Monthly Bulletin of Economic Trends

February 2016

Plans for wage rises in the private sector, 2016

In the course of its latest business climate survey HCCI Institute for Economic and Enterprise Research (IEER) examined potential changes in wages in the year 2016. According to our estimation enterprises plan raising gross salaries by 3.0-3.2%. This is an average wage growth, which slightly exceeds last year's increase.

Plans for wage rises

The IEER Business Climate Survey is conducted twice a year on a large sample (largest among Hungarian business climate surveys). It includes questions about business leaders' intentions concerning wage rises in the next twelve months. Responders are required to give the answer as a percentage. Positive values signify rises while negative values mean reductions[1]. In the 2015 October wave 3145 leaders responded these questions. We weighted data by spatial composition and contribution to the GDP simultaneously.

Our results show that companies in the private sector plan on raising wages by an average of 3.0-3.2% this year.

This is lower than previous years' gross average wage rises. However, it is higher than IEER's estimation about wage increases in 2015. (According to the Hungarian Central Statistical Office's calculations gross salaries grew by 3.8% between January and November 2015[2]. Compared to this IEER estimations of 2.6-2.8% are pessimistic.)

In summary, if these plans come true, wages will be raised by a similar or slightly higher rate in 2016 as they were in 2015.

[1] During the analysis we excluded answers that indicated changes bigger than 30% (42 cases) because in these cases there is a chance that the responder misunderstood the question. These false answers would distort our results significanty. The survey question was the following: „What percentage will wages be raised in your company in 2016? In case wages will be decreased please enter a negative number".

[2] https://www.ksh.hu/docs/hun/xftp/gyor/ker/ker1511.html

Sources: Hungarian Central Statistical Office, IEER

* Corporate intentions.
Average expectations estimated by IEER.

Statistics of IEER estimation of expected changes in wages

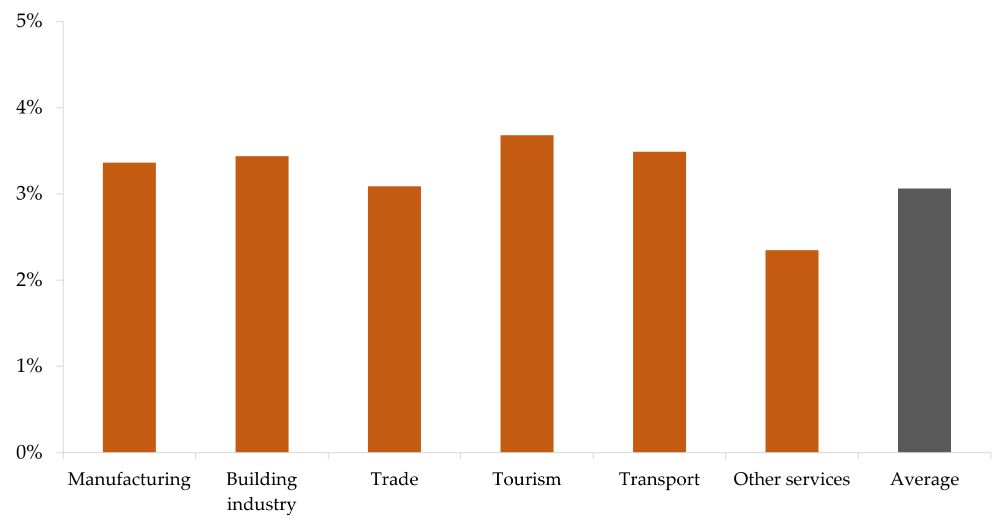
	Average	Sample size	Standard deviation	Median	Standard error
2015	2.7	2882	3.1	3	0.06
2016	3.1	3139	3.1	3	0.06

Differences between groups of companies

According to the analysis by sectors of the economy, wage rises are expected to be the highest in the tourism sector (3.7%).

Companies providing business services have the lowest planned wage increase rate (2.4%).

