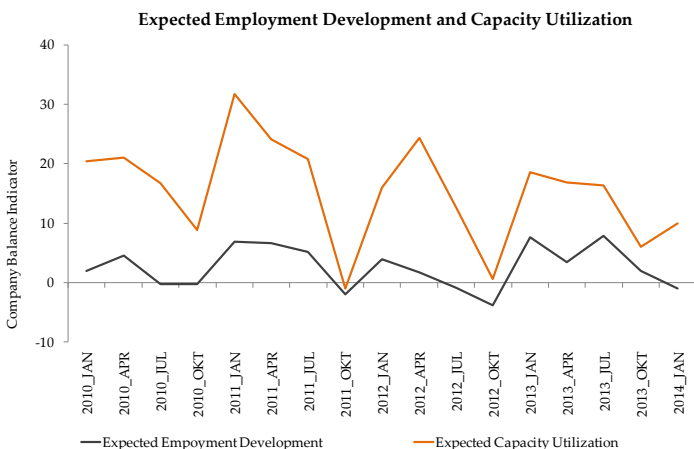
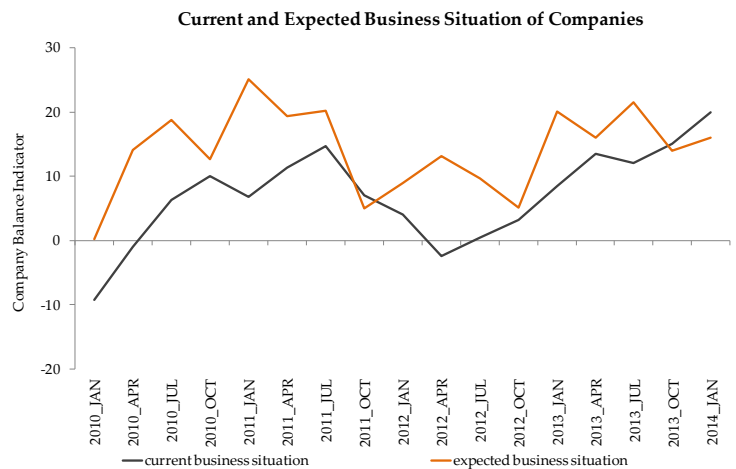
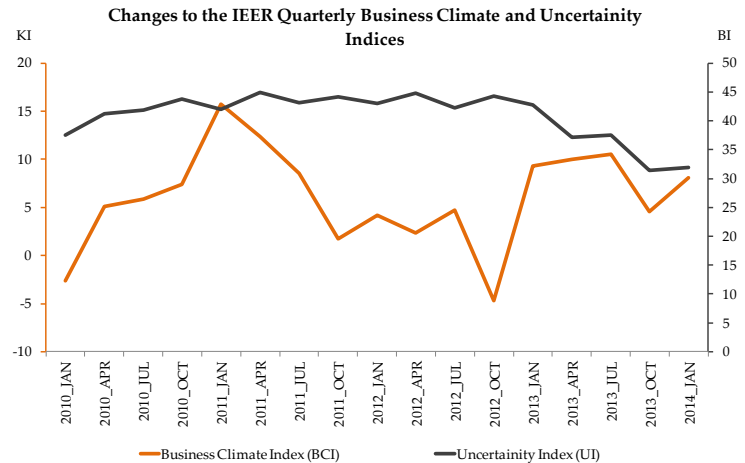


Since 2010 the HCCI Institute for Economic and Enterprise Research (IEER) has been conducting a business climate survey on a quarterly basis, the seventeenth taking place in January of this year. In this survey 400 company managers reported on the current and expected business climate. The results of the January 2014 survey indicate that compared to the previous quarter business confidence improved among Hungarian companies.

The IEER Quarterly Business Climate Index rose from 5 points (October 2013) to 8 points, approaching the level measured one year ago (in January 2013 the index was 9 points). The value of the Uncertainty Index was at the 32-point level, just one point over the October value, so it is still lower as was found in previous surveys. This suggests that although the perception of the improving trend remained diverse within the business sector, opinions of improvements have become more consistent.

