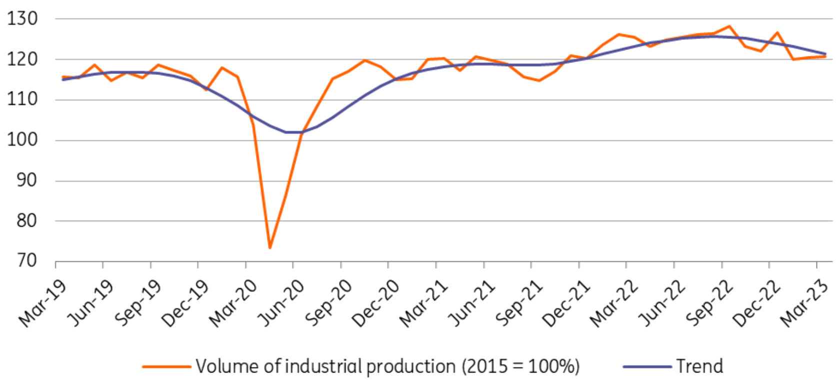


Source: HCSO, ING

Even though the Statistical Office will only release the detailed data next week (12 May), the preliminary statement highlights that the majority of the manufacturing subsectors contributed to the production decline. As always, the exceptions remain electrical- and transport equipment manufacturing (e.g. EV batteries and cars), which back in March both expanded on a yearly basis. In contrast, the other two most important sectors: electronics and food manufacturing recorded declines in production.

As we previously pointed out, only the industrial output related to the automotive sector can breathe any kind of life into Hungary's industry, widely driven by export sales. The decline in domestic demand i.e. the fall in demand for consumer goods and capital goods, means that sectors producing for the domestic market continue to underperform. In addition, order books in these sectors are likely to remain below last year's levels, which means that their prospects are not particularly favourable. Therefore, rationalisation of production could continue alongside high costs.

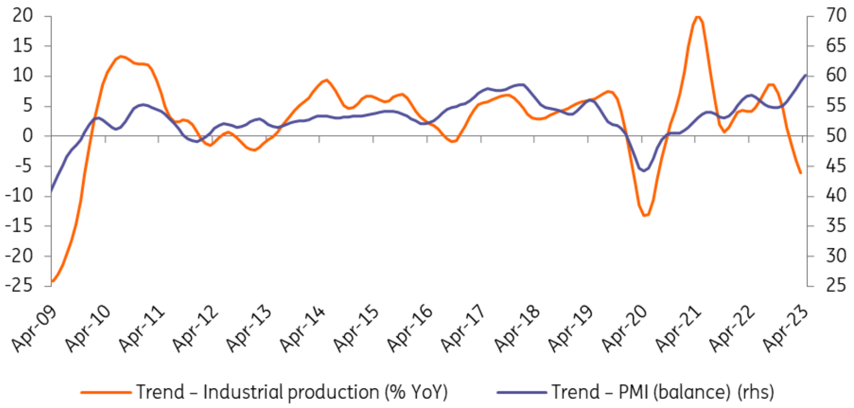
Volume of industrial production



Source: HCSO, ING

In light of March's data, we can safely conclude that the positive industrial picture presented by the Hungarian PMI readings will be nowhere near reality for many months. We believe that the reason for the divergence lies in over-representation of the largest export-oriented industries. Meanwhile, the slump in the performance of smaller manufacturers and more domestically-oriented sectors with a more modest weight is amply offsetting production indicators that are in some way linked to the automotive sector. Therefore we call for a review of the methodology used to compile the index, which provides no meaningful information on the performance of industry. In any case, the movement of the Hungarian manufacturing PMI cannot be considered representative or indicative.

Manufacturing PMI and industrial production trends



Source: HALPIM, HCSO, ING

Overall, the industrial performance in the first quarter of this year (-4% QoQ drop) supports our expectation that the economy will continue to remain in technical recession in the first quarter of 2023. For the last three months, the bleak industrial performance was driven by weak domestic demand, along with some export hiccups. However, there is no doubt that the latter could still be able to make some positive contribution to overall GDP, especially in services exports. In our view, weak household consumption activity, coupled with grim industrial performance in the first quarter will certainly be a significant drag on growth, hence our expectation of a continuation of the technical recession.

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