The dilemma of Hungary's strong labour market

A strengthening labour market during a technical recession is something which we are not used to seeing. Yet, Hungary's labour metrics have been improving recently, raising the pro-inflationary risk once we emerge from the real economic downtrend

The Hungarian labour market is very resilient

The Hungarian Central Statistical Office (HCSO) has released the latest set of labour market data (wages and the unemployment rate). Wage growth remained strong in April, despite lower bonus payments, with the drop in real wages roughly unchanged compared to the previous month. Labour market participation has risen and remains close to record high levels, as the cost-of-living crisis encourages a willingness to work. This, along with still present labour shortages in some sectors, is helping to lower the unemployment rate during a technical recession.

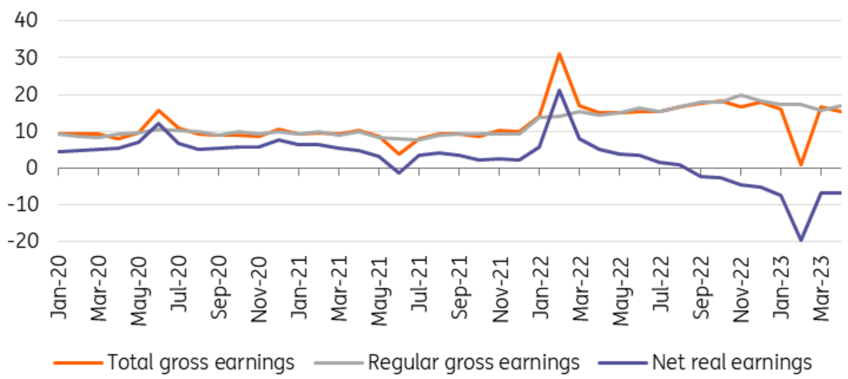
Regular wage growth picked up again

Starting with wages, outflows remained quite strong, with average gross wages rising by 15.5% year-on-year (YoY) in April 2023. However, the yearly based figure was slightly lower than our own expectations, as we had anticipated higher bonus payments. In this regard, regular gross earnings rose by 16.9% on a yearly basis in April, breaking a four-month-long streak of deceleration in the growth rate of regular gross earnings.

Median wage growth in April was 16.4% YoY, which is slightly higher than the growth rate of average gross wages. In our view, this signals that higher earners missed out on last year's bonus payments. On the other hand, another interpretation could be that the wages of those earning below the average wage increased more. This would be in line with Hungary's structural problem of labour shortages, which remain highest in the sectors where earnings opportunities are below average wages.

As positive as these figures look, the purchasing power of wages has nevertheless continued to remain deeply in negative territory. The only silver lining is that the 6.9% drop in real wages in April is matching the drop in real wages in March, so at least the situation hasn't worsened as sky-high inflation dampens households' purchasing power. April has been the eighth consecutive month in which real wage growth was negative, but we believe that this trend will break around the end of the third quarter thanks to the ongoing disinflation process.

Nominal and real wage growth (% YoY)

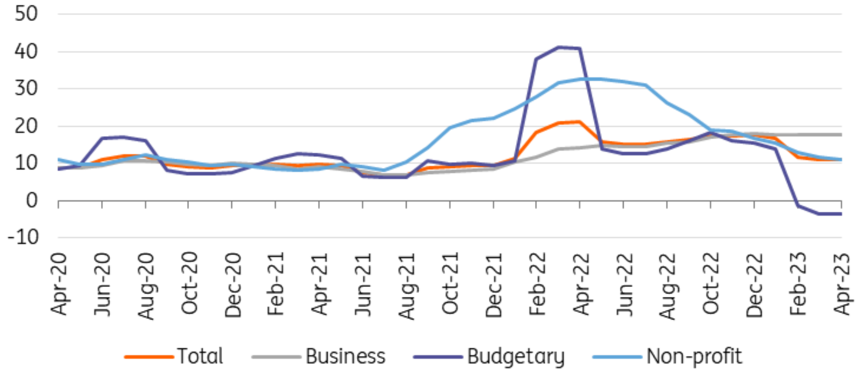


Source: HCSO, ING

Looking at the divergence in wage growth between the private and public sectors, the impact of bonuses is clearly visible. While public sector wage growth accelerated to 13.4%, private sector wage growth slowed to 16.4%. This is in line with our previously mentioned view; that this year in April higher earners missed out on last year's bonus payments.

From a sectoral perspective, wages grew above average in almost all sectors, with construction and financial services being the only two exceptions. The former is hardly surprising, given that construction activity is suffocating under high interest rates and shrinking order books. As for financial services, a mere 2.4% increase in average wages was registered, which signals that this was the main area where bonuses were not paid to the same extent as last year.

