

The joint empirical research of the National Labor Office (NLO) and HCCI Institute for Economic and Enterprise Research (IEER) on the short-term economic outlook and labor market decisions of private sector firms was conducted for the eighth time in September and October 2014. For the latest survey of the Short-term Labor Market Forecast the staff of NLO and IEER interviewed the managers of 7,179 firms about their current and expected demand for labor.

According to the data the Hungarian economy did not reach its pre-crisis level at the end of last year despite the fact that 2014 generated a GDP growth which had not been seen in a long time. The engine of Hungarian industrial growth continued to be industrial exports, especially exports to Germany.

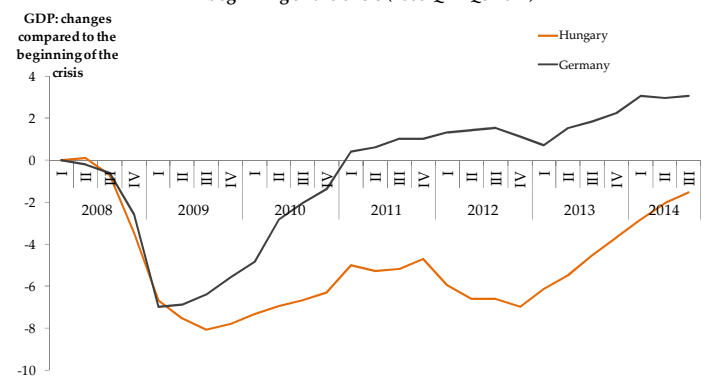
Based on the results of employee number changes, the employment rate has steadily increased in 2014. The number of employees in the private sector has increased in the first and second quarters by 2.3 and 2.8 percent respectively. According to the forecast of IEER, based on the expectations for 2015, the employment index is expected to stagnate. The likely scenario is that in 2015 the number of employees may increase by 1.3 percentage point for the construction sector and 0.9 percentage point for retail. In contrast, a 7.5 percentage point decrease is expected for services while a 9.3 percentage point decline is likely for mainly exporting firms.

## Business Situation

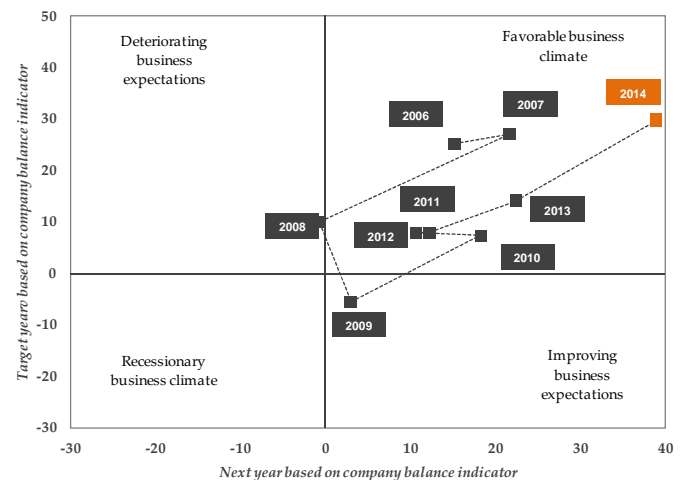
If we look at quarterly GDP changes compared to the beginning of the financial crisis, it is clear that the economic recovery in Hungary was much slower compared to Germany, which is the most important export market for the Hungarian economy. On the one hand, the drop of Hungarian GDP was deeper and, secondly, the recovery started later. While the pace of the decrease was almost the same for both economies, by the first quarter of 2009 the recovery of the German economy was much faster and more invigorated. By the beginning of 2011 it had returned to the pre-crisis level and has since been increasing steadily. The Hungarian economy, however, still did not reach the pre-crisis level at the end of 2014, despite growing steadily since 2013 and with a GDP growth in 2014 that have not been seen in a long time. The engine of Hungarian industrial growth continues to be industrial exports, especially exports to Germany, but Hungarian companies were not able to fully exploit the German recovery – the growth in demand and in import demand.