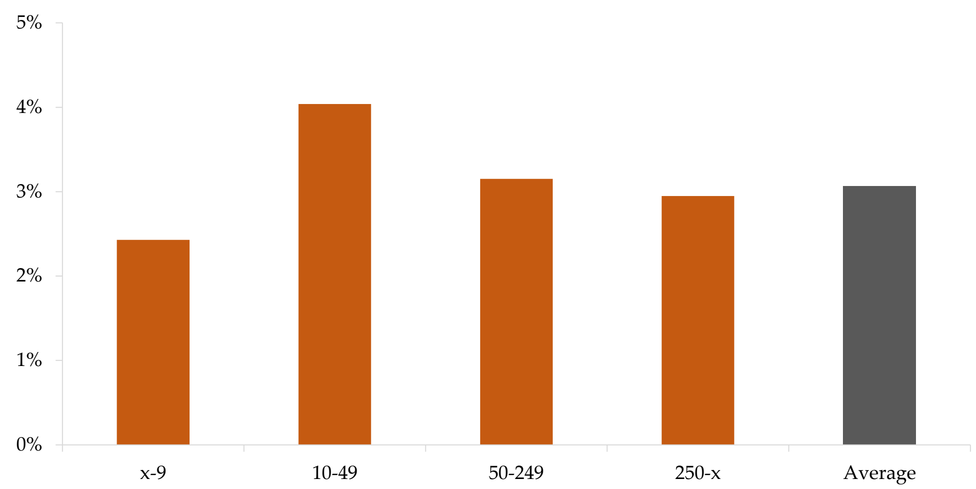
Expected wage rise rates by sectors



Source: IEER

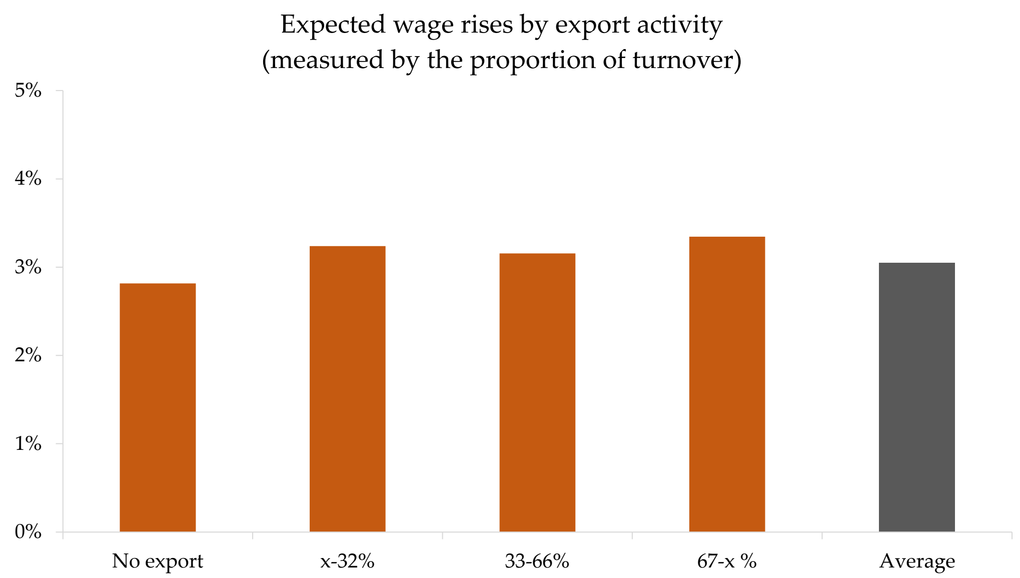
Regarding the size of the enterprises, those employing 10-49 people stand out as they are expected to raise salaries by an average of 4.0%. There might be a 2.4% increase in wages at companies with no more than 9 employees.

Expected wage rises by company size (number of employees)



Source: IEER

Planned wage rise is higher among wholly or partly foreign-owned firms (3.2%) than among solely domestically owned ones. Regarding export activity, companies that gain more than two-thirds of their income from exports have higher wage increase plans (3.4%) than those that do not export (2.8%). These data show that foreign relations are related to the extent of average planned wage rises in the year 2016.



