

FLASH REPORT

3 June 2019

What slowdown? Hungary's economy switched into top gear in Q1

- Hungary's GDP grew by 5.3% YoY in Q1 2019 (in non-adjusted terms). The currently published figure was the same as the flash estimate. The annualized QoQ growth rate was 6% in Q1, up from 4.4% in Q4, the KSH statistical office said. Our in-house adjustment shows 5.4% annualized QoQ rate, after 5.0% in Q4.
- **Non-farm GDP** surged 5.6% YoY (Q4: 5.0%), and its annualized QoQ growth rate accelerated to 6.0%, from 5.1% in the previous quarter. **Non-farm private sector's** GDP grew by 7.0% YoY (Q4: 6.1%) and its annualized QoQ growth rate accelerated to 7.2% from 6.0%.
- Big picture: the Hungarian economy is definitely in the mature phase of the business cycle, when domestic demand is the main driver. The accelerating inflation (not only in the case of consumer prices, but also in the case of various producer prices), the deteriorating external balance, and rapidly increasing investment rate all suggest that the capacity bottlenecks in the economy became even more binding and the positive output gap is widening.
- The performance of the Hungarian economy was surprisingly strong in Q1; we had expected in the autumn that the GDP growth might reach its cyclical peak in Q3. Nevertheless, after the first monthly statistics had been published about the first quarter, it became clear that Hungary's GDP growth may have accelerated further in Q1. The (earlier) unexpectedly strong GDP growth in Q1 was definitely the consequence of the very strong investment activity. Construction output grew by 48.3% YoY in Q1 and by 15% on QoQ basis (not annualized). Naturally, it was reflected also in the fixed capital formation figure, which grew by 23.4% YoY, and investment rate reached 26.5% (seasonally adjusted) in Q1. This is 4.2 ppts higher than one year ago. Investment rate may draw closer to 29% by the end of this year. Fixed capital formation contributed with 4.4 ppts to the total 5.3% GDP growth.
- The growth of fixed capital formation was widespread among the economic sectors. Non-financial corporations' borrowing activity also points to strong willingness to invest in the corporate sector. The current pace of NFCs' loan growth is very strong also in historical comparison. Despite the robust growth of the construction sector in Q1, the orders stock level jumped to its previous high's level. This means an extreme amount of new orders booked in Q1, so in our view the construction sector may uphold the current production level in the coming quarters.
- Households' consumption expenditure perfectly matched our medium-term forecast: it soared 5.1% YoY (Q4: 5.0%, Q3: 5.4%), while its annualized QoQ growth rate decelerated to 4% from the previous quarter's 5% figure. Looking ahead, we think the annualized QoQ growth rate may stabilize around 4.5% in the coming quarters. Our in-house seasonal adjustment shows that consumption growth may have already reached its cyclical peak in 2018 H2. The growth in retail sales and real wages, as well as the evolution of consumer confidence all suggest that the cyclical peak may be over, but we do not expect sharp deceleration. In the short run, the announced demography programme can give some new impetus to consumption growth, but we think it will rather boost housing investment.
- Other sectors' consumption can also be in line with our medium-term forecast. Even though the consumption of the non-profit sector grew at a surprisingly strong pace (20% QoQ, annualized), the government's consumption grew slower than we had expected. So, these factors roughly counterbalance each other.
- The positive growth contribution of net exports was also a surprise, particularly in the light of the fixed capital formation figure. We see that in Q1, the calendar effect appeared stronger in the export figure than in imports. Furthermore, in the preliminary CA statistics, the NEO (net error and omissions) widened significantly. The current high NEO is expected to decline after data revisions and when more detailed data become available, so we cannot rule out a revision in the net exports figure.

