INFLATION REPORT

2024
DECEMBER

'... wise is the man who can put purpose to his desires.'

Miklós Zrínyi: The Life of Matthias Corvinus

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Act CXXXIX of 2013 on the Magyar Nemzeti Bank designates achieving and maintaining price stability as the primary objective of the Magyar Nemzeti Bank (MNB), the central bank of Hungary. Over the long term, low inflation ensures higher economic growth and a more predictable economic environment, while moderating the cyclical fluctuations that impact both households and companies. Without prejudice to its primary objective, the MNB supports the maintenance of the stability of the financial intermediary system and the enhancement of its resilience and its sustainable contribution to economic growth, as well as the economic and environmental sustainability policy of the government using the instruments at its disposal.

In the inflation targeting system in use since August 2005, the central bank has sought to attain price stability by ensuring an inflation rate near the 3 percent medium-term target. The Monetary Council, the supreme decision-making body of the Magyar Nemzeti Bank, performs a comprehensive review of expected developments in inflation every three months, in order to establish the monetary conditions consistent with achieving the inflation target. The Monetary Council takes its decisions on the basis of and in accordance with the objectives set out in the Act on the Magyar Nemzeti Bank. Accordingly, in its decisions, it takes into account, among other things, prospective economic developments, the inflation outlook, financial and capital market trends and risks to stability.

In order to provide the public with a clear insight into how the central bank's monetary policy works and to enhance transparency, the Bank publishes the information available at the time of making its monetary policy decisions. The Inflation Report presents the inflation forecasts prepared by the Directorate Economic Forecast and Analysis, the Directorate Monetary Policy and Financial Market Analysis, the Directorate Fiscal Analysis and the Directorate Financial System Analysis, as well as the macroeconomic developments underlying these forecasts. The forecast is based on the assumption of endogenous monetary policy. In respect of economic variables exogenous to monetary policy, the forecasting rules used in previous issues of the Report are applied.

The analyses in this Report were prepared under the general direction of the Executive Director of Economic and Fiscal Analysis and Statistics. The Report was prepared by staff at the MNB's Directorate Economic Forecast and Analysis, Directorate Monetary Policy and Financial Market Analysis, Directorate Fiscal Analysis, Directorate Financial System Analysis and Directorate for International Monetary Policy Analysis and Training of Economic Sciences. The Report was approved for publication by Barnabás Virág, Deputy Governor responsible for Monetary Policy, Financial Stability and International Relations.

The Report incorporates valuable input from other areas of the MNB and the Monetary Council's comments.

The projections are based on information available for the period ending 22 December 2024.

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The Monetary Council's key findings related to the Inflation report

THE MONETARY COUNCIL'S KEY FINDINGS RELATED TO THE INFLATION REPORT

The primary objective of the Magyar Nemzeti Bank (MNB) is to achieve and maintain price stability. Without prejudice to its primary objective, the Magyar Nemzeti Bank preserves financial stability and supports the Government's economic and environmental sustainability policy.

Economic output in the European Union expanded at a moderate pace in the third quarter; however, the unfavourable outlook for industrial production in Europe and the generally tense geopolitical situation pose risks.

The EU economy expanded by 1.0 percent in 2024 Q3 year-on-year. Incoming data were slightly above expectations. The economic performance of Germany, Hungary's main trading partner, grew slightly, by 0.1 percent on a quarterly basis. In 2024 Q3, US GDP expanded by 2.7 percent, while growth in the Chinese economy amounted to 4.6 percent; thus growth is still buoyant in both economies, albeit with a slight deceleration. In terms of external economic trends, the unfavourable outlook for industrial production in Europe and the generally tense geopolitical situation pose risks.

In the European Union, the consumer price index dropped to 2.1 percent in September year-on-year before edging up slightly to 2.3 percent in October.

Based on data available, in most EU Member States – 19 countries – inflation in November exceeded the October data. Within the region, inflation rose in Slovakia (3.2 percent), while it moderated in Poland (4.6 percent) and remained at the same level in the Czech Republic (2.8 percent) in November. Based on preliminary data, euro area inflation stood at 2.3 percent in November compared to 2.0 percent in October. Inflation in the United States has been below 3 percent since July, and it was 2.7 percent in November.

Among the major global central banks, the European Central Bank (ECB) lowered its policy rate by 25 basis points both in October and December. At its November meeting, the Federal Reserve (Fed) decreased the target range for the federal funds rate by 25 basis points to 4.50–4.75 percent. In the region, the Czech central bank continued to lower its base rate, while the Polish and Romanian central banks maintained their policy rates in the past quarter.

At its rate-setting meetings in October and December, the ECB cut its key deposit rate by 25–25 basis points, lowering the rate to 3 percent overall. In its press release, the central bank expressed that, based on the inflation outlook, the dynamics of underlying inflation and the monetary policy transmission, disinflation was on track. The ECB also indicated that it would continue to make decisions in a data-driven manner, and that it did not intend to commit to a predetermined interest rate path. In the United States, at its November meeting the Fed lowered the target range for the federal funds rate by 25 basis points to 4.50–4.75 percent. Although further progress has been made towards the central bank's inflation target of 2 percent in recent months, inflation remained at a somewhat higher level. According to the statement of the Fed's Open Market Committee, the risks to achieving its employment and inflation goals are nearly balanced. The Chairman of the Fed expressed that economic activity was expanding at a solid pace and labour market conditions continued to ease.

In the region, the Czech central bank cut its policy rate by 25–25 basis points each at its September and November policy meetings, bringing down the base rate to 4 percent. The Polish and Romanian central banks did not change interest rate conditions, with the Polish central bank keeping its policy rate at 5.75 percent and the Romanian central bank at 6.50 percent during the last quarter.

In the past quarter, global investor sentiment was volatile and deteriorating, overall, primarily affected by the economic policy implications of the US presidential election, geopolitical risks linked to the conflicts in Ukraine and the Middle East, and expectations regarding the interest rate policies of major central banks.

Amid rising uncertainty, global investor sentiment deteriorated in the period leading up to the US presidential election in early November. The rise in volatility affected bond markets the most, but volatility in foreign currency rates and developed stock market indices also increased. Following the US elections, the intensification of global trade disputes and the risks related to geopolitical conflicts and developments in the domestic politics of some countries in Europe were the main drivers of asset price developments. In parallel with the strengthening of the dollar, the rise in developed stock markets typically exceeded the levels seen in emerging regions. Emerging market currencies depreciated on average in the past quarter.

Market expectations diverged for interest rate paths in the US and Europe. As a result of favourable macroeconomic data from the United States, the interest rate path expected from the Fed shifted upwards, while expectations about the ECB's interest rate path shifted downwards on the back of unfavourable incoming macroeconomic data. The US ten-year yield rose to 4.24 percent, while the German yield fell to 2.12 percent. Long-term yields in the region increased by 10–40 basis points. The dollar strengthened significantly against developed market currencies in the past quarter, appreciating by 6 percent against the euro, 4.3 percent against the Swiss franc and 7.1 percent against the Japanese yen.

Gas prices in Europe rose sharply to an annual high last quarter, primarily owing to heightened risks to the security of supply driven by geopolitical conflicts. The temporary intensification of geopolitical conflicts also pushed up oil prices per barrel temporarily, but overall, the decline continued in the last quarter, reflecting the ceasefire agreement in Lebanon and expectations for a further weakening demand.

Decoupling from regional currencies, the forint weakened considerably in the past quarter. Government bond yields and interbank yields both increased during the period.

Following the interest rate decision in September, the forint depreciated against the euro in the run-up to the US elections, broadly consistent with the currencies of the region. From the beginning of November, the dollar strengthened against the euro at an accelerating pace, which, together with the intensification of domestic risk factors, weakened the forint to a greater extent relative to other regional currencies. The short end of the government bond market yield curve fell by 15 basis points on average, while the long end shifted upwards by 15 basis points. Short-term interbank rates also edged up by 15 basis points on average as the further rate cuts expected previously in the near term priced out as a result of the deterioration in sentiment.

There were three credit rating agency revisions in the last quarter. S&P kept the current stable outlook for Hungary's investment grade rating unchanged, Moody's revised the stable outlook to negative, while Fitch Ratings upgraded the former negative outlook to stable. In addition to macroeconomic fundamentals, the perception of fiscal and monetary policy outlook had a key role in the assessment of the credit rating agencies.

In Hungary, inflation stood at 3.2 percent in October, while consumer prices rose by 3.7 percent in November year-on-year. On average, inflation may range between 3.6–3.7 percent this year, 3.3–4.1 percent in 2025 and 2.5–3.5 percent in 2026 and 2027.

In November 2024, inflation rose to 3.7 percent, while core inflation declined to 4.4 percent. The rise in the CPI was mainly driven by the accelerating growth rate of fuel prices. The decline in core inflation can be attributed to the continued disinflation of market services prices from high levels. In November, the extent of repricings for industrial goods was below, while for market services and food it was above the historical average. The downward trend in households' inflation expectations reversed since August, and in November inflation expectations in Hungary rose in line with those in the region.

Inflation is expected to increase further temporarily until January 2025 and may be above the central bank tolerance band. Disinflation will restart thereafter, in 2025 Q1. In 2025, inflation is expected to remain within the tolerance band for most of the year, before returning to the 3 percent central bank target in a sustained manner at the beginning of 2026. The slowdown in price dynamics is driven by more subdued underlying developments compared to the MNB's earlier expectations, and more moderate backward-looking repricings next year. The exchange rate depreciation seen in past months as well as changes to the system of excise duties are likely to slow disinflation next year. At around 4.5 percent, core inflation, which captures the underlying trends of inflation, will remain at around its current level in the coming months, before moderating from spring 2025 onwards to around 3 percent by the second half of the year. According to the

MNB's forecast, annual inflation may range between 3.6–3.7 percent on average this year, 3.3–4.1 percent in 2025 and 2.5–3.5 percent in 2026 and 2027. The MNB's 2025 projection for inflation has been revised upward compared to the September projection. The shift can be attributed to the pass-through of recent exchange rate changes into consumer prices, rising food commodity prices and the excise duty increase from January 2025, the effects of which are partly offset by more moderate underlying inflation. Anchoring inflation expectations, maintaining financial market stability and disciplined monetary policy are essential for the CPI to return to the central bank's target in a sustained manner.

In 2024 Q3, the economic performance in Hungary declined. Therefore, growth is likely to remain subdued this year as a whole, supported mainly by household consumption. The Hungarian economy is expected to grow by 0.3–0.7 percent in 2024, and expand by 2.6–3.6 percent in 2025, 3.5–4.5 percent in 2026, and 2.5–3.5 percent in 2027.

In 2024 Q3, the Hungarian economy contracted by 0.8 percent year-on-year and by 0.7 percent quarter-on-quarter. The slowdown was driven by a decline in the performance of industry, construction and agriculture, while the growth contribution of services was positive. Consumption continued to increase in line with rising real wages. Household consumption rose by 4.5 percent year-on-year in the third quarter, supporting GDP growth by 2.0 percentage points. A sharp fall in investments held back economic growth by 4.0 percentage points. Investments fell in sectors producing for the domestic and export markets, in the public sector and in sectors indirectly linked to the government, and the decline was only partly offset by an increase in household investments. With exports falling by 1.9 percent and imports by 0.9 percent, net exports restrained growth by 0.9 percentage points in the third quarter. The tightness of the labour market has eased in recent quarters. Following a decline in September, the number of persons employed stabilised in October, and thus remains at a high level of 4.7 million. The unemployment rate remained low at 4.5 percent.

Household consumption, gradually expanding in 2024, is expected to be the driver of growth looking ahead, supported by the launch of the Subsidised Workers' Credit Programme and an increase in family tax allowances, in addition to a rise in real wages. However, the investments are expected to fall significantly this year, restraining economic growth in 2024. This is primarily attributed to a contraction in public and corporate investments, which cannot be offset by the moderate increase in household investments. Surveys indicate that the long shadow of inflation, the lack of demand, and uncertainty continue to hamper corporate developments. Partial replacement of delayed investments in the corporate sector will start in 2025 in parallel with the persistent improvement in demand. A subdued European economy will continue to restrain domestic exports in the short term. At the same time, ongoing and newly announced significant capacity-increasing foreign direct investments will boost exports from mid-2025, while Hungary's export market share will also increase. The Hungarian economy is expected to grow by 0.3–0.7 percent in 2024, and expand by 2.6–3.6 percent in 2025, 3.5–4.5 percent in 2026, and 2.5–3.5 percent in 2027.

Trends in domestic lending continue to have a dual nature: the household credit market continued to pick up, while corporate credit demand remained low.

The annual growth rate of corporate loans in the total financial intermediary system accelerated by 1.6 percentage points compared to the previous quarter, reaching 6.9 percent at the end of 2024 Q3. The total amount of housing loans originated by credit institutions in the third quarter increased by 130 percent compared to the low base of the previous year, while that of personal loans originated was 57 percent higher. Based on the responses to the Lending Survey, banks expect unchanged demand for unsecured loans, while housing loans are likely to see an upswing in demand in the current and the next quarter. The annual growth rate of household loans outstanding may stand at 9 percent at the end of 2024 and, as a result of real economic fundamentals supporting retail lending and the launch of the Subsidised Workers' Credit Programme, growth may peak at around 14 percent at the end of 2025.

The annual growth rate of corporate loans in the total financial intermediary system accelerated by 0.1 percentage points compared to the previous quarter, reaching 3.8 percent at the end of 2024 Q3. However, the outstanding borrowing of micro, small and medium-sized enterprises stagnated in annual terms. In the third quarter of the year, the value of newly originated corporate loans –without current account loans – was 19 percent lower than the level seen a year earlier. Based on the responses to the Lending Survey, banks perceived a moderation in demand in the third quarter, and looking ahead to 2024 Q4 and 2025 Q1, demand is expected to remain unchanged. Given the contraction in investments and the uncertain outlook for economic growth, the annual growth rate of corporate credit is expected to reach 3 percent at the end of

2024 before stabilising at around 8–9 percent from 2025 H2, in parallel with the upswing in economic activity, the launch of the Demján Sándor Programme and the easing of uncertainty.

The current account surplus continues to increase.

The improvement in the external position continues in 2024. This year's increase in the current account surplus is predominantly owing to a more favourable external trade balance. This is partly due to a further, moderate improvement in the terms of trade and the increasing surplus of the goods balance, reflecting lower imports as a result of declining investments. Besides normalising external demand, the rising export market share resulting from the more intense use of existing capacities and ongoing projects becoming operational is expected to lead to a sustained surplus in the external position across the forecast horizon. The surplus on services will stabilise above 5 percent of GDP in the coming years. As a result, the current account surplus is expected to be 1.5–2.7 percent of GDP in 2024, 1.0–2.4 percent in 2025, 1.5-3.1 percent in 2026 and 1.8–3.6 percent in 2027.

According to the MNB's forecast, the budget deficit-to-GDP ratio will be 4.4–4.8 percent in 2024 and 3.4–4.2 percent in 2025. Thereafter, the deficit may range between 2.8–3.8 percent in 2026 and between 2.2–3.2 percent in 2027. The improvement in the balance in 2024 has been driven by falling energy expenditures resulting from the stabilisation of energy prices and restrained public investment. The 2025 budget bill confirmed the deficit target of 3.7 percent, the achievement of which will be mainly supported by a significant decline in government interest expenditures and tax measures aimed at increasing revenues. According to the MNB's projection, the primary balance excluding interest expenditures is likely to reach near-equilibrium levels over the entire forecast horizon. The reduction of public debt in 2024 is significantly hampered by the high cash flow deficit, subdued economic growth and the revaluation of foreign currency debt; however, the MNB expects the debt-to-GDP ratio to fall below 70 percent by the end of the forecast horizon as the deficit gradually declines.

Based on the Monetary Council's risk assessment, the baseline projection is surrounded by upside risks to inflation and downside risks to growth.

The Monetary Council highlighted three alternative risk scenarios around the baseline projection in the December Inflation Report. In the scenario that assumes prolonged weakness in European economic activity, economic growth and inflation are both likely to be lower compared to the baseline. The scenario featuring increased trade policy tensions is consistent with a higher inflation and lower growth path than the baseline. The risk scenario assuming capital outflows from emerging economies is also consistent with higher inflation and a lower growth path. In addition to the scenarios highlighted, the Monetary Council discussed other alternative paths, including a faster recovery in consumption, slower investment growth and faster improvements in productivity and energy efficiency.

SUMMARY TABLE OF THE BASELINE SCENARIO

(Data show annual changes and the forecast is based on endogenous monetary policy.)

	2023	2024	2025	2026	2027
	Actual	Forecast			
Inflation (annual average)					
Core inflation	18.2	4.6 - 4.7	3.2 - 3.8	2.6 - 3.2	2.6 - 3.2
Core inflation excluding indirect tax effects	18.1	4.6 - 4.7	3.0 - 3.6	2.6 - 3.2	2.6 - 3.2
Inflation	17.6	3.6 - 3.7	3.3 - 4.1	2.5 - 3.5	2.5 - 3.5
Economic growth					
Household final consumption expenditure	-1.9	3.9 - 4.1	4.3 - 5.1	3.5 - 4.5	2.7 - 3.7
Government final consumption expenditure[1]	4.1	(-0.1) - 0.1	(-0.1) - 0.7	0.0 - 1.0	(-0.1) - 0.9
Gross fixed capital formation	-7.8	(-12.3) - (-11.7)	3.5 - 6.5	2.6 - 5.4	1.5 - 4.5
Domestic absorption	-5.6	(-0.5) - 0.1	2.8 - 4.6	2.0 - 3.6	1.7 - 2.9
Exports	1.5	(-2.4) - (-1.8)	3.6 - 5.6	6.1 - 7.9	5.1 - 6.9
Imports	-3.8	(-3.3) - (-2.7)	4.4 - 6.6	4.9 - 6.9	4.4 - 6.4
GDP	-0.9	0.3 - 0.7	2.6 - 3.6	3.5 - 4.5	2.5 - 3.5
Labour productivity[2]	-1.1	0.3 - 0.5	2.7 - 3.7	2.9 - 4.3	2.1 - 3.5
External balance[3]					
Current account balance	0.7	1.5 - 2.7	1.0 - 2.4	1.5 - 3.1	1.8 - 3.6
Net lending	1.7	2.2 - 3.4	2.6 - 4.0	3.3 - 4.9	3.0 - 4.8
Government balance[3]					
ESA balance	-6.7	(-4.8) - (-4.4)	(-4.2) - (-3.4)	(-3.8) - (-2.8)	(-3.2) - (-2.2)
Labour market					
Whole-economy gross average earnings[4]	14.3	12.9 - 13.1	8.6 - 9.6	10.0 - 11.2	6.7 - 8.0
Whole-economy employment	0.6	0.0 - 0.1	(-0.3) - 0.1	0.1 - 0.8	(-0.2) - 0.6
Private sector gross average earnings[4]	16.3	11.6 - 11.8	8.5 - 9.5	8.5 - 9.7	8.8 - 10.0
Private sector employment	1.0	(-0.1) - 0.0	(-0.1) - 0.3	0.3 - 0.8	0.0 - 0.5
Unemployment rate	4.1	4.5 - 4.6	4.1 - 4.3	3.2 - 3.8	2.9 - 3.9
Private sector nominal unit labour cost	17.7	12.6 - 12.9	8.0 - 9.4	4.5 - 6.2	4.6 - 6.3
Household real income[5]	0.2	4.7 - 4.9	3.7 - 4.4	4.1 - 5.1	2.6 - 3.6

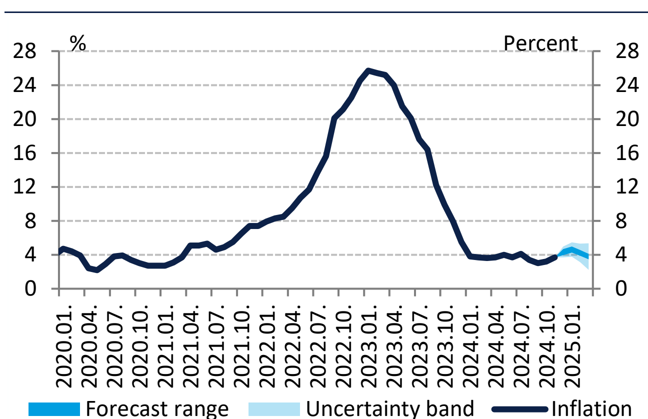
[1] Government final consumption expenditure includes final consumption expenditure of general government and non-profit institutions.
[2] Whole economy, based on national accounts data.
[3] As a percentage of GDP.
[4] For full-time employees.
[5] MNB estimate.

1 Inflation and real economy outlook

1.1 Inflation forecast

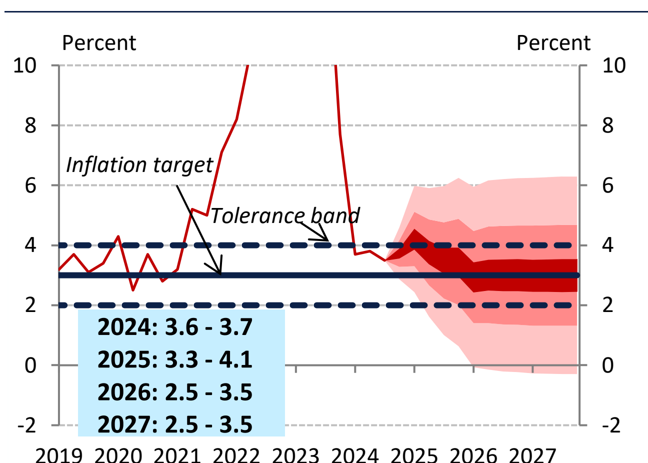
Consumer prices rose by 3.7 percent year-on-year in November. Inflation will continue to rise until January 2025 and may remain above the central bank's tolerance band. The disinflationary trend will resume in 2025 Q1. Next year, inflation will remain within the tolerance band for most of the year, before returning to the central bank's target of 3 percent on a sustained basis in early 2026. The slowdown in price dynamics is supported by more subdued underlying processes than the MNB had previously expected, as well as more moderate retrospective repricings next year. The exchange rate depreciation seen in recent months and changes to the excise tax system will slow down the disinflation process next year. Core inflation, which captures the underlying trajectory of inflation, will stay at a similar level to the current rate of around 4.5 percent in the coming months, before moderating from spring 2025 onwards to around 3 percent in the second half of the year. Inflation may average between 3.6 and 3.7 percent this year, 3.3 and 4.1 percent in 2025, and between 2.5 and 3.5 percent in 2026 and 2027. Core inflation excluding indirect tax effects is projected to be between 4.6 and 4.7 percent in 2024, between 3.0 and 3.6 percent in 2025 and between 2.6 and 3.2 percent in 2026 and 2027.

Chart 1-1: Monthly evolution of the near-term inflation forecast



Note: Annual change. The uncertainty band shows the uncertainty around the forecast range with regards to the root mean squared error of previous years' near-term forecasts.
Source: HCSO, MNB

Chart 1-2: Fan chart of the inflation forecast



Note: Based on seasonally unadjusted data.
Source: HCSO, MNB

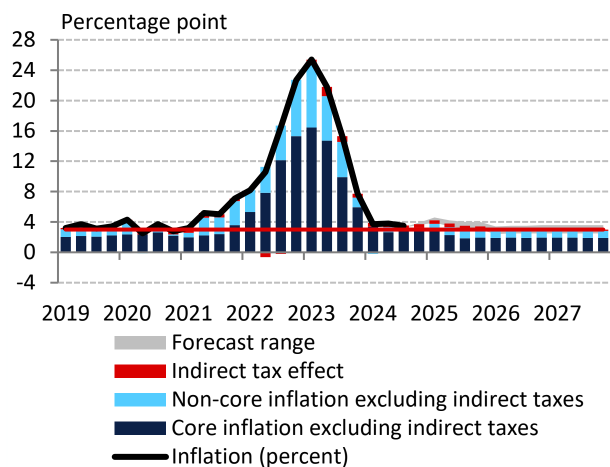
Inflation will continue to rise until January 2025 and may remain above the central bank's tolerance band. The disinflationary trend will resume in 2025 Q1 (Chart 1-1). Core inflation, which captures the underlying trajectory of inflation, will remain at a similar level to the current rate of around 4.5 percent in the coming months.

Next year, inflation will remain within the tolerance band for most of the year, before returning to the central bank's target of 3 percent on a sustained basis in early 2026. The MNB's forecast for 2025 has increased compared to the September inflation forecast. This shift is explained by the pass-through of recent exchange rate changes into consumer prices, rising food commodity prices and the January 2025 excise tax increase; the effects of these factors are partly offset by more moderate underlying inflation rates. **Inflation may average between 3.6 and 3.7 percent in 2024, 3.3 and 4.1 percent in 2025, and between 2.5 and 3.5 percent in 2026 and 2027** (Chart 1-2).

We forecast that core inflation excluding indirect tax effects, which captures the underlying inflation processes, may range from 4.6–4.7 percent in 2024, 3.0–3.6 percent in 2025 and 2.6–3.2 percent in 2026 and 2027. Our forecast for core inflation excluding indirect tax effects next year is unchanged from the September forecast. In the autumn months, price dynamics for market services and industrial goods were more favourable than previously forecast. This will lead to more moderate core inflation in the short term, but its impact will be gradually offset over the coming year by the expected pass-through of the recent weakening of the forint exchange rate.

The higher food price change in recent months is being driven by a return to rising global food commodity prices on an annual basis. Higher repricing will continue to push

Chart 1-3: Decomposition of our inflation forecast



Note: The decomposition is based on the midpoint for the forecast range.
Source: HCSO, MNB

Table 1-1: Development of trade balance as a percentage of GDP

		2024	2025	2026	2027
Core inflation excluding indirect tax effects		4.6 - 4.7	3.0 - 3.6	2.6 - 3.2	2.6 - 3.2
Core inflation		4.6 - 4.7	3.2 - 3.8	2.6 - 3.2	2.6 - 3.2
Non-core inflation	Unprocessed food	1.6	7.8	5.0	4.5
	Fuel and market energy	0.0	3.6	2.8	3.5
	Regulated prices	2.5	1.4	1.8	1.8
	Alcohol and tobacco	4.4	5.1	3.9	3.9
Inflation		**3.6 - 3.7**	**3.3 - 4.1**	**2.5 - 3.5**	**2.5 - 3.5**

Note: Percent. The table is based on the midpoint of the forecast range.
Source: MNB

up unprocessed food inflation in the first half of next year as well. For the product category, we forecast price increases of around 1.6 percent this year, 7.8 percent next year, 5.0 percent in 2026 and 4.5 percent in 2027.

The average annual price of vehicle fuel and market energy is expected to remain unchanged this year, and rise by 3.6 percent next year, 2.8 percent in 2026 and 3.5 percent in 2027 (Table 1-1). The higher fuel price forecast compared to September is explained by the increase in excise duties. From 2025, an inflation-linked increase in excise duties will be introduced, affecting the product categories alcohol and tobacco as well as fuels. Our assumption for world oil prices in USD terms fell slightly compared to the September estimation, but with regard to the domestic petrol price level this was offset by the change in the HUF exchange rate observed since September. The world price of Brent crude oil has seen significant fluctuations, hovering around USD 70-82/barrel in October, before stabilising between USD 70-75 in November. The increased volatility of world oil prices in recent months adds uncertainty to our fuel price forecast. European gas and electricity prices remain below pre-Russian war levels, with world gas prices ranging between EUR 40-50/MWh. Prices of goods and services with regulated prices are forecast to rise by around 2.5 percent in 2024. Our forecast is based on the technical assumption that the measures affecting retail energy prices remain unchanged over the entire forecast horizon.

Box 1-1: Assumptions applied in our forecast

As Hungary is a small, open economy, our forecasts for the most important macroeconomic variables are fundamentally influenced by developments in external factors. A brief presentation of changes in external assumptions helps make the forecast more transparent (Table 1-2).