Source: IEER

Falling commodity prices

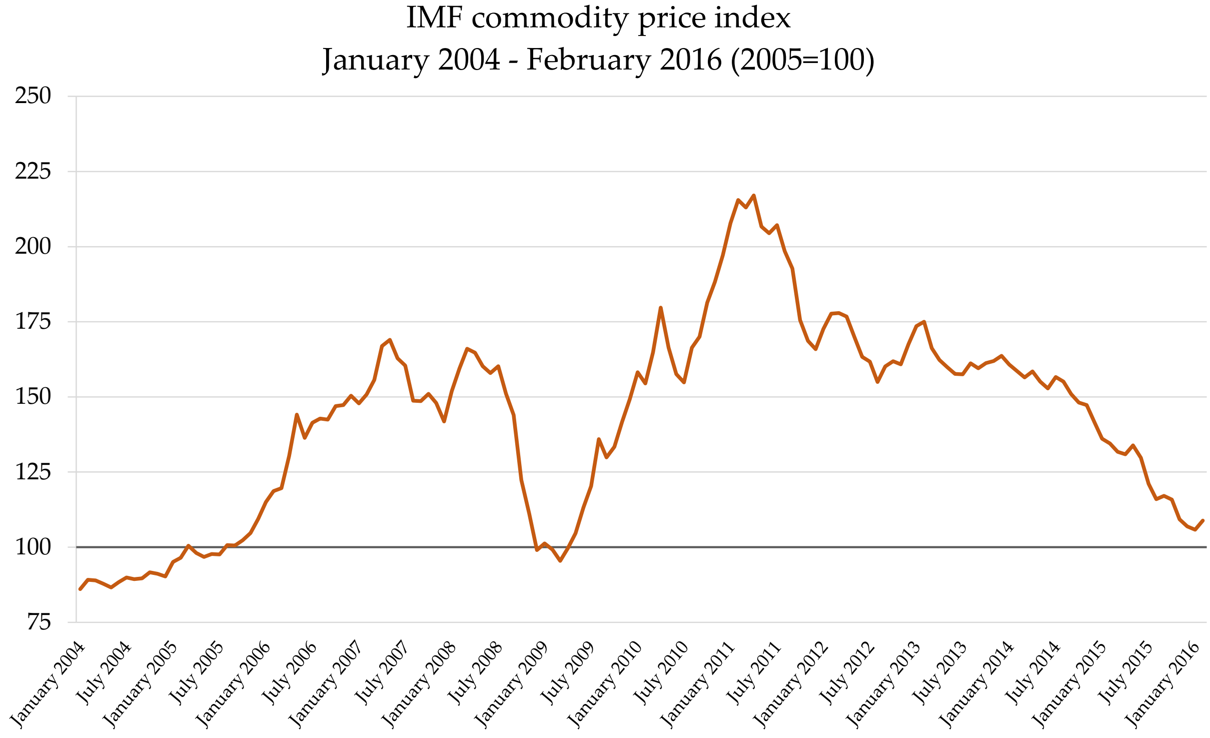
For the first two months of 2016 the dive in world market prices for energy, precious metals and industrial metals continued. The fundamental cause is the end of the commodity boom of 2004-2011 and subsequent oversupply, but growth disruptions in the emerging economies (especially China) and the Federal Reserve's interest rate increase also play important roles in the process. Falling commodity prices seem to have a positive effect on net importers of raw materials such as Hungary, but global financial uncertainty and stress in the emerging economies can have an adverse effect on the Hungarian economy as well.

Concerns as the year begins

The year 2016 started with a gloomy global economic outlook, which was partly raised by the fact that global commodity prices fell steeply throughout 2015. Compared to their level at the beginning of 2013, prices for energy, precious metals and industrial metals had fallen by 30 to 70 percent by the end of last year. In mid-2015 analysts expected prices to normalize within a few months, but even now there are no signs of a change close at hand, which is alarming.

The reasons for the fall in commodity prices are complex. In addition to supply and demand factors the optimistic atmosphere dominating commodity markets between 2004 and 2011 plays an important role in it, as well as two of the most important global processes: the appreciation of the US dollar and the slowdown of the Chinese economy.

Analysts contend that these factors and their contexts will define the development of the world economy in 2016.