Trading Desks

Dealing code: OTPH
Live quotes at
OTP BLOOMBERG page

This report is available at
BLOOMBERG:
OTP/Macroeconomics
Research page

Fixed Income Desk

András Sovány
+36 1 288 7561
SovanyA@otpbank.hu

Benedek Károly Szűts
+36 1 288 7560
SzutsB@otpbank.hu

FX Desk

András Marton
+36 1 288 7523
MartonA@otpbank.hu

József Horváth
+36 1 288 7514
Horvath.Jozsef@otpbank.hu

Money Market Desk

Gábor Fazekas
+36 1 288 7536
FazekasGa@otpbank.hu

Gábor Heidrich
+36 1 288 7534
HeidrichG@otpbank.hu

Judit Szombath
+36 1 288 7533
SzombathJ@otpbank.hu

FX Option Desk

Gábor Réthy
+36 1 288 7524
RethyG@otpbank.hu

Máté Kelemen
+36 1 288 7525
KelemenMat@otpbank.hu

Analyst

Győző Eppich
+36 1 374 7274
eppichgyo@otpbank.hu

- After the release of the very strong business cycle indicators about Q1, we raised our GDP forecast for 2019 from 3.8% to 4.5%, mainly because of one reason: we increased significantly our forecast on fixed capital formation growth from 9.8% to 15.6%. Nevertheless, we still think risks are lying on the upside. Hungary's 'economy protection plan', announced on 30 May, has only minor effect on GDP growth and most of its measures will not come into force before 2020. The biggest action is the two-percentage-point cut in social contributions (taking effect on 1 July 2019), but it had been already announced under the tripartite six-year wage agreement. So, we have incorporated this measure into our baseline already. Other measures mean roughly HUF 100 bn (<0.25% of GDP) easing on the budget balance, but it is gross effect. The net effect may be less than 0.2% of GDP.

Main macro forecasts

Key economic indicators							OTP	
	2013	2014	2015	2016	2017	2018	2019F	2020F
Nominal GDP (at current prices, bn HUF)	30 248	32 583	34 379	35 474	38 355	42 073	45 770	49 039
Real GDP change	2.1%	4.2%	3.5%	2.3%	4.1%	4.9%	4.5%	3.1%
Household final consumption	0.5%	2.4%	3.7%	3.4%	4.1%	4.6%	4.5%	3.7%
Household consumption expenditure	0.2%	2.8%	3.9%	4.0%	4.7%	5.3%	4.6%	4.2%
Collective consumption	6.6%	10.0%	0.0%	0.9%	2.0%	-2.1%	4.3%	1.6%
Gross fixed capital formation	9.8%	12.3%	4.7%	-11.7%	18.2%	16.5%	15.6%	5.5%
Exports	4.2%	9.1%	7.2%	5.1%	4.7%	4.7%	3.3%	5.2%
Imports	4.5%	11.0%	5.8%	3.9%	7.7%	7.1%	6.5%	6.0%
in percent of GDP	-2.6%	-2.6%	-1.9%	-1.6%	-2.2%	-2.2%	-1.8%	-1.6%
General government debt (in percent of GDP)	77.1%	76.6%	76.7%	76.0%	73.6%	70.8%	68.7%	65.4%
Current account (EUR bn)*	3.9	1.6	3.1	7.1	3.5	0.6	-1.3	-1.6
in percent of GDP	3.8%	1.5%	2.8%	6.2%	2.8%	0.5%	-0.9%	-1.1%
Gross nominal wages**	4.1%	3.6%	4.4%	6.5%	12.9%	9.2%	7.6%	6.1%
Gross real wages	2.3%	3.9%	4.5%	6.1%	10.3%	6.2%	4.3%	3.7%
Gross disposable income***	2.5%	4.5%	5.9%	2.2%	9.0%	8.1%	7.6%	6.6%
Gross real disposable income	0.7%	4.7%	5.9%	1.8%	6.5%	5.1%	4.4%	4.2%
Employment (annual change)	1.7%	5.3%	2.7%	3.4%	1.6%	1.1%	-0.1%	0.1%
Employment domestic concept w/o public workers	0.5%	3.4%	1.7%	3.1%	3.1%	2.4%	0.1%	0.4%
Unemployment rate (annual average)	10.2%	7.7%	6.8%	5.1%	4.2%	3.7%	3.7%	3.6%
Inflation (annual average)	1.7%	-0.2%	-0.1%	0.4%	2.4%	2.8%	3.1%	2.3%
Base rate (end of year)	3.00%	2.10%	1.35%	0.41%	0.03%	0.13%	0.40%	0.90%
1Y Treasury Bill (average)	4.11%	2.28%	1.17%	0.77%	0.09%	0.25%	0.46%	0.93%
Real interest rate (average, ex post)	2.3%	2.5%	1.2%	0.4%	-2.2%	-2.5%	-2.6%	-1.3%
EUR/HUF exchange rate (average)	297.0	308.6	309.9	311.5	309.3	318.9	320.1	320.0
EUR/HUF exchange rate (end of year)	296.9	314.9	313.1	311.0	310.1	321.5	320.0	320.0

