Hungary posts strong but unsustainable GDP growth

Under normal circumstances, the fanfares would trumpet optimism after an above 8% GDP growth. The reality is, however, that we might have already seen the best from Hungary's economy for this year and it's going to be downhill from now on

Hungary's spectacular growth rate is set to be as temporary as Budapest's cherry blossom

8.2%

GDP growth (YoY)

ING forecast 9.2% / Previous 7.1%

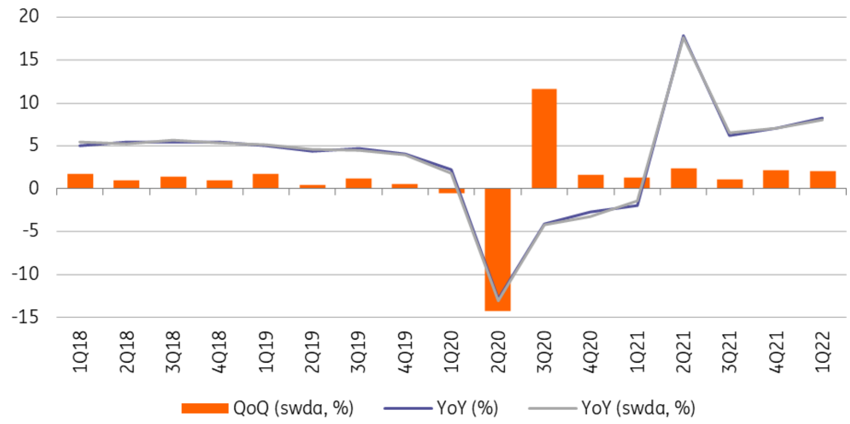
Better than expected

Hungarian GDP growth shows early resilience

Expectations, in general, were relatively positive regarding Hungary's first-quarter GDP data even though the Ukraine war and its negative economic implications have cast a shadow on the growth outlook. And yet, actual GDP growth in the first quarter came in higher than market consensus, although fell short of ING's ultra-optimistic expectations.

The Hungarian economy achieved a 2.1% Quarter-on-Quarter GDP growth in the January–March period, which is only 0.1ppt lower than the performance in the last quarter of 2021. On a yearly basis, the volume of GDP was up by 8.2% in 1Q22, helped by not just the strong quarterly performance but the low base provided by the Covid-situation a year ago. In a nutshell, the Hungarian economy has shown early resilience to the first wave of the shock of the war.

Hungary's real GDP growth



Source: HCSO, ING

When it comes to the detail, the Hungarian Central Statistical Office revealed some qualitative information in its flash report, while quantitative details will be released on June 1. The statement highlighted that almost all industries contributed to the growth while underscoring the performances of food, petroleum, and electrical equipment manufacturing. On the services side, retail trade, accommodation & food service activities along with logistics moved the needle mostly for the GDP growth figure. We hardly can see any surprises in this data. With households spending their saving accumulated during the Covid lockdowns and new government transfers, consumption was clearly a driver of growth.

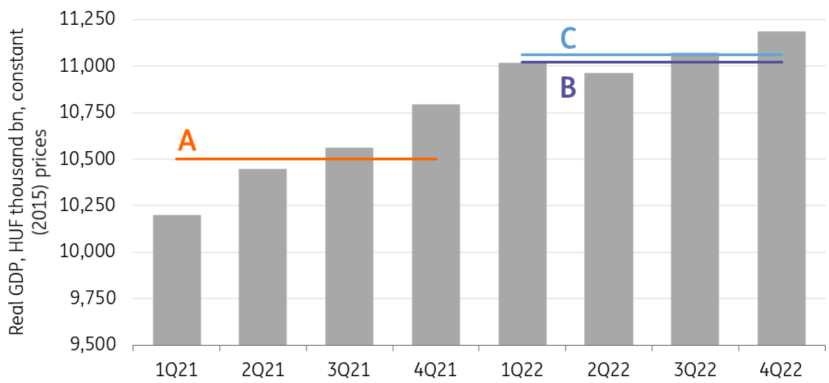
Compared to ING’s view, it is hard to point to one single sector where the economy performed weaker than we anticipated. That said, we think that the difference could come from an overestimation of the impact of government transfers and public spending during the first quarter of 2022. The full truth will be revealed when we will see the detailed statistics.

What does this strong start mean for 2022?

Under normal circumstances, after an 8.2% year-on-year GDP growth, economists would talk in superlatives about the 2022 outlook. The “only” caveat is that we have everything, except a normal economic environment. The war in Ukraine goes on and it seems this terrible situation will linger. Sanctions on Russian energy imports could remain on the table, which raises the uncertainty regarding the coming quarters. China’s Covid issues are putting further pressure on the already squeezed global value chains, while companies are trying to find new sources to serve still soaring demand.

With such uncertainty, the best what we can do is draw a line in the sand. The so-called carry-over effect comes in handy in such cases. Conceptually, carry-over effects denote the annual average rate of growth that would result if the level of GDP reached in the fourth quarter of a given year were to remain constant throughout the subsequent year. If you also know the first quarter's performance, you know not just the carry-over effect but a major part of the growth within the year. Thus, it reduces the uncertainty of the forecast even more. According to our estimation, if the Hungarian economy were to stagnate during the coming three quarters, taking into consideration last year's average real GDP and this year's first-quarter data, GDP growth could be only a tad lower than 5.0% in 2022 (the % difference between line B and line A, in the chart below.)

The impact of the carry-over effect and the first quarter GDP growth in Hungary



Source: HCSO, ING

So, the only question remains, whether Hungary will be able to muddle through this year without a technical recession. If businesses feared that the recent problems would persist for a longer period, stock orders would not be still positive in construction and industry. Undoubtedly, there are issues with the supply side; suppliers can deliver more slowly. But as the backlog of orders shows, production will speed up as soon as there are some solutions to the supply-side bottlenecks. If companies were afraid of the future, they would lay off their workers. In contrast, there is a labour shortage in the Hungarian economy and employers are willing to raise wages in a high-inflation environment to keep the labour force in-house.

Against this backdrop, we see the chances of a technical recession as rather moderate, but not negligible during the second and third quarters of 2022. If Hungary can avoid the series of negative quarter-on-quarter performances, GDP growth could remain above 5% this year. The chart above calculates a minor drop in the second quarter and with some moderate strengthening in economic activity during the second half of the year, translating into a 5.4% GDP growth (% difference between line C and line A).

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