Source: IMF

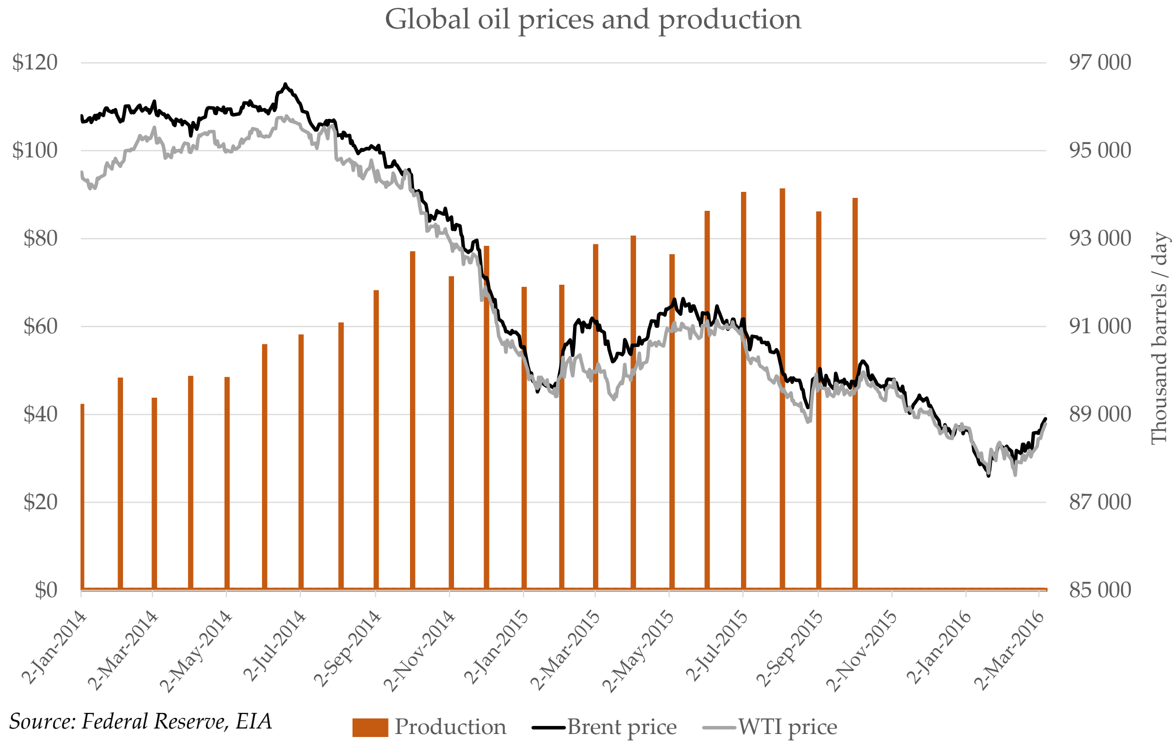
The commodity super cycle

The global prices of raw materials have been moving cyclically during the 20th and 21st centuries. They followed a rhythm that was different from that of the equity and currency exchange rates. As raw materials are real, tangible and storable products, their prices are impacted by supply and demand rather than overall financial conditions.

From the 1900s onwards, periods of large price hikes were followed by declines. Higher prices encouraged an increase in the production, but then the additional quantities of supply drove prices down. The average length of both the rise and fall periods was 7-8 years.

The last boom in commodity prices lasted from 2004 to 2011. During this period investments were created in related industries for building new capacities, but when supply increase rate overtook the rise in demand prices began to fall. Producers increased production volume in order to maintain sales, thus a deflationary spiral took shape. Many investments were financed from loans, which made producers vulnerable.

This scenario fits the markets of industrial and precious metals, but in the case of petroleum additional factors played a role in the maintenance of oversupply. Most of the extra capacities built during the upturn period were created in order to produce shale oil in America, which has been done more and more efficiently over the years. However, in order to displace US producers, not only did OPEC (Organization of Petroleum Exporting Countries) maintain oil production but even increased it. Importantly, this process, which started in the autumn of 2014, did not lead to the expected results: prices fell to historic lows and global markets are drowning in oil. In addition, the lifting of sanctions against Iran drove another major producer back to the oil market.