Table 1-2: Main external assumptions of our forecast

Technical assumptions	2024		2025		2026		2027	Change		
	Previous	Current	Previous	Current	Previous	Current	Current	2024	2025	2026
EURUSD	1.09	1.08	1.11	1.05	1.11	1.05	1.05	-0.9%	-5.0%	-5.0%
Oil (USD/barrel)	79.7	79.8	71.8	70.3	71.2	68.9	68.8	0.1%	-2.1%	-3.2%
Oil (EUR/barrel)	73.1	73.7	64.9	66.8	64.3	65.5	65.4	0.9%	3.1%	1.9%
Gas (EUR/MWh)	33.4	34.8	38.5	44.0	38.8	35.7	34.1	4.1%	14.4%	-8.0%
Euro area inflation (%)	2.5	2.4	2.2	2.1	1.9	1.9	2.1	-0.1 pp.	-0.1 pp.	0.0 pp.
Euro area real GDP (%)	0.8	0.7	1.3	1.1	1.5	1.4	1.3	-0.1 pp.	-0.2 pp.	-0.1 pp.
GDP growth of Hungary's main export partners* (%)	1.2 - 1.8	1.2 - 1.6	1.5 - 2.2	1.5 - 2.2	1.3 - 2.2	1.3 - 2.2	1.4 - 2.3	-0.1 pp.	0.0 pp.	0.0 pp.

Note: Annual average in the case of oil prices. *Growth rate of Hungary's 21 most important export partners weighted by share in exports.
Source: Bloomberg. Consensus Economics. MNB. ECB

Our forecast for external demand has not changed significantly over the forecast horizon. In the third quarter, the annual growth rate of the economy of the European Union was a moderate 1.0 percent, with growth of 0.4 percent versus the second quarter. GDP growth slowed somewhat in the US and China, but remained strong. The US economy expanded by 2.7 percent on an annual basis and 0.7 percent on a quarterly basis. In 2024 Q3, growth in China amounted to 4.6 percent, while GDP expanded by 0.9 percent quarter-on-quarter. In terms of external economic trends, there are risks related to the unfavourable outlook for industrial production in Europe, as well as the ongoing war between Russia and Ukraine and the intense geopolitical situation, with special regard to trade tensions. Based on business confidence indicators, consumer confidence remains low in the EU economies despite some further improvement. Meanwhile, business sentiment stagnated in services and deteriorated somewhat in industry. The actual figures for recent months have been consistent with expectations overall, with no significant change to the global and European growth outlook for this year relative to the September forecast; consequently, our external demand assumption has also remained unchanged over the forecast horizon. The moderate growth rate observed in the EU's major economies is likely to continue in 2025 H1.

The ECB revised down its inflation and growth projection for 2024 and 2025 compared to the September forecast. According to the ECB's December forecast, inflation in the euro area is projected at 2.4 percent in 2024, 2.1 percent in 2025, 1.9 percent in 2026 and 2.1 percent in 2027. Compared to the September projections, the inflation estimates for 2024 and 2025 have been revised down by 0.1 percentage point. The ECB also expects GDP growth in the euro area to be 0.1 percentage point lower than previously anticipated for 2024, resulting in a growth rate of 0.7 percent for this year. Compared to the September forecast, growth expectations for 2025 have been revised down by 0.2 percentage point, with growth next year forecast to be 1.1 percent. Economic growth is projected to reach 1.4 percent in 2026 and 1.3 percent in 2027.

Brent crude oil prices exhibited increased volatility in the autumn months. After reaching a three-year low in early September, mounting geopolitical conflicts temporarily pushed up the price of oil per barrel. However, owing to expectations of a ceasefire agreement in Lebanon and further weakening in demand, the decline continued overall in the previous quarter. The price of Brent crude oil is currently fluctuating between USD 70 and 75 per barrel. However, in the short term one upside risk is that OPEC+ once again postponed the start of crude oil output rises by an additional three months, until 2025 Q2. In addition, geopolitical conflicts may continue to pose significant risks to the evolution of global oil prices. The difference between the price of Brent and Russian Ural crude persisted during the past period.

Domestic price for petrol and diesel increased in the autumn months. Russian Ural crude oil continues to reach Hungary via pipeline. However, Brent is the benchmark for petrol and diesel prices, which implies that its price in USD and the USD/HUF exchange rate have a significant impact on fuel prices. Following a downward trend in the summer months, market prices of petrol and diesel have been on the rise since the second half of September. The increase in domestic petrol

prices may have been influenced by rising profit margins, while the decline in oil prices nominated in USD was offset by changes in the HUF exchange rate since September.

Global gas and electricity prices have increased recently, but remain below the levels seen before the Russia–Ukraine war. The market prices of petrol and diesel in Hungary and in Europe track the Dutch TTF gas price, which reached its historical peak of over EUR 300 in August 2022. Following a steady decline in gas prices since December 2022, the Dutch TTF gas price is currently around EUR 40–50/MWh. European gas prices have increase slightly in recent months overall. This was driven by increasing geopolitical risks, in particular, uncertainties about transit flows from Ukraine, and the expected colder winter weather and resulting higher energy demand compared to recent years. Changes in gas prices also affect electricity prices through gas-fired power plants. Electricity prices spiked in October and November, but have since consolidated somewhat. The 7-day moving average for the German Phelix electricity price was around EUR 125 in November, which exceeds the average price of nearly EUR 100 typical for 2023.

The budget deficit-to-GDP ratio is projected to be 4.4–4.8 percent in 2024 and 3.4–4.2 percent in 2025, depending on macroeconomic developments. Thereafter, the deficit may be in the range of 2.8–3.8 percent in 2026 and 2.2–3.2 percent in 2027. The decline in budget deficit in 2024 is supported by lower energy expenditures due to the stabilisation of energy prices, and decreasing public investment expenditure. The 2025 budget bill confirmed the deficit target of 3.7 percent of GDP, which will be supported primarily by a substantial reduction in public interest expenses and revenue-increasing tax measures, while stimulus measures will increase the deficit. The reduction of public debt in 2024 is significantly constrained by the high cash deficit, the moderate economic expansion and the revaluation of foreign currency debt; however, we expect the debt ratio to fall below 70 percent of GDP by the end of the forecast horizon as the deficit gradually declines.

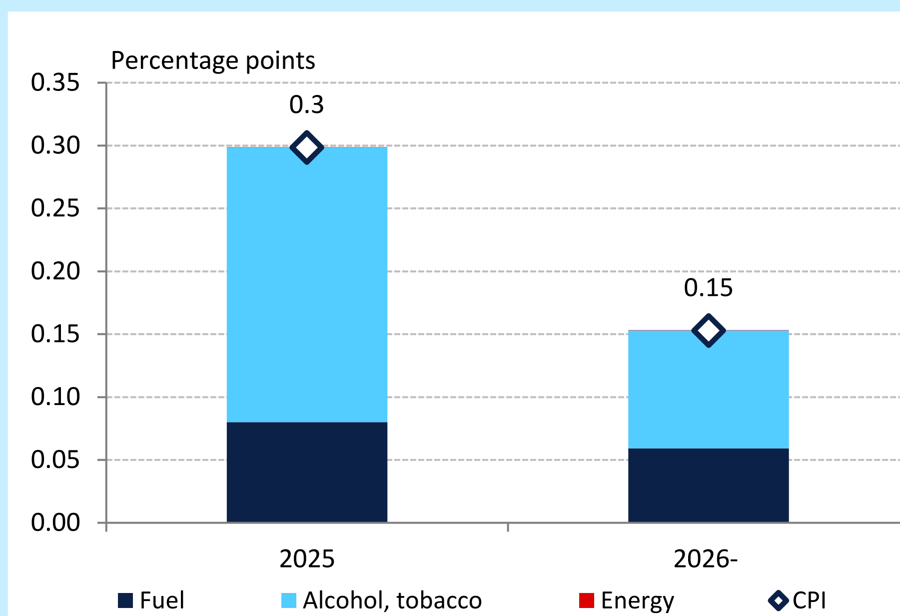
Restrictions on the availability of EU funds continue to create considerable uncertainty for the budget. Hungary has access to a total of EUR 12.2 billion in the 2021–2027 cohesion cycle. However, access is still not available to non-repayable grants from the Recovery and Resilience Facility (RRF) and cohesion funds representing a total of EUR 16 billion, the majority of which is linked to the implementation of the 27 super-milestones defined by the Commission. Based on budget data for the first eleven months, it may be related to restrictions on access to EU funds that expenditures and revenues related to the EU funds remain substantially below what can be expected on the basis of appropriations. This points to few advance payments and a low level of the utilisation of funds.

Box 1-2: Inflationary effect of the inflation-linked increase in excise tax

Under the proposed tax law amendments, an inflation-linked tax hike will be introduced in 2025 for certain tax categories. From 2025, the **registration tax, vehicle tax, transfer duty and the excise tax on fuel and alcohol products** will increase each year by the annual rate of inflation of July of the previous year. In addition, from the beginning of 2025, there will be a one-off, 8-percent increase in the excise tax on tobacco products and a 20-percent increase in company car tax, with the annual inflation-linked tax raise taking effect at the beginning of 2026.

According to our estimates, the newly announced tax hike may raise the rate of price increases by 0.3 percentage point in 2025 and by 0.1–0.2 percentage point in each year from 2026 (Chart 1-4). The impact on consumer prices can be primarily attributed to the excise tax increases, while changes in other taxes do not influence inflation significantly. The impact of the tax increase in 2026 and subsequent years may differ from the above if inflation in July of the previous year deviates significantly from 3 percent. Every 2-percentage-point difference changes the impact on consumer prices by 0.1 percentage point.

Chart 1-4: Impact of the inflation-linked excise tax increase on inflation



Source: HCSO, MNB calculation

In the past, excise tax was raised on a case-by-case basis rather than on a regular, annual basis. Since 2010, the excise tax on petrol has increased once, on gas oil twice and on alcohol products three times, on a non-transitory basis. By contrast, the excise tax on tobacco products has been increased up to several times a year, more than 15 times in total since 2010.

The growth rate of excise tax rates and inflation has been similar in the past overall. Since 2010, the excise tax rate has increased by 93.4 percent for all products concerned, while consumer prices have risen by 88.5 percent, overall. This rate also includes a 258-percent hike in the excise tax on tobacco products. The excise tax rate rose by 31.6 percent for fuels and 46.6 percent for alcohol products. The rate of excise tax increases surpassed the rate of inflation only for tobacco products, while it was significantly lower for fuels and alcohol products.

European Union rules and the depreciation of the exchange rate have also contributed to the fact that in the past excise tax hikes exceeded inflation. Around one half of the excise tax increases (40.7 percentage points) can be attributed to compliance with EU legislation. Since the beginning of 2017, Hungary has been subject to EU legislation that prescribes a minimum rate of excise tax on certain items. The minimum rate is specified in euros; accordingly, when the exchange rate depreciates the HUF rate needs to be raised to comply with the rules. For alcohol and fuels, Hungary has always met the minimum required tax levels; for tobacco, however, a gap between required and actual tax levels has been continuous between 2017 and 2020, averaging 10 percent.

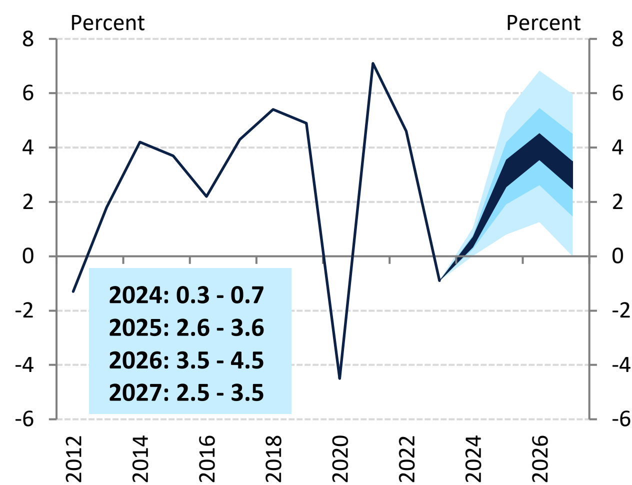
A backward-looking increase in the excise tax improves predictability but after a high inflation period, it slows down the moderation of inflation. As with all backward-looking repricing, this measure restrains a sharp rise in inflation but decelerates disinflation.

The measure links the excise tax increase at the beginning of the year to the inflation observed in the previous July. In retrospect, the July inflation figures did not deviate unilaterally from the annual averages. There was a noticeable difference in 2010–2011 and 2022, when the gap to the annual average was close to or slightly above 0.8 percentage point.

1.2 Real economy forecast

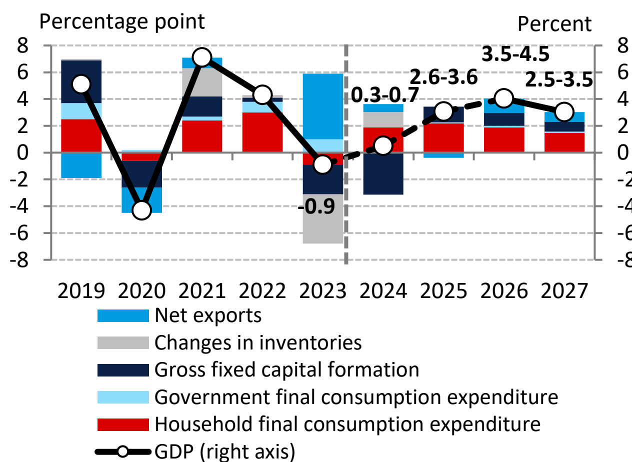
GDP growth is likely to remain subdued this year, with the Hungarian economy expanding by 0.3–0.7 percent. Growth will be supported mainly by the expansion of market services, whereas the performance of industry, construction and –due to the adverse weather conditions at the end of the summer – agriculture is restraining economic growth. On the consumption side, household consumption and net exports are expected to be the main contributors to GDP growth this year, while investment is expected to slow sharply as a result of the decline in business sentiment. Growth may pick up from mid-2025, in conjunction with a recovery in external economic activity, new industrial capacities starting production and certain government programmes. Favourable real income developments, the government measures announced and buoyant retail lending will spur consumption growth. The investment rate will stabilise in both nominal and real terms from 2025. Domestic industrial production and exports will be boosted by the recovery in external economic activity and the start of production by the large-scale vehicle and battery manufacturing investments from 2025. The growth in Hungary's external market share could accelerate in 2026. We forecast GDP growth to continue at 2.6–3.6 percent in 2025, 3.5–4.5 percent in 2026 and 2.5–3.5 percent in 2027.

Chart 1-5: Fan chart of the GDP forecast



Note: Based on unadjusted data.
Source: HCSO, MNB

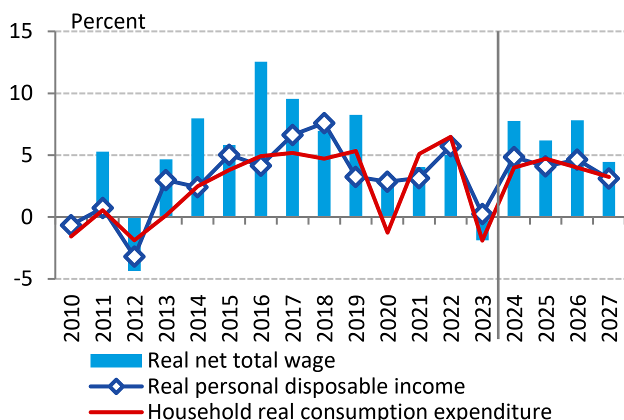
Chart 1-6: Expenditure side decomposition and forecast of GDP



Note: Government final consumption expenditure includes final consumption expenditure of general government and non-profit institutions.
Source: HCSO, MNB

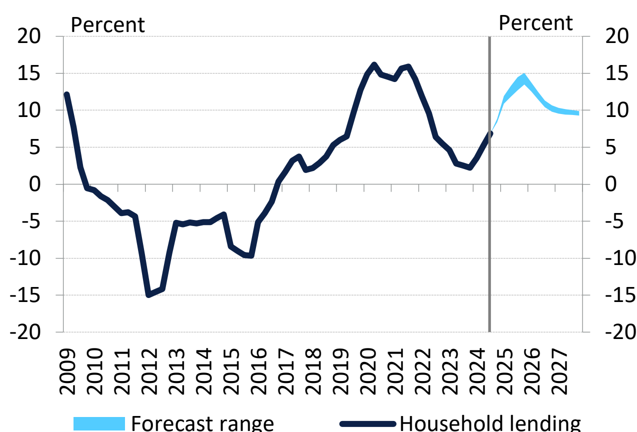
GDP growth is expected to remain subdued this year, with the Hungarian economy expanding by 0.3–0.7 percent. Several factors will support stronger growth in 2025. In 2024 Q3, Hungarian GDP contracted by 0.8 percent compared to the same period of the previous year and by 0.7 percent compared to the previous quarter. The incoming data was below our expectations outlined in the September Inflation Report. Positive real wage growth and favourable household income trends will support continued expansion in demand for services. The unfavourable business sentiment in industrial production and forward-looking indicators suggest that industrial output may remain subdued over the short term. A turnaround in industrial production is expected in the second half of next year, in line with the improvement in industrial production of Hungary's main trading partner, Germany, which market analysts project for mid-2025, stimulating domestic industrial activity from the demand side (see Box 3-1 for a discussion of the cyclical relationship between the two economies). The domestic industrial turnaround is also supported by specific factors: major investments by certain domestic automotive and battery companies will be completed and companies may start production in 2025 (see Box 1-3 for more details). Trends in the construction industry are moving in two different directions: while the contract portfolio, new contracts and housing permits rose substantially in the third quarter, the construction sentiment index remains at a low level. From the beginning of 2025, economic recovery programmes and targeted measures (rural home renovation programme, dormitory building programme, Workers' Loan Scheme, making pension savings available for housing purposes) could provide an additional boost to the construction sector, which may support economic growth next year. Overall, agriculture is expected to slow growth by 0.3 percentage point this year due to the drought this summer. **GDP**

Chart 1-7: Annual changes in net total wage, personal disposable income and household consumption expenditure in real terms



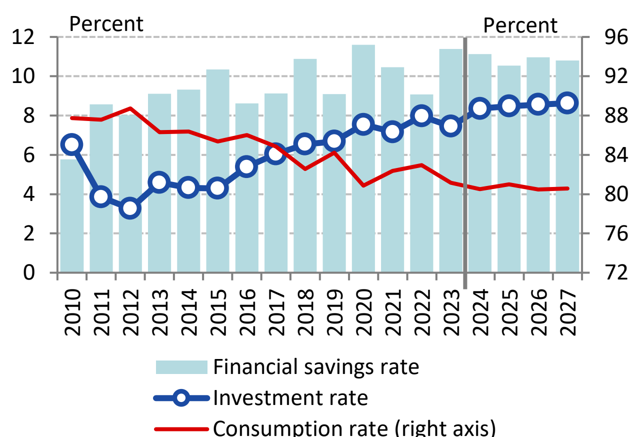
Source: HCSO, MNB

Chart 1-8: Forecast for lending to households



Note: Transaction-based, year-on-year data. 2019 Q3 data adjusted for transactions of lombard loans. Source: MNB

Chart 1-9: Evolution of households' consumption, investment and financial savings rates as a percentage of disposable income



Source: HCSO, MNB

growth is projected to range between 2.6–3.6 percent in 2025, 3.5–4.5 percent in 2026 and 2.5–3.5 percent in 2027 (Chart 1-5 and Chart 1-6).

Driven by favourable wage and income trends, we expect household consumption to increase in 2024 and to accelerate further in 2025 (Chart 1-7). We project that real disposable income will grow by 4.7–4.9 percent this year, with consumption expanding in line with this, by between 3.9–4.1 percent. We have raised our forecast for household consumption for next year, due to the government measures announced since the end of September. The Workers' Loan Scheme, extending the age limit for taking up a prenatal baby support loan to 35 years and the family tax allowance support the recovery in demand. In addition to government programmes, lower government bond yields than in the previous period and maturing income outflows are expected to also contribute to further expansion in consumption. In addition to government measures and rising real income, household demand will be boosted by an expected increase in household credit. Demand for both housing and consumer credits is expected to rise as a result of the stabilising economic environment and lower inflation (Chart 1-8). Based on our current estimates, loans for workers could raise household lending dynamics by 3.7 percentage points by the end of next year, which could push household credit growth to a peak of around 14 percent in 2025. Consumption is forecast to grow by between 4.3 and 5.1 percent in 2025, 3.5 and 4.5 percent in 2026 and 2.7 and 3.7 percent in 2027.

In 2025, the household savings rate as a share of income is expected to be lower than this year, with the increase in consumption and investment rates also supported by government programmes announced for next year. In response to an uncertain economic environment and high inflation, households accumulated substantial savings in 2023, while at the same time their consumption rate fell. This year, we expect a moderate decline in the savings and consumption rate and an increase in the investment rate. From 2025 onwards, the household investment rate is projected to stabilise at 8–9 percent, the savings rate at 10-11 percent and the consumption rate at around 80 percent (Chart 1-9).

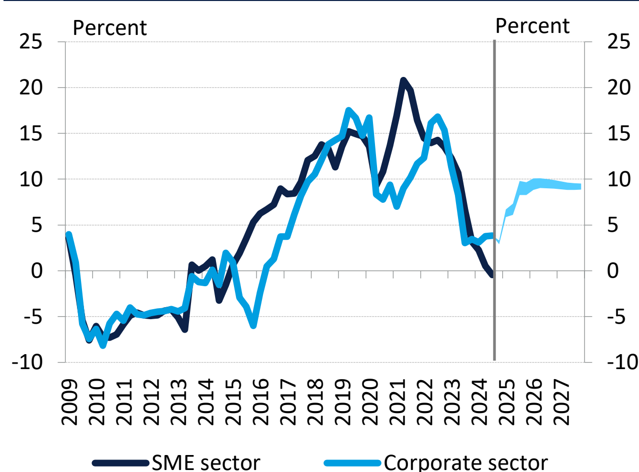
Following a sharp fall in investment this year, the investment rate will stabilise in both nominal and real terms. Low-capacity utilisation, the weak European economy, geopolitical tensions, persistently high price levels and the long shadow of inflation all point to a decline in investment this year. Consequently, corporate and government investment has declined, and this was only

Table 1-3: Evolution of gross fixed capital formation and investment rate

	2023	2024	2025	2026	2027
Gross fixed capital formation	-7.8	-12.0	5.0	4.0	3.0
Government investments	-2.7	-18.1	2.4	3.7	-8.0
Private investments	-9.0	-10.5	5.5	4.1	5.3
Investment rate	26.0	23.7	24.2	24.4	24.7
Real investment rate	24.6	21.5	21.9	21.9	21.9

Note: The values represent the middle of the forecast range. Year-on-year growth for gross fixed capital formation and investment rate as a proportion of GDP. Real investment rate calculated at 2021 prices. Source: MNB

Chart 1-10: Annual changes in lending to non-financial corporations and SMEs



Note: Transaction-based, year-on-year data. The SME sector does not include the self-employed. The growth rate of the overall corporate sector is based on the total amount of outstanding credit to the entire financial intermediary system.
Source: MNB

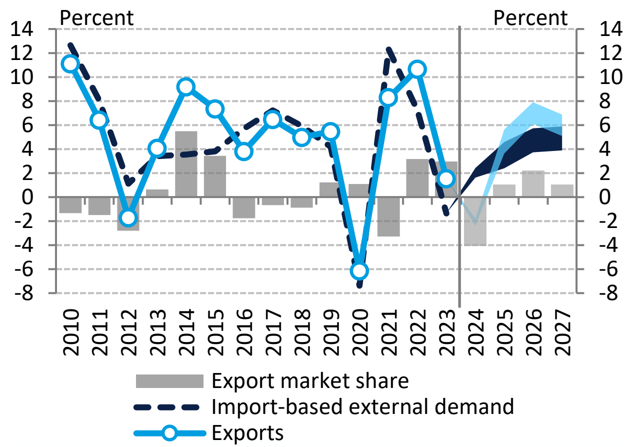
partly offset by the expansion in household investment. From 2025 onwards, investment growth is expected to resume, mainly thanks to private sector investments. The investment rate will stabilise in both nominal and real terms (Table 1-3). We expect the annual change in investment to come in at (-12.3)–(-11.7) percent in 2024, 3.5 to 6.5 percent in 2025, 2.6 to 5.4 percent in 2026 and 1.5 to 4.5 percent in 2027.

In parallel with the recovery in corporate credit markets, the volume of business investments may expand from 2025, bolstered by government-supported programmes, improving business confidence and resurgent demand. Based on the responses to the lending survey, banks perceived a decline in demand in the third quarter and foresee stagnation in demand in 2024 Q4 and 2025 Q1. We estimate that corporate credit growth could reach 3 percent at the end of 2024 and stabilise at 8–9 percent from 2025 H2 until the end of the forecast horizon (Chart 1-10). Weak business confidence, low capacity utilisation and subdued external demand will lead to a decline in business investment in 2024. From 2025 onwards, thanks to improving business sentiment and external demand, some postponed projects may start to be realised, and corporate investment may rise until the end of the horizon.

Household investment is expected to increase over the forecast horizon. The value of housing loans contracted by credit institutions in 2024 Q3 increased by 130 percent compared to the low base in the same period of the previous year, pointing towards an increase in housing investment. From the beginning of next year, the Workers' Loan Scheme, the ability to use voluntary pension savings for housing purposes and the Rural Home Renovation Programme may further boost household investment. Looking ahead, a slightly increasing share of household's income is being spent on investment. Public investment is expected to decline significantly this year, in line with government plans.

As the European economy recovers and significant industrial investment begin production, domestic exports should be able to expand substantially from the second half of next year. In the third quarter of this year, exports fell by 1.9 percent on an annual basis. Industrial production and the trend in industrial new orders from abroad point to a further decline in exports in the final quarter of the year, with overall exports expected to fall by 1.8–2.4 percent this year. In early 2025, the recovery in exports will be retarded by the persistently low levels of investment and the weak industrial outlook in Europe. From the second half of next

Chart 1-11: Changes in export market share



Note: Export market share based on the average of the forecast range.
Source: HCSO, MNB

year, we expect a strong expansion in exports of goods as the investments in electric car and battery production start work and Hungary's external demand gains momentum. In line with the incoming data, our forecast for not only this year but also next year is lower than in September, with domestic exports expected to grow by 3.6–5.6 percent in 2025. We expect growth of 6.1–7.9 percent in 2026 and 5.1–6.9 percent in 2027. Hungary's share of the export market is expected to shrink temporarily this year, with growth accelerating in 2026 (Chart 1-11).

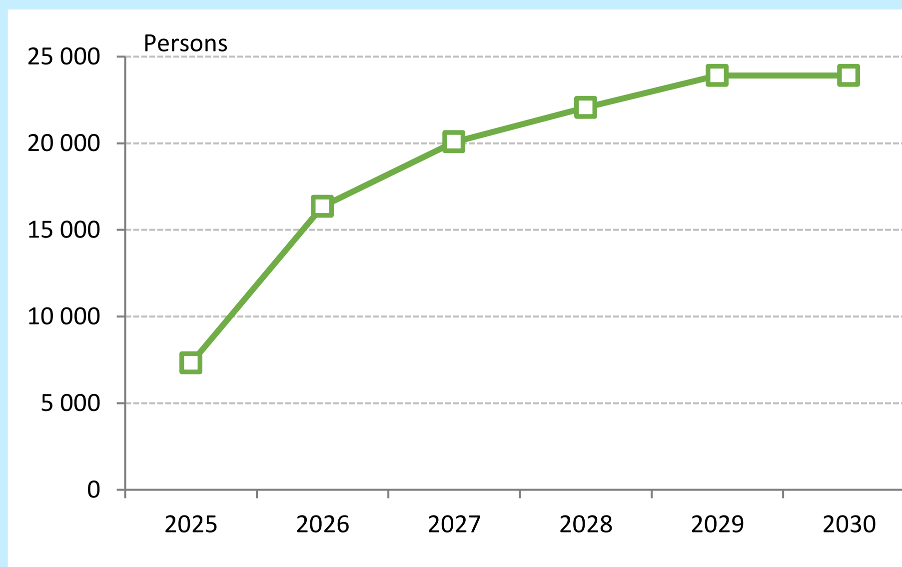
In 2024, imports are expected to decline in line with the fall in exports. The decrease in imports in 2024 Q3 was better than expected, as this item fell by 0.9 percent on an annual basis, mainly due to lower exports and investment, while household consumption boosted imports slightly over the past four quarters. With exports and investment recovering from next year, imports are expected to expand by 4.4–6.6 percent in 2025, 4.9–6.9 percent in 2026 and 4.4–6.4 percent in 2027.

Box 1-3: Impact of the entry into production of large investments

In 2025, three large foreign direct investments are expected to start production in Hungary. Among the automotive investments, the BMW plant in Debrecen, announced in 2018, and the BYD plant in Szeged, announced in 2023, while in the battery sector, the CATL plant in Debrecen, announced in 2022, are expected to start operations. The direct and indirect effects of the production of the three plants on gross domestic product are examined based on the number of persons employed.