According to the latest Short-term Labor Market Forecast by IEER the subjective assessment of the business situation of firms continued to improve after a positive shift that occurred in 2013. The general business situation indicator is at 30 points, which means that the rate of companies considering that their current business situation is favorable is 30 percentage point higher compared to those that see it as unfavorable. The business expectations for 2015 are more optimistic than at any time in the recent years: the expected business situation indicator is at a level of 39 points. Optimism can be traced back to the expectations of the

Where are we in the crisis? Quarterly changes in GDP compared to the beginning of the crisis (2008 Q1 - Q3 2014)



Source: IEER, own calculations



Source: NLO, IEER, 2006-2014

services sector, those in the fields of tourism and hospitality, as well as the foreign-owned and exporting companies.

### Staff changes in the private sector

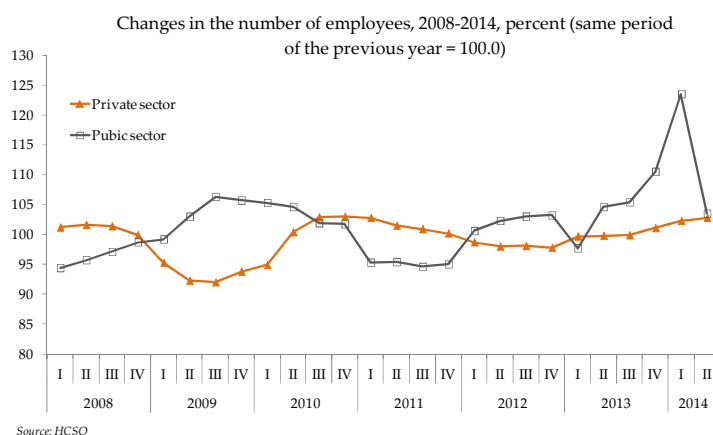
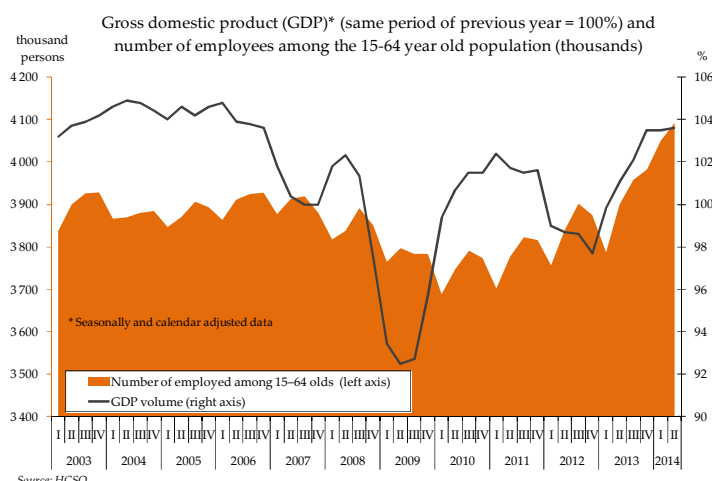
The number of employees increased in the first half of 2010, and then started to decline. In 2011, GDP growth began to slow down, while the number of employees increased slightly. In 2012, the GDP dropped by 1.7% while the number of employees showed a sharp increase and returned to pre-crisis levels as a result of the rapid growth in the number of community service workers. In 2013, the GDP increased by 1.1% while employment likewise increased – also due to the continued increase in the number of community service workers. The continuation of this trend can be observed in 2014, as GDP in the first quarter grew by 3.5% compared to the same period of the previous year, in the second quarter it increased by 3.6%, and in the third quarter by 3.1%, with the employment rate similarly increasing.

Because of the economic crisis, in the course of 2009 the number of private sector employees significantly declined by around 5-8% in all quarters. In 2010, the rate of decline began to slow, and then in the second half of the year we experienced growth of around 3%. In 2011, the growth rate continuously weakened and by the end of the year the data showed stagnation. In 2012 a decline of 1-2% was experienced for each quarter and in 2013 the negative trend continued. In the first three quarters there was a slight decline of less than 1% in the number of employees in the private sector, yet in the fourth quarter a 1.1% increase occurred. In 2014, the first and second quarters showed an increase of 2.3% and 2.9% respectively in the number of employees in the private sector.