Overall, we can conclude that the business confidence indicators rebounded in the last quarter of 2013 compared to the positive level at the beginning of 2013 (relative to 2012) following a lurch experienced in the third quarter of 2013.

The IEER Quarterly Business Climate Index consists of ten components. Behind the rise in the index are the current and expected business and earnings situations, the favorable outlook of orders, investment activity, and more optimistic expectations about the level of capacity utilization. By comparison, production levels stagnated over the past six months, there were similar expectations in this regard for employment numbers, and the future prospects of companies were increasingly negative.



Macroeconomic trends: A moderate recovery. Quarterly forecast of Ifo, Insee, and Instat institutes

As projected, GDP in the Eurozone expanded by a meagre 0.1% in Q3 2013, as export growth fell sharply. Economic activity is expected to accelerate modestly over the forecast horizon (+0.2% in Q4 2013, +0.2% in Q1 2014 and +0.3% in Q2 2014) with a gradual shift in growth engines from external to domestic demand. Continued tight fiscal policy in many member states together with persistent labour-market slack conducting to a stagnant real disposable income will lead to limited private consumption growth. Investment is forecast to increase thanks to the gradual acceleration in activity and the need to renew production capacity after a marked phase of adjustment. Under the assumptions that the oil price stabilizes at USD 110 per barrel and that the euro/dollar exchange rate fluctuates around 1.36, headline inflation is expected to remain well below 2% (0.9% in Q1 2014 and 1.1% in Q2 2014). The major upside risk to this scenario is a stronger than expected investment growth, led by improved access to credit. A stagnation in private consumption triggered by continued labour market weakness and weaker external demand in emerging economies are key downside risks.

Stable industrial production in Q4 2013

The business surveys have picked up since mid-2013, despite a dip in October. After a decrease in Q3 (-0.1%), industrial production fell sharply in October, in part because of a working day effect in Germany not captured by working day adjustment procedures¹. Industrial production is expected to remain stable in Q4 2013, and to regain some momentum in Q1 and Q2 2014 (+0.7% and +0.8% respectively), on the back of brightening prospects for external and internal demand.

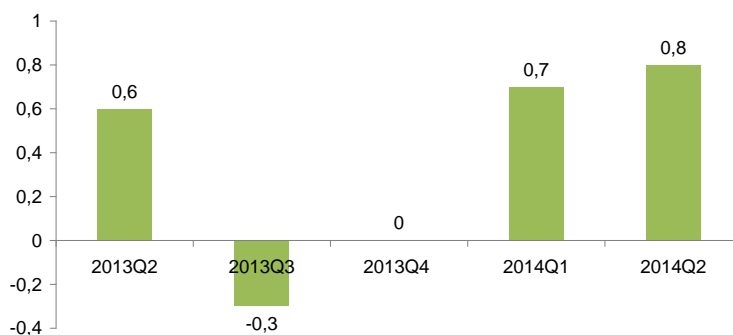
Moderate upswing in activity in 2014

In the third quarter of 2013, euro area GDP slowed down (+0.1% after +0.3% in Q2), mainly because of weaker export growth in most Eurozone economies. We forecast a moderate growth in Q4 (+0.2%), on the back of a rebound in France and a progressive strengthening of the recovery in Spain.

As suggested by the business surveys, activity is likely to continue to grow at a moderate pace in the first half of 2014, helped by a recovery in private investment and declining negative fiscal impulse from macroeconomic policies. Exports are expected to slowly gain momentum over the forecast horizon as growth picks up again in emerging economies (particularly China and Central European countries) and activity remains buoyant in the US, the UK, and Japan.