The number of persons employed may gradually increase as production rises (Chart 1-12). Employment growth was estimated on the basis of press information and factual data on a major automotive investment in Hungary in the 2010s. In 2025, the total number of persons employed in the three factories may be close to 7,300, which we estimate will peak at around 24,000 in 2029.

Chart 1-12: Total number of people employed by BMW, BYD and CATL

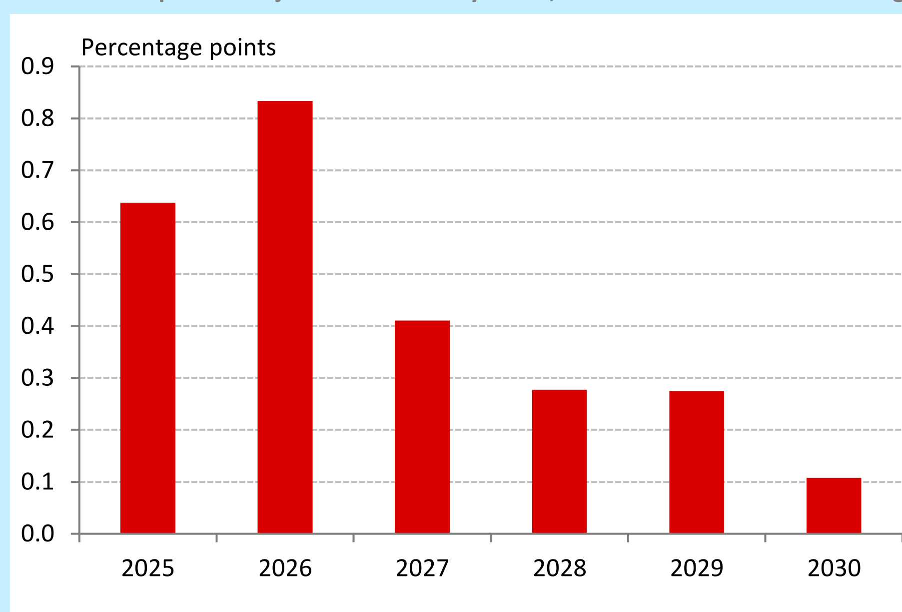


Source: Press releases, MNB

The value added of production was calculated using the wage bill. The wage bill is calculated by multiplying the number of employees by the estimated gross wages. Based on the reports of the automotive and battery industry factories already operating in Hungary, the ratio of the wage bill to value added can be calculated and used to estimate the value added of the production of BMW, BYD and CATL. In addition to the value added generated directly, we have also estimated the indirect value added through suppliers using the Input Output-Table (IOT).

In 2026, output from the three factories may add around 0.8 percentage point to GDP growth. The effect on GDP growth is due to the gradual change in output growth between years, so its value differs from the share of GDP. The three factories could raise GDP growth by 0.6 percentage point in 2025 and by 0.8 percentage point in 2026, taking into account indirect effects. However, as the production of factories gradually reaches their planned capacity, their impact on GDP growth will also diminish after 2026 (Chart 1-13).

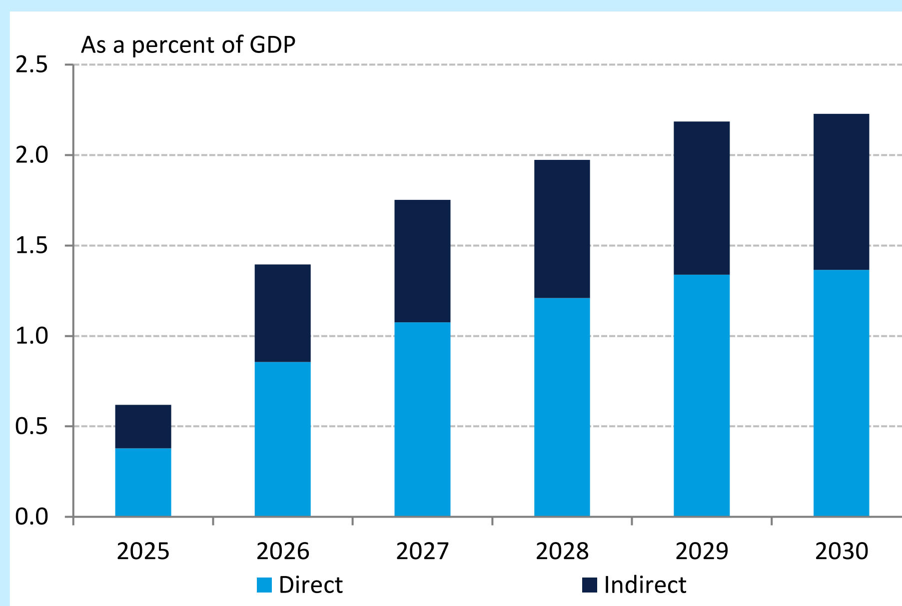
Chart 1-13: The impact of major investments by BMW, BYD and CATL on annual GDP growth



Source: Press releases, MNB

By 2030, the value added of the new factories could account for more than 2 percent of GDP (Chart 1-14). In 2025, direct value added could account for 0.4 percent and indirect value added for 0.2 percent of gross domestic product in the three factories combined. Untill the end of the decade, the share in GDP will rise steadily as production rises, so that by 2030 the share of direct value added may be 1.4 percent and that of value added by suppliers 0.9 percent. However, the impact on GNI is smaller, because we estimate that a large share of capital income and part of labour income from value added may also go to foreign actors.

Chart 1-14: Value added of BMW, BYD and CATL as a share of current price GDP



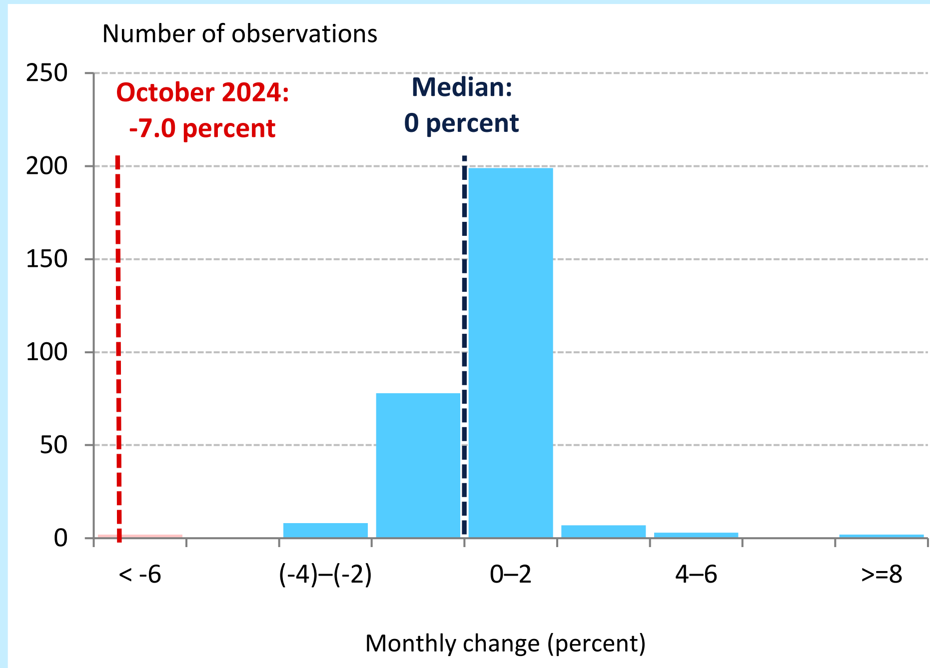
Source: Press releases, MNB

Box 1-4: Correction of profit inflation

In October, the Consumer Price Index was lower than the expectations of both the central bank and analysts: prices declined in several sectors, signalling a possible correction in the profit inflation of 2022–2023. During the inflationary waves in Hungary, companies increased their prices in excess of their costs, which contributed significantly to the surge in inflation. In parallel, price hikes higher than justified by costs resulted in dynamically rising corporate profits in 2022–2023. The rise in domestic profits has significantly exceeded the regional and EU averages in recent years. In some sectors producing for the domestic market, the profitability of companies has soared. Sectors such as mobile phone and internet services (105 percent), pet food (93 percent) and distilled spirits (283 percent) reported a steep rise in profit in 2022–2023. Above-average profit increases were also observed in pasta production (265 percent) and preserved flour products (107 percent).

Inflation data for October indicate price cuts or unexpectedly low price increases in several sectors that have seen profits surge higher in recent years. Repricing was also moderate in November in these sectors. Representing an unprecedented monthly decline, the price of mobile phone and internet services fell by 7 percent in October (Chart 1-15). There were no changes to prices in the mobile phone and internet services sector in November. The consumer price of pet food has dropped by 7.3 percent since January 2024. For the first time since 2015, the price of spirits decreased in October with no significant price change in November. Since May 2024, the consumer prices of pasta and preserved flour products have fallen by 4.1 and 4.5 percent, respectively.

Chart 1-15: Histogram of monthly price changes for mobile phone and internet services



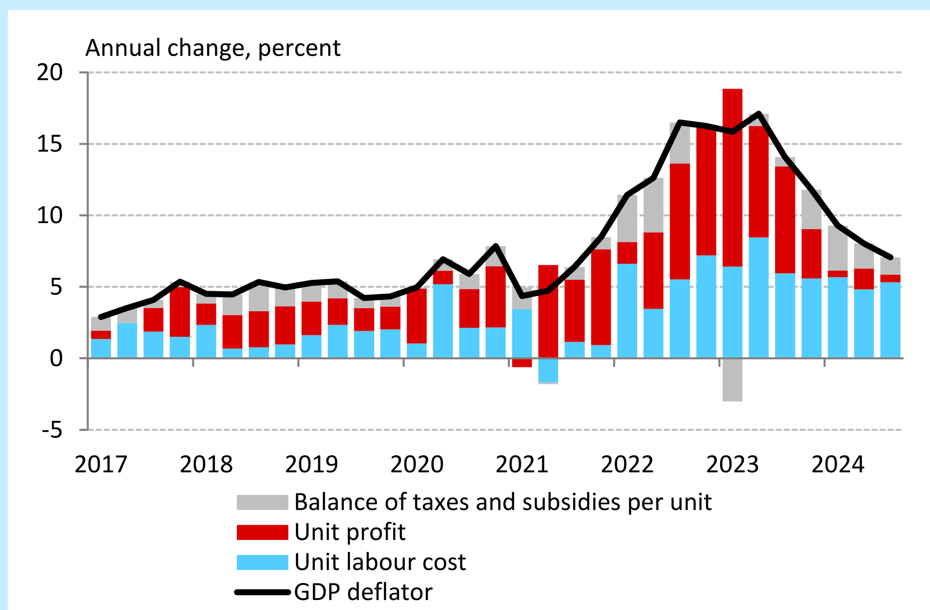
Note: Based on data from January 2000 to November 2024.

Source: HCSO, MNB calculation

The correction in profit rates can also be perceived at the level of the national economy. Since 2023 Q1, the contribution of profits to the GDP deflator has decreased considerably (Chart 1-16). However, despite a substantial slowdown in the rise in profit, its level and its share in the output of the national economy remain high. In 2023, the profit share of current price GDP was 2.8 percentage points higher than the average share recorded between 2017 and 2019.

As a result of the decline in the high profit levels, inflation remained moderate despite rising costs. This process is reflected in the fact that even though import prices have been rising since May 2024 and industrial producer prices since July, consumer prices of industrial goods have fallen by 0.6 percent since July. The limited pass-through of costs will continue to be conditional on a high degree of competition in the market. The negative output gap may also limit the pass-through of cost increases.

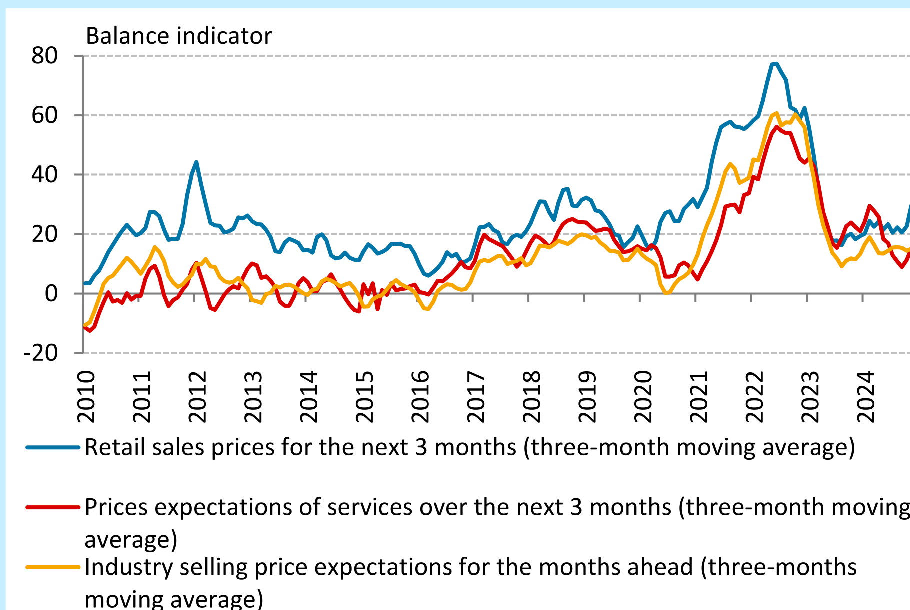
Chart 1-16: Income-side decomposition of the GDP deflator



Source: MNB, HCSO, Eurostat

The sustainability of the profit inflation revision is also shaped by corporate price expectations (Chart 1-17). Price expectations in the retail and services sector, which had been at moderate levels earlier in the year, rose sharply in November. As a result, for the first time in four months, price expectations in the two sectors are now above the average seen during the period of price stability. The possible persistence of higher corporate price expectations may indicate that the cost increases observed in recent months and the acceleration of imported inflation may also be reflected in consumer prices, albeit with a lag. Therefore, repricing in early 2025 will be of particular importance, as it may determine the sustainability of the profit inflation correction.

Chart 1-17: Expected evolution of the prices of services, retail and industrial sales prices

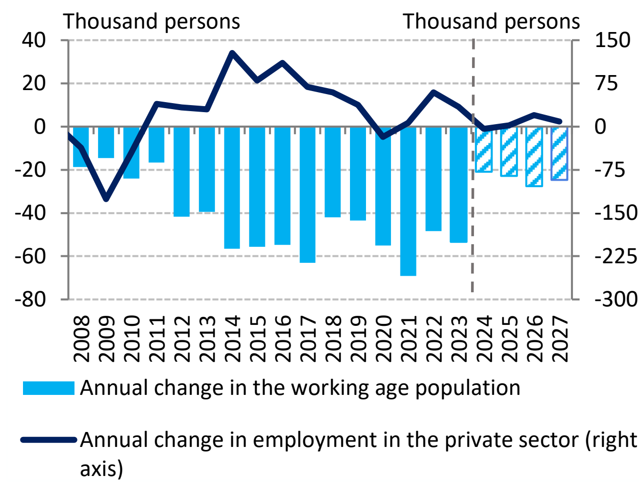


Source: MNB calculations based on European Commission data

1.3 Labour market forecast

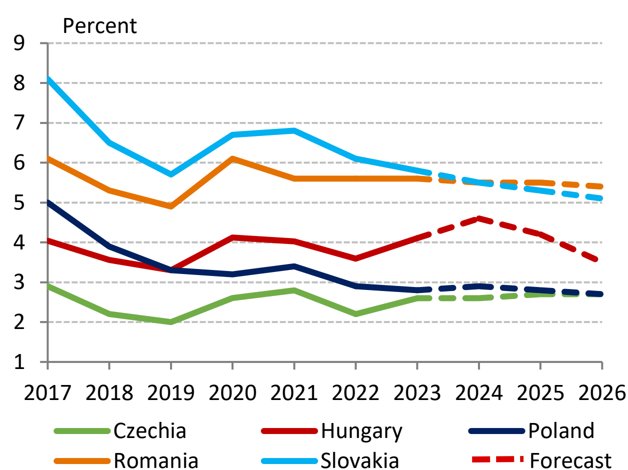
Employment stabilized in October after a decline in September, thus remaining at a high level of 4.7 million people. Private sector employment is not expected to change substantially this year, as a consequence of weak economic performance and falling labour demand. The unemployment rate may amount to between 4.5 and 4.6 percent this year and between 4.1 and 4.3 percent in 2025. Wage growth in 2025 is driven mainly by the increase in the minimum wage early next year, easing labour market tightness and continued high inflation expectations by households. In the private sector, average wages are expected to rise between 11.6 and 11.8 percent this year and between 8.5 and 9.5 percent next year.

Chart 1-18: Annual change in working age population and number of persons employed in the private sector



Note: The number of persons employed refers to those aged 15–74, but the projection for the working age population refers to those aged 15–64. The number of employed persons is based on the midpoint of the forecast range.
Source: Eurostat, HCSO, MNB

Chart 1-19: Change in the unemployment rate



Note: Data on Hungary based on the midpoint of the forecast range.
Source: Eurostat, European Commission, HCSO, MNB

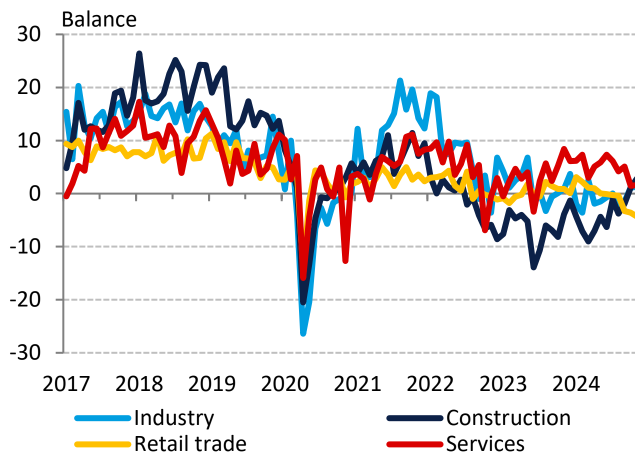
Private sector employment is expected to be close to stagnant this year. Employment in the national economy was at a lower level in September and October than in previous months, and demand for labour also decreased. Employment may fall in 2024 Q4 before it begins to rise from 2025. Even with the gradual recovery in economic activity, we expect only a slow increase in employment for the rest of the forecast period, in view of the demographic constraints on employment growth (Chart 1-18). According to our current forecast, the number of persons employed in the private sector may change by between –0.1 and 0.0 percent in 2024, and between –0.1 and 0.3 percent in 2025. Thereafter, it may rise by 0.3–0.8 percent in 2026 and by 0.0–0.5 percent in 2027.

The unemployment rate may increase somewhat for the rest of the year before embarking on a decline next year. The unemployment rate stood at 4.6 percent in 2024 Q3, reflecting a moderate increase from the previous quarter. We expect the unemployment rate to peak in 2024 Q4 and start declining from 2025 Q1. Our current forecast for the unemployment rate is 4.5–4.6 percent for this year and 4.1-4.3 percent for 2025. Subsequently, in parallel with the economic upswing, the rate is expected to fall to 3.2- 3.8 percent in 2026 and be between 2.9 and 3.9 percent in 2027 (Chart 1-19).

Labour market tightness is easing and labour demand is declining. The tightness of the labour market has eased in recent quarters. The number of job vacancies continued to fall across a wide range of sectors of the economy on an annual basis, with manufacturing, transportation and storage, tourism and real estate reporting the largest declines in the third quarter. According to the latest ESI survey, the majority of companies in construction, industry and other services expect their workforce to increase in the coming months. By contrast, companies expecting a decline in the number of employees in the next three months are in the majority in retail trade (Chart 1-20).

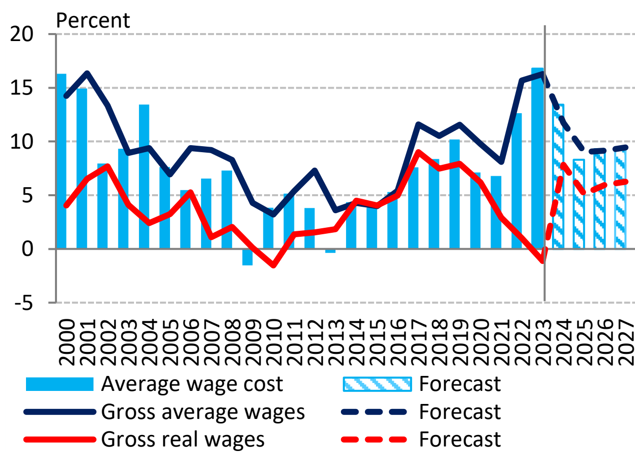
In 2024, nominal wage growth in the private sector will be lower than last year as inflation moderates and labour demand decreases. Real wages are expected to increase considerably, as real wages have been on the rise since

Chart 1-20: Employment expectations in the ESI business survey



Note: The balance is positive (negative), if the majority of companies plans to hire (lay off). Seasonally adjusted data.
Source: European Commission

Chart 1-21: Annual changes in gross average wages and average labour cost in the private sector



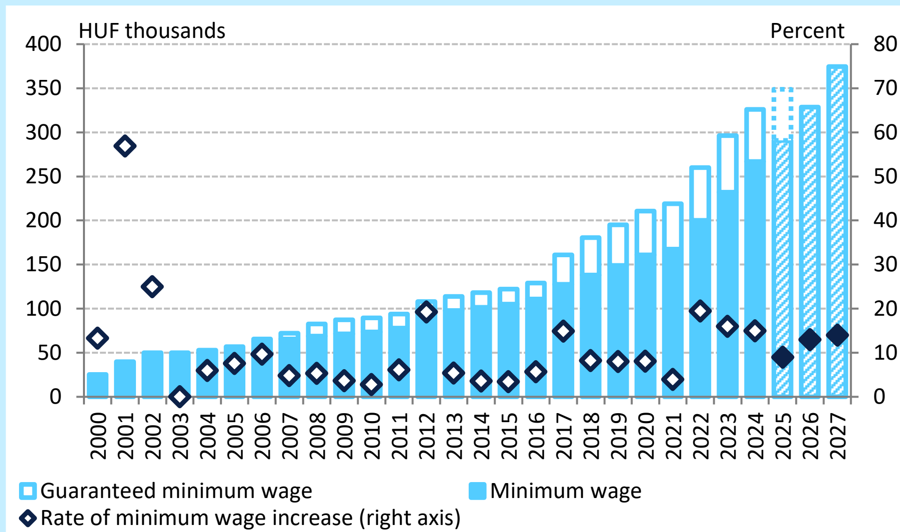
Note: Based on the midpoint of the forecast range.
Source: HCSO, MNB

September 2023, due to the steep decline in inflation. The announced minimum wage agreement will have a tangible impact on wage growth in the coming years. In January 2025, the minimum wage is set to increase by 9 percent and the guaranteed minimum wage by 7 percent. The minimum wage will increase by 13 percent in 2026 and 14 percent in 2027. Higher wage growth is also supported by the fact that households' inflation expectations remain above the actual figures, while wage growth is restrained by the easing of labour market tightness since mid-2022. Even so, underlying wage developments remained strong. Wages in the private sector may rise by 11.6–11.8 percent this year. Nominal wage growth is expected to be 8.5–9.5 percent in 2025, 8.5–9.7 percent in 2026 and 8.8–10.0 percent in 2027. In the private sector, real wages may increase by 7.8-7.9 percent in 2024, 4.6–5.6 percent in 2025, 5.3-6.6 percent in 2026 and 5.6–6.9 percent in 2027 (Chart 1-21).

Box 1-5: Macroeconomic impact of the minimum wage increase

From 1 January 2025, the minimum wage will increase by 9 percent to HUF 290,800 and the guaranteed minimum wage will rise by 7 percent to HUF 348,800 in Hungary (Chart 1-22). Under the agreement between workers' and employers' interest groups and the government, the minimum wage will rise by 13 percent in 2026 and 14 percent in 2027, provided that the macroeconomic expectations set as a condition for the wage plan materialise. The parties agreed to renegotiate the agreement in the event of significant deviations from the expectations. According to the announcement, the convergence of the minimum wage and the guaranteed minimum wage will continue.

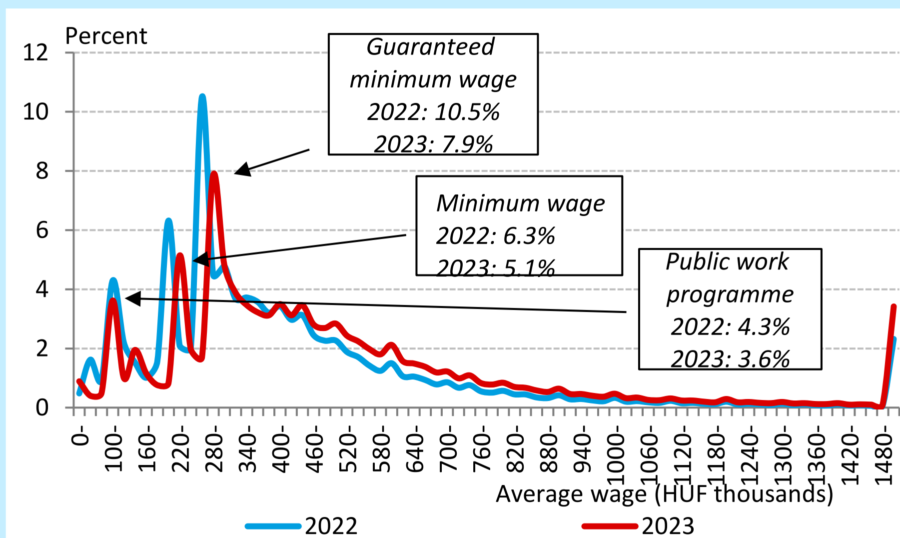
Chart 1-22: Evolution of the minimum wage and the guaranteed minimum wage



Source: HCSO, press information

Regulated wages directly affect around 17 percent of employees, while wage increases may have an indirect impact up to the average wage to avoid wage compression. Around 5 percent of workers earn a minimum wage and 8 percent a guaranteed minimum wage; if those earning wages in between the two are considered, the total share of workers amounts to around 17 percent (Chart 1-23). However, the increase in the mandatory minimum wage also affects higher earners, as it would create wage tensions if the wage advantage of workers in jobs requiring higher skills, experience or qualifications is reduced or eliminated by the increase in the minimum wage. According to our estimate, an increase in regulated wages may have an impact up to the average wage.

Chart 1-23: Distribution of earnings in Hungary (2022–2023)



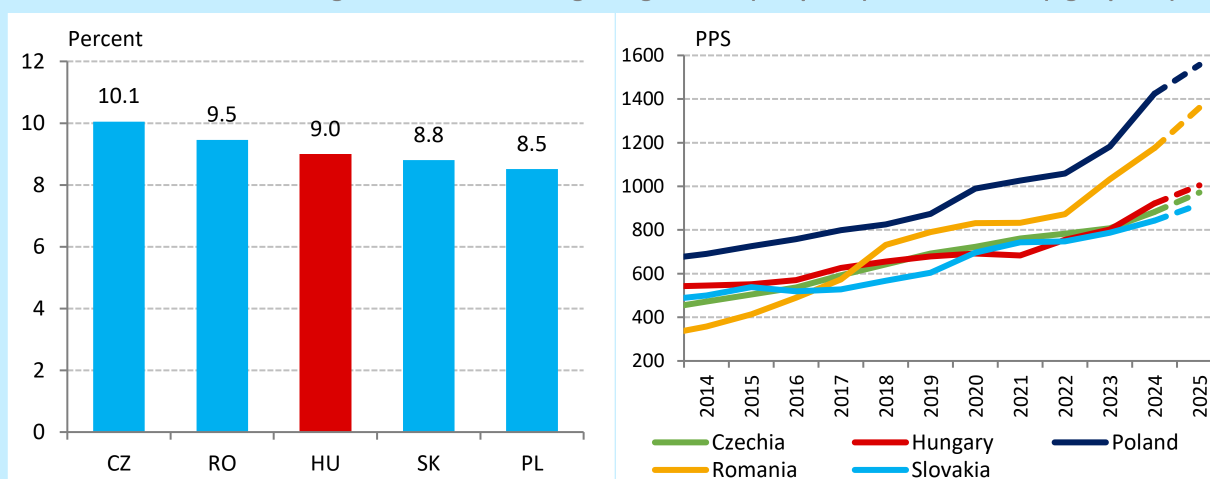
Note: Ratio of the number of earners in a given category to the number of earners in the contribution database of the NTCA. Source: NTCA

The increase in administrative wages in 2025 is consistent with underlying wage developments of around 9 percent; consequently, the aggregate wage index will only be moderately affected. Over the remaining years of the three-year wage agreement, the minimum wage increases of 13 percent and 14 percent may have a more significant macroeconomic impact. Stronger wage growth will boost households' disposable income, and as those earning the minimum wage and guaranteed minimum wage have a high marginal propensity to consume, they may spend a larger part of their surplus income on consumption. In the corporate segment, more significant wage increases may result in increased costs, which may force companies to raise prices without a corresponding increase in productivity; however, the productivity and profitability of companies is heterogeneous according to sectors and firm sizes. To mitigate the increase in costs, during the three years of the wage agreement, employers will have to pay social contribution tax on minimum wage earners based on the previous year's minimum wage.