According to the Short-term Labor Market Forecast by IEER in 2014, akin to 2013, the number of companies which increased staff numbers is 14 percentage points higher than those that reduced. Expectations for 2015 have formed in a similar way, so stagnation is expected for the employment index. Improvement of employment trends seems less robust compared to what we have seen in the improvement of business climate.

According to the raw data of the survey, based on the responses of companies which generally express exaggerated optimism, a 1.76 percentage point increase is expected in employment, against which – taking into account the adjustment of IEER – a 3.7 percentage point decline is more likely to occur. With a significant improvement in the macroeconomic environment, stagnation can not be excluded just as an unanticipated deterioration in conditions can result in a decrease of 6.9% in employment in the private sector.

According to the likely scenario the number of employees will increase by 1.3 percentage points in the construction



industry and by 0.9 percentage points in retail. In contrast, for other sectors of the economy it is likely to decline, especially for the services sector, where we forecast a decline of 7.5 percentage points. The likely scenario states that for predominantly export-oriented enterprises a decline of 9.3 percentage points in 2015 can be expected.

## Macroeconomic trends: European Economic Forecast for Hungary

In the following a brief analysis gives an insight into the macroeconomic trends summarized by the Winter 2015 European Economic Forecast of the European Commission. The focus is on the key macroeconomic data for the EU and Hungary in the forecast period 2015-2016. The European Commission forecasts a slowdown in Hungarian economic growth, which is estimated at the level of 3.3% in 2014, 2.4% in 2015 and 1.9% in 2016. For the EU level a slower economic growth is projected. Besides, a current account surplus and positive labor market trends are expected both in the EU and Hungary. Inflation is projected to slowly rise while the general government deficit will be below the Treaty reference value of 3% in 2015 and 2016. The debt to GDP ratio is expected to slightly decrease in the EU and Hungary.

### Slow economic growth in the EU and Hungary

In the European Economic Forecast Winter 2015, the European Commission predicted a slower growth rate both in the eurozone and in the EU. Annual GDP growth in the EU is forecasted at 1.7% in 2015 and 2.1% in 2016. Domestic demand is expected to be the growth driver. Namely, the recent decline in oil prices is expected to boost EU growth by raising domestic demand. In addition, the measures of the ECB should support credit demands, which would result in a higher investment activity. Also, the European Commission's Investment Plan for Europe should contribute to investment growth.

Hungary's annual GDP growth is estimated at the level of 3.3% in 2014. Factors contributing to annual growth are growing domestic demand, higher absorption of EU funds and the Loans for Growth Program of the Central Bank, which provide loans to SMEs. However, the European Commission expects a slowdown in the growth. The growth is projected at 2.4% in 2015 and further to 1.9% in 2016. The reason for the decline of growth is the expectation that investment activity will slow down. Besides, a decrease in the absorption of EU funds is expected in 2016.

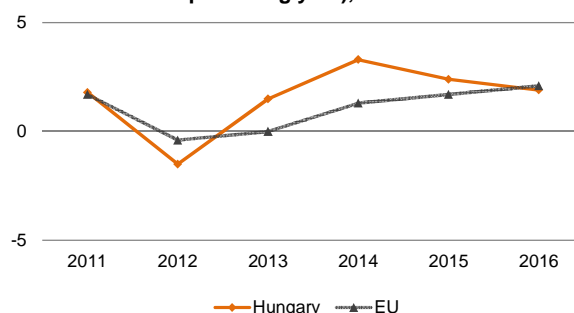
Hungary will continue to have a current account surplus, which is estimated at 4.4% of GDP in 2015 and 4.9% in 2016. The EU's current account surplus will slightly rise from 1.6% in 2014 to 1.9% in 2015 and 2016. However, there are considerable differences in the balances of trade of EU countries.