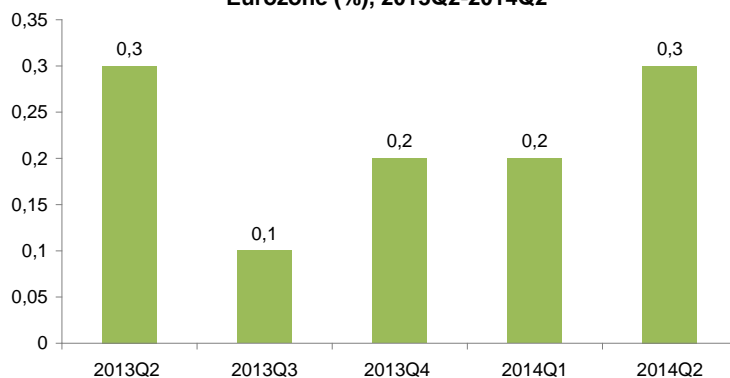
The gap between Eurozone countries growth, although persisting, is likely to contract again.

Forecasted increase in industrial production compared to previous quarter, Eurozone (%), 2013Q2-2014Q2



Source: Eurostat and Ifo-INSEE-ISAE-ISTAT forecasts

Forecasted GDP growth compared to previous quarter, Eurozone (%), 2013Q2-2014Q2



Source: Eurostat and Ifo-INSEE-ISAE-ISTAT forecasts

¹ The 3rd of October (day of German reunification) was a Thursday. Many workers took an additional day off on Friday the 4th.

Domestic demand improving gradually

Given the moderate recovery lying ahead, labour market conditions are expected to remain subdued over the forecast horizon. Employment is projected to stabilize gradually, and productivity is forecast to continue to pick up slowly as it has done since the beginning of 2013. Nominal wages are likely to increase moderately over the forecasting period, though unemployment rates will remain at record-high levels, and fiscal policies are expected to become a little less restrictive. The decrease in purchasing power should thus ease over the forecasting period. Consumption should pick up slightly (+0.1% for Q4 2013 and Q1 2014, +0.2% in Q2 2014) as households are expected to gradually reduce their precautionary savings with business and employment prospects improving.

Bank lending conditions have stopped tightening in the Eurozone since the start of 2013. In addition, the gradual upswing in activity and the need to renew production capacity after a marked phase of adjustment are expected to sustain the recovery in equipment investment. In the construction sector, the drop in investment is projected to slow down. Total investment, despite the subdued public component, is thus expected to moderately gain momentum over the forecast horizon (+0.2% in Q4 2013, +0.3% in Q1 2014 and +0.4% in Q2).

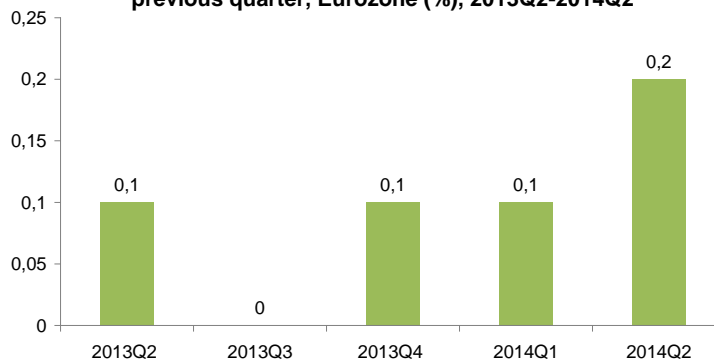
Inflation to remain stable at a low level

After peaking at 2.9% year-on-year in Q4 2011, headline inflation has fallen to 0.8% in Q4 2013. It is expected to reach 0.9% in Q1 2014 and rise slightly to +1.1% year-on-year in Q2 2014, sustained by energy prices, under the assumption that the Brent price remains stable at \$110 while the USD/Euro exchange rate fluctuates around 1.36, and under the effect of the gradual exit from year-on-year figures of the drop in energy prices that occurred in spring 2013.

Core inflation is forecast to remain stable at a low level (0.8% in Q4 2013, 0.7% in Q1 and 0.9% in Q2 2014), dampened by the high unemployment rates in most Eurozone countries.