Several factors may moderate the inflationary effect of the minimum wage increase. The inflationary effect on the demand side may be moderate because with a negative output gap, it is more difficult for companies to pass on cost increases to consumer prices (Chart 3-20). Cost-push inflation effects may be mitigated by the low Hungarian wage share, which may allow higher wage costs to be absorbed (at the expense of profits) without the need for significant repricing. Finally, a higher rate of productivity growth may allow profitability to be maintained without raising prices. That said, productivity growth that remains persistently below wage growth may increase inflationary pressure. Without competitiveness reforms, higher corporate wage costs may only be covered by price increases, which would upset the balance and lead to persistently elevated inflation.

At purchasing power parity, the value of the minimum wage in Hungary is above five other countries in the European Union in 2024 (including the Czech Republic and Slovakia from the countries in the region). The minimum wage increases envisaged for 2025 in the V4 countries and Romania are similar in magnitude to those in Hungary. From 1 January 2025, the minimum wage will rise by 10.1 percent in the Czech Republic, 9.5 percent in Romania, 8.8 percent in Slovakia and 8.5 percent in Poland. As regards long-term developments in minimum wages, trends in minimum wages do not show significant differences in Hungary, the Czech Republic and Slovakia (Chart 1-24). Starting from a level comparable to that of the other Visegrád countries in the early 2000s and exhibiting higher dynamics than its peers, the minimum wage in Poland has surpassed that of the other countries in the region. The pace of progress is even faster in Romania: the lowest Romanian wages are now in the top half of the EU ranking at purchasing power parity (among the 22 Member States with minimum wages), similar to Poland.

Chart 1-24: Minimum wage increases at the beginning of 2025 (left panel) and their level (right panel)



Note: The minimum wage increase for 2025 is compared to the minimum wage at the end of 2024, based on values given in national currency. 2024 and 2025 figures are based on 2023 PPP ratios. In case of minimum wage changes during the year, annual data is given as a time-weighted average. In Romania, super-gross wages were introduced in 2018.
Source: Eurostat, MNB calculation based on press information

Table 1-4: Changes in projections compared to the previous Inflation Report

	2023	2024		2025		2026		2027
	Actual	Previous	Current	Previous	Current	Previous	Current	Current
Inflation (annual average)								
Core inflation	18.2	4.6 - 4.9	4.6 - 4.7	3.2 - 3.8	3.2 - 3.8	2.6 - 3.3	2.6 - 3.2	2.6 - 3.2
Core inflation excluding indirect tax effects	18.1	4.6 - 4.9	4.6 - 4.7	3.0 - 3.6	3.0 - 3.6	2.6 - 3.3	2.6 - 3.2	2.6 - 3.2
Inflation	17.6	3.5 - 3.9	3.6 - 3.7	2.7 - 3.6	3.3 - 4.1	2.5 - 3.5	2.5 - 3.5	2.5 - 3.5
Economic growth								
Household final consumption expenditure	-1.9	3.4 - 4.0	3.9 - 4.1	3.4 - 4.4	4.3 - 5.1	2.9 - 3.9	3.5 - 4.5	2.7 - 3.7
Final consumption of government[1]	4.1	(-0.1) - 0.7	(-0.1) - 0.1	(-0.3) - 0.9	(-0.1) - 0.7	(-0.1) - 1.1	0.0 - 1.0	(-0.1) - 0.9
Gross fixed capital formation	-7.8	(-7.2) - (-5.8)	(-12.3) - (-11.7)	1.5 - 4.5	3.5 - 6.5	1.5 - 4.5	2.6 - 5.4	1.5 - 4.5
Domestic absorption	-5.6	(-1.1) - 0.3	(-0.5) - 0.1	2.1 - 3.7	2.8 - 4.6	1.9 - 3.4	2.0 - 3.6	1.7 - 2.9
Exports	1.5	(-1.5) - (-0.3)	(-2.4) - (-1.8)	4.9 - 6.7	3.6 - 5.6	5.3 - 7.1	6.1 - 7.9	5.1 - 6.9
Imports	-3.8	(-3.8) - (-2.6)	(-3.3) - (-2.7)	4.7 - 6.7	4.4 - 6.6	3.4 - 5.4	4.9 - 6.9	4.4 - 6.4
GDP	-0.9	1.0 - 1.8	0.3 - 0.7	2.7 - 3.7	2.6 - 3.6	3.5 - 4.5	3.5 - 4.5	2.5 - 3.5
Labour productivity[2]	-1.1	0.9 - 1.2	0.3 - 0.5	2.6 - 3.6	2.7 - 3.7	3.3 - 4.6	2.9 - 4.3	2.1 - 3.5
External balance[3]								
Current account balance	0.7	1.4 - 2.6	1.5 - 2.7	2.0 - 3.4	1.0 - 2.4	2.3 - 3.9	1.5 - 3.1	1.8 - 3.6
Net lending	1.7	2.7 - 3.9	2.2 - 3.4	4.0 - 5.4	2.6 - 4.0	4.2 - 5.8	3.3 - 4.9	3.0 - 4.8
Government balance[3]								
ESA balance	-6.7	(-4.7) - (-4.3)	(-4.8) - (-4.4)	(-4.2) - (-3.2)	(-4.2) - (-3.4)	(-3.8) - (-2.8)	(-3.8) - (-2.8)	(-3.2) - (-2.2)
Labour market								
Whole-economy gross average earnings[4]	14.3	12.8 - 13.2	12.9 - 13.1	7.5 - 8.6	8.6 - 9.6	7.8 - 9.1	10.0 - 11.2	6.7 - 8.0
Whole-economy employment	0.6	0.4 - 0.5	0.0 - 0.1	(-0.3) - 0.4	(-0.3) - 0.1	(-0.2) - 0.6	0.1 - 0.8	(-0.2) - 0.6
Private sector gross average earnings[4]	16.3	11.6 - 11.9	11.6 - 11.8	8.0 - 8.9	8.5 - 9.5	7.1 - 8.2	8.5 - 9.7	8.8 - 10.0
Private sector employment	1.0	0.3 - 0.4	(-0.1) - 0.0	0.0 - 0.5	(-0.1) - 0.3	0.0 - 0.5	0.3 - 0.8	0.0 - 0.5
Unemployment rate	4.1	4.2 - 4.3	4.5 - 4.6	3.6 - 3.9	4.1 - 4.3	3.3 - 4.0	3.2 - 3.8	2.9 - 3.9
Private sector nominal unit labour cost	17.7	11.4 - 12.0	12.6 - 12.9	3.5 - 5.0	8.0 - 9.4	2.7 - 4.4	4.5 - 6.2	4.6 - 6.3
Household real income[5]	0.2	5.7 - 6.1	4.7 - 4.9	2.6 - 3.8	3.7 - 4.4	2.6 - 3.8	4.1 - 5.1	2.6 - 3.6

[1] Government final consumption expenditure includes final consumption expenditure of general government and non-profit institutions.
[2] Whole economy, based on national accounts data.
[3] As a percentage of GDP.
[4] For full-time employees.
[5] MNB estimate.

Table 1-5: MNB baseline forecast compared to other forecasts

	2024	2025	2026	2027
Consumer Price Index (annual average growth rate, %)				
MNB (December 2024)	3.6 - 3.7	3.3 - 4.1	2.5 - 3.5	2.5 - 3.5
Consensus Economics (November 2024)[1]	3.6 - 3.8 - 4.1	2.2 - 3.6 - 4.4		
European Commission (November 2024)[2]	3.8	3.6	3.2	
IMF (October 2024)	3.8	3.5	3.1	3.0
OECD (December 2024)	3.8	3.3	2.9	
Reuters survey (December 2024)[1]	3.6 - 3.7 - 3.7	3.3 - 3.9 - 4.2	3.0 - 3.6 - 4.2	
GDP (annual growth rate, %)				
MNB (December 2024)	0.3 - 0.7	2.6 - 3.6	3.5 - 4.5	2.5 - 3.5
Consensus Economics (November 2024)[1]	0.5 - 1.0 - 1.7	1.4 - 2.7 - 3.8		
European Commission (November 2024)[2]	0.6	1.8	3.1	
IMF (October 2024)	1.5	2.9	3.0	3.0
OECD (December 2024)	0.6	2.1	2.9	
Reuters survey (December 2024)[1]	0.4 - 0.6 - 0.8	2.0 - 2.5 - 3.3	2.7 - 3.5 - 4.5	
Current account balance[3]				
MNB (December 2024)	1.5 - 2.7	1.0 - 2.4	1.5 - 3.1	1.8 - 3.6
European Commission (November 2024)[2]	2.1	1.2	1.0	
IMF (October 2024)	1.6	0.6	0.5	0.7
OECD (December 2024)	2.7	2.5	2.4	
Budget balance (ESA 2010 method)[3]				
MNB (December 2024)	(-4.8) - (-4.4)	(-4.2) - (-3.4)	(-3.8) - (-2.8)	(-3.2) - (-2.2)
Consensus Economics (November 2024)[1]	(-5.5) - (-4.9) - (-4.5)	(-4.8) - (-4.2) - (-3.7)		
European Commission (November 2024)[2]	-5.4	-4.6	-4.1	
IMF (October 2024)	-5.0	-4.6	-3.5	-3.0
OECD (December 2024)	-4.9	-4.3	-3.8	
Reuters survey (December 2024)[1]	(-5.0) - (-4.7) - (-4.5)	(-4.5) - (-4.1) - (-3.7)	(-4.5) - (-3.5) - (-2.9)	
Forecasts on the GDP growth rate of Hungary's trade partners (annual growth rate, %)				
MNB (December 2024)	1.2 - 1.6	1.5 - 2.2	1.3 - 2.2	1.4 - 2.3
ECB (December 2024)	0.7	1.1	1.4	
Consensus Economics (November 2024)[1]	1.1	1.6		
European Commission (November 2024)[2]	1.1	1.7	1.9	
IMF (October 2024)[2]	1.2	1.6	1.9	1.8
OECD (December 2024)[2]	1.2	1.8	2.0	

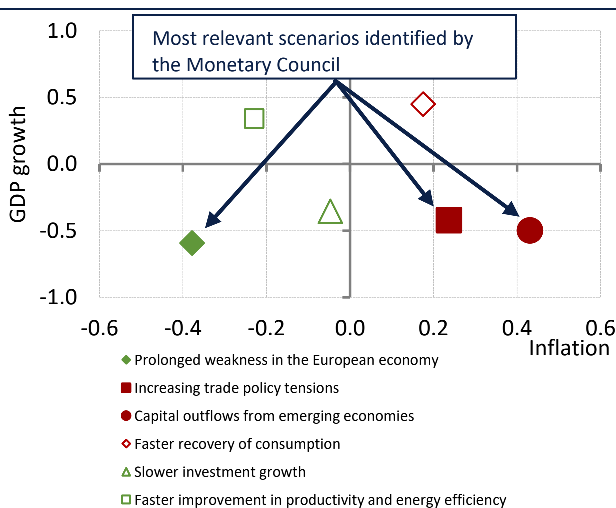
[1] For Reuters and Consensus Economics surveys, in addition to the average value of the analysed replies, we also indicate the lowest and the highest values to illustrate the distribution of the data.
[2] Values calculated by the MNB; the projections of the named institutions for the relevant countries are adjusted with the weighting system of the MNB, which is also used for the calculation of the bank's own external demand indices. Certain institutions do not prepare forecast for all partner countries.
[3] As a percentage of GDP.

Source: Consensus Economics, ECB, European Commission, IMF, OECD, Reuters poll, MNB

2 Effects of alternative scenarios on our forecast

The Monetary Council highlighted three alternative risk scenarios around the baseline projection in the December Inflation Report. In the scenario that assumes prolonged weakness in European economic activity, economic growth and inflation are both likely to be lower compared to the baseline. The scenario featuring increased trade policy tensions is consistent with a higher inflation and lower growth path than the baseline. The risk scenario assuming capital outflows from emerging economies is also consistent with higher inflation and a lower growth path. In addition to the scenarios highlighted, the Monetary Council discussed other alternative paths, including a faster recovery in consumption, slower investment growth and faster improvements in productivity and energy efficiency.

Chart 2-1: Risk map: effects of alternative scenarios on the baseline forecast



Note: The risk map presents the average difference between the inflation and growth path of the alternative scenarios and the baseline forecast over the monetary policy horizon. The red markers represent tighter and the green markers represent looser monetary policy than in the baseline forecast.
Source: MNB

Prolonged weakness in the European economy

In 2024 Q3, GDP growth in the European Union slowed year-on-year, while Germany's economic output declined slightly. In the European Union, GDP for 2024 Q3 grew by 1.0 percent on an annual basis, while increasing by 0.9 percent in the euro area. In Germany, which is Hungary’s main trading partner, economic output contracted by 0.3 percent versus the same period last year. Industrial production in the euro area continued to fall, with an annual decline of 2.8 percent registered in September. Retail sales growth slowed to 1.9 percent in October.

The purchasing managers' index (PMI) for manufacturing fell in the euro area in November, remaining below the expansion threshold. At the same time, the economic sentiment indicator (ESI) worsened by 0.7 points in October and did not change substantially in November. The German PMI remained at a low level in the autumn months. German private sector business activity and the manufacturing PMI remained below the threshold in the autumn months, despite a slight increase in October. According to a survey by the ifo Institute, the outlook for German manufacturing, and especially for the automotive industry, remains unfavourable.

Market analysts' expectations for 2024 and 2025 forecast subdued growth in the euro area. The median of Bloomberg analysts' expectations is for the European Union to expand by 1.0 percent in 2024 and 1.5 percent in 2025, while Germany is projected to expand by –0.1 and 0.7 percent, respectively. At the same time, the global economy is expected to grow at a rate of 3.1 percent in both years.

If the **risk scenario of prolonged weakness in the European economy** materialises, growth in the EU, and within that especially in Germany, and, in line with this, in Hungary will be more moderate than in the baseline scenario. The

slowdown in the European Union economy continues to weigh on the growth prospects of the German export sector. The subdued performance of Hungary’s external markets hampers domestic export performance via a decline in external demand, thus contributing to a slowdown in GDP growth. In addition, a lower domestic inflation path compared to the baseline is achieved due to lower external inflation.

Increasing trade policy tensions

In recent months, the US presidential election was a key aspect from the perspective of global economic growth. A majority in the Senate and the House of Representatives will provide the next US government significant legislative power. The new administration may introduce additional import tariffs, as announced so far, with the aim of improving the external balance and stimulating job creation and economic growth. A wide range of tariffs have been mentioned in the president-elect's communications so far, targeting China, Canada and Mexico, and more generally as well. In addition, there is a risk that customs duties against the EU could be extended, and rates of duty increased. In this respect, the focus was mainly on the exports of European car manufacturers, which may have a significant impact on the sector, which is of particular importance for Hungary.

The extension of protectionist measures poses a substantial risk to global economic growth. At the beginning of November, the US imposed a new export ban on certain components for chip production against China, in response to which the Chinese authorities announced an immediate ban on exports to the US of several rare metals that are important for the production of semiconductor components. Measures already in place and those expected in the future could further reduce trade between the US and China and the rest of the world, which would also reduce the dynamics of global trade. At the same time, global value chains may become fragmented, and increased trade tensions could lead to a global economic slowdown. Because of their integration into global supply chains, the vulnerability of small, open economies may increase substantially. 2.9 percent of Hungary's goods exports and 19.7 percent of the EU's goods exports go directly to the US. As exports to the US fall, the EU economy may slow down, which could also drag down the domestic economy embedded in it.

In our alternative path, we expect duties and restrictions on world trade to increase. The future protectionist economic policies of the new US administration, in particular the imposition of tariffs against China and the EU,

and the ongoing geopolitical tensions could result in a more moderate expansion of world trade than assumed in the baseline. As a result, weaker external demand may also dampen domestic export performance. In addition, the realisation of risks will lead to higher global inflation. In this alternative scenario, the external inflation environment will thus be higher than expected, causing a ripple effect in domestic prices. The scenario is consistent with a higher inflation and lower growth path than the baseline.

Capital outflows from emerging economies

In recent months, risk aversion towards emerging markets has increased, with this development intensifying after the US elections. In addition to geopolitical conflicts, the US presidential election has been the focus of market participants in recent months. Developed market risk indicators typically rose in the run-up to the US presidential election day and then declined significantly thereafter. The US dollar strengthened significantly in November, with capital outflows in emerging markets starting in October in parallel with this.

Geopolitical conflicts have intensified in the past quarter. Both the protracted war between Russia and Ukraine and the escalation of conflicts in the Middle East have increased uncertainty in markets and fuelled risk aversion, especially towards emerging markets. In 2024, Hungary and similar emerging market economies experienced an overall capital outflow.

In our alternative path, we expect increasing capital outflows. As the US dollar strengthens further and geopolitical tensions intensify, market sentiment towards emerging markets deteriorates further. In this environment, risk aversion towards emerging markets rises in a more permanent and stronger manner. Although several of Hungary's fundamentals (current account balance, primary budget balance, inflation) have improved significantly by regional standards, investors differentiate on the basis of other criteria in the current environment. This may result in capital withdrawal and a further rise in inflation, which warrants tighter monetary conditions. As risks rise, confidence declines, leading companies to postpone investments, while savings motives may again play a stronger role in consumption decisions. The scenario is consistent with higher inflation and a lower growth path.

Other risks

In addition to the highlighted scenarios, the Monetary Council considered three other alternative paths.

In the **alternative scenario of a faster recovery in consumption**, the additional income from sustained high real wage growth, interest payments on government bonds and the measures announced by the government will increasingly feed through to consumption as lending picks up and the precautionary motive unwinds. The faster recovery of consumption is consistent with a higher growth and inflation path compared to the baseline scenario.

In a scenario with a slower investment growth trajectory, business confidence rebounds more slowly as a result of geopolitical uncertainties and a protracted industrial recovery, and a pick-up in national economic investment thus continues to be delayed. The slower recovery in investment is consistent with a lower growth path.

In the risk scenario with a faster improvement in productivity and energy efficiency, the shift to an intensive growth model further stimulates growth in the domestic economy, mainly on the supply side, via improved competitiveness. Competitiveness may improve more strongly than assumed in the baseline scenario in the event that more of the 330 steps to improve competitiveness are carried out, and if energy efficiency improvements are enhanced by implementing the 144 points from the discussion paper ‘Sustainable Balance and Catching-up’, accelerating a green transition. Completion of the targeted measures significantly improves productivity, leading to a lower cyclical position in the domestic economy. This is consistent with a lower inflation path and higher economic output.

3 Macroeconomic overview

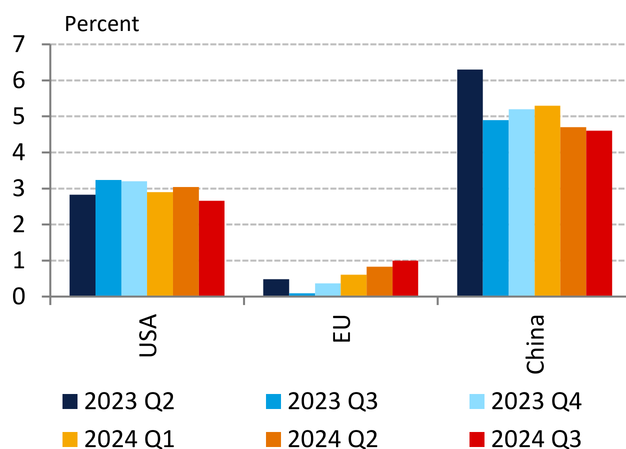
3.1 Evaluation of the international macroeconomic developments

In 2024 Q3, economic growth in the European Union continued to slowly accelerate. Economic growth in the US and China remains buoyant, but a slight deceleration has been seen. The intense geopolitical situation and subdued growth prospects in Europe still represent a major risk to the external outlook. Investor sentiment was volatile in the previous quarter, with an overall deterioration on the back of an expected intensification of global trade disputes, geopolitical risks linked to the hotspots in Ukraine and the Middle East, and macroeconomic data from the US and Chinese economies. Emerging regions were particularly affected by this deterioration in sentiment. At its November rate-setting meeting, the Federal Reserve lowered the target range for the federal funds rate by 25 basis points to 4.50–4.75 percent. Based on market pricing, the Fed may cut the federal funds rate further this year. In both October and December, the ECB cut its key deposit rate by 25 basis points. In the region, at its September and November policy meetings the Czech central bank cut its key policy rate by 25 basis points each time. Both the Romanian and Polish central banks decided to keep the base rate unchanged in the past quarter.

3.1.1 International economic trends

Economic growth in the European Union continued to slowly recover in 2024 Q3 (Chart 3-1). Overall, the performance of European economies were slightly above expectations. On a seasonally and calendar-adjusted basis, in 2024 Q3 economic output in the EU and the euro area expanded by 1.0 percent and by 0.9 percent, respectively, in a year-on-year view. Value added in Hungary's main trading partner, Germany, contracted by 0.3 percent year-on-year in 2024 Q3. Among the countries in the region, GDP grew in Czechia (+1.3 percent), Poland (+1.7 percent) and Slovakia (+1.7 percent) in year-on-year terms. GDP contracted on a quarterly basis in 6 of the 27 countries of the European Union.

Chart 3-1: GDP growth in the world's leading economies

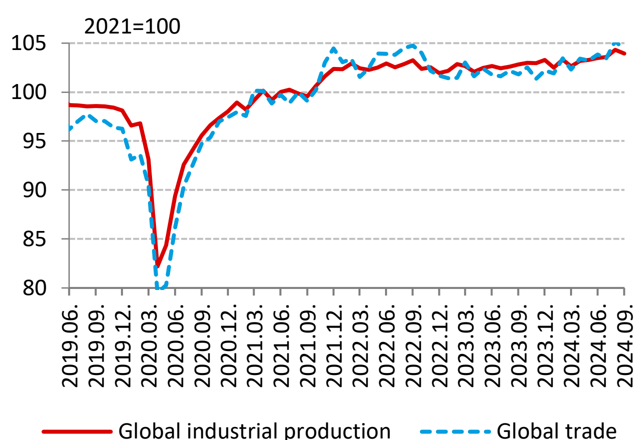


Note: Annual growth. In case of the EU, the calculation is based on seasonally and working day adjusted data.
Source: Trading Economics, FRED, Eurostat

From a high level, GDP growth in the US decelerated somewhat in year-on-year terms. The US economy grew by 2.7 percent on an annual basis, while on a quarterly basis, it expanded by 0.7 percent. Growth was supported by a continued, strong expansion in household consumption. The dynamics of consumption growth, and hence GDP growth, may moderate in line with the easing of labour market tightness. According to the IMF's latest forecast, GDP is expected to grow by 2.8 percent this year and 2.2 percent next year.

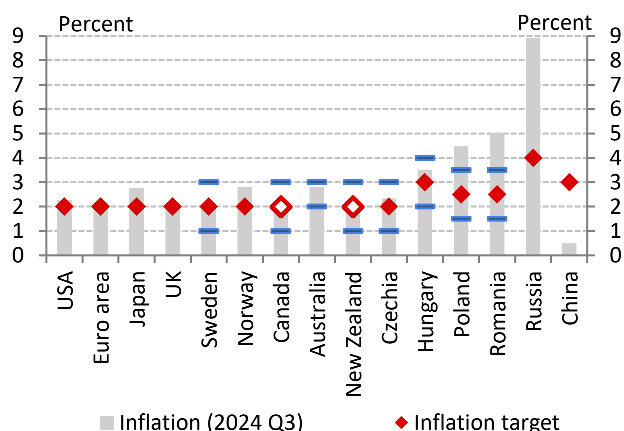
China's growth decelerated somewhat in 2024 Q3, but remained buoyant, expanding at a year-on-year rate of 4.6 percent and 0.9 percent on a quarterly basis. While industrial production and exports exhibit steady growth, consumer confidence remains low; therefore, the contribution of household consumption to growth declined relative to previous quarters. Looking ahead, the contribution from domestic items may be boosted by the stimulus package with nearly USD 1,400 billion announced

Chart 3-2: Development of global industrial production and global trade



Note: Based on seasonally adjusted data.
Source: CPB

Chart 3-3: Inflation targets of central banks and actual inflation



Note: The blue lines represent the inflation control range in Australia, Canada and New Zealand, while in other countries they mark a permissible fluctuation band. In Canada and New Zealand the mid-point of the target band is accentual, which is marked by empty diamond.
Source: OECD, FRED, National Institute of Statistics Romania, Statistics Sweden, Federal State Statistics Service

in early November. For this year, based on the IMF's forecast, at around 4.8 percent, economic growth may fall slightly short of the government's target of 5 percent, while GDP may grow by 4.5 percent in 2025.

Risks to the external outlook are posed by the unfavourable outlook for industrial production in Europe, as well as the ongoing war between Russia and Ukraine and the intense geopolitical situation. In 2024 Q3, global trade in goods and industrial production increased (Chart 3-2). Global economic activity continued to be supported by tight labour markets in advanced economies. The global and European growth outlook for this year is essentially unchanged compared to the September forecast. Consumer confidence in the EU economies improved to some degree, as measured by sentiment indices. Business confidence stagnated in services and deteriorated somewhat in industry.

3.1.2 International monetary policy, inflation and financial market trends

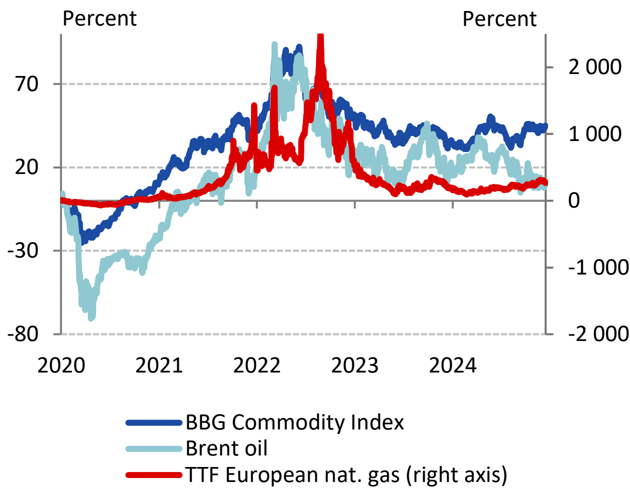
Global inflation moderated somewhat further in the past quarter, with several countries coming close to their central bank targets (Chart 3-3). Global oil prices have been volatile in recent months, but stabilised between USD 70-75 in November. The price of natural gas continued to rise from a low level, but remains below the level observed before the Russia–Ukraine war (Chart 3-4).

Inflation in the United States has been volatile in recent months. In the US, annual rate of CPI inflation rose from 2.4 percent in September to 2.6 percent in October and 2.7 percent in November. The PCE inflation index dropped from 2.3 percent in August to 2.1 percent in September and then rose again to 2.3 percent in October. In terms of the structure of inflation, services continued to make the largest contribution, as market services inflation advanced from 3.7 percent in September to 3.9 percent in October.

At its November meeting, the Fed lowered the target range for the federal funds rate by 25 basis points to 4.50-4.75 percent. According to the Committee, the risks to achieving its employment and inflation goals are close to balanced. At the press conference following the decision, Jerome Powell said that according to recent indicators, economic activity was expanding at a solid pace and that labour market conditions continued to ease. He stressed that the outcome of the US presidential election would have no effect on the Fed's policy decisions.