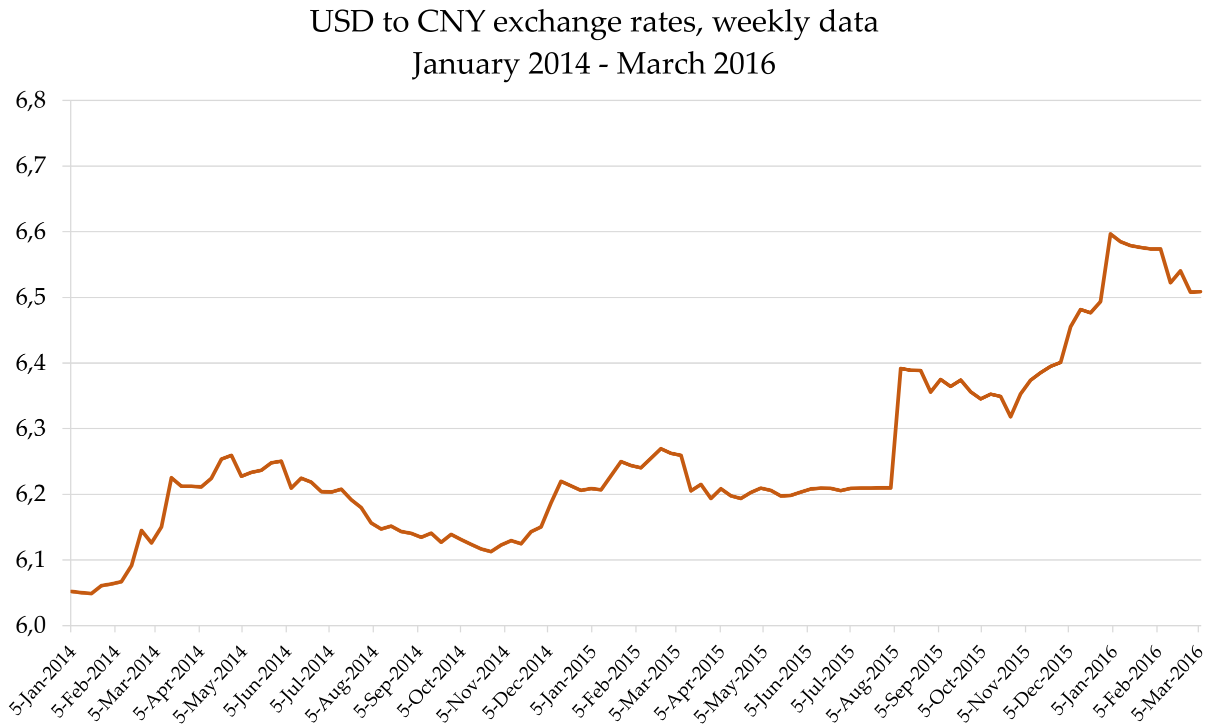
Source: Federal Reserve, EIA

Problems on the demand side

The demand side of the global commodity markets are also depressed. In the case of energy prices, an important trend is the increasing energy efficiency of vehicles and other products of high energy usage. Furthermore, the slowdown or even recession of emerging economies, primarily the BRICS group (Brazil, Russia, India, China and South Africa) has a significant impact on commodity markets. It results in that demand for raw materials increase slower than expected and slower than the growth of supply.

The slowdown in China brings about the most severe consequences. Due to the devaluation of the Yuan the purchasing power of Chinese consumers has been decreasing, which affects the commodity markets. More importantly, however, there is a decline in raw material intensive investments, for which the weakness of the Chinese real estate market is responsible. Some analysts proclaimed the end of the era of big construction projects in China, which had created a huge demand in the market for raw materials such as steel and copper. Further development may be implemented by the expansion of services.

The securities markets in China were characterized by uncertainty over the past year, which itself is not a factor on the global economic level, since not many foreign investors are present on Chinese stock exchanges. However, many see a loss in the confidence and credibility of the state leading Communist Party due to their frequently unprepared, poorly communicated and executed actions. This adds to the concerns about the Far Eastern superpower.