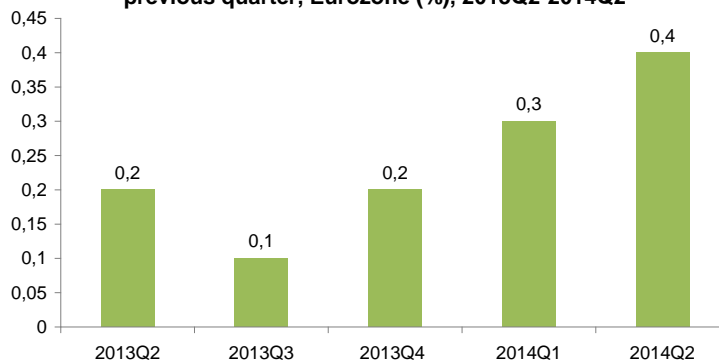
Source: Euro-zone Economic Outlook. January 10, 2014
(<http://www.cesifo-group.de/ifoHome/facts/Forecasts/Euro-zone-Economic-Outlook/Archive/2014/eeo-20140110.html>)

Forecasted increase in consumption compared to previous quarter, Eurozone (%), 2013Q2-2014Q2



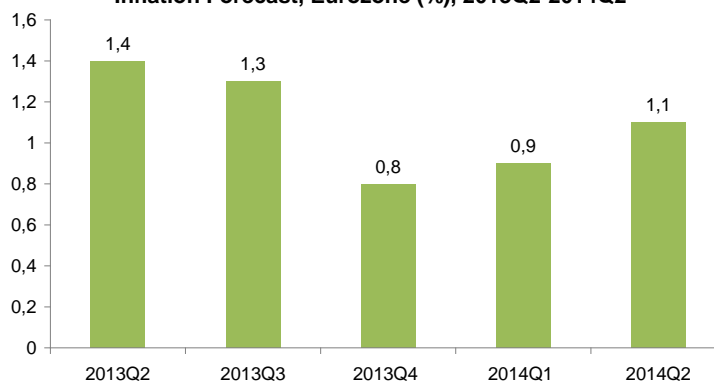
Source: Eurostat and Ifo-INSEE-ISAE-ISTAT forecasts

Forecasted increase in investment compared to previous quarter, Eurozone (%), 2013Q2-2014Q2



