CEE SPECIAL REPORT

Divergent growth paths of Czechia and Hungary

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November 25, 2025

Note: Past performance is not necessarily indicative of future results.
CEE8: Croatia, Czechia, Hungary, Poland, Romania, Slovenia, Slovakia, Serbia.

Czechia & Hungary: Comparison of economic performance

Czechia and Hungary are **two small open economies that are prone to similar impacts from the global environment** on their economic development. In terms of structure, both economies rely on the manufacturing sector to a great extent, with high importance for automotive production. Both countries could take advantage of independent central bank actions and monetary policy channels to influence inflation development and economic growth. **Since the pandemic, these two countries have followed quite divergent paths of recovery, however**. Hungary recovered after COVID-19 promptly, while growth in Czechia has been picking up since 2024 more visibly. We wonder why and try to zoom in on the possible explanations behind this economic divergence.

- **Households in Czechia suffered from the highest loss of purchasing power in response to the inflation shock in 2022. Also, Czechia allowed high energy prices to be passed onto households to a large extent while Hungary opted for wide range of price caps.**
- **In Hungary, the lack of RRF funds strongly impacts investment activity (unprecedented fall of investment, although from a high level, i.e. investment-to-GDP ratio one of the highest in the region)**
- **Divergent monetary policy and real interest rate levels**
- **Different fiscal paths, as Czechia has consolidated public finances to a greater extent**

Czechia & Hungary: Comparison of economic performance

More detailed view on local policies that could have impacted the recovery over the last five years.

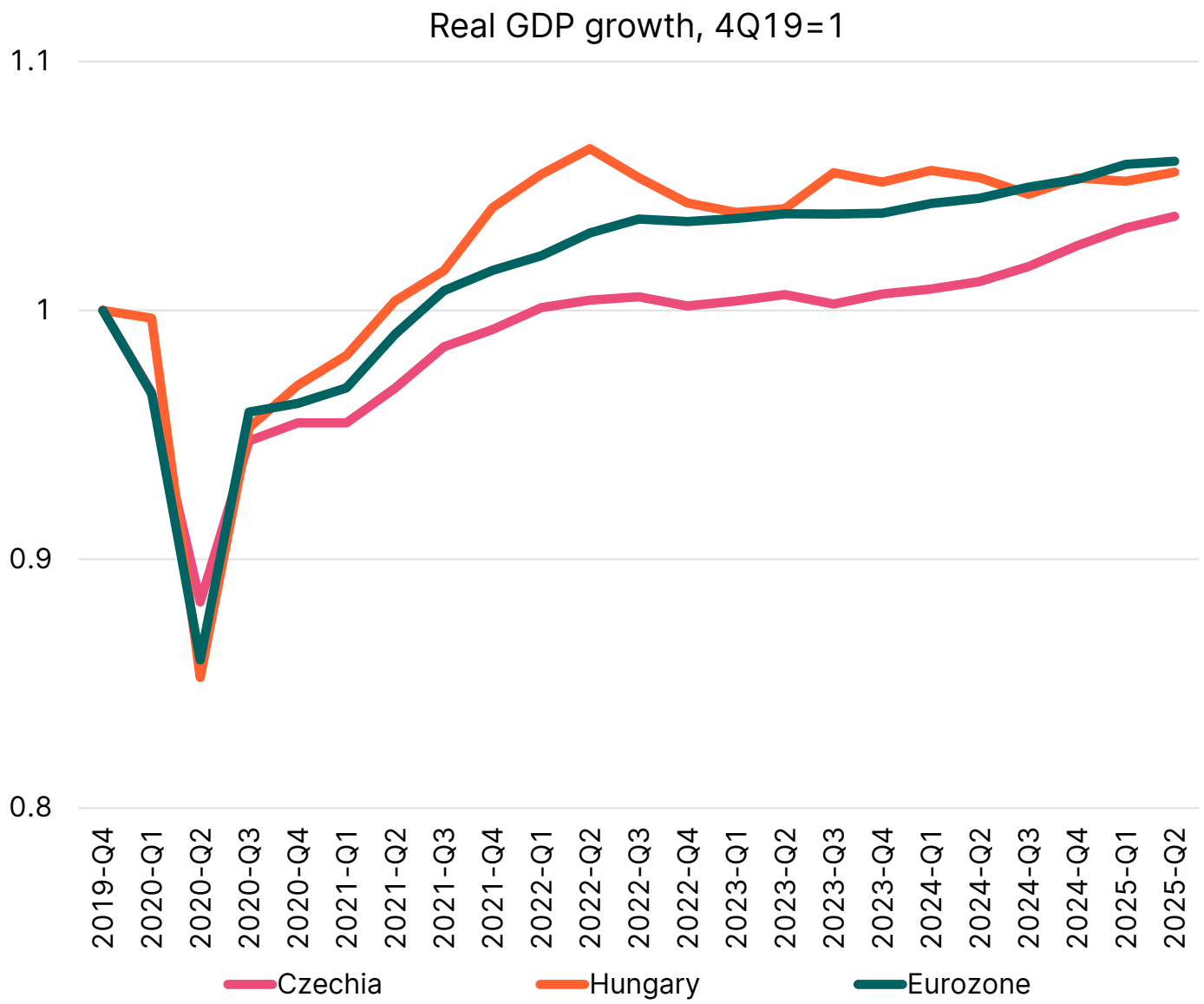
1) The Czech central bank reacted slightly faster to inflation increases and was cautious with restarting monetary easing at first. Hungary needed to tighten monetary conditions to a much greater extent, as dynamic depreciation of the Hungarian forint in fall 2022 forced the central bank to deliver a prompt response and hike the effective interest rate to 18%.