Sources: CSO, MNB, OTP Bank

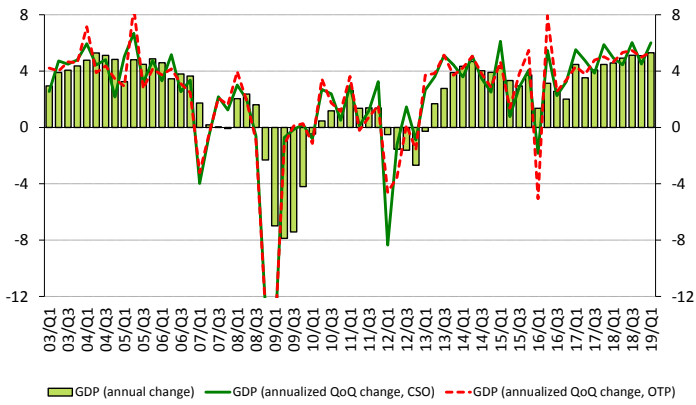
*: Official data of balance of payments (excluding net errors and omissions)

** : Total wages including accrual based salaries in governmental sector. In the case of private sector wages we calculated with whitening effect filtered wages and we adjusted the changeable seasonality of the bonus payments.

***: Calculation based on financial accounts data

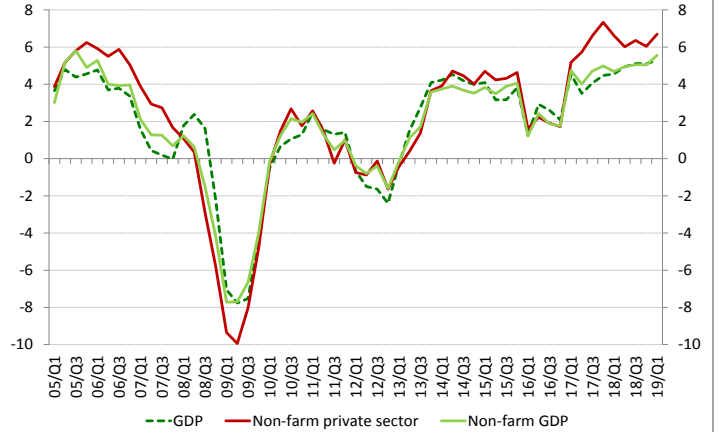
****: According to the preliminary financial accounts data the government surplus was 4.3% of GDP in 2011. Due to methodological reasons the official data that is publishing in April 2012 can be different

Chart 1: Summary chart of GDP growth
(annual and annualized QoQ growth rates, %)



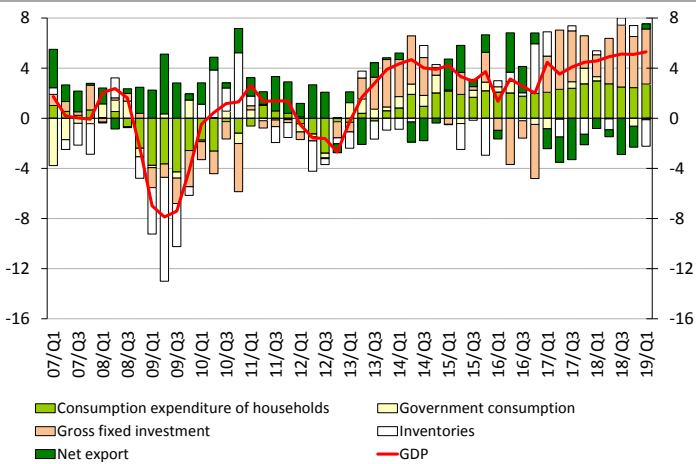
Sources: KSH, OTP Research

Chart 2: Different indicators of economic activity
(annual changes, %)