Source: Eurostat and Ifo-INSEE-ISAE-ISTAT forecasts

Inflation Forecast, Eurozone (%), 2013Q2-2014Q2



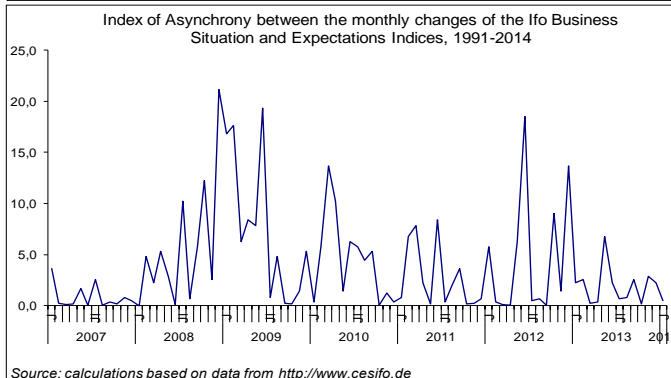
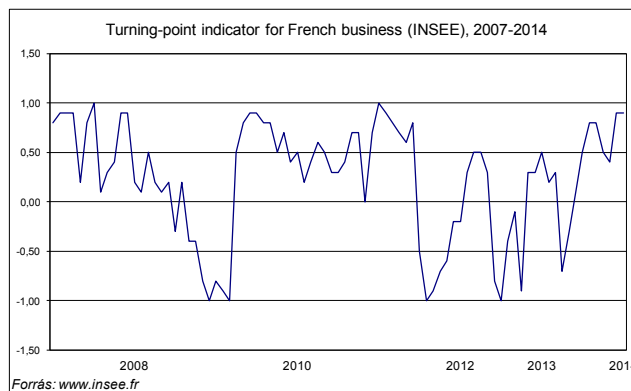
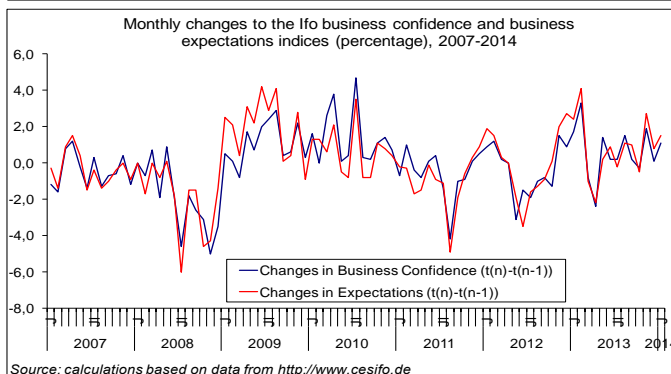
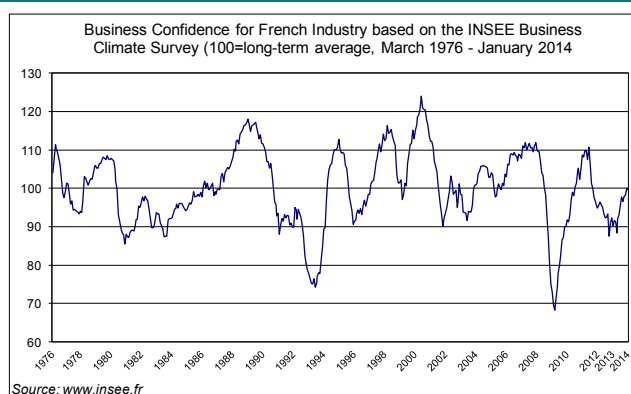
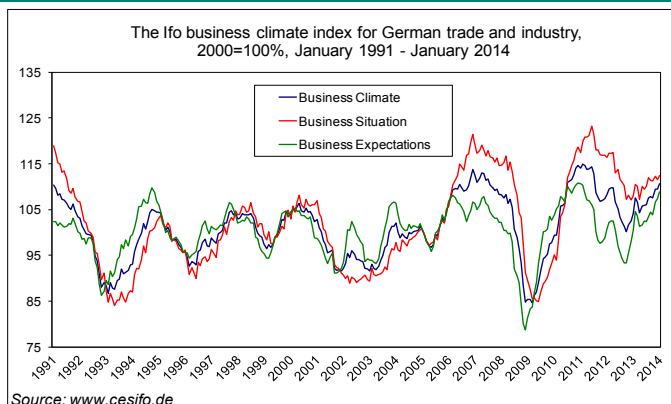
Source: Eurostat and Ifo-INSEE-ISAE-ISTAT forecasts

International trends

The Ifo Business Climate Index for German industry and trade rose again in January 2014 for the third consecutive month. Satisfaction with the current business situation rose to the highest level seen since June 2012. Expectations for the next six months became more optimistic again and reached the highest levels measured in over three years. The gap between the current business situation and the expected developments, as calculated by the IEER index of asynchrony, fell in January, thus the business confidence index showed less uncertainty than in the previous month. Ifo analysts see the German economy starting the new year very positively. (Source: Ifo, <http://www.cesifo-group.de>)

According to the French statistical office's (INSEE) survey of business leaders interviewed in January, the position of French industrial activity remained unchanged compared to the previous month. The INSEE business confidence index was stable at its long-term average. The value of the turning point indicator was unchanged and remained stable in the favourable business climate zone. The indicator for the individual business forecast of company managers increased and now exceeds its average value. The overall outlook index – which represents a summary of respondent opinions on French industrial activity as a whole – rose in January compared to the previous month, and was above its long-term average.

(Source: INSEE, <http://www.insee.fr>)



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In case of publication, please cite as follows:
HCCI IEER Monthly Bulletin of Economic Trends,
2014 / February, Budapest,
2014-03-10