2) The monetary easing cycle in Hungary (beginning in 2H23) was disrupted due to volatility on the FX market (the Hungarian central bank paused when the policy rate reached 6.5%), while Czechia brought the key interest rate toward 3.5%, which seems to be the terminal rate for the time being (until a reaction is needed in the future).

3) Fiscal policy development in Czechia (consolidation of budget gap) most likely added to the slower recovery prior to 2024, while in Hungary fiscal discipline was milder.

4) Households in Czechia were hit the hardest in terms of real wage loss following the inflation shock. Moreover, households in Czechia faced higher energy price increases than in Hungary. At the same time, both countries maintained quite high saving rates; therefore, the contribution of private consumption to GDP growth in Czechia was much lower compared to Hungary.

5) On the other hand, Hungary suffered from a fall of investment and low utilization of RRF funds. While Czechia had already had half of RRF grants disbursed, Hungary did not utilize the RRF grants almost at all. The flow of EU funds and investment growth go hand in hand. The fact that Hungary has not been receiving any payments lately affected the investment cycle to a great extent.

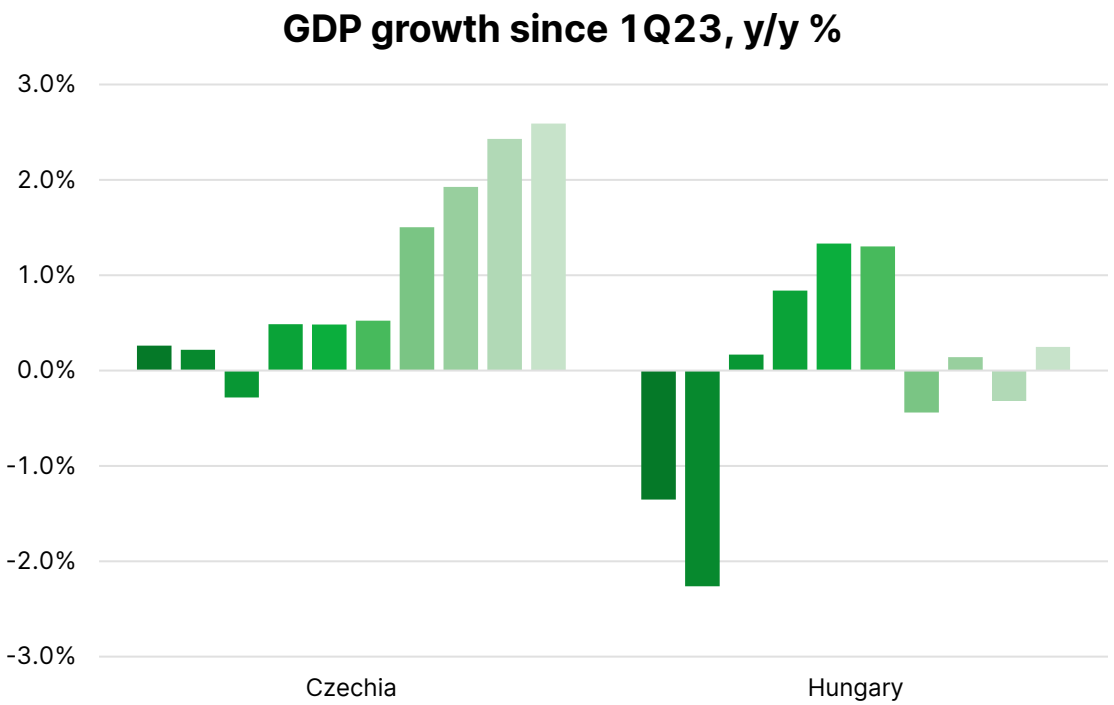