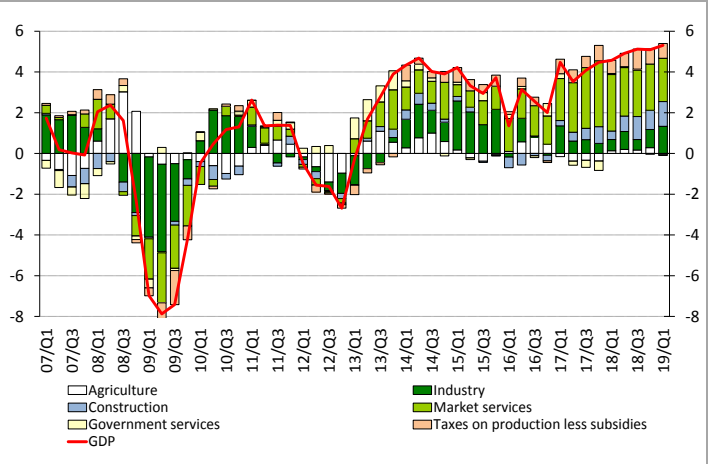
Sources: KSH, OTP Research

Chart 3: Decomposition of GDP growth by expenditure-side items
(quarterly data, %)



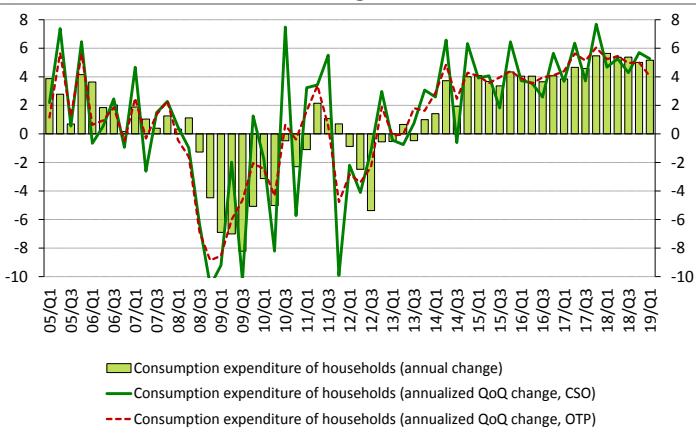
Sources: KSH, OTP Research

Chart 4: Decomposition of GDP growth by production-side items
(quarterly data, %)



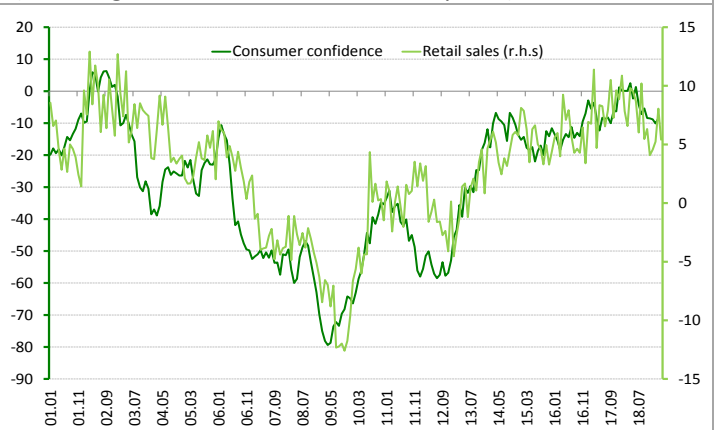
Sources: KSH, OTP Research

Chart 5: Consumption expenditure of households
(annual and annualized QoQ growth rates, %)



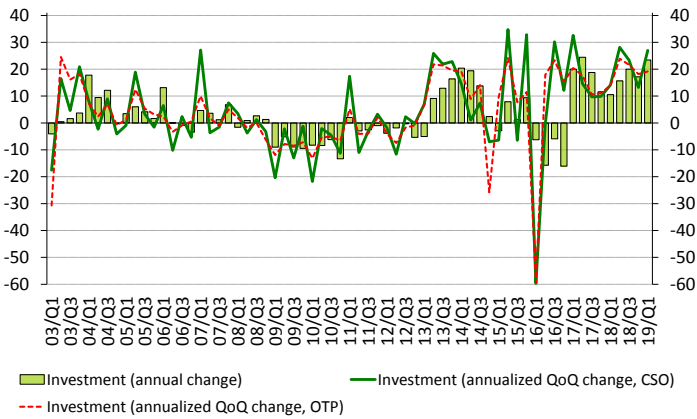
Sources: KSH, OTP Research

Chart 6: Retail sales and consumer confidence
(annual growth rate, % and balance point)