### Labor market situation in the EU and Hungary

EU's employment level has begun to rise in 2014 and the growth rate is expected to remain between 0.7% and 0.9% in the period of 2015 and 2016. Major labor market reforms related to flexible working arrangements, wage bargaining and tax wedge should contribute to job creation.

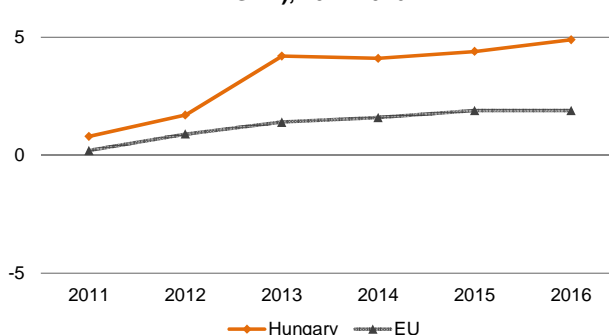
In Hungary a 3.7% employment growth was recorded in 2014, which was supported by job creation in the private and public sectors. Unemployment rate both in Hungary

Gross domestic product (percentage change on preceding year), 2011-2016



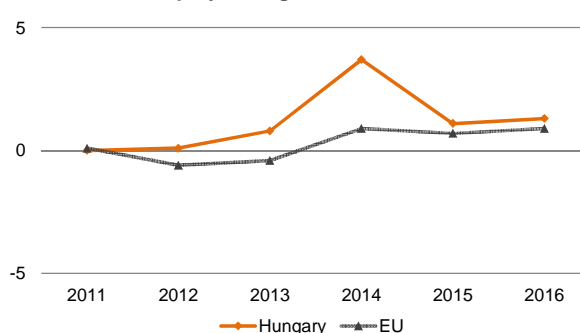
Source: European Commission

Current-account balance (as a percentage of GDP), 2011-2016



Source: European Commission

Employment growth, 2011-2016



Source: European Commission

and in the EU is expected to decrease further. Unemployment rate in Hungary is lower than the EU average as it was 7.7% in 2014 and it is projected to decline to 7.4% in 2015 and 6.6% in 2016, largely due to further increase of demand in the public sector (community service workers).

### Inflation

The sharp fall in oil prices should push inflation rates downwards in 2015. The HICP inflation (Harmonised Index of Consumer Prices) is projected at 0.2% in 2015 for the EU, before rising to 1.4% in 2016. During the last four years, Hungarian inflation was the lowest in 2014 (0.0%). It is expected to rise to 0.8% in 2015 and 2.8% in 2016.

### The general government deficit below the Treaty reference value

The EU's general government deficit has recorded a declining trend from 2011 to 2014, which is expected to continue in the forecast period. This is the result of EU's fiscal measures which have been undertaken since 2010. General government deficit is projected to fall below 3% in the EU (2.6% in 2015 and 2.2% in 2016).

According to preliminary results, Hungarian public deficit was 2.6% of the GDP in 2014. The Commission projects a deficit of 2.7% of GDP for 2015, which will decrease by 0.2 percentage point in 2016. Still, the projected general public deficit will remain below the Treaty reference value of 3%.

Absorption of EU funds in Hungary is expected to decline by 2% until 2016. In addition, the Commission states that higher than expected correction of EU funds could negatively affect the budget.

### The public debt to GDP ratio

In the EU, the public debt to GDP ratio has been increased from 81.3% in 2011 to 88.4% in 2014. In 2015, the debt to GDP ratio is expected to decrease by just 0.1 percentage point while it is forecasted to fall to 87.6% in 2016. Namely, it is expected that the rise of inflation and the growth of GDP will lead to a fall in the debt to GDP ratio over the forecast period.