Source: Investing.com

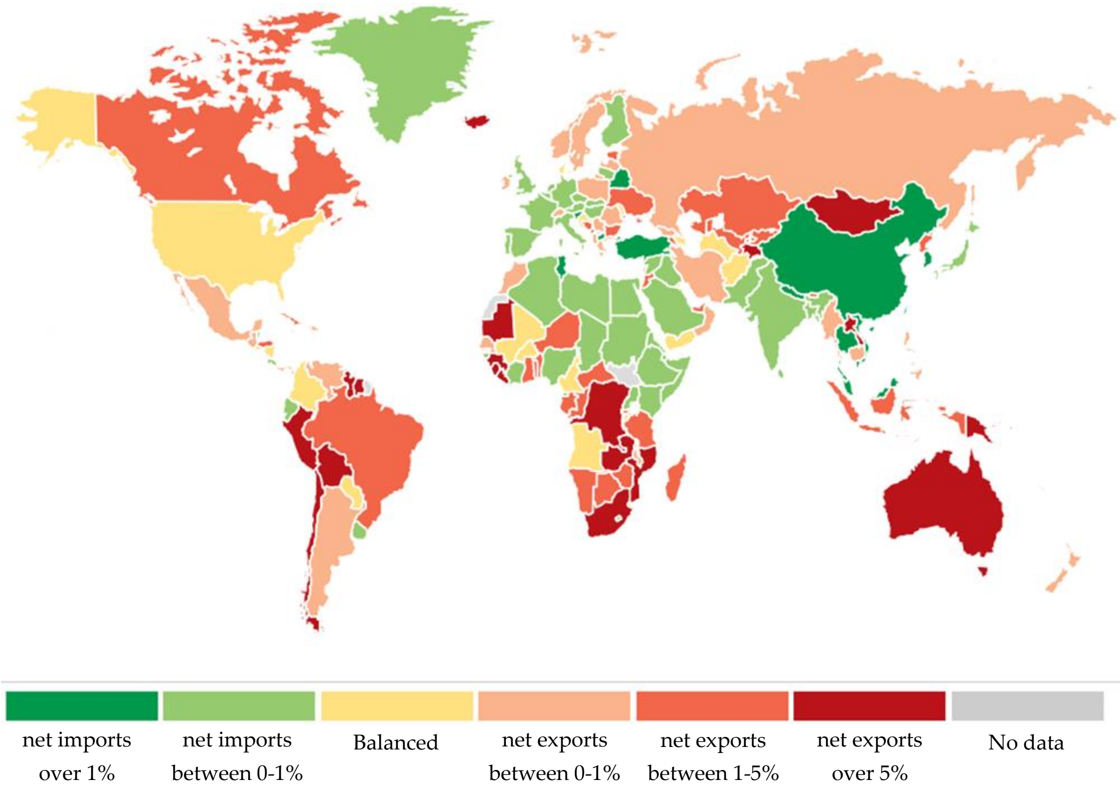
Dollar appreciation

At the end of 2015 Federal Reserve raised interest rates for the first time since July 2006. As a result, the US dollar appreciated to a decade high in January 2016. As the global commodity markets operate in dollar-denominated prices, this contributed to the fall in prices significantly. What is more, it is likely that the December rate hike was just the beginning of a long cycle of interest rate increases, which could lead to further appreciation of the US dollar.

Consequences

Economies that rely on the export of raw materials are vulnerable to a sharp fall in prices. To protect themselves they devalue their currencies; although this puts extra pressure on dollar-indebted countries. In parallel, low prices are favourable for commodity importers – including Hungary – as it means that households have more disposable income which, in turn, can help to increase growth. In addition to this, the decline in commodity prices dampens inflation, which makes monetary easing possible. However, the difficulties of emerging economies affect the whole world through global financial markets, so it is possible that the negative effects of the fall in commodity prices will eventually spill over and reach us as well.

Importers and exporters of industrial metals, 2010-2013 average, percentage of GDP



Source: http://www.economist.com/blogs/graphicdetail/2015/08/commodity-dependency

International trends

Development of production, consumption and employment in certain globally significant economies, compared with expectations and values of the previous period.