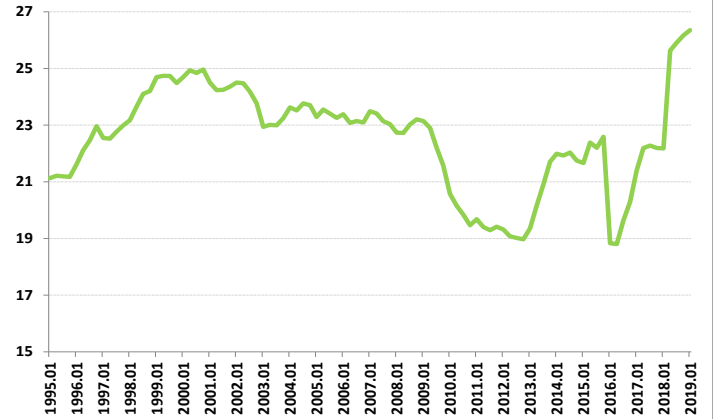
Sources: KSH, OTP Research

Chart 7: Fixed capital formation
(annual and annualized QoQ growth rates, %)



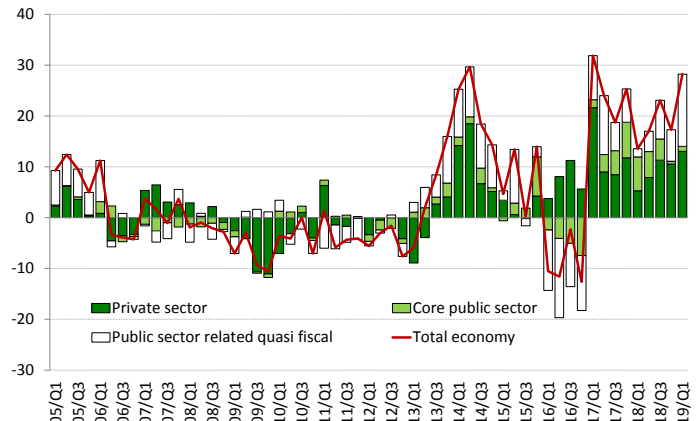
Sources: KSH, OTP Research

Chart 8: Investment rate
(% of GDP)



Sources: KSH, OTP Research

Chart 9: Decomposition of investment growth by sector
(ppts contribution)



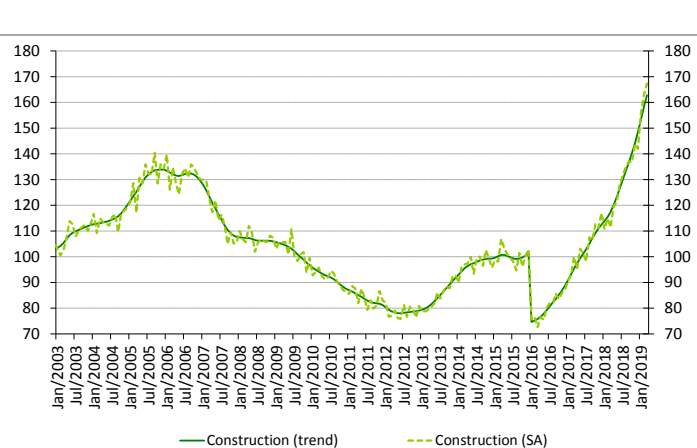
Sources: KSH, OTP Research

Chart 10: NFCs' performing loan growth (YoY, %)