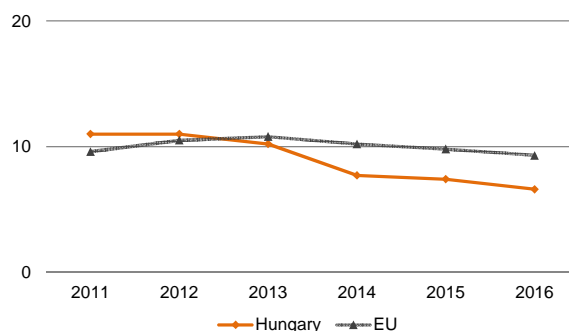
Contrary to the situation at EU level, Hungary has experienced mostly a decline in the public debt to GDP ratio since 2011. The debt to GDP ratio was increased to 77.7% only in 2014, due to the weakening of the forint. The Hungarian debt to GDP ratio is forecasted to fall to 77.2% in 2015 and 76.1% in 2016.

Source:

European Commission: *the European Economic Forecast, Winter 2015*

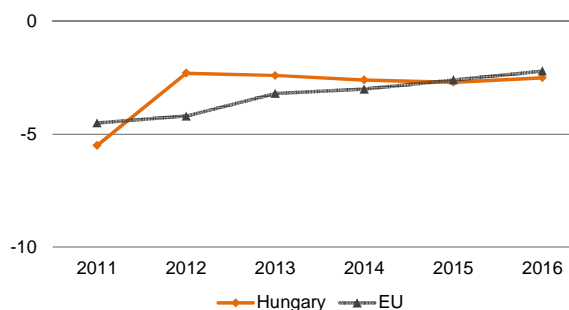
[http://ec.europa.eu/economy\\_finance/eu/forecasts/2015\\_winter\\_forecast\\_en.htm](http://ec.europa.eu/economy_finance/eu/forecasts/2015_winter_forecast_en.htm)

Unemployment rate, 2011-2016



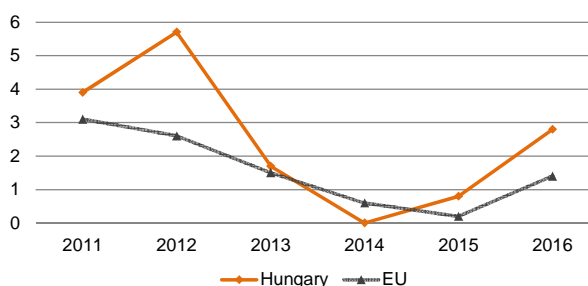
Source: European Commission

General government balance (as a percentage of GDP), 2011-2016



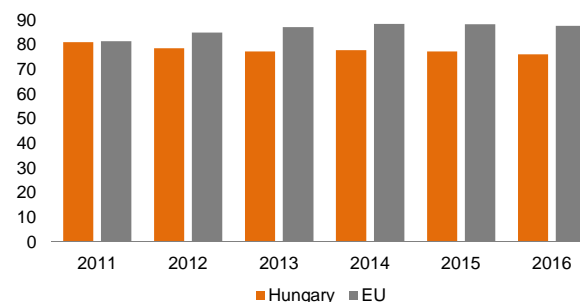
Source: European Commission

Harmonised index of consumer prices (percentage change on preceding year), 2011-2016