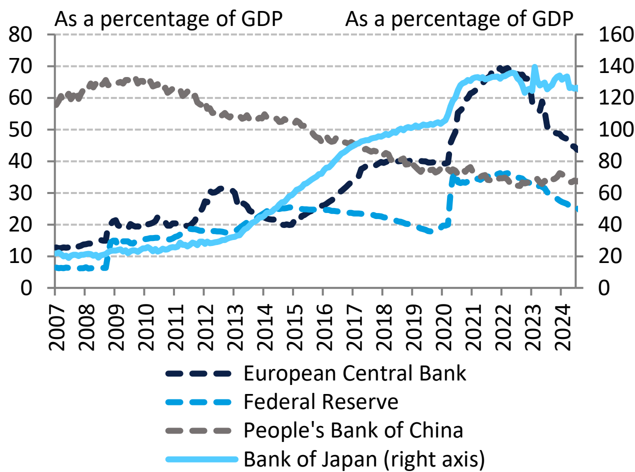
The gradual decline in the Fed's balance sheet total continued during the past quarter, standing at

Chart 3-4: Commodity prices



Note: The figure shows the change compared to January 2020.
Source: Bloomberg

Chart 3-5: Balance sheet totals of globally important central banks



Source: Databases of central banks, Eurostat, FRED

USD 6,952 billion or 23.7 percent of GDP at the beginning of December 2024 (Chart 3-5).

Inflation in the euro area fell to 1.7 percent in September, below the central bank's 2-percent inflation target, before rising back to the central bank's target in October, and then advancing further to 2.3 percent in November. Core inflation was 2.7 percent both in October and November.

At its October and December rate-setting meetings, the ECB cut its key deposit rate by 25 basis points each time, bringing the key deposit rate down to 3.0 percent. The ECB based its decision on its current view of the inflation outlook, the dynamics of underlying inflation trends and the strength of monetary transmission. Following the December interest rate decision, ECB President Christine Lagarde noted that while inflation had approached the central bank's target, the fight against inflation was not over yet. She added that domestic inflation remained high, and the intensification of geopolitical tensions posed upward inflationary pressure. By the beginning of December 2024, the ECB's balance sheet total had fallen to EUR 6,351 billion or 42.7 percent of GDP (Chart 3-5).

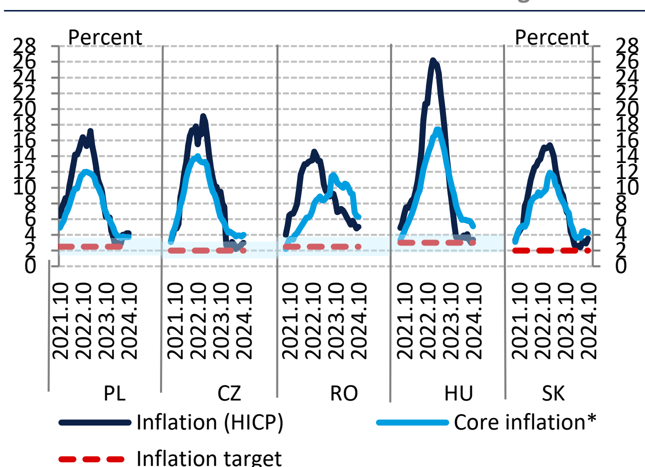
At its October policy meeting, the Bank of Japan maintained the interest rate on excess reserves at 0.25 percent. The annual rate of inflation dropped from 2.5 percent in September to 2.3 percent in October. Inflation is forecast to be around 2 percent next year and the year after. Underlying inflation trends are expected to strengthen gradually as inflation expectations increase in response to rising wages. Kazuo Ueda, Governor of the Bank of Japan, said that the central bank was ready to raise interest rates again at a cautious pace if necessary.

China's central bank reduced the interest rate on its benchmark one-week reverse repo instrument by 20 basis points to 1.5 percent and the interest rate on its two-week reverse repo instrument from 1.95 percent to 1.85 percent. The central bank revised its previous benchmark medium-term lending rate from 2.3 percent to 2.0 percent. The central bank also lowered the minimum reserve ratio for the largest and medium-sized banks by 0.5 percentage point to 9.5 and 7.5 percent, respectively. In addition, it introduced two new instruments to support the equity market and adjusted the terms of its refinancing facility to support housing purchases by state-owned enterprises. Inflation fell from 0.4 percent in September to 0.3 percent in October and 0.2 percent in November. The central bank's total assets stood at 34.5 percent of GDP in October.

The Bank of Poland left the policy rate unchanged at 5.75 percent in the past quarter. Inflation is expected to remain significantly above the NBP target in the coming quarters primarily due to the phasing out of the regulatory price caps on households' energy prices. Inflation increased from 4.9 percent in September to 5.0 percent in October and remained unchanged in November. The Harmonised Consumer Price Index was 4.2 percent both in September and October (Chart 3-6).

The Czech central bank cut its policy rate by 25 basis points each time at its September and November policy meetings. Policymakers reaffirmed their commitment to pursuing tight monetary policy in order to keep inflation close to the central bank's target of 2 percent in the long term. Overall, the risks and uncertainties surrounding inflation are pointing slightly upwards, and in the central bank's view inflationary pressures in the services sector have intensified again. Aleš Michl, Governor of the Czech central bank, indicated that the monetary easing cycle could be suspended, should the need arise. Inflation advanced to 2.8 percent in October from 2.6 percent in September and remained unchanged in November. The Harmonised Consumer Price Index climbed to 3 percent in October (Chart 3-6).

Chart 3-6: Inflation and core inflation in the region



Note: Annual change, percent. * In the case of core inflation, we use the definition of the Eurostat (inflation excluding energy, food, alcohol and tobacco). The blue area indicates the tolerance band around the inflation targets.
Source: Eurostat

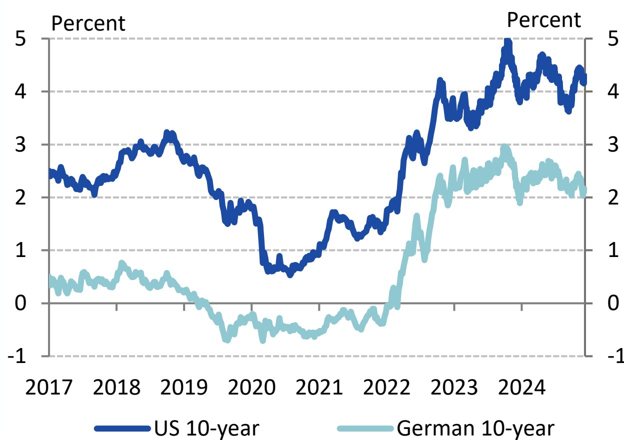
At its October and November policy meetings, the Romanian central bank opted to maintain its policy rate at 6.50 percent. There are considerable uncertainties surrounding the inflation outlook, primarily stemming from the current and future stance of fiscal policy, labour market tightness, wage dynamics and future energy price developments. The annual rate of inflation increased from 4.6 percent in September to 4.7 percent in October and to 5.1 percent in November. According to the Harmonised Index of Consumer Prices (HICP), the annual rate of inflation fell to 4.8 percent in September 2024 from 5.3 percent in August, before rising to 5 percent in October (Chart 3-6).

Investor sentiment was volatile in the previous quarter, with an overall deterioration on the back of an expected intensification of global trade disputes, geopolitical risks linked to the hotspots in Ukraine and the Middle East, and macroeconomic data from the US and Chinese economies. Emerging regions were particularly affected by the deterioration in sentiment. Moreover, geopolitical conflicts may also pose additional significant risks, primarily via the energy sector. In the period preceding the US presidential election in early November, global investor sentiment deteriorated with a parallel rise in uncertainty, while financial market volatility increased. This shift affected bond markets the most, but volatility in foreign

exchange rates and developed stock market indices also rose. Following the election, asset prices were mainly driven by expectations of the economic policy stance regarding the new US administration and the interest rate policies of developed market central banks. The interest rate path priced in by the market shifted upwards for the Fed, owing favourable economic data, and downwards for the ECB, as a result of unfavourable macroeconomic data, contributing to a significant strengthening of the US dollar during the period.

Long bond yields in the USA rose and the US dollar strengthened significantly. The US 10-year yield rose by almost 60 basis points to 4.3 percent, while the German 10-year yield moved down by 4 basis points to 2.16 percent (Chart 3-7). The Japanese 10-year yield rose 20 basis points from the previous quarter to reach 1.04 percent. Emerging bond market yields also rose during the period, with the Romanian 10-year yield up 35 basis points, the Hungarian 10-year up 4 basis points, the Czech yields up 25 basis points and the Polish yield up 38 basis points. The MSCI index of developed economy equities rose 4.1 percent, while the emerging market index rose by 0.8 percent. During the quarter, the euro and the pound sterling weakened against the US dollar by 6.1 percent and 4.5 percent, respectively, while the Swiss franc depreciated by 4.9 percent and the Japanese yen by 6.8 percent.

Chart 3-7: US and German 10y-government bond yields



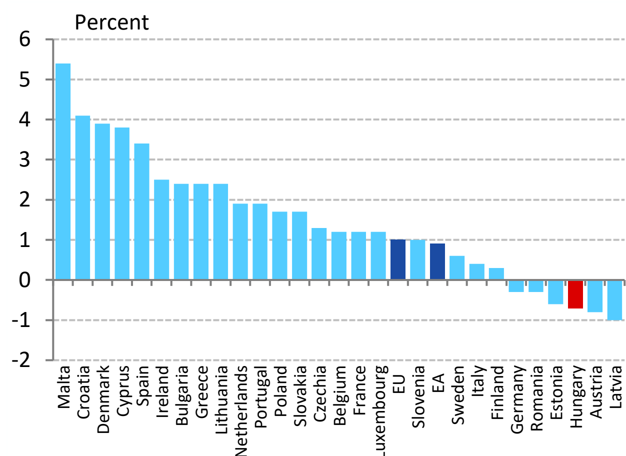
Source: Bloomberg

Based on market pricing, the Fed may keep lowering interest rates this year. The Fed and the ECB reduced interest rates at their policy meetings in the past quarter, and market pricing for the final interest rate decision of the year suggests an almost 100-percent chance of an interest rate cut by the Fed, while for the ECB, the market-priced probability of a 50-basis point reduction in January is also around 100 percent.

3.2 Analysis of the production and expenditure side of GDP

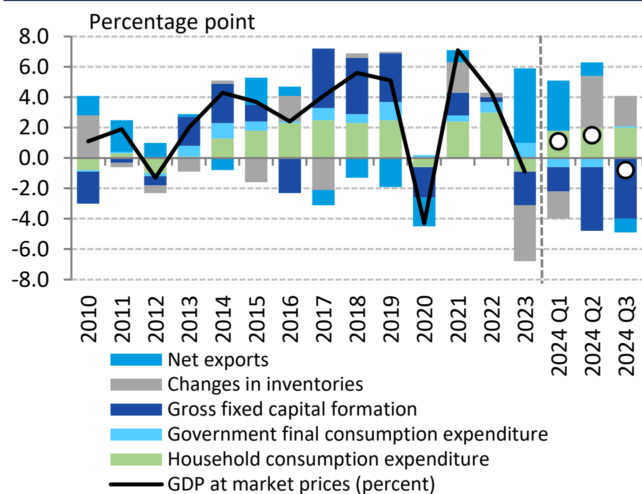
In 2024 Q3, gross domestic product decreased by 0.8 percent on an annual basis based on unadjusted data. According to seasonally, calendar-adjusted and balanced data, value added decreased by 0.7 percent both on an annual and quarterly basis. The Q3 contraction in the national economy was primarily linked to production sectors, with the expansion in services cushioning the decline. In terms of expenditure, besides household consumption, changes in inventories supported year-on-year economic growth, while investment and net exports restrained growth.

Chart 3-8: Annual GDP change in EU countries in 2024 Q3



Note: Seasonally and calendar adjusted data.
Source: Eurostat

Chart 3-9: Annual change in decomposition of expenditure side GDP



Note: Government final consumption expenditure includes final consumption expenditure of general government and non-profit institutions. Changes in inventories includes acquisitions less disposals of valuables.
Source: HCSO, MNB

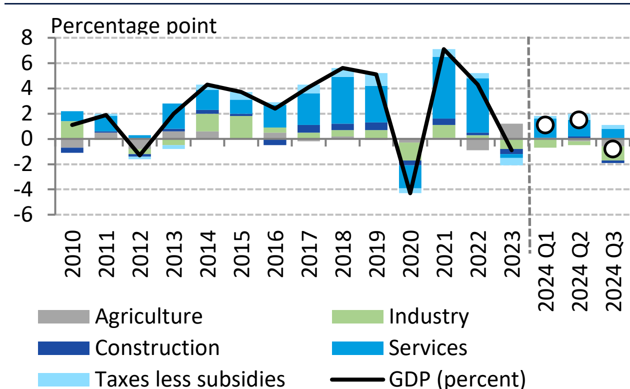
Based on raw data, in 2024 Q3 Hungary's gross domestic product decreased by 0.8 percent on an annual basis. The incoming data fell short of our expectations in the September Inflation Report. According to the seasonally, calendar-adjusted and balanced data used for international comparison, Hungarian GDP contracted by 0.7 percent on both an annual and quarterly basis. GDP expanded by 1.0 percent in the European Union and by 0.9 percent in the euro area in the third quarter (Chart 3-8).

Consumption growth continued in line with positive real wage dynamics and favourable household income trends. Household consumption expenditure increased by 4.5 percent in 2024 Q3 versus the same prior-year period, contributing 2.0 percentage points to economic growth (Chart 3-9). The domestic consumption expenditure of households rose by 4.1 percent. Domestic consumption expenditure increased in all groups: the volume of durable goods increased by 1.6 percent, while that of semi-durable goods by 4.6 percent, non-durable goods by 4.8 percent and services by 4.0 percent. Final collective consumption expenditure rose by 0.9 percent in the third quarter.

In October 2024, retail sales were up 3.6 percent, and the inflation-adjusted sales of online cash registers rose by 4.9 percent year-on-year. Online cash register sales differ from retail sales in that they include a part of, for example, sales from catering, taxi services and accommodation services.

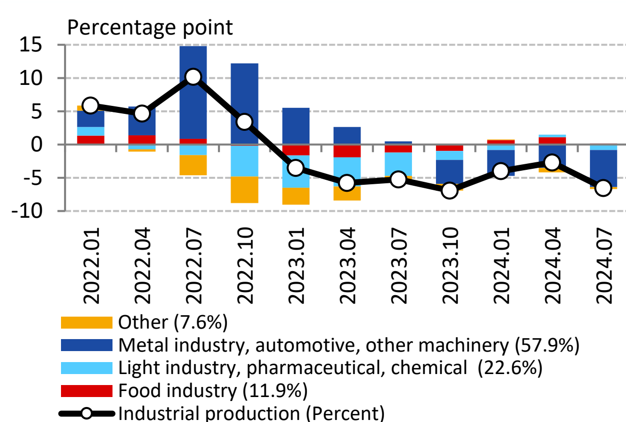
In 2024 Q3, gross fixed capital formation contracted by 14.0 percent on an annual basis, decelerating economic growth by 4.0 percentage points. Construction projects shrank by 13.3 percent, and investment in machinery and equipment fell by 18.4 percent. Of the individual sectors of the national economy, the only area where investment showed an expansion was real estate transactions related to households (+10.9 percent). The decline in investment in sectors producing for exports exceeded 25 percent for the second quarter in a row, while investment in (quasi-fiscal) sectors indirectly linked to the government dropped by 15.4 percent, and investment in the narrowly defined public sector (public administration, education, health) fell by 22.4 percent after four quarters of expansion.

Chart 3-10: Annual change in decomposition of production side GDP



Source: HCSO

Chart 3-11: Sectoral breakdown of annual change in domestic industrial production



Note: The 2023 weight of the sectors in industrial production is given in brackets. Without water and waste management industry. Total industrial production does not include the performance of enterprises with less than five employees. Source: HCSO, MNB

As in the previous quarter, the change in inventory substantially increased the annual change in GDP by 2.0 percentage points in 2024 Q3.

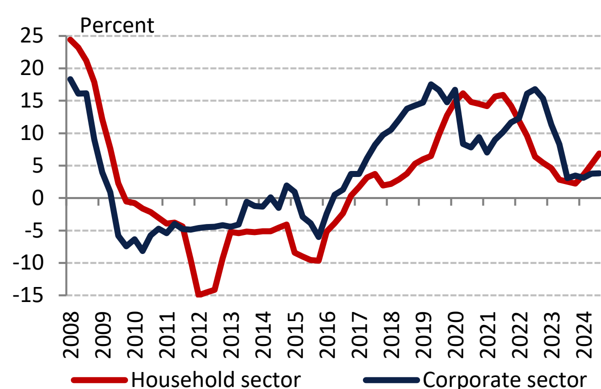
In 2024 Q3, the contribution of net exports turned negative, reducing GDP growth by 0.9 percentage point. This was because the volume of imports (–0.9 percent) decreased to a lesser extent than that of exports (-1.9 percent). Exports of goods fell by 3.4 percent, while exports of services increased by 2.1 percent compared to the same period of the previous year. Imports of goods contracted by 1.5 percent, while imports of services grew by 0.9 percent. The trade balance showed a surplus of EUR 1.8 billion in the third quarter. The terms of trade deteriorated by 1.2 percent year-on-year, reflecting negative contributions from mineral fuels, food, machinery and transport equipment. In October 2024, the balance of foreign trade product turnover showed a surplus of EUR 965 million, according to preliminary data. Compared to the previous month, the balance improved by EUR 16 million, while compared to the same period of the previous year, the balance worsened by EUR 127 million. The balance adjusted for VAT residents showed a surplus of EUR 198 million. In October, the value of goods exports calculated in euros decreased by 0.8 percent on an annual basis. The nominal value of goods imports expressed in euros increased by 0.2 percent over the course of one year.

The contraction in the national economy in the third quarter was primarily linked to production sectors, with the expansion in services cushioning the decline (Chart 3-10). Industrial output fell by 4.4 percent compared to the same period of the previous year, including a 6.2 percent contraction in the value added of manufacturing. Among the manufacturing sectors, the largest contributors to the decline were the metal industry, automotive and other machinery (Chart 3-11).

Construction sector output fell by 4.0 percent in the third quarter versus the same prior-year period. Construction of buildings decreased by 2.2 percent and construction of other structures by 11.0 percent year-on-year in the third quarter. At the end of September, the volume of construction contracts was 36.0 percent higher than in the same period of the previous year, while the volume of new contracts increased by 2.7 percent.

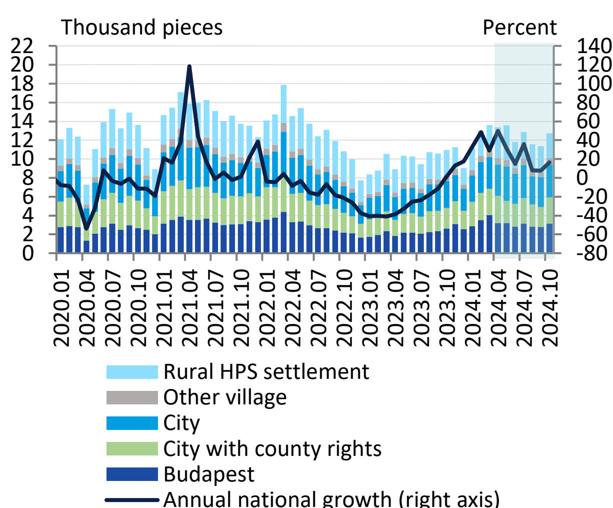
In the third quarter, the value added of agriculture was 14.9 percent lower than in the same period of the previous year. The drought may have had the strongest impact on the maize and sunflower seed harvest in the third quarter, while wheat and barley yields were lower, owing to a decline in the harvested area.

Chart 3-12: Annual change in lending to non-financial corporates and households



Note: Data for the corporate and household segments are based on transactions with the total financial intermediary system.
Source: MNB

Chart 3-13: Number of housing market transactions by settlement type



Note: Only taking into account 50-percent and 100-percent private acquisitions. From January 2023 to March 2024, the data of the NTCA fee database are adjusted based on the estimation of the level of processing by type of settlement. Based on transactions and estimated market share of real estate agents in the highlighted months.
Source: Housing market intermediary database, MNB, NTCA

Overall, the value added of services rose by 1.9 percent in 2024 Q3. The expansion was broad-based, with the largest increase recorded by the HCSO in the arts, recreation and other services sector (+5.9 percent). In addition, the value added of transportation and storage rose by 2.8 percent, that of information and communication increased by 2.6 percent, while that of tourism, finance and insurance advanced 2.4 percent. The value added of trade and the repair of motor vehicles, two major contributor sectors, increased by 1.3 percent. Services linked to the government (public administration, defence, compulsory social security, education, human health and social care) grew by 1.9 percent overall. Human health and social care grew by 2.3 percent and education by 3.8 percent, while public administration, defence and compulsory social security rose by 0.4 percent.

In 2024 Q3, demand in the market of loans to households remained buoyant, while banks perceived a 'wait-and-see' attitude for corporate loans. The annual growth rate of the total financial intermediation system's lending to households and corporations amounted to 6.9 percent and 3.8 percent, respectively, at the end of September (Chart 3-12). In the corporate segment, the annual growth rate of SME loans – which is more consistent with underlying developments – decelerated by 1.0 percentage point to –0.4 percentage point at the end of September. In the third quarter, new contracts signed in the household segment increased by 72 percent, while they declined by 19 percent year-on-year in the corporate segment. Based on the responses to the lending survey, banks perceived a pick-up in demand for consumer loans in the third quarter, while a smaller group of banks reported fading demand in the corporate loan market.

The number of sales in the housing market continues to rise in a year-on-year comparison (Chart 3-13). In 2024 Q3, the number of private housing transactions amounted to 35,800 nationwide, up 16 percent from the number of transactions recorded in the same period last year. In the third quarter, the number of housing market sales increased by 31 percent in annual terms in Budapest, 16 percent in towns with county rights, 18 percent in other towns and only 3 percent in villages eligible for the rural Home Purchase Subsidy Scheme for Families. According to the MNB's house price index, nominal house prices rose by 9.3 percent in 2024 Q2 nationally compared to the same period last year, with Budapest also seeing an increase of 9.3 percent, towns 8.7 percent on average and villages 9.1 percent. Preliminary data suggest that the annual growth rate of house prices may have accelerated to 12.8 percent nationally and 14.7 percent in Budapest in 2024 Q3.

Box 3-1: Divergence in Hungarian and German economic performance

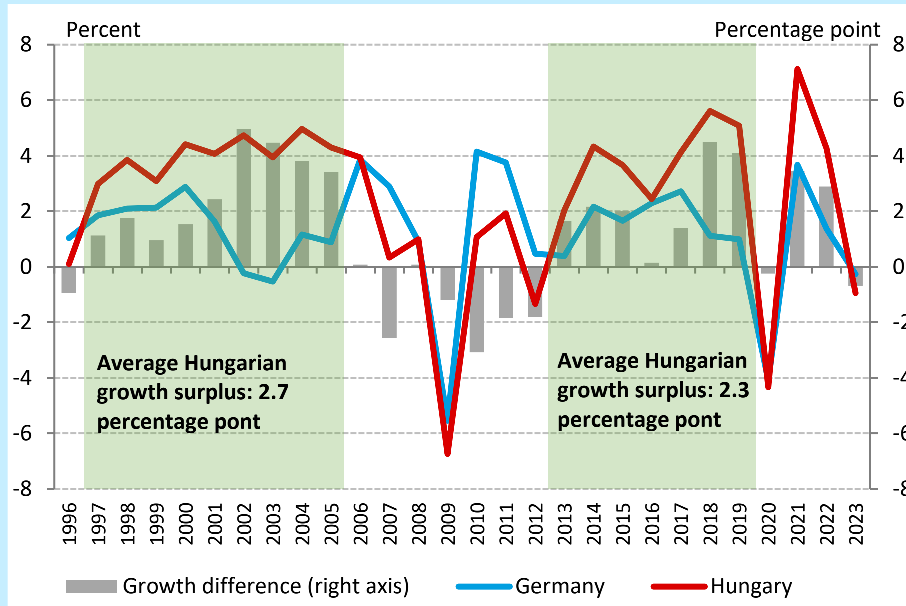
The performance of the Hungarian economy depends heavily on its main external trade partner, Germany. German-owned companies employ nearly 230,000 people, representing 4.9 percent of the total workforce. Together, these companies accounted for 7.2 percent of Hungarian added value in 2022. Accordingly, Germany is also Hungary's most important trade partner, accounting for more than one quarter of Hungarian exports of goods and nearly one fifth of exports of services. Traditionally, manufacturing, including the automotive industry and its supplier sectors, has the largest German presence (Audi, BMW, Mercedes, Robert Bosch), but, for example, Deutsche Telekom is also an important employer in telecommunications.

The two economies have had strong industrial and trade relations since the early 1990s. Many major German industrial companies (including Siemens, Bosch) established themselves in Hungary immediately after the regime change, with Audi producing engines at its plant in Győr since 1994 and cars since 1998. The Mercedes plant in Kecskemét has been operating since 2012, while the BMW plant in Debrecen, which is due to start production in the second half of 2025, marks another important milestone in automotive relations. **Due to the close relationship between the two countries, the development of economic cycles is similar, but the Hungarian economy experiences a more profound impact from these cycles.** The dynamics of Hungarian GDP are more prone to swings than that of Germany. In periods of upswing, Hungarian growth typically outpaces that of Germany, but crises also have a stronger impact on output.

Sustained additional GDP growth emerged in the periods from 1997 to 2005 and 2013 to 2019 (Chart 3-14). Whereas Germany was characterised by high unemployment and low GDP growth in the late 1990s and early 2000s, which led to the country being dubbed the 'sick man of Europe', Hungary experienced dynamic growth during this period. Thanks to pro-growth economic policies gaining ground by the late 1990s and new industrial capacities being built, Hungary became the frontrunner in the region. The healthy, balanced growth lasted until 2002, but then the balance was upset. Although growth continued for several years, significant imbalances built up, which came to the fore during the financial crisis. In the period between 1997 and 2005, Hungarian GDP grew, on average, at a 2.7 percentage point higher rate than that of Germany.

The shift in Hungary's economic policy after 2010 also resulted in significant additional growth. After the financial crisis and then the euro area sovereign debt crisis, the German economy grew in the range of 1-3 percent with relatively stable employment, but by the late 2010s, it was already facing structural problems. In Hungary, the shift in economic policy in the early 2010s, with a focus on increasing employment, enabled the country to maintain both economic growth and fiscal balance. After the reforms took effect, Hungarian GDP grew, on average, by 3.9 percent a year between 2013 and 2019, at a 2.3 percentage point higher rate than that of the German economy. Overall, in addition to periods of upswing, timely and balanced economic reforms were also necessary to achieve sustained additional growth.