Wage dynamics (three-month moving average, % YoY)



Source: HCSO, ING

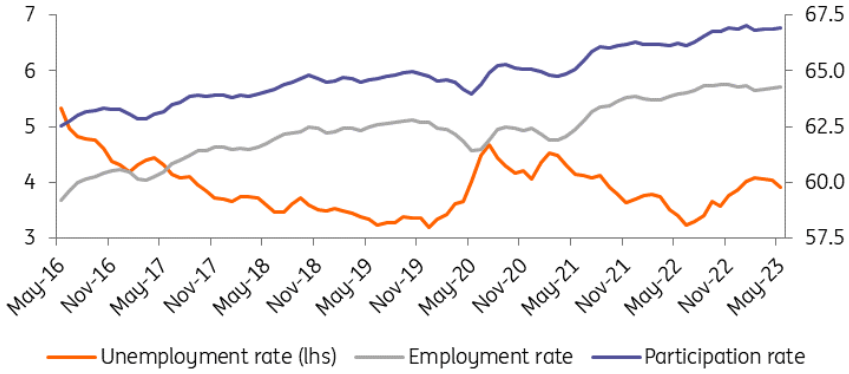
Going forward, we expect the 2023 full-year wage growth to be around 15-16%. As cumulative average wage growth was 12% in the first four months of the year, we expect some strengthening for the rest of the year. One reason for this is the wage agreement reached during the year for some parts of the public sector. In addition, as the economy slowly recovers in the second half of the year, demand for labour may remain strong (counterbalancing the seasonal effects) pushing up the pace of wage growth further.

Unemployment rate keeps lowering

Speaking of demand for labour, unemployment continues to fall in Hungary, according to the latest HCSO model estimate for May. It shows that the number of unemployed has shrunk to 186,000. Meanwhile, the official unemployment rate indicator (used in international comparisons), the three-month moving average survey, also showed a decline, to 3.9% in the March-May period. Of course, these indicators are still above their levels of a year ago, but it seems particularly surprising that labour market indicators are improving during a technical recession. It also shows that this current crisis is unlike anything we have seen before.

Looking at the monthly data, we can see that in recent months the fall in unemployment has gone hand-in-hand with a rise in employment, while the number of labour market participants has remained broadly stable (fluctuating within a statistical margin of error). The employment rate has again approached its historical peak and is not far away from reaching it. Official three-month average-based statistics show a similar trend. Thus, it appears that sectors that are facing labour shortages and remain confident about the future (for example, because they have higher order books than a year earlier) can absorb the right labour from the potential labour pool.

Historical trends in the Hungarian labour market (%, 3-m moving average)



Source: HCSO, ING

This is also reflected in the increase in the number of people hired in recent months in agriculture, industry and in accommodation and food services. The biggest question is what will happen when the positive seasonal effects fade, which have been present in both agriculture and tourism-related sectors since the spring. Presumably, by the time the seasonal effects fade out, the Hungarian economy will slowly start to find its feet in the second half of the year.

Against this backdrop, it is therefore possible that labour market indicators will weaken somewhat after the summer period before improving again. However, contrary to our previous expectations, we no longer expect the unemployment rate to move up to 4.5%. Even if there is a rise, the peak could be in the immediate vicinity of 4%. The various surveys also suggest that only a very small percentage of companies plan to cut back labour in the future and that the focus over the next 12 months may be on retaining recent staff.

What is a blessing now could also be a curse

Although a still-tight labour market and high wage growth can keep the Hungarian economy broadly afloat and prevent it from sinking into a deeper recession, it could still cause problems as the real economic recovery gets underway. At present, the biggest drag on the Hungarian economy is extremely high inflation. However, towards the end of the year, inflation could fall below the rate of wage growth. In the meantime, the structural labour shortage issue will strengthen further as well, pushing companies to raise wages to keep recent staff or be able to hire new employees as Hungary makes its way towards an economic upturn.

The renewed expansion of purchasing power could even bring with it a surge in consumption and thus a renewed strengthening in the repricing power of companies. For the time being, we see this as only a moderate risk, given that a large part of the population has dug deep into its savings, so the focus is likely to be on replenishing depleted savings first. However, if the labour market remains this strong, this reserve accumulation could take place faster than expected, and in a still high inflation environment – well above the 3% inflation target – another price shock could develop in the Hungarian economy. This could turn a blessing into a curse, as a persistently high inflation environment cannot be part of a sustainable macroeconomic path.

Author

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

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("**ING**") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies).* The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

 ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.