Source: European Commission

General government gross debt (as a percentage of GDP), 2011-2016

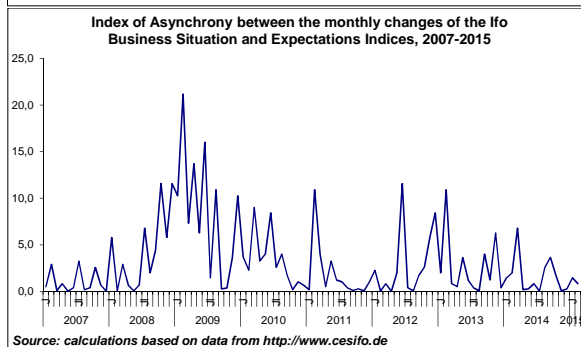
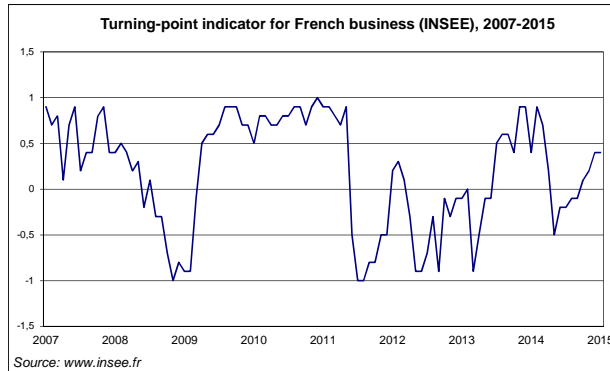
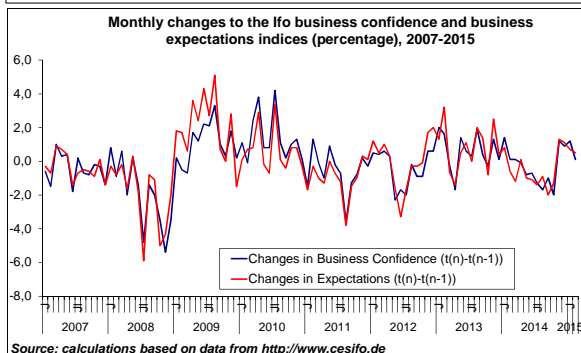
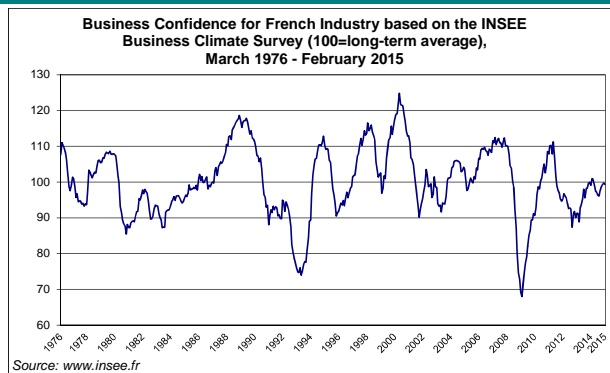
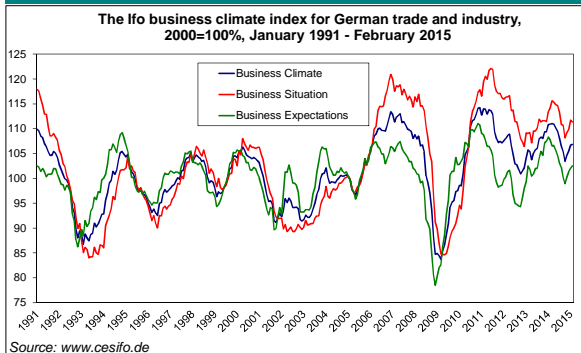


Source: European Commission

## International trends

The Ifo Business Climate Index for industry and trade in Germany rose in February 2015 to 106.8 points from 106.7 points in January. The business climate index has reached a turning point in November 2014. Assessments of the current business situation have decreased by 0.4 point in February. Expectations with regard to the months ahead are brighter. The gap between the current business situation and the expected developments, as calculated by the IEER Index of Asynchrony, decreased in February, so the business confidence index showed lower uncertainty than in the previous month. According to Ifo analysts, companies expressed greater confidence in future business developments and the German economy is proving robust in the face of geopolitical uncertainty. (Source: Ifo, <http://www.cesifo-group.de>)

Results from the February survey by the French statistical office (INSEE) show that the business climate of industry in France has slightly fallen compared to the previous month. The composite indicator which measures it has decreased by one point and remains at a level (99) very close to its long-term average (100). The turning-point indicator is stable and remains in the zone indicating a favourable short-term economic situation. The balance on opinions on past change in production is stable but remains below its long-term average. The balance of opinions on personal production expectations is also stable but at a level which is above its long term average. The balance of general production expectations, which represents business managers' opinion on French industry as a whole, has increased by 2 points compared to the previous month and is slightly above its long-term average. (Source: INSEE, <http://www.insee.fr>)



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In case of publication please cite as follows:  
IEER Monthly Bulletin of Economic Trends,  
March / 2015, Budapest,  
2015-04-14