		Vonatkozási időszak	Tényadat	Várakozások	Előző időszak
Germany	Unemployment Change (thousand persons)	(Feb)	-10	-10	-19
	Manufacturing Purchasing Managers Index	(Feb)	50.5	50.2	50.2
	IFO Business Climate Index[1]	(Feb)	105.7	106.7	107.3
France	INSEE Business Climate Index[2]	(Feb)	100		102
USA	Nonfarm Employment Change (thousand persons)	(Feb)	214	190	193
	Core Retail Sales, monthly change	(Jan)	0.2%	0.1%	0.2%
	Philadelphia Fed Manufacturing Index	(Feb)	-2.8	-3.0	-3.5
China	Manufacturing Purchasing Manager's Index	(Feb)	49.0	49.3	49.4

[1] http://www.cesifo-group.de/ifoHome.html

[2] http://www.insee.fr/en/themes/indicateur.asp?id=105

Source of the remaining data: http://worldeconomiccalendar.com

The German manufacturing purchasing managers index in February reached higher than expected, although IFO Business Climate Index fell once again. The American economy surpassed the expectations in terms of employment, retail and manufacturing. Conversely, Chinese manufacturing purchasing managers index was lower than projected.

Sources of the article "Falling prices":
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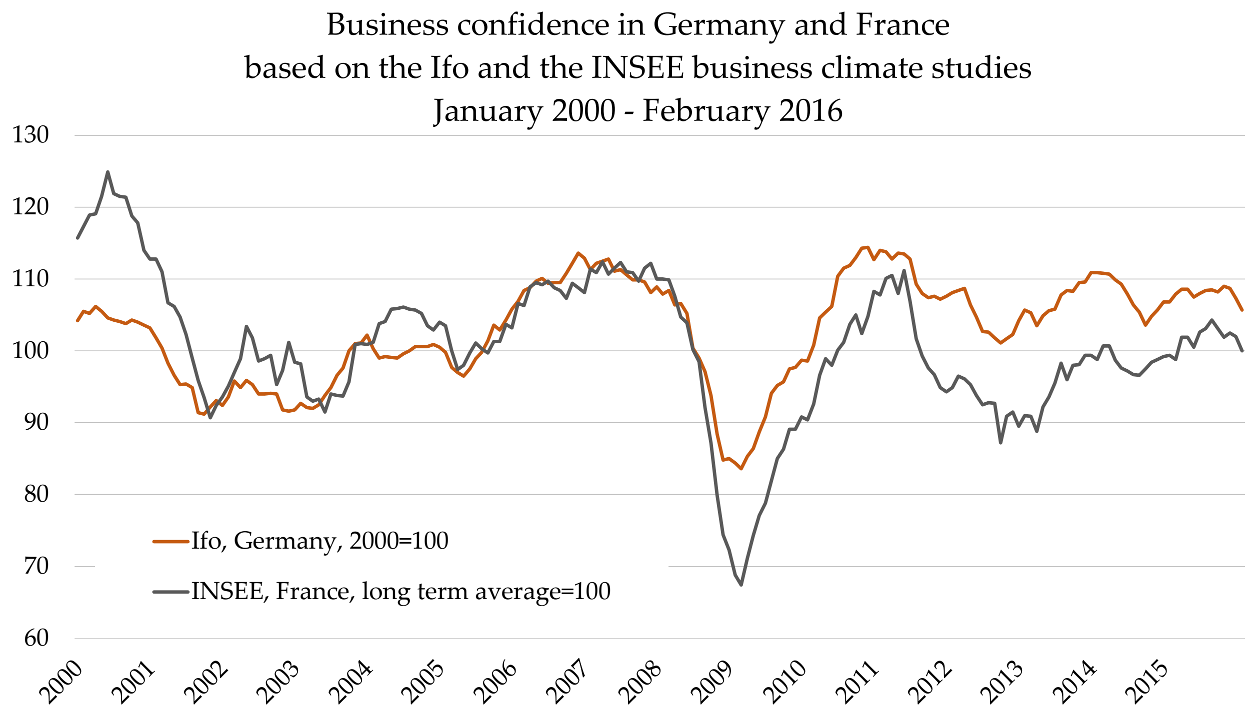
http://www.economist.com/blogs/graphicdetail/2015/08/commodity-dependency

Long-term changes in the business confidence indices



Sources: www.cesifo.de, www.insee.fr

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