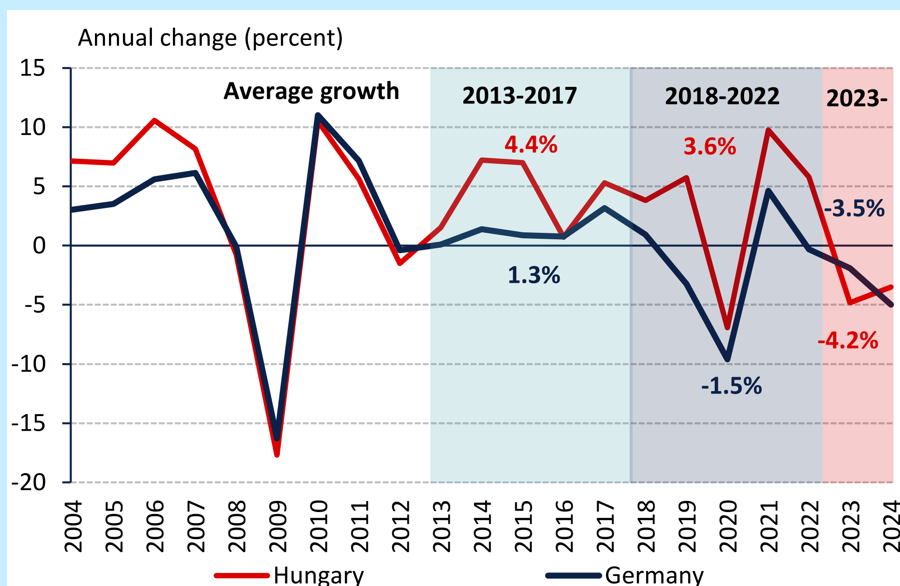
Chart 3-14: Annual change in Hungarian and German GDP



Source: Eurostat

Additional growth in the Hungarian industry was tied to periods with significant foreign working capital inflows into Hungary and the Hungarian export market share increased due to the restructuring of the production chain (Chart 3-15). Until the 2008–2009 financial crisis, industrial output in the two countries was similar. Subsequently, a structural transformation took place in Hungarian output: while in the 2000s the largest contributor to growth was electronics production, with the decline of this sector in Hungary, car manufacturing rose to dominance from the 2010s. This is well illustrated by the fact that between 2010 and 2019, Hungarian industrial output grew, on average, by 4.6 percent a year, with the automotive sector contributing 2.3 percentage points on average. This was propelled by significant investments by Mercedes and Audi in the early 2010s, boosting the Hungarian export market share, on average, by 3.2 percent annually between 2013 and 2015**.** Meanwhile, German industrial output continued to grow, albeit at a lower rate than before, until 2017**. With stronger growth dynamics in Hungary, the additional growth of Hungarian industry averaged 1.5 percentage points a year between 2013 and 2017.**

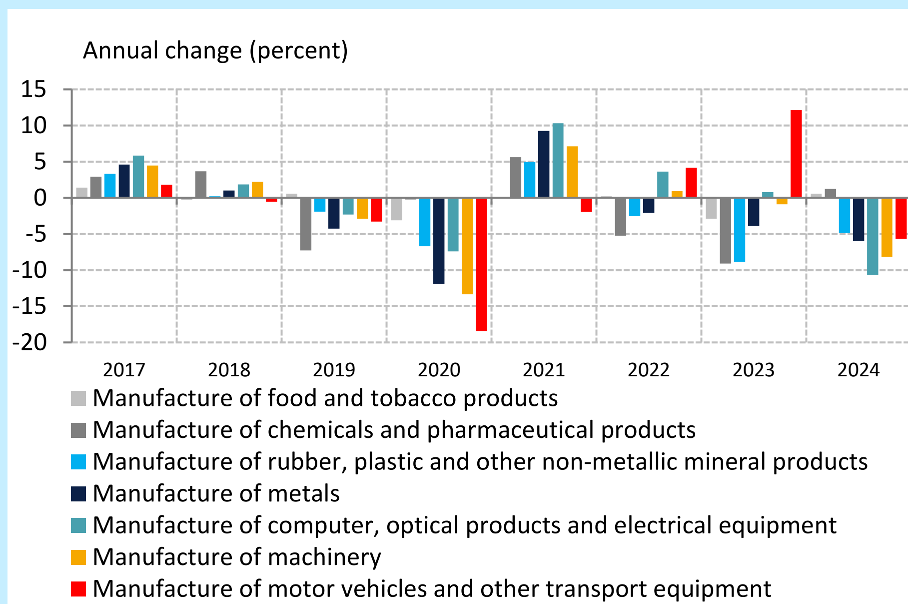
Chart 3-15: Evolution of industrial output levels in Hungary and Germany



Note: Based on seasonally and calendar adjusted data. Growth figures for 2024 based on data for the first ten months.
Source: Eurostat

Structural issues in German industry became increasingly pronounced after 2018. In Germany, industrial output declined by an average of 1.5 percent annually between 2018 and 2022, while until the second half of 2022 Hungary recorded growth similar to that in the 2010s, resulting in an annual average additional domestic growth rate of 5.1 percentage points over this period. Looking at individual sectors, it is clear that the decline in output was widespread across German industry (Chart 3-16). The difference between the two countries is striking in the case of the automotive industry, a key sector for Hungary: while in Germany, output in this sector decreased, on average, by 4.0 percent between 2018 and 2022, it increased, on average, by 2.0 percent during the same period in Hungary. The underperformance of the German automotive industry was mainly due to the rise of electromobility and the slow pace of the green transition. Despite the difficulties in the German automotive industry, Hungarian car manufacturing, which depends mainly on the performance of German factories, showed no signs of slowing down until 2023. The reason is that, while German plants were operating at increasingly lower utilisation rates, output in Hungarian factories did not decline significantly, other than due to the shock caused by Covid-19. This is apparent in Audi's output figures: in 2015, 13.6 percent of their cars manufactured in Europe were made in Győr (159,842 units), but this share rose to 18.1 percent (176,493 units) in 2023. Consequently, recent structural difficulties affected Hungarian output to a lesser extent. The expansion of the Hungarian industry was also promoted by investments in battery manufacturing, mainly related to Korean companies (Samsung, SK).

Chart 3-16: Year-on-year change in major German industrial subsectors



Note: Based on seasonally and calendar adjusted data. For 2024, based on data for the first nine months. The sectors shown in the chart account for nearly two-thirds of German industrial output.
Source: Eurostat

From late 2022, the impact of the energy crisis and the lacklustre European economic situation reached Hungarian industry. From 2023 to September 2024, domestic industrial output fell by 4.2 percent on average, exceeding the 3.5-percent decline seen in German industry over the same period. Weak performance in both economies was initially attributed to a fall in energy-intensive sectors. From late 2023, shrinking demand for electric cars and the weak European economic situation led to a significant downturn in the car manufacturing and electrical equipment sectors, including battery production.

As the European economy recovers, Hungarian and German industries may grow again. As in previous periods of industrial upswing, Hungarian output and industrial exports may experience a major boost from the inflows of working capital in recent years: investments in the automotive (BMW, BYD) and battery industries (CATL) could start production from 2025. At the same time, the German economy and industrial production chain face significant challenges. The difficulties experienced by the German automotive industry are exacerbated by new emissions limits coming into effect next year, forcing manufacturers to increase the share of pure electric vehicles in new sales, potentially resulting in the growth of the share of electric vehicles in European sales. However, it is not clear whether the safeguard duties imposed will be able to stop the rise of Chinese producers and whether the expected response from China will cause disruptions in battery supply

chains, where the exposure of European producers remains significant. An additional risk is posed by potential US import cuts, as the US is an even more important market for the European automotive industry than China: in terms of value, in 2023, 10.6 percent of the value of European road vehicle exports went to China, while 19.3 percent to the US. Moreover, it has not been possible for the decline of German industry to be offset by other sectors in the short term. Germany is lagging far behind in the field of information technologies (IT), with the European Commission's survey showing that, in terms of research and development (R&D) spending, 50.1 percent of the total R&D spending by the largest German companies in 2022 was related to the automotive industry, compared to only 8.5 percent for the IT sector. By contrast, this ratio was 54.6 percent for the IT sector in the United States and 31.4 percent in China.

3.3 Labour market

Employment in the national economy stabilized in October after a decline in September, but remains at a high level. The level of labour market activity has also moderated in recent months. The unemployment rate stood at 4.5 percent in October. The number of job vacancies in the private sector did not change significantly in the third quarter of 2024, indicating that the decline in labor demand has stopped. In the private sector, average gross earnings rose by 11.9 percent in September compared to the same quarter of the previous year.

3.3.1 Employment and unemployment

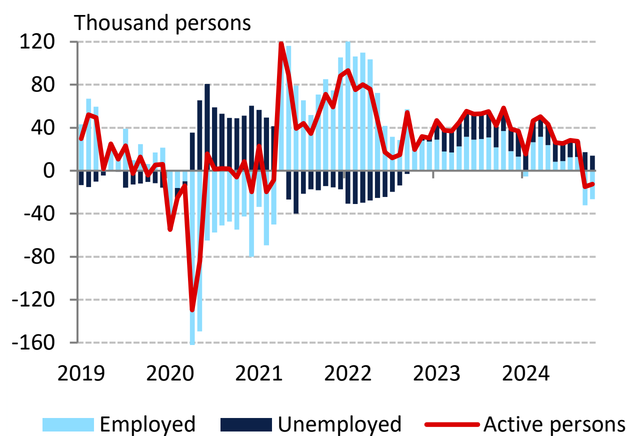
Employment in the national economy remains at a high level. In October 2024, the number of employed persons aged 15–74 was 4,699,000, representing a decline of 27,000 versus the same period of the previous year (Chart 3-17). In September, the HCSO updated the employment and unemployment statistics with the lower-than-expected 2022 Census data. As a result, the level of employment fell by 20,000 to 30,000 in the past period, while unemployment data did not change perceivably. Based on seasonally adjusted data, the number of employed persons increased by 2,000 in October compared to the previous month.

Employment is developing differently in individual sectors. Based on detailed sectoral data available at quarterly frequency, employment in market services increased in the third quarter compared to the same period of the previous year, with manufacturing recording a moderate decline, and construction and agriculture seeing a more significant year-on-year decline. Within the sector of market services there are diverging sectoral trends. While employment decreased in trade, transportation and storage, it rose in administrative and support service activities, financial and insurance, information and communication, as well as professional, scientific and technical activities (Chart 3-18). Within the public sector, employment stagnated in education, declined in public administration, and increased in health services on an annual basis. The number of job vacancies has not changed significantly in the third quarter. In 2024 Q3, the total number of full-time equivalent (FTE) jobs was 0.8 percent below the level recorded in the same prior-year period.

Unadjusted data indicate that the unemployment rate was 4.5 percent in October 2024. Calculated with the HCSO methodology using a three-month moving average, the unemployment rate stood at a similar level – around 4.6 percent – on average between August and October 2024. The domestic unemployment rate remains low by international standards.

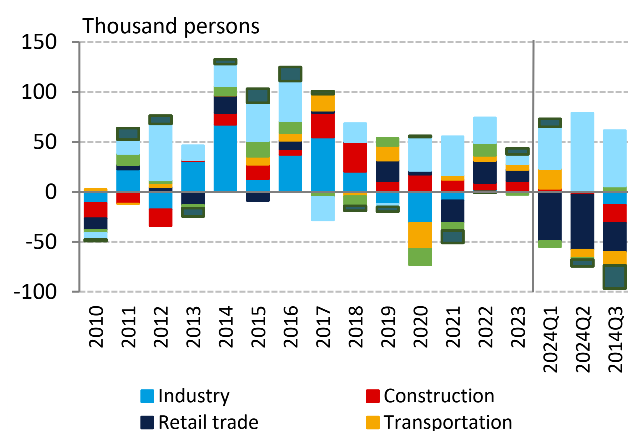
Labour market activity has declined in recent months. Based on seasonally adjusted data, the number of persons in the labour force has been on a decline since March, which

Chart 3-17: Decomposition of annual changes in the labour force participation



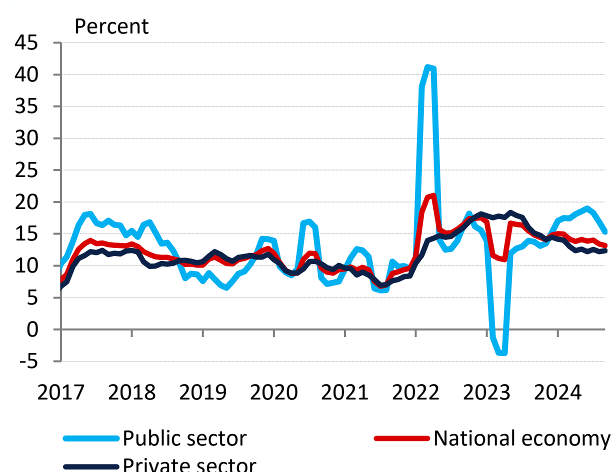
Source: HCSO

Chart 3-18: Decomposition of annual changes in private sector employment



Note: * Other industry and service sector branches.
Source: HCSO

Chart 3-19: Annual change in gross average wages in the national economy



Note: Quarterly moving averages.
Source: HCSO

has been linked to an erosion in employment in recent months. Since September, we have observed a considerable year-on-year decline in the level of the labour force, which was 13,000 persons lower in October compared to the same period last year.

3.3.2 Wages

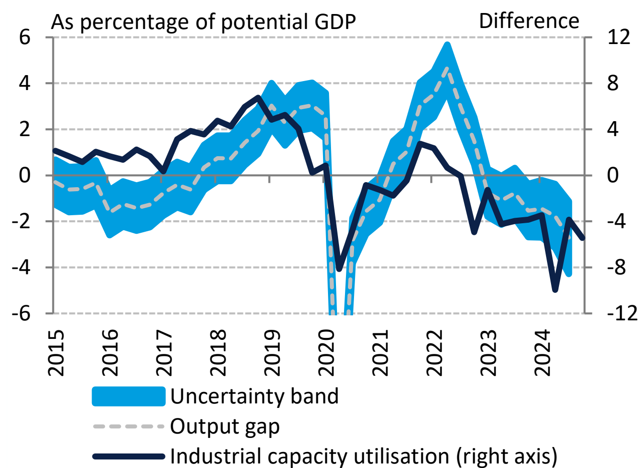
Wage trends remain strong, but wage growth is decelerating. In September 2024, average gross earnings in the private sector increased by 11.9 percent and regular earnings rose by 12.2 percent on an annual basis, while bonus payments fell short of the levels seen in previous years. The annual growth rate of gross and regular earnings also decelerated somewhat. Annual wage growth in the public sector decreased sharply compared to the first half of the year, standing at 14.1 percent in September. For the national economy as a whole, gross average earnings increased by 12.5 percent (Chart 3-19).

Among the countries in the region, nominal wage growth in Hungary was the second highest after Romania in September 2024. Earnings grew by 16.4 percent in Romania, 10.3 percent in Poland and 4.7 percent in Slovakia on an annual basis. For Czechia, wage data are only available at quarterly frequency, with average wages rising by 4.1 percent in the second quarter. Real wages in Romania and Hungary rose at the fastest pace in the region in September. Since the beginning of this year, real wages have increased in all countries of the region.

3.4 The cyclical position of the economy

In 2024 Q3, the Hungarian economy declined by 0.8 percent in year-on-year terms, and a 0.7-percent on a quarterly basis. The subdued economic output in the past quarter was largely due to negative contributions from industry, construction and agriculture. We estimate that GDP was still below its potential level in 2024 Q3. The cyclical position of the economy has been negative since the beginning of 2023 and has thus had a disinflationary effect. The capacity utilisation of manufacturing companies is below the historical average, while production expectations for the coming months show improvement.

Chart 3-20: Uncertainty band of the output gap and the industrial capacity utilisation



Note: The estimation uncertainty band covers one standard deviation. Output gap excluding agriculture performance. In the case of industrial capacity utilisation, deviation from the historical average.
Source: ESI, HCSO, MNB estimation

The cyclical position of the economy is estimated to have been negative since the beginning of 2023 and has thus had a disinflationary effect. The output of the Hungarian economy contracted by 0.8 percent in 2024 Q3 compared to the same quarter of the previous year, and by 0.7 percent relative to the previous quarter. In line with the subdued economic performance, the output gap, excluding the performance of agriculture, remains in negative territory (Chart 3-20). The poor growth outlook in Europe and the intense geopolitical situation pose a risk to the external outlook. The external output gap – which has an effect on the Hungarian cyclical state – remains in a moderately negative territory as well.

According to questionnaire surveys, the capacity utilisation of manufacturing companies is below the historical average, but production expectations have improved. Capacity utilisation has deteriorated slightly quarter-on-quarter, but production expectations for the coming months have improved and are above the historical average.

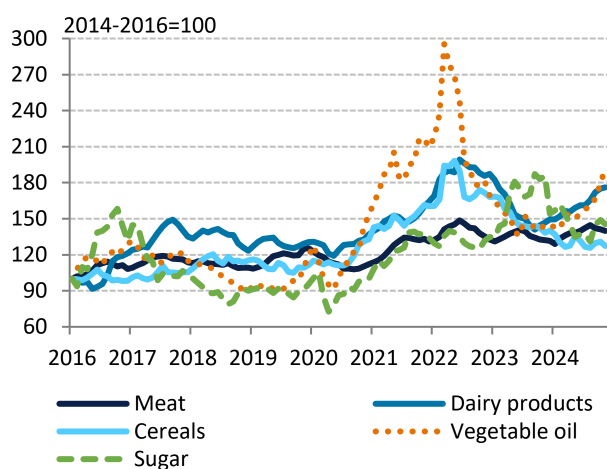
3.5 Costs and inflation

In November 2024, consumer prices rose by 3.7 percent in a year-on-year comparison. Both core inflation and core inflation excluding indirect tax effects fell to 4.4 percent. The annual rate of inflation rose by 0.5 percentage point compared to the previous month, which largely reflected an accelerating growth rate in fuel prices. Our indicators capturing more persistent inflation trends remained broadly unchanged. On a monthly basis, the price of the overall consumer basket and the price of the basket based on core inflation rose by 0.5 percent and 0.3 percent, respectively. The rate of price increases compared to the previous month was significantly higher than the historical average for inflation and moderately elevated for core inflation.

3.5.1 Producer prices

Global food prices rose by 0.5 percent in November compared to the previous month. In the autumn months, the rise in vegetable oil, sugar and dairy product prices was offset to a small degree by a month-on-month decline in meat prices. According to the FAO, food prices rose by 5.7 percent compared to November 2023, driven by a significant year-on-year increase in the price of vegetable oil and dairy products. Vegetable oil prices rose by 32.2 percent in year-on-year terms and by 7.5 percent on a monthly basis, primarily owing to lower-than-expected global production. Dairy prices rose by 20.1 percent year on year and by 0.6 percent compared to October. Grain prices fell by 8.0 percent in annual terms and by 2.7 percent on a monthly basis. Meat prices were 5.9 percent higher than in November last year and 0.8 percent lower than in October. World sugar prices dropped by 21.7 percent year on year and by 2.4 percent on a monthly basis (Chart 3-21).

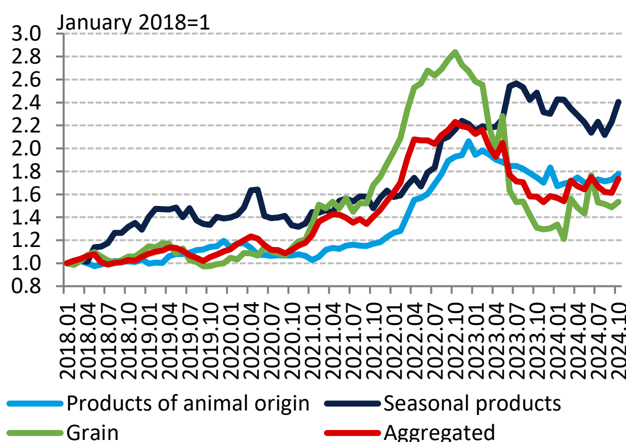
Chart 3-21: Development of world market prices of food



Source: FAO

In October, domestic agricultural producer prices increased by 7.6 percent in a month-on-month comparison. On an annual basis, prices rose by 9.9 percent, which marks the highest annual increase since March 2023. Among the component items, the producer price index for grains increased the most in annual terms, rising by 17.2 percent. The price level of animal products was 1.7 percent higher compared to October last year. Producer prices for seasonal products decreased by 3.2 percent over one year (Chart 3-22).

Chart 3-22: Development of agricultural prices



Note: Based on seasonally adjusted data

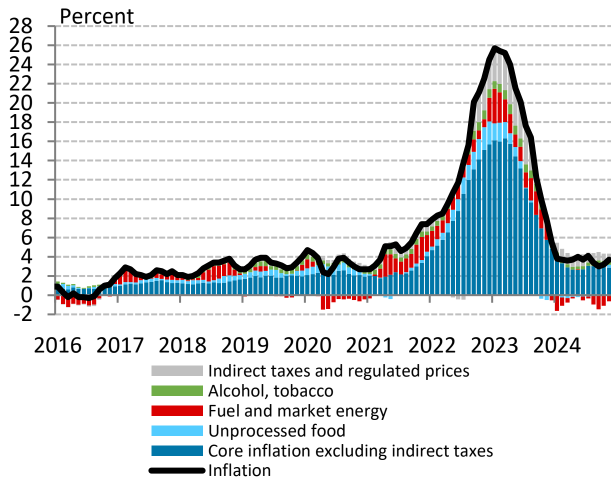
Source: HCSO

Producer prices for manufactured goods for domestic sale fell by 0.5 percent on an annual basis in October 2024. Domestic sales prices in the manufacturing sector increased by 1.2 percent compared to October last year. Producer prices were 2.5 percent higher in the food sector, while in the energy sector they were 4.0 percent lower than in the same period of the previous year.

3.5.2 Consumer prices

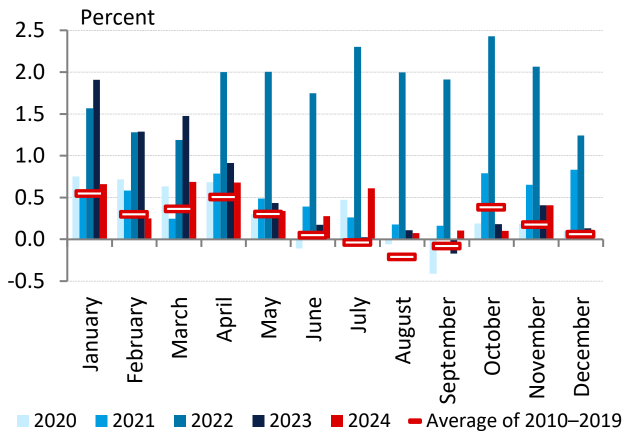
Consumer prices rose by 3.7 percent year on year in November. The consumer price index rose by 0.5 percentage point compared to the previous month. The

Chart 3-23: Decomposition of inflation



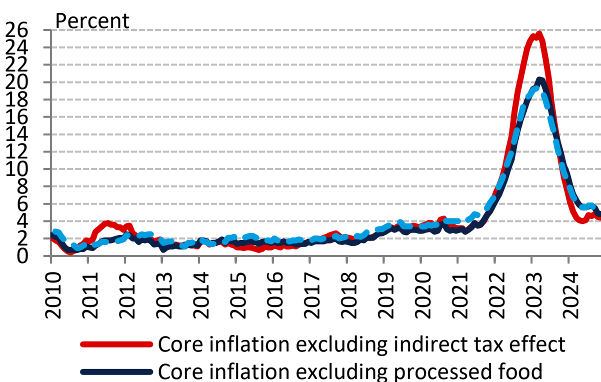
Source: MNB calculation

Chart 3-24: Monthly price changes of consumer prices excluding fuel and regulated prices



Note: Tax-adjusted, seasonally unadjusted monthly change
Source: MNB calculation based on HCSO data

Chart 3-25: Underlying inflation indicators



Note: Core inflation excluding processed foods with unchanged content is equivalent with the earlier demand sensitive inflation. The new name is justified by the fact that the previous name may be ambiguous in a period of significant cost shocks with general effects. Source: MNB calculation based on HCSO data

rise in inflation largely reflected an accelerating growth rate in fuel prices (Chart 3-23). On a monthly basis, the price of the overall consumer basket and the price of the basket calculated excluding fuel and regulated product prices rose by 0.5 percent and 0.4 percent, respectively (Chart 3-24). The price of the core inflation basket increased by 0.3 percent. The rate of price increases compared to the previous month was significantly higher than the historical average for inflation and moderately elevated for core inflation. Month-on-month core inflation excluding processed food prices, which better reflects the underlying trends, amounted to 0.2 percent.

Core inflation and core inflation excluding indirect tax effects both declined to 4.4 percent. Both indicators decreased by 0.1 percentage point, driven by the continued disinflation in market services prices. Indicators capturing more persistent inflation trends remained broadly unchanged in November (Chart 3-25). On a shorter basis (annualised 3-month-on-3-month), core inflation fell while inflation rose slightly.

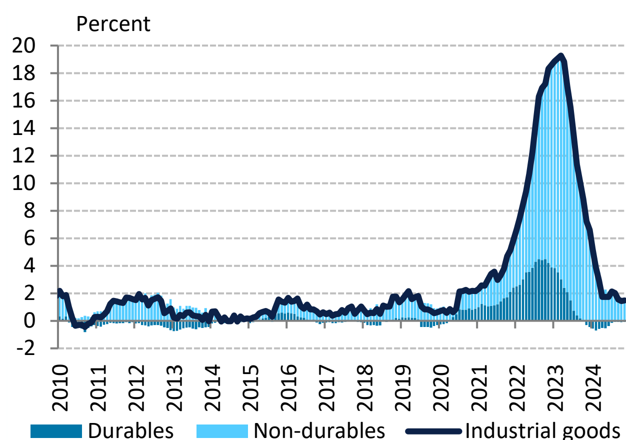
Annual inflation of tradables rose to 1.5 percent in November. On a monthly basis, the price of this product group increased by 0.1 percent (Chart 3-26 and Chart 3-27). Non-durable prices rose by 0.2 percent, while durable prices were down by 0.3 percent. The change in the forint exchange rate observed since September has not been reflected in the pricing of tradables.

The annual price index of market services declined to 8.2 percent. On a monthly basis, prices increased by 0.4 percent. The price rises were explained by the inflation of healthcare services prices (Chart 3-28).

Inflation for alcohol and tobacco products amounted to 4.0 percent. Compared to October, the price of this product group increased by 0.3 percent.

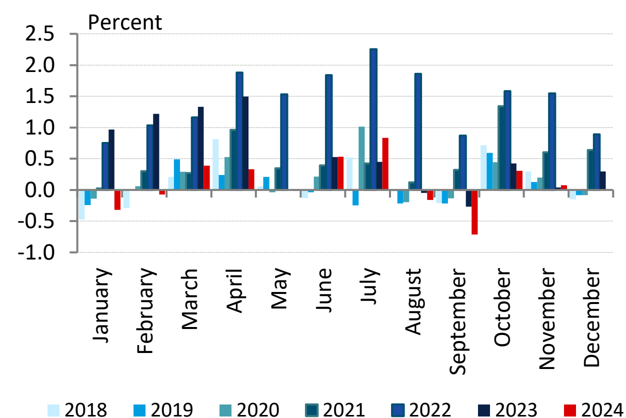
Food inflation according to the MNB's classification rose to 3.8 percent in November. Within this product group, unprocessed food and processed food prices rose by 6 percent and 2.7 percent, respectively, in annual terms. According to data released by the HSCO, food prices increased by 4.9 percent, which includes a rise of 7.9 percent in restaurant meal prices. Compared to October, prices of unprocessed food rose by 2.1 percent, primarily due to the increases in fresh vegetable and egg prices. Processed food prices were up 0.3 percent higher on a monthly basis, largely driven by the rises in the prices of milk and dairy products, as well as fruit juice.

Chart 3-26: Inflation of industrial goods



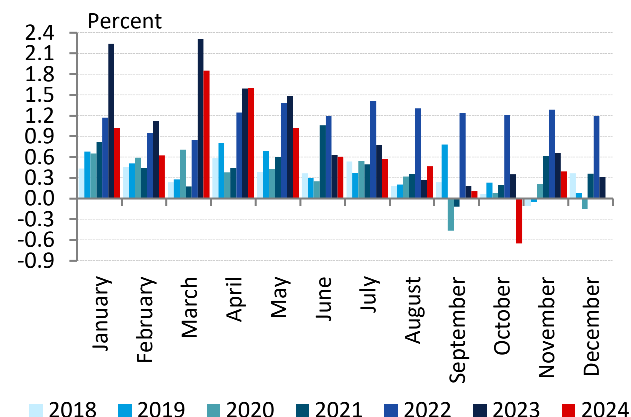
Note: Year-on-year change, excluding the effect of indirect taxes.
Source: MNB calculation based on HCSO data

Chart 3-27: Monthly price changes of traded goods



Note: Seasonally non-adjusted, tax adjusted monthly change.
Source: MNB calculation based on HCSO data

Chart 3-28: Monthly price change of market services



Note: Tax-adjusted, seasonally unadjusted monthly change.
Source: HCSO, MNB

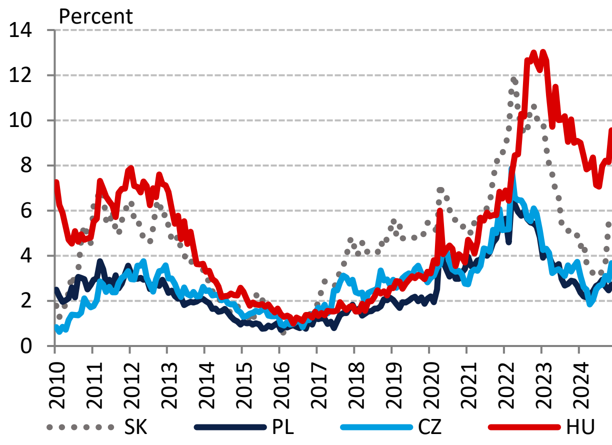
Fuel prices rose by 2.3 percent month-on-month, which may have been driven by an increase in margins. On an annual basis, prices increased by 0.7 percent.

The inflation rate in November was in line with the projection in the September Inflation Report, with core inflation coming in below the projection.

3.5.3 Inflation expectations

The downward trend in household inflation expectations has ended since August. Compared to 2024 Q3, inflation expectations increased in all countries of the region except Poland (Chart 3-29).