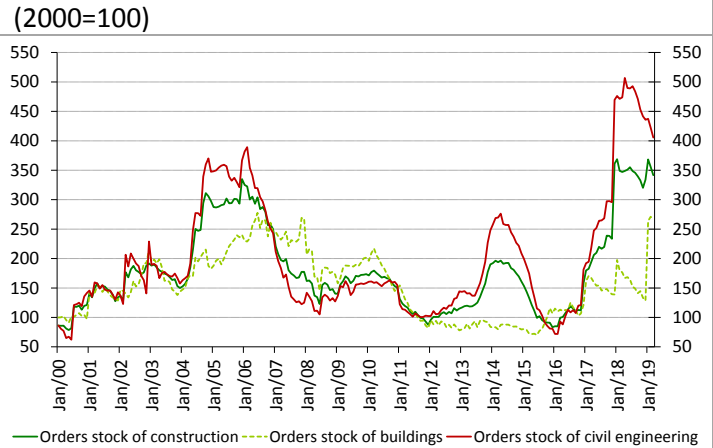
Sources: MNB, OTP Research

Chart 11: Construction output (2015=100)



Sources: KSH, OTP Research

Chart 10: Orders backlog in the construction sector
(2000=100)



Sources: KSH, OTP Research

1. **The statements in this document shall not be considered as an objective or independent explanation of the matters. Please note that this document (a) has not been prepared in accordance with legal requirements designed to promote the independence of investment research, and (b) is not subject to any prohibition on dealing ahead of the dissemination or publication of investment research.**
2. This communication does not contain a comprehensive analysis of the described issues. No part, chapter, or the entirety of this information shall be considered as investment recommendation, an offer or solicitation for the purchase or sale of any financial instrument, inducement to invest, financial or investment analysis, investment research or marketing communication, not even if any part of this document contains a description of a certain financial instrument in terms of its possible price or yield development, and the related investment options; the data herein are for informational purposes only. This document shall not be considered as investment recommendation falling under Directive 596/2014/EU of the European Parliament and of the Council. This document does not take into account investors' individual interests, circumstances, or objectives; therefore, in the absence of personal recommendation, it shall not be considered as investment advice. OTP Bank intends to make this document available to its clients or to the public, or to make it accessible to other persons in such a way that allows this document to be disseminated to the public.
3. Information herein reflects the market situation at the time of writing. However, it provides only momentary information and may change as market conditions and circumstances develop. You may request more information from OTP Bank. Although the information in this document has been prepared in good faith from sources that OTP Bank believes to be reliable, we do not represent or warrant its accuracy or completeness. This document was prepared using data, facts and information from the following essential sources: Bloomberg, Reuters, KSH (Hungarian Central Statistical Office), Eurostat, Magyar Nemzeti Bank (Hungary's central bank) ÁKK (Hungary's Government Debt Management Agency), and European Central Bank (ECB). The opinions and estimates in this document are based on the opinion of OTP Research's analyst(s) at the time when the document was prepared, and they may be subject to change at any time in the future without further notice. You may receive different recommendation from the staff of OTP Bank, in particular if you are provided investment advice based on an investment advice agreement.
4. This publication contains generic presentation of information and knowledge, thus it does not take into account the individual clients' unique and special interests, financial condition, or their ability and willingness to take risks. Therefore please contact our staff or contact your banking consultant for advice before you make an investment decision. The assessment and the consideration of the individual circumstances is provided by the suitability and appropriateness tests that assess clients' financial knowledge, experience, risk-taking abilities, as well as the examination of the target market.
5. Before making an informed decision to invest and to use the services, please carefully read through all documents, including the documentation, prospectus, regulations, terms and conditions, announcements and key information documents for that product/service, and carefully consider the subject, the risk, the fees and costs of your investment, the possibility of any loss, and seek information about the tax regulations regarding the product and the investment. The prices of financial instruments and securities are changing, outright sales are realized at then current market prices, which may involve losses. The information and opinions in this document do not substitute or take the place of the issuance documentation for the given financial assets (e.g. prospectus, fund management rules), or their brochures or announcements.
6. You assume total responsibility and risk for any specific decision or investment; OTP Bank shall not be held responsible for the effectiveness of investment decisions or for reaching your purpose, nor for the individual investment decision made based on this document or any part thereof, or for their consequences.
Investments in financial instruments carry a certain degree of risk, which may affect the effectiveness of the investment decision, and investors may not receive the whole amount they expected the investment to yield in their investment targets; they may not preserve even the invested amount, therefore the invested capital might even decrease, be wholly lost, or even lead to additional payment obligation.
