Hungarian retail sales fall off a cliff

The retail sector continues to suffer amid sky-high inflation, with the volume of retail sales contracting since December 2022. Going forward, we see continued weakness as household purchasing power deteriorates further

-10.1%

Volume of retail sales (YoY, wda)

ING estimate -8.6% / Previous -4.5%

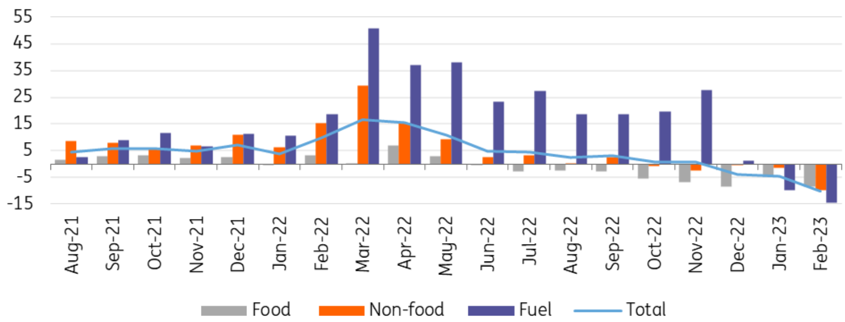
Worse than expected

After January's very disappointing performance, the Hungarian retail sector continues to suffer amid the cost-of-living crisis, as the volume of retail sales in February declined by 10.1% year-on-year (YoY), adjusted for calendar effects. We were already pessimistic about the January and February readings, but the final data exceeded even our bleakest expectations.

As far as monthly dynamics are concerned, the 10.1% YoY drop was the result of a 2.0% month-on-month (MoM) plunge in sales volume compared to January 2023. With the latest data in hand, we can conclude that February is the third consecutive month in which the volume of retail sales has been contracting both on a yearly and monthly basis, which echoes negative momentum on both fronts.

Out of the three main components of retail sales, food retailing displayed the least contraction both on a YoY and MoM basis, as it registered an 8.6% decline compared to February 2022. On a monthly basis, food retailing only decreased by 0.1%, thus the stark yearly drop is almost entirely due to base effects. Amid 43.3% YoY food inflation in February, households are significantly reducing their food consumption compared to a year earlier, which has resulted in a sharp fall in food retailing. With real wages falling steadily for five months – which in our view will continue in months ahead – the loss in household purchasing power will further constrain food consumption, and thus lead to further intense yearly based declines in the volume of food sales.

Breakdown of retail sales (% YoY, wda)

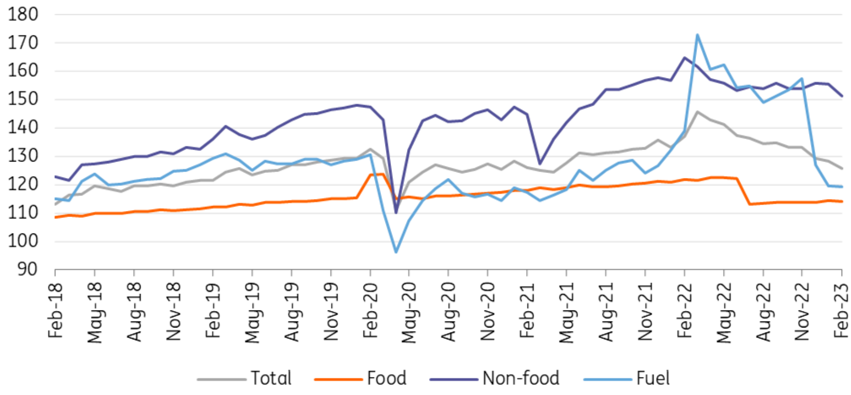


Source: HCSO, ING

Non-food retailing also experienced a shrinkage in both monthly and yearly comparisons, with the latter declining by 9.8%. Monthly dynamics show that out of the three components of retail sales, non-food retailing experienced the biggest monthly decline, as the volume of sales fell by 2.8% in non-food shops. Broad-based weakness can be observed among all sub-sectors within non-food shops, with manufactured goods registering the biggest one-month drop, with a 6.5% contraction. In our view, this is alarmingly indicative of the continued deterioration in domestic demand towards manufactured goods, which can explain why, going forward, the Hungarian industry can mostly rely only on external demand.

To get a complete picture, besides contracting food and non-food retailing, the volume of fuel sales fell both on a yearly and monthly basis, registering a decline of 14.5% YoY. With fuel sales dropping only by 0.3% MoM, we can conclude that just like in the case of fuel retailing, the very sharp yearly drop is almost entirely due to base effects. This sharp contraction hardly comes as a surprise, given that a year ago fuel price caps kept prices artificially low, before the cap ended on 7 December 2022. Against this backdrop, we believe that fuel retailing will continuously post year-on-year contractions due to the same base effect dynamics.

Retail sales volume in detail (2015 = 100%)

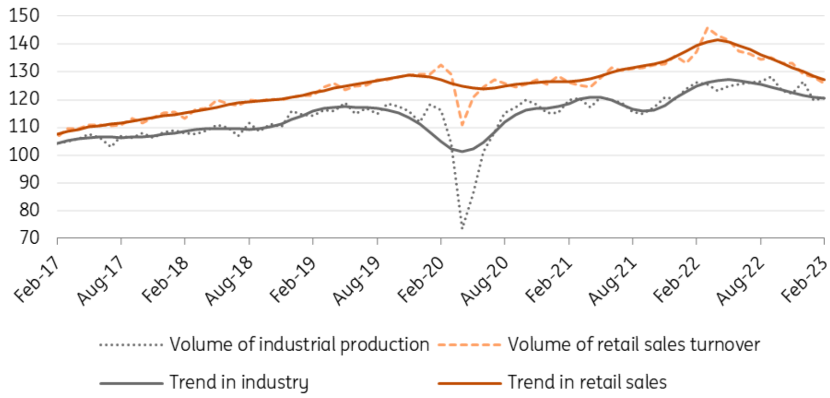


Source: HCSO, ING

Looking ahead, we believe that the retail sector will continue to suffer due to households' deteriorating purchasing power. Monthly dynamics suggest that non-food retailing will see the biggest monthly falls as households prioritise buying food. We believe that as a result of continued negative real wage growth (fifth consecutive month) consumers will continue to cut back on non-food products. For this reason, we believe that on a monthly basis, food retailing will continue to stagnate or slightly contract, but we see more room for contraction regarding non-food and fuel retailing.

Even though the inflation peak is behind us, we need to wait a few more months until real wage growth flips back to positive territory, which in our view will happen in the third quarter. Until then, we expect continued weakness regarding the volume of retail sales. The main question for the months ahead remains how long households can smooth consumption by tapping into savings, thus evading a complete collapse in retail sales.

Trends in industry and retail sales (Volume of production and turnover, 2015 = 100%)



Source: HCSO, ING

Until that turnaround happens, industry will also have a hard time with dropping internal demand.

In general, the recent downtrend both in industry and retail sales suggests that economic activity in the first quarter might be even weaker than we expected before the February figures. The latest nowcast of the National Bank of Hungary pointed to a sharp quarterly drop in performance and now we tend to agree with that assessment. Seeing the latest economic activity figures, we think the quarter-on-quarter real GDP drop could be shallower than 1%.

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