Chart 3-29: Inflation expectations in the region



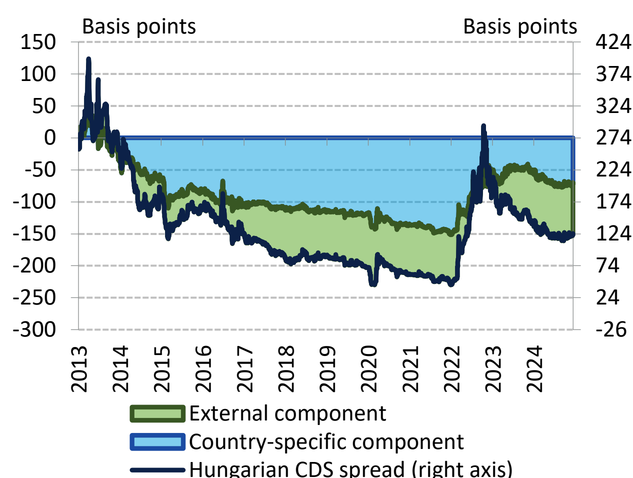
Source: MNB calculations based on European Commission data

4 Financial markets and interest rates

4.1 Domestic financial market developments

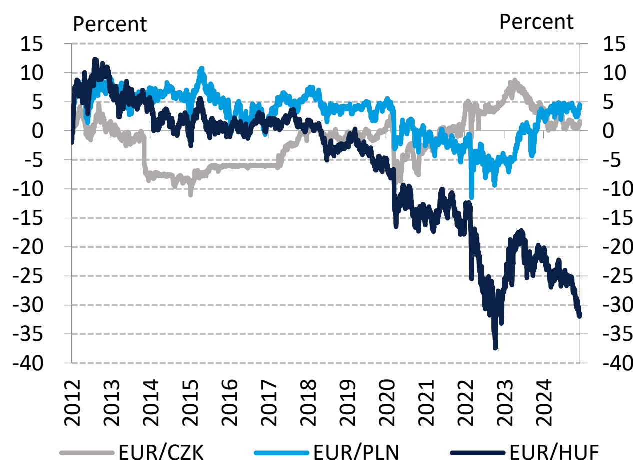
In the past quarter, global investor sentiment was volatile and deteriorating, overall, primarily due to the economic policy implications of the US presidential election, geopolitical risks linked to the hotspots in Ukraine and the Middle East, and expectations regarding the interest rate policies of major central banks. Market interest rate paths diverged between the US and Europe. Positive macroeconomic data from the United States shifted the interest rate path expected from the Fed upwards, while the ECB's interest rate path shifted downwards on the back of unfavourable incoming data. Decoupling from regional currencies, the forint weakened considerably in the past quarter. Government bond yields and interbank yields, as well, increased during the period.

Chart 4-1: Components of 5-year Hungarian CDS spread



Note: The decomposition method used can be found in the MNB Bulletin: Variance decomposition of sovereign CDS spreads, Kocsis – Nagy (2011).
Source: Bloomberg, MNB

Chart 4-2: Exchange rates in the region



Note: Changes compared to beginning of 2012. Positive values mean an appreciation of the currency.
Source: Bloomberg

4.1.1 Risk assessment of Hungary

Hungary's credit spread increased during the period. Exhibiting minor shifts, the spread was volatile in the past quarter, rising by 11 basis points, overall, to 125 basis points, with country-specific factors playing the larger role (Chart 4-1).

4.1.2 Foreign exchange market trends

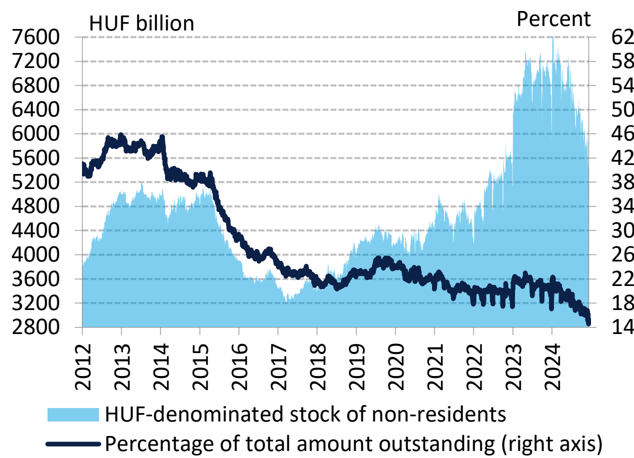
On the whole, the forint weakened against the euro by 3.7 percent during the period, driven by country-specific factors, besides the significant strengthening of the US dollar. Decoupling from regional currencies, the forint depreciated gradually, with minor interruptions only during the period (Chart 4-2). In the region, the Polish zloty appreciated by 0.2 percent, while the Czech koruna appreciated by 0.1 percent. The Romanian leu weakened by 0.1 percent. The forint depreciated by 10.5 percentage points against the US dollar, while the Romanian leu and the Czech koruna weakened by 6.4 percent and the Polish zloty by 6.3 percent.

4.1.3 Government securities market and changes in yields

Non-residents' holdings of government securities fell during the past quarter. Non-residents' holdings of HUF government securities decreased by HUF 785 billion to HUF 5,571 billion in the period. The share of the forint in government bonds also declined in the last quarter to around 15.3 percent (Chart 4-3).

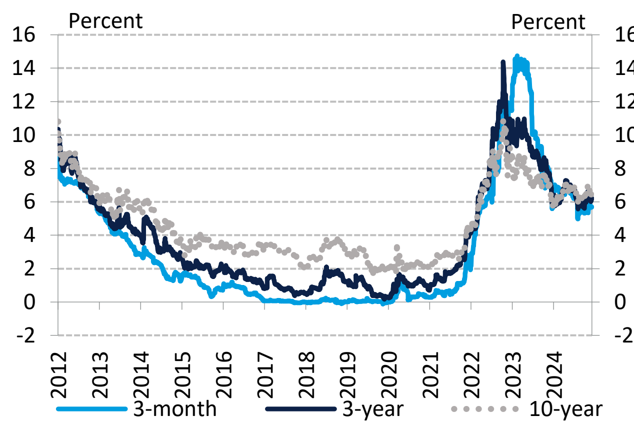
Demand at discount treasury bill auctions was mostly weak in the last quarter. By contrast, bids for government bonds nearly 1.5 times higher on average than the planned issuance were accepted at government bond auctions. Average discount Treasury bill and bond auction yields also rose in the last quarter. The average yields of the 3-month discount Treasury bill auction increased by 30 basis points, while that of the 10-year bond auction increased by 27 basis points.

Chart 4-3: HUF-denominated government securities held by non-residents



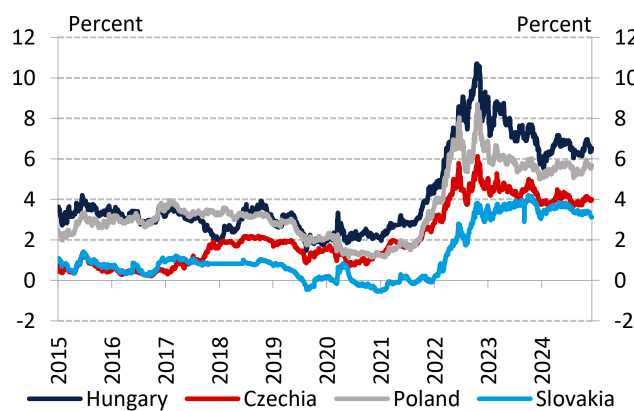
Note: The chart shows the stock of T-bills and T-bonds.
Source: MNB

Chart 4-4: Yields of benchmark government securities



Source: Government Debt Management Agency (ÁKK)

Chart 4-5: 10-year government benchmark yields in CEE countries



Source: Bloomberg

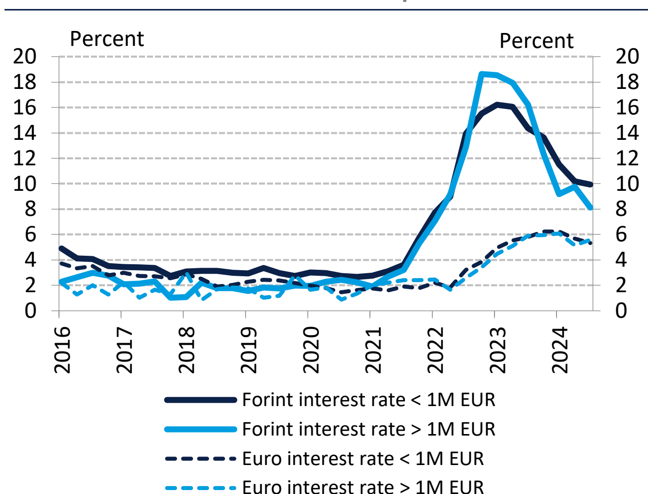
The government bond market yield curve as a whole shifted upwards in the period (Chart 4-4). Overall, the 5-year yield moved down 8 basis points, while the 3-year yield increased by 27 basis points and the 10-year yield increased by 9 basis points in the past quarter. Regarding interbank yields, the 3-month BUBOR rose by 5 basis points to 6.5 percent.

Long-term benchmark yields in the region typically increased in the past quarter. 10-year yields rose by 35 basis points in Romania, 38 basis points in Poland and 25 basis points in the Czech Republic, while they fell by 23 basis points in Slovakia (Chart 4-5).

4.2 Credit conditions of the financial intermediary system

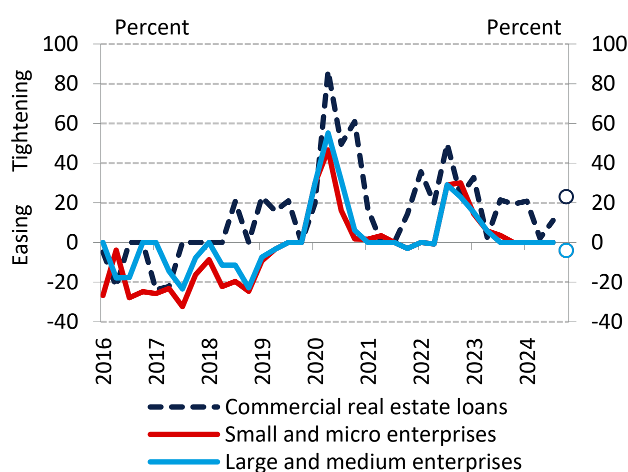
In 2024 Q3, banks left credit conditions for corporate loans broadly unchanged and, looking ahead to the next six months, they do not intend to change them significantly. In the third quarter of the year, banks reported lower demand for corporate HUF loans and short-term loans in the corporate segment, while demand for long-term loans remained at a low level. Looking ahead, banks expect demand for foreign currency loans to pick up. Banks' lending capacity remains high. Banks have not changed their standards for housing loans, while 40 percent of banks eased their conditions for consumer loans. Looking ahead to the next six months, credit conditions are expected to remain unchanged in both retail segments, and while the recovery in unsecured lending is not expected to continue, demand for housing loans may pick up again in the next six months.

Chart 4-6: Interest rates on new corporate loans



Note: Loans with variable interest rate or with up to 1-year initial rate fixation. From 2015, based on data net of money market loans exceeding EUR 1 million.
Source: MNB

Chart 4-7: Changes in credit conditions in corporate sub-segments



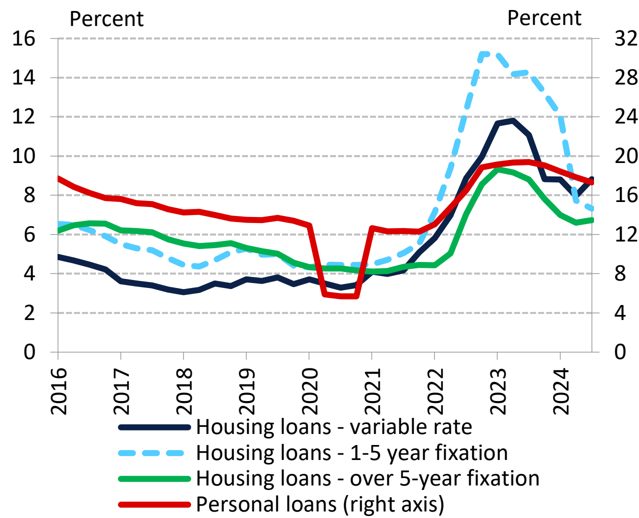
Note: Net percentage balance of respondents tightening/easing credit conditions weighted by market share. Forecast for 2024 Q4 and 2025 Q1. Source: MNB, based on banks' responses

4.2.1 Corporate credit conditions

HUF lending rates continued to decline in 2024 Q3, as borrowing costs eased. Net of money market transactions, the average interest rate on newly contracted, mostly market-based corporate HUF loans with variable interest rates within a 12-month period decreased by 0.2 percentage point for low-amount loans and 1.6 percentage points for large-amount loans relative to the previous quarter. The average interest rate on contracted corporate HUF loans fell further in parallel with the decline in borrowing costs and stood at 8.5 percent overall at end-September (Chart 4-6). The interest rate on low-amount EUR loans fell by 34 basis points and that on large-amount EUR loans increased by 43 basis points in the third quarter of the year. The average financing cost of EUR-denominated corporate loans was 5.6 percent at end-September.

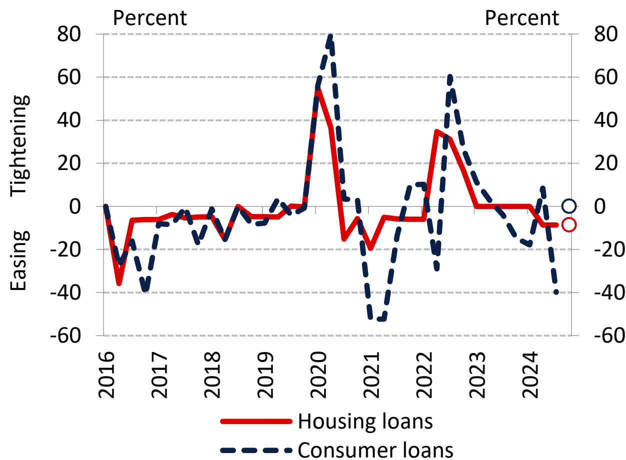
In 2024 Q3, banks left corporate lending conditions unchanged overall and looking ahead they do not intend to broadly change conditions in the next six months. Overall, one tenth of responding banks tightened conditions for commercial real estate loans and 41 percent for loans financing office buildings in consideration of rising vacancy rates and waning risk tolerance. Banks' lending capacity remains high. Banks do not plan to make significant changes to corporate lending standards in any size category in the next six months. At the same time, banks remain more cautious in financing commercial real estates, with 23 percent and 53 percent of lenders tightening standards for logistics centres and office buildings, respectively (Chart 4-7). In terms of loan demand, one fifth of banks reported a decline in corporate loan demand in 2024 Q3, which primarily affected HUF loans and short-term loans. The former may also have reflected the effect of HUF-denominated loans with favourable interest rates that ceased to exist with the expiration of subsidised lending programmes. Similar to the second quarter, demand for long-term corporate loans remained low. Looking ahead to the next six months, only 6 percent of banks expect

Chart 4-8: Annual percentage rate of charge on new household loans



Note: Quarterly average of lending rates on newly disbursed loans. State-subsidised loans fall into the 1-5 year fixation category before January 2024, and into the variable rate category from January 2024. For these loans, the interest rate in the figure also includes the subsidy paid by the state.
Source: MNB

Chart 4-9: Changes in credit conditions in the household sector



Note: Net percentage balance of respondents tightening/easing credit conditions weighted by market share. Forecast for 2024 Q4 and 2025 Q1.
Source: MNB, based on banks' responses

corporate loan demand to pick up overall, but one third of the institutions expect an upturn in foreign currency loans.

4.2.2 Household credit conditions

The average interest rate on long-term fixed-rate housing loans did not change significantly during the quarter. The average APR of housing loan contracts signed in 2024 Q3 for loans with fixed interest rates for a term of over 5 years – which cover the majority of market-based loans – amounted to 6.7 percent in September 2024 following a 14-basis point increase from 6.6 percent in June 2024 (Chart 4-8). The application of the voluntary APR ceiling by the majority of banks between 9 October 2023 and 30 June 2024 reduced interest rates on new housing loans by 1.2 percentage points on average; at the same time, since the elimination of the ceiling in June, interest rates on housing loans have increased only slightly.[1] In 2024 Q3, the volume of Certified Consumer-friendly Housing Loans (CCHL) with an interest rate period of at least 5 years accounted for 24 percent of newly disbursed housing loans, while the share of loans with a fixed-term interest-rate period of at least 10 years was 98 percent.[2] The average smoothed APR for personal loans decreased by 52 basis points to 17.3 percent at the end of the period under review.

Regarding housing loans, banks did not change lending conditions in general, while price conditions are expected to be eased in line with the recovery in the housing market. Based on responses to the Lending Survey, in 2024 Q3 banks left the lending conditions of housing loans unchanged overall; nevertheless, following the elimination of the voluntary APR ceiling, 51 and 56 percent of the institutions raised their interest rate spreads on housing loans and the interest rate premium on riskier loans, respectively. Driven by market share objectives, 40 percent of banks eased conditions on consumer loans (Chart 4-9). Looking ahead to 2024 Q4 and 2025 Q1, responding banks plan to ease price conditions for housing loans in line with the recovery in the housing market; however, they do not envisage any significant changes to consumer loan conditions. In the third quarter, 22 percent of banks perceived a decline in demand for housing loans, but looking ahead to 2024 Q4 and 2025 Q1 a net 16 percent of banks expect demand to pick up again. A net 80 percent of the institutions surveyed observed a pick-up in demand for consumer loans, but looking ahead, they expect demand for loans to remain unchanged.

[1] For a more detailed analysis of the effects of the APR ceiling and the estimation methodology, see Box 3 in the May 2024 Financial Stability Report.

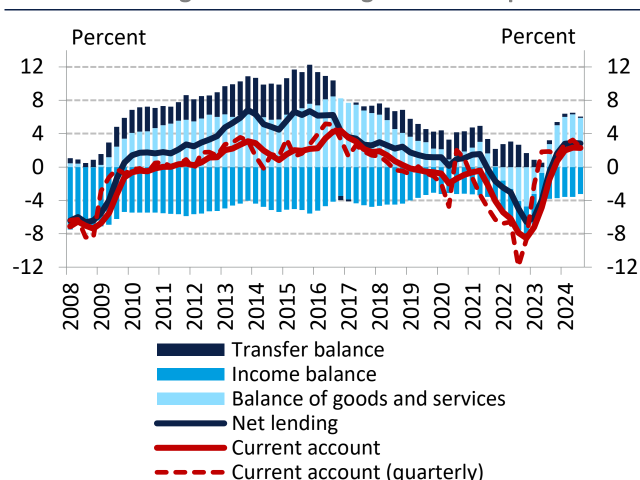
[2] The calculation also takes into account HPS Plus loans which, in terms of methodology, are considered variable-rate loans according to the legal requirements, whereas in terms of their client interest rate they should be considered fixed-rate loans, as they cannot exceed 3 percent.

5 Balance position of the economy

5.1 External balance and financing

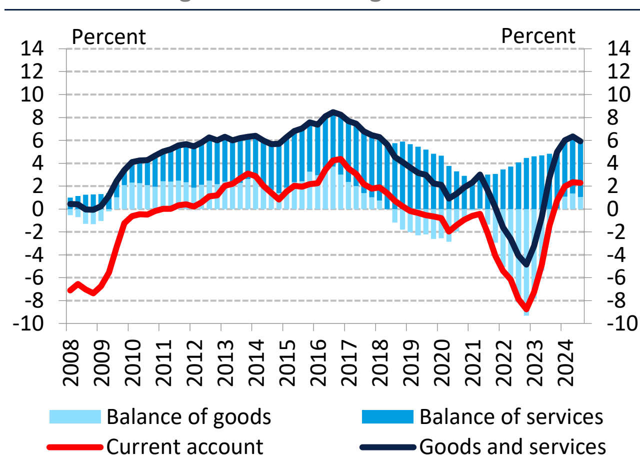
According to preliminary monthly data, the current account still showed a significant surplus of 2.3 percent of GDP in 2024 Q3. The external balance remained stable as a result of an improvement in the income balance and a decline in the trade balance. In terms of financing, Hungary's net debt liabilities decreased during the quarter in parallel with significant FDI inflows. In the second quarter, gross external debt was close to 64 percent of GDP, with the net ratio at around 11 percent.

Chart 5-1: Changes in net lending and its components



Note: Cumulated four-quarter values, as a percentage of GDP.
Source: MNB

Chart 5-2: Changes in balance of goods and services



Note: Cumulated four-quarter values, as a percentage of GDP.
Source: MNB

5.1.1 Developments in Hungary's external balance position

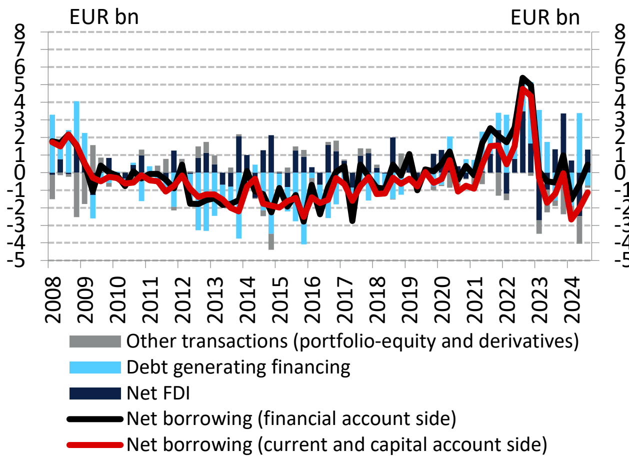
In 2024 Q3, the external balance indicators continue to point to significant net lending (Chart 5-1). Based on preliminary monthly data, as in the previous quarter, the current account surplus in the third quarter was 2.3 percent of GDP for the four quarters. The stable surplus resulted from the fact that the improvement in the income deficit was offset by the decline in the trade surplus. As in the second quarter, the transfer balance remained at 0.2 percent of GDP, well below the typical levels observed previously. Another contributor was the significant expenditure arising in the quarter as a result of the fine imposed by the European Court of Justice for breaching EU immigration policy.

The balance of services continues to play a key role in current account developments, while risks surrounding the goods balance are less pronounced (Chart 5-2). After the financial crisis, the balance of services was a major contributor to favourable changes in the external balance. As with exports, the pandemic temporarily restrained trade in services, but the surplus in services embarked on a growth path again from 2021, and in 2022 it considerably dampened the negative impact of the soaring energy prices on the external balance. In addition, in recent quarters the negative effect of declining exports on the external balance has been also offset by their high import content. In addition to subdued exports, which also reflected the fall in industrial production, the decline in the energy balance (albeit now at a slower pace) and low investment activity both contributed to a fall in imports, which was only partly offset by the mounting demand for imports triggered by rising consumption. At the same time, the balance of services surplus as a share of GDP remained stable at almost 5 percent, contributing significantly to the current account surplus.

5.1.2 Developments in financing

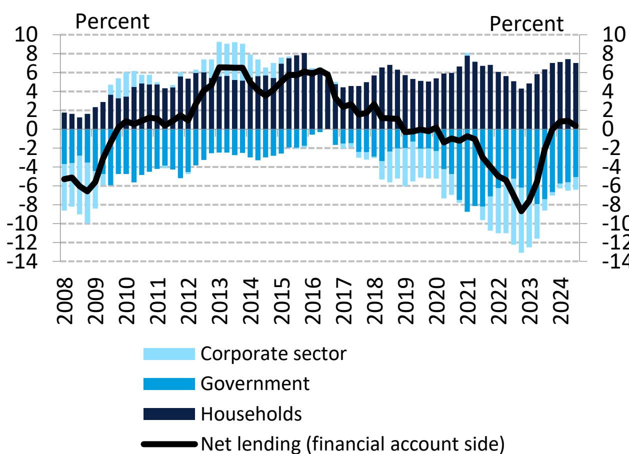
In 2024 Q3, FDI inflows were significant, while debt liabilities declined (Chart 5-3). Following the decline observed in 2024 Q2, which was related to one-off items,

Chart 5-3: Structure of net lending



Note: The net lending from the financial account side corresponds to the sum of current account, capital account and the BOP balance of statistical errors and omissions. From an economic point of view, fundamental developments in the dynamics of debt ratios are not affected by the switch between gold bullion and unallocated gold accounts and so this technical effect is excluded from time series.
Source: MNB

Chart 5-4: Decomposition of net lending by sectors



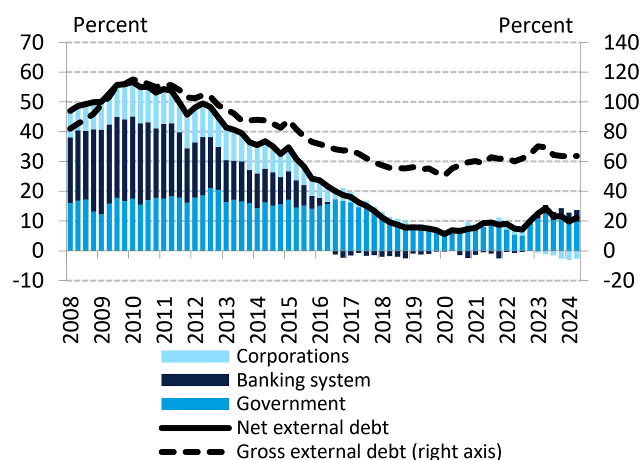
Note: Four-quarter cumulation, as a percentage of GDP.
Source: MNB

net FDI inflows rose sharply in Q3, primarily due to reinvestment by foreign companies and slightly curbed by the dividend payments of foreign companies. The quarter saw resident investors purchase a significant amount of foreign investment units and stocks, while non-residents also purchased Hungarian stocks at a similar rate. In parallel with FDI inflows, net external debt decreased. The banking sector contributed to the decline in net external debt by reducing its long-term debt and the portfolio of short-term and commercial loans extended to the corporate sector, while in the case of the consolidated general government the MNB's discount bond issuance had the opposite effect.

In 2024 Q3, the net borrowing of the government was offset by net financial savings in the private sector (Chart 5-4). The net borrowing of the general government continued to ease, thanks to substantially lower public investment and higher tax revenues from labour. In addition, moderating energy expenses and the deficit-reducing measures announced in early July also supported the improvement in net borrowing. Net financial savings in the private sector fell slightly, but remain high. Household net savings dropped to 7 percent of GDP, reflecting the unwinding of precautionary motives in the household sector. Net borrowing by companies started to rise again, reflecting the decline in previously high profitability levels.

At the end of June 2024, after a moderate increase, the economy's net external debt stood at 11.1 percent of GDP (Chart 5-5). The increase in the indicator was linked to the upward effect of transactions in the second quarter. The main contributors to the increase in net external debt were the banking sector and the general government. At the end of the quarter, Hungary's gross external debt stood at 63.7 percent of GDP.

Chart 5-5: Development of net external debt by sectors



Note: From an economic point of view, fundamental developments in the dynamics of debt ratios are not affected by the switch between gold bullion and unallocated gold accounts and so this technical effect, as well as intercompany loans, are excluded from time series. As a percentage of GDP.
Source: MNB

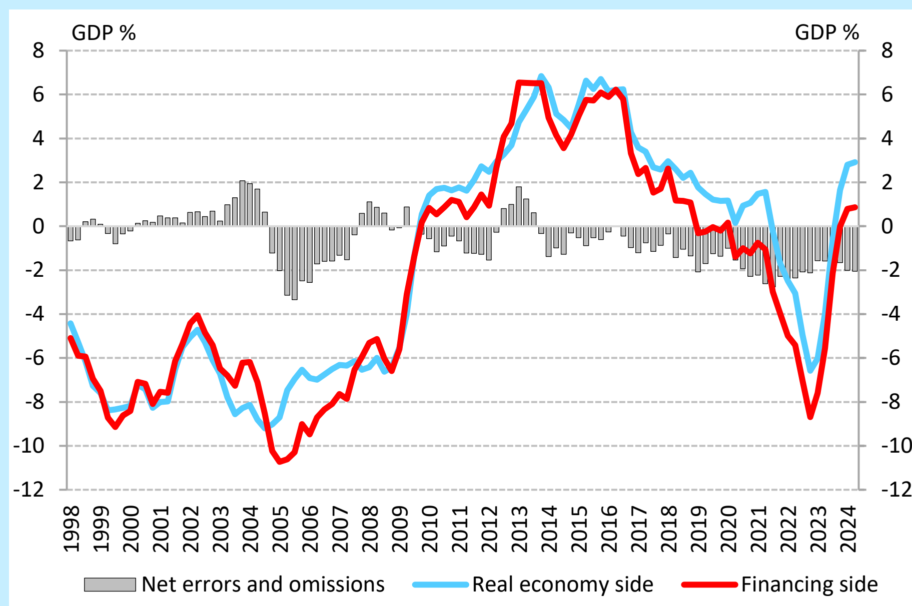
Box 5-1: Evolution of net errors and omissions in the current account

The net lending or net borrowing of a country can be calculated from the financing side, which indicates the real economy flows reflecting external trade and income trends and the underlying financial flows. The statistics calculated from both sides help to make the final result even more robust and substantiated. The reason for this theoretical identity, in simple terms, is that a country should finance from abroad whatever it acquires from abroad, and what it sells abroad generates the same amount of net foreign investment. In practice, however, the external balance indicators calculated from both sides are consistently different due to the different data sources used to calculate them, as well as incomplete or sometimes different observations over time, and sometimes errors on the part of data providers. This discrepancy is reflected as a statistical error, i.e. the net errors and omissions (NEO) item in the balance of payments statistics and the integrated presentation of national accounts. The reason for the use of different data sources is that the real economy and the financing processes are partly channelled through other economic agents (e.g. financial intermediaries) in the economy, and therefore, net lending and net borrowing materialise at other economic agents and sectors of the real economy or financing, and are evened out at the level of the national economy as a whole. Therefore, fundamentally, NEO does not signal that transactions are not observed; it signals that they are only visible in either one of the two views, or that it is not possible to measure them in a unified way.