7. Trading with leveraged products (such as foreign exchange contracts) or with shares and indices that have underlying products carries a considerable amount of risk, and these products are not suitable for all investors. Trading with leveraged products carries the risk of losing all capital, and it may incur losses that exceed the amount invested.
8. **The figures and information described herein refer to yields or changes in the past. Past performance is not a reliable indicator of future yields, changes, or performance.** The changes on money and capital markets, the fluctuation of prices, the development of investments and their yields are influenced by the combined effect of multiple factors; one important factor of them is the change in investors' expectations. **The development of prices, the future yield of financial assets, indices or indicators, the examination of their changes, trends, and future performance is based on estimations and forecasts, which forecasts do not allow reliable conclusions to be drawn about the future moves of prices, real future yields, changes, or performance.** For each product and service, please assess their tax accounting implications, and other tax consequences, taking into account that they cannot be precisely assessed without knowing the effective tax regulations or the client's individual circumstances; and these legislative provisions as well as the circumstances may change over time.
9. This document shall not be a basis for any further analysis in relation to the financial instruments contained therein. Any reference in this document to the future distribution of a financial instrument shall be construed as indicative, preliminary and informative, and any analysis of such financial instrument is exclusively based on publicly available information listed in the respective prospectus or announcement. The content of this document shall not imply that OTP Bank acts as an agent, a fiduciary, or an advisor to, or on behalf of, any prospective purchaser of the financial instruments discussed herein.
10. For certain persons, access to the products and/or services discussed in this document may not be granted, or it may be limited. The act of preparing this document by OTP Bank, its uploading to the website, its publication may under no circumstances be considered as OTP Bank's intention to make available the product and/or service information in the prospectus to persons whom any country or state prohibits from having or obtaining the given product and/or service, including the promotion and the advertisement thereof.
11. OTP Bank maintains a conflict of interest policy and it keeps such records, and it also has requirements that regulate the transmission of bank secrets and securities secrets, which requirements shall be considered as the effective internal organizational and management solutions as well as information barriers to prevent or manage conflicts of interest.
OTP Bank has developed appropriate internal procedures for (i) the personal transactions and trading of financial analysts and other relevant persons, (ii) the physical separation of the financial analysts involved in the production of investment research and other relevant persons; moreover, information barriers have been implemented, (iii) for accepting and managing incentives and remuneration.
Please be informed that OTP Bank is entitled to deal or trade as market maker, acting in good faith and in accordance with the usual way of market-making, with the financial instruments distributed by the issuer(s) specified in this document, as well as to provide other investment activities or ancillary (investment) services, and/or other financial or ancillary financial services to the issuer and other persons.
12. Previous documents on investing in this asset or product are available on the website of OTP Research: www.otpresearch.com
13. OTP Bank (company registration number: 01-10-041-585; registered seat: Nádor utca 16., Budapest H-1051, Hungary. Supervisory authority: Magyar Nemzeti Bank (National Bank of Hungary – H-1054 Budapest, Szabadság tér 9); financial customer services: H-1013 Budapest, Krisztina krt. 39. PSZÁF licence numbers: III/41.003-22/2002 and E-III/456/2008; further information: <https://www.otpbank.hu/portal/hu/Megtakaritas/Ertekpapir/MIFID>). All rights reserved. This document is solely owned by OTP Bank. No part of this material can be reproduced, re-used, disseminated, made available, re-published, referenced to, or inserted in other websites or services without the prior written consent of OTP Bank.
14. If you received this document from OTP Bank Plc, then it was sent to you with your previous consent. You may withdraw this permission by sending an e-mail to research@otpbank.hu or by writing a letter to 'Research Center', Hungary H-1051, Budapest, Nádor utca 21. Please refer to your name and e-mail address in both cases.
Data management registration number: NAIH-89457/2015
15. The personal data in this investment research are processed by OTP Bank. The legal basis for processing the data is the legitimate interest of OTP Bank. The detailed information about the processing of personal data and the related rights of data subjects is available [here](#).

This document was prepared on 03 June 2019.