The ratio of NEO to GDP increased following the EU accession, which entailed the easing of foreign trade and foreign exchange barriers. The BOP balance of net errors and omissions – as a statistical discrepancy that can be extracted from statistical releases – is an indicator of balance of payments statistics and the national accounts statistic based thereon. The more controlled foreign trade and the tighter foreign exchange management, the lower the discrepancy, as more complete administrative data are available. By contrast, more liberal foreign trade and full currency convertibility will significantly fragment data sources and hinder the complete collection of data. Accordingly, the statistical error (Chart 5-6) has increased and become unidirectional since Hungary's EU accession in 2004, in contrast to its small volume and multidirectional nature in the pre-accession period. The abolition of intra-EU customs borders has made it more difficult to measure external trade in goods and services, especially imports and hence, net lending in the real economy has been consistently more favourable

since 2004 than the balance calculated from the financing side. Between 2008 and 2019, the average statistical error was 0.6 percent of GDP. The level of errors and omissions also increased from 2020, with the statistical error rising to around 2 percent of GDP.

Chart 5-6: Four-quarter ratio of net errors and omissions to GDP

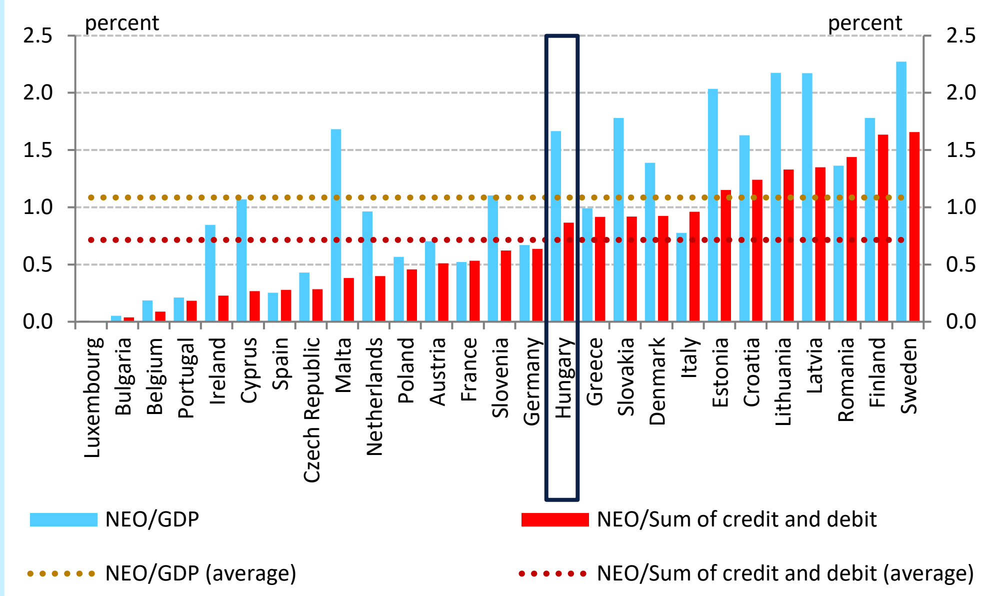


Source: MNB

The pandemic and the energy price surge pose a number of new challenges for the accurate monitoring of balance of payments items, which can only be captured by statistical offices with a lag. In addition to the volatility of exchange rates, product prices and owner's incomes, the propagation of e-commerce and private imports and the easier availability of external assets contributed to the increase in the statistical error. On the one hand, as the Covid-19 pandemic materialised, changes in consumption patterns accelerated with a surge in the purchase of goods and services through electronic channels, and subsequently, a surge in private physical imports by households. On the other hand, the jump in energy prices multiplied the size of derivative transactions in certain energy commodities compared to previous periods, but this has not always been tracked correctly by data suppliers. Finally, on the financing side, the growth in the private sector's external assets also required the inclusion of new data sources. Some of these phenomena have already been addressed by statistical offices (the size of the NEO has already declined significantly in recent quarters). However, the statistical monitoring of some phenomena is still in progress in cooperation between the HCSO and the MNB, and the estimates developed will be retrospectively incorporated into the balance of payments statistics in the March 2025 data revision, which is expected to reduce the statistical error.

The net errors and omissions compared to the current account credit and debit data slightly exceeded the EU average in 2023. While the domestic value of NEO was roughly in line with the typical level in EU countries on average in the years before the pandemic, it has slightly exceeded it in recent years. In terms of the ratios of absolute values to GDP in 2023, the Hungarian value is at the end of the top third of EU countries. By contrast, measuring the error against the size of the revenue and expenditure sides of the current account, the domestic value is roughly in the middle of the EU countries and only slightly exceeds the average of other countries (Chart 5-7).

Chart 5-7: Absolute size of NEO in relation to GDP and current account transactions in 2023



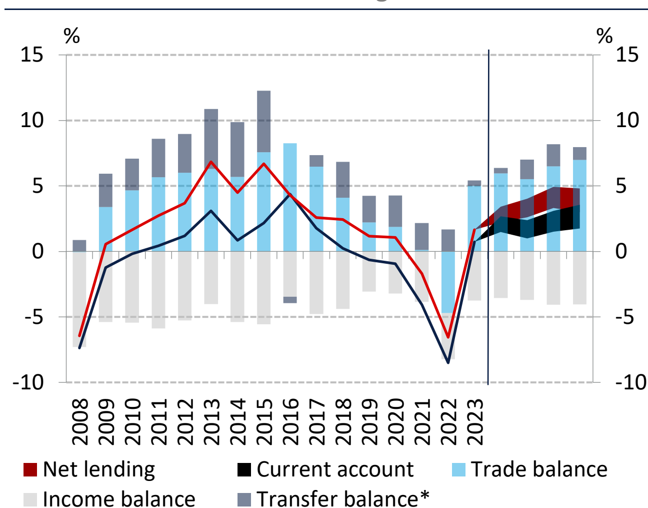
Source: MNB

5.2 Forecast for Hungary's net lending position

The current account surplus will decline somewhat next year before improving gradually until the end of the forecast horizon, driven mainly by developments in the trade balance. In addition to the better terms of trade, decreasing investment contributes to the expected improvement in the balance in 2024. Export growth is expected to pick up in 2025, as the utilisation of existing capacities improves and investment in progress is put into operation. It should be noted, however, that the investment turnaround expected for next year and rising consumption will entail a temporary decline in Hungary's external position. From 2026, domestic consumption will taper off while exports continue to expand strongly, which will lead to a gradual improvement in the external balance over the rest of the forecast horizon. Based on trends in sector financing, the improvement in the external balance primarily reflects the gradual shrinking of the general government deficit, while the financial savings of the private sector will be high.

The increase in external balance indicators is driven by an improvement in the foreign trade balance (Chart 5-6). The current account, which showed a modest surplus in 2023, will improve markedly this year, thanks to a continued rise in the foreign trade surplus. This is mainly due to the moderate further improvement in the terms of trade and the rising balance of goods due to lower investment. From 2025, with external demand normalising, Hungary's share of the export market is expected to grow, with better utilisation of existing capacities and ongoing investment being put into operation, which may be reflected in stronger exports and a further improvement in the external balance (more details on the temporary decline expected for 2025 are presented below). The deficit on the income balance will remain at high levels as a result of the prolonged effect of higher interest rates, while the extra profit tax will significantly reduce the profits generated by foreign companies in 2024 and 2025. Overall, the current account surplus will gradually expand over the forecast horizon, as will net lending in line with the utilisation of EU transfers.

Chart 5-8: Evolution of net lending



Note: As a percentage of GDP. * The sum of the balance of the current transfers and the capital account balance.
Source: MNB

The energy balance deficit will continue to shrink significantly in 2024 before a temporary deterioration in 2025, followed by an improvement from 2026. The combination of falling gas prices and subdued energy demand was reflected in the lower energy deficit in 2024 H1. The subdued investment activity may result in a high surplus on the balance of other goods this year. In 2025, imports will increase on the back of the rebound in consumption and investment and the increase in the deficit of the energy balance (primarily due to rising gas prices at the end of 2024), which points to a smaller surplus on the balance of goods. In parallel, amid the accelerating export growth resulting from the upturn in external demand, the surplus on the balance of other goods will rise significantly over the rest of the forecast horizon. The surplus on the balance of services will stabilise at above 5 percent of GDP in the coming years (Table 5-1).

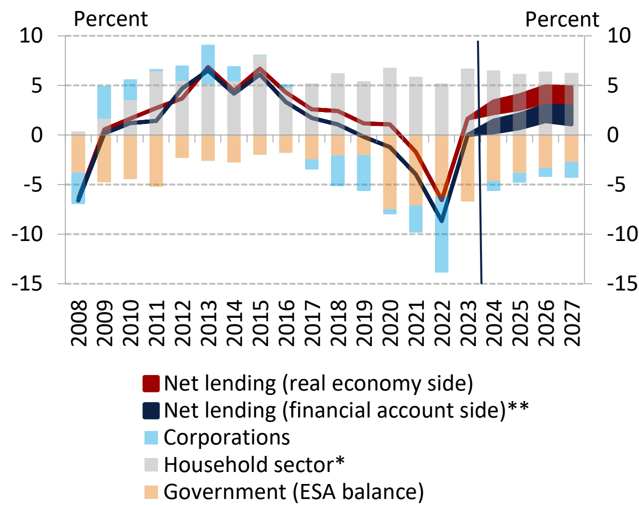
Table 5-1: Development of the trade balance as a percentage of GDP

	2023	2024	2025	2026	2027
Balance of goods	0.0	0.9	0.3	1.3	1.8
Balance of energy	-4.7	-3.4	-3.7	-3.4	-3.2
Balance of other good	4.7	4.3	4.0	4.7	5.0
Balance of services	5.0	5.1	5.2	5.2	5.2
Trade balance	**5.0**	**6.0**	**5.5**	**6.5**	**7.0**

Source: HCSO, MNB

Based on the sectoral financing approach, in parallel with the decline in the fiscal deficit, the private sector's net

Chart 5-9: Changes in the savings of sectors



Note: As a percentage of GDP. * Net financial saving of households does not contain the pension savings of those who return to the public pension system. The net savings in the financial accounts differ from the data in the chart. ** We expect that 'Net errors and omissions' (NEO) will return to the historical average.
Source: MNB

position remains high (Chart 5-9). The lower fiscal deficit is attributable to higher tax revenues in 2024, in conjunction with decelerating and then stagnating public investment growth and declining energy expenditures over the outlook horizon, coupled with decreasing interest expenses from 2025 onwards. As a result of slowly decreasing precautionary motives of households, net financial savings may decline slightly this and next year, then stabilizes at a high level with increasing incomes in the second half of the forecast horizon. The outlook for lower profits will increase the net borrowing of firms in 2024, but this will decline again due to the rebound in exports in response to the recovery of the external environment in the second half of the forecast horizon and the utilisation of EU transfers.

5.3 Fiscal developments

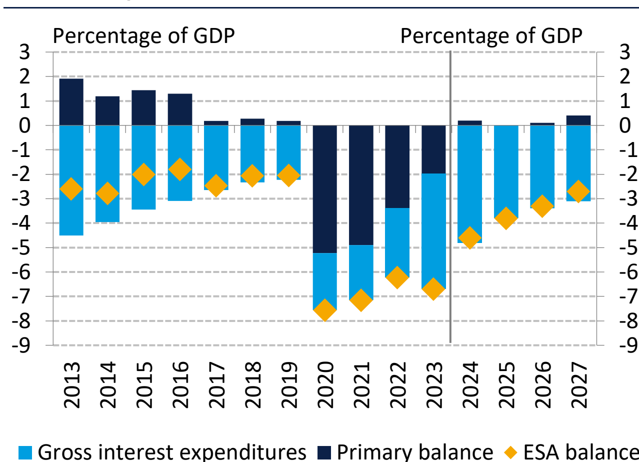
The budget deficit-to-GDP ratio is projected to be 4.4–4.8 percent in 2024 and 3.4–4.2 percent in 2025, depending on macroeconomic developments and fiscal expenditures. Thereafter, the deficit may be in the range of 2.8–3.8 percent in 2026 and 2.2–3.2 percent in 2027. The 2024 reduction in the budget deficit is supported by lower energy expenditure, owing to the stabilisation of energy prices, and decreasing public investment expenditure. The 2025 budget bill confirmed the deficit target of 3.7 percent of GDP, which will be supported primarily by a substantial reduction in public interest expenditures and revenue-increasing tax measures, while stimulus measures will increase the deficit. The reduction of public debt in 2024 is significantly constrained by the high cash deficit, the moderate economic expansion and the revaluation of foreign currency debt; however, we expect the debt ratio to fall below 70 percent of GDP by the end of the forecast horizon as the deficit gradually declines.

Table 5-2: General government balance indicators

	2024	2025	2026	2027
ESA balance	(-4.8) – (-4.4)	(-4.2) – (-3.4)	(-3.8) – (-2.8)	(-3.2) – (-2.2)
Primary ESA balance (point estimate)	0.2	0.0	0.1	0.4
Gross interest expenditures	4.8	3.8	3.4	3.1

Note: As a percent of GDP. The time series of the primary ESA balance (point estimate) are consistent with the midpoint of the ESA balance forecast bands.
Source: HCSO, MNB

Chart 5-10: Changes in the fiscal balance and government interest expenditures



Note: The time series of the ESA balance and the primary ESA balance after 2023 are point estimates, which are consistent with the midpoint of the ESA balance forecast bands.
Source: HCSO, MNB

5.3.1 Main balance indicators

According to our forecast, the government sector's accrual-based deficit-to-GDP ratio may amount to 4.4-4.8 percent in 2024 (Table 5-2). Our forecast range suggests that the achievement of the 4.5-percent deficit target may be supported by lower energy prices and reduced public investment spending, but will also be hampered by lower-than-planned tax revenues. Achieving the deficit target requires maintaining control over expenditures at the end of the year, in addition to the measures already announced to offset the high government interest expenditures and tax revenues falling significantly short of the appropriation.

According to our forecast, the budget deficit target of 3.7 percent set in the Budget Act for 2025 is achievable, supported by the announced revenue-increasing measures, while the stimulus programmes will increase the deficit.

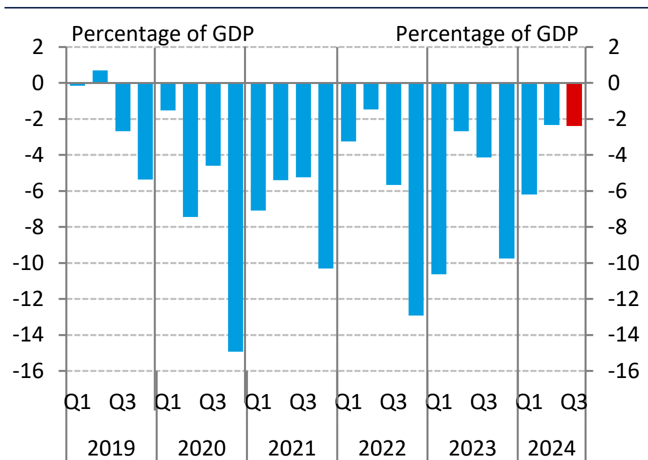
Looking ahead to the remaining years of the forecast horizon, the deficit may be in the range of 2.8–3.8 percent in 2026 and may drop further by 2027 (Chart 5-10). The primary balance is close to equilibrium levels over the forecast horizon; consequently, we expect the overall deficit to decline gradually, in parallel with gross government interest expenses.

5.3.2 Budget balance in 2024

We forecast the budget deficit to amount to 4.4-4.8 percent of GDP in 2024, depending on tax revenue developments and year-end expenditures. Based on the general government data from the preliminary financial accounts released by the MNB, the accrual-based budget deficit for 2024 Q3 amounted to 2.4 percent of quarterly GDP (Chart 5-11). The budget's cash flow deficit stood at HUF 3,284 billion at the end of November, accounting for almost 69 percent of the October EDP report's cash flow deficit target of HUF 4,790 billion.

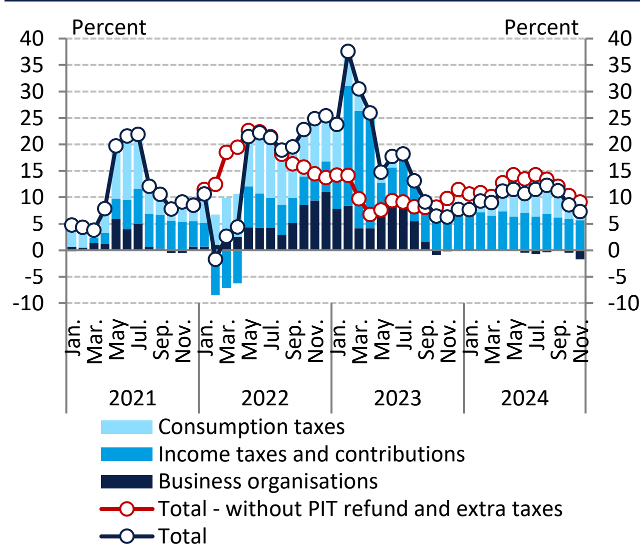
The primary balance is expected to be near equilibrium levels again in 2024, in contrast to the large deficits seen in

Chart 5-11: Accrual balance of the general government sector



Note: The data show the net lending capacity of general government as reported in the preliminary financial accounts published by the MNB.
Source: MNB

Chart 5-12: Evolution of tax and contribution revenues in 2021–2024, year-on-year, 3-month moving average



Source: HST, MNB

the past four years. However, the interest expenditure-increasing effect of the high inflation in the past two years is expected to be the highest this year, pushing gross accrual-based government interest expenditures up to 4.8 percent of GDP in 2024. As inflation declines, interest expenditures will gradually fall in the coming years, leading to a decline in budget deficit, provided that the primary balance is in equilibrium.

Revenues in 2024 may be significantly below the figures foreseen in the Budget Act, mainly due to a shortfall in value-added tax revenues. By the end of November, the annual growth in the tax and contribution revenues of the general government still falls short of the summer values (Chart 5-12).

Public investment in 2024 is expected to fall from the higher levels observed in previous years, reflecting subdued investment spending and the slow absorption of EU funds.

5.3.3 Budget balance in 2025

Our forecast for the accrual-based deficit-to-GDP ratio is 3.4–4.2 percent in 2025; therefore, the deficit target is achievable depending on macroeconomic conditions and fiscal expenditures. The 2025 budget bill sets the accrual deficit-to-GDP ratio of the general government at 3.7 percent of GDP for 2025, representing a decline of 0.8 percentage point relative to this year's target of 4.5 percent. The decline in the deficit is strongly supported by a decline in interest expenditures, mainly due to the repricing of inflation-linked government securities to lower interest rates.

The 2025 budget bill includes revenue-increasing measures amounting to 0.4 percent of GDP, in addition to the measures announced earlier in July (Table 5-3). The recently announced new measures include a one-off 8-percent increase in tobacco excise duty, a one-off 20-percent increase in company car tax and inflation-linked tax increases for the car tax, transfer duty and excise duty (fuel and alcohol); moreover, from 2026 an increase in the registration tax, company car tax and tobacco excise duty. Other new measures include the introduction of a global minimum tax in the form of a tax advance for the year 2025 and an increase in the number of tax rates for mining fees. The retail sales tax will be adjusted, while the suspension of the advertising tax will remain in place next year and the aviation pollution tax will be introduced.

In addition to measures aimed at increasing revenues, the 21-point Economic Policy Action Plan announced in October includes economic stimulus measures that will result in an increase in the budget deficit, the budgetary

Table 5-3: Budgetary impact on revenues of new tax measures announced in October 2024 (HUF billion)

Tax/discount	Fiscal impact in 2025 (HUF billion)
Excise duties	80
Global minimum tax advance	75
CO_2 quota tax	72
Mining royalty	40
Lump sum taxes of motor vehicles	33
Aviation environmental pollution tax	20
Retail tax	15
Elimination of PHEV tax credits	12
Total	**347**

Source: Government announcements, MNB calculations

impact of which was taken into account in the 2025 budget. As part of the action plan, the family tax and contribution allowance will be increased by 50 percent from 1 July 2025 and then doubled from the beginning of 2026. A Workers' Loan Scheme will be introduced, and measures to improve housing conditions in both Budapest and rural areas will include the development of a housing programme for young people, the launch of a Rural Home Renovation Programme and the maintenance of a reduced 5-percent VAT rate on the sale of new residential property until the end of 2026. As part of the Demján Sándor Programme, a high-amount capital financing programme for SMEs – the SME Investment-stimulating Support Programme – and the exports promotion loan programme of Eximbank Zrt. will be re-launched. The social contribution tax relief included in the three-year wage agreement in itself only slightly reduces the tax and contribution revenues from labour.

5.3.4 Budget balance for 2026 and 2027

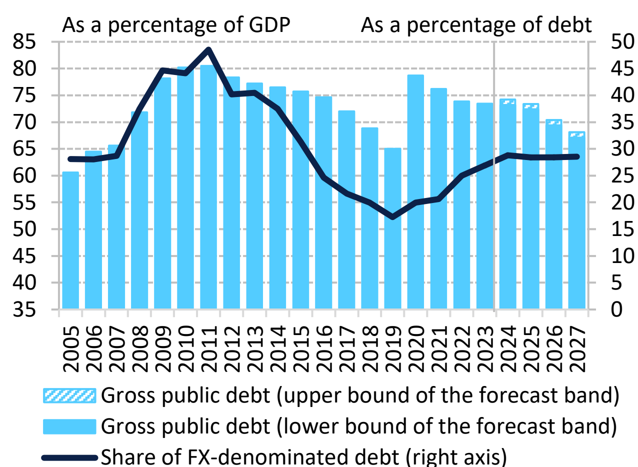
In the remaining years of the forecast horizon, we expect the primary balance to remain in equilibrium and accordingly the public deficit to decrease as interest expenses gradually decline. Based on our December technical forecast, we expect the deficit to range from 2.8 to 3.8 percent for 2026 and around 2.2 to 3.2 percent for 2027. In addition to interest expenditures, the decline in the deficit is supported by the expected macroeconomic path, lower energy expenditure and investment, as well as the announced measures.

5.3.5 Risks surrounding the baseline scenario

The macroeconomic environment has a significant impact on tax revenues. The budget balance is subject to risks on the revenue side, primarily based on the revenue dynamics regarding consumption taxes.

Restrictions on the availability of EU funds continue to create considerable uncertainty for the budget. Hungary has access to a total of EUR 12.2 billion in the 2021-2027 cohesion cycle. However, access is still not available to non-repayable grants from the Recovery and Resilience Facility (RRF) and cohesion funds representing a total of EUR 16 billion, the majority of which is linked to the implementation of the 27 super milestones defined by the Commission. It may be related to restrictions on access to EU funds, that based on budget data for the first eleven months, expenditures and revenues related to the EU funds remain substantially below what could be expected on the basis of appropriations. This points to few advance payments and a low level of the utilisation of funds.

Chart 5-13: Gross public debt forecast



Note: The time series of the gross public debt and the share of FX-denominated debt after 2023 are point estimates
Source: MNB, ÁKK

5.3.6 Expected trends in public debt

According to the preliminary financial accounts data, the gross public debt-to-GDP ratio was 76 percent at the end of 2024 Q3. The debt ratio increased by 1.4 percentage points year-on-year and by 2.6 percentage points from its value at the end of 2023. The rise in government debt was driven by high net issuance, which suggests that most of the annual issuance had already been realised in the first half of the year.

According to our forecast, the gross public debt-to-GDP ratio will be between 73.2 and 74.2 percent at the end of 2024. The decline in the debt-to-GDP ratio in 2024 is surrounded by risks due to a higher-than-expected cash flow deficit, the moderate growth outlook for the real economy, a revaluation of foreign currency debt and uncertainties surrounding the level of debt issuance outside central government (Chart 5-13). However, the decline in the debt ratio in 2024 may be supported by low net government debt issuance in 2024 Q4 after the substantial debt issuance seen thus far. We expect the debt-to-GDP ratio to fall below 70 percent of GDP by the end of the forecast horizon as the deficit gradually declines.

Changes in the EUR/HUF exchange rate affect the debt ratio via the revaluation of foreign currency debt. The lower the share of foreign currency debt in government debt is, the smaller this effect is. At present, a HUF 10 change in the EUR/HUF exchange rate alters the public debt-to-GDP ratio by almost 0.6 percentage point. Foreign currency issuances during the year led to an increase in the share of foreign currency debt in government debt.

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Mátyás Hunyadi

(23 February 1443 – 6 April 1490)

He ruled from 1458 to 1490 as King of Hungary, and had been Czech king from 1469 and Prince of Austria from 1486. Hungarian tradition regards him as one of the greatest Hungarian kings whose memory is preserved in many folk tales and legends. He is also known as Matthias Corvinus, King Matthias the Just or officially as Matthias I, but commonly he is simply denoted as King Matthias.

His father, János Hunyadi, the regent of Hungary, was one of the most outstanding military leaders and strategists in the country's medieval history who triumphed at the Battle of Nándorfehérvár in 1456. Matthias' mother was Erzsébet Szilágyi, and he had an elder brother, László Hunyadi. The future king was brought up by his mother and nurse until the age of six, and was subsequently placed under the supervision of his tutors. János Hunyadi did not have a chivalrous education in mind for his son: first, it was a Polish humanist, Gergely Szánoki who introduced him to the realm of knowledge, then this task was assigned to János Vitéz. Mátyás was brought up and educated in a humanistic spirit to become a versatile and curious-minded person who had been taught canon and constitutional law, arts and Latin. In addition to Hungarian, he also spoke German and Czech.

After the death of László V, his uncle, Mihály Szilágyi, and the armed forces supporting Hunyadi exercised pressure to have Matthias crowned as King of Hungary on 24 January 1458. Even in the early years of his reign Matthias had troubles both with the magnates of the country and Emperor Frederick III of the Holy Roman Empire. As the king was still a minor, parliament appointed Mihály Szilágyi to act as regent on his behalf. However, Matthias did not tolerate any guardianship and pushed his uncle to the background who devised a plot against the king in response. Returning from battle with the Turks, the king had the rebels captured and he imprisoned his uncle in the castle of Világos.

Upon his ascension to the throne the annual income of the treasury hardly exceeded 110 to 120 thousand forints. During his rule spanning thirty-two years the king managed to multiple revenues from taxes. Considering the average of the taxes levied, less the revenues from the Czech and Austrian provinces, this yearly amount approximated 628,000 forints and may as well reached 900,000 gold forints in the most prosperous years. This was still much less than the annual revenue of the western powers of the age. In order to raise the low income of the treasury, reform-like and comprehensive financial actions were needed. Matthias recognised that a centralised, nationwide financial system was the only solution to the problem, and that the royal revenues had to be directed to a single person, the treasurer. The reforms of Matthias were adopted by parliament and his decrees were promulgated on 25 March 1467.

We can get a glimpse of the cultural life in the royal court, which represented the elite of European civilisation at the time, at the partly reconstructed Royal Palace in Visegrád. The most distinguished pieces of the cultural legacy of Matthias are the Corvinian books, richly illustrated volumes of the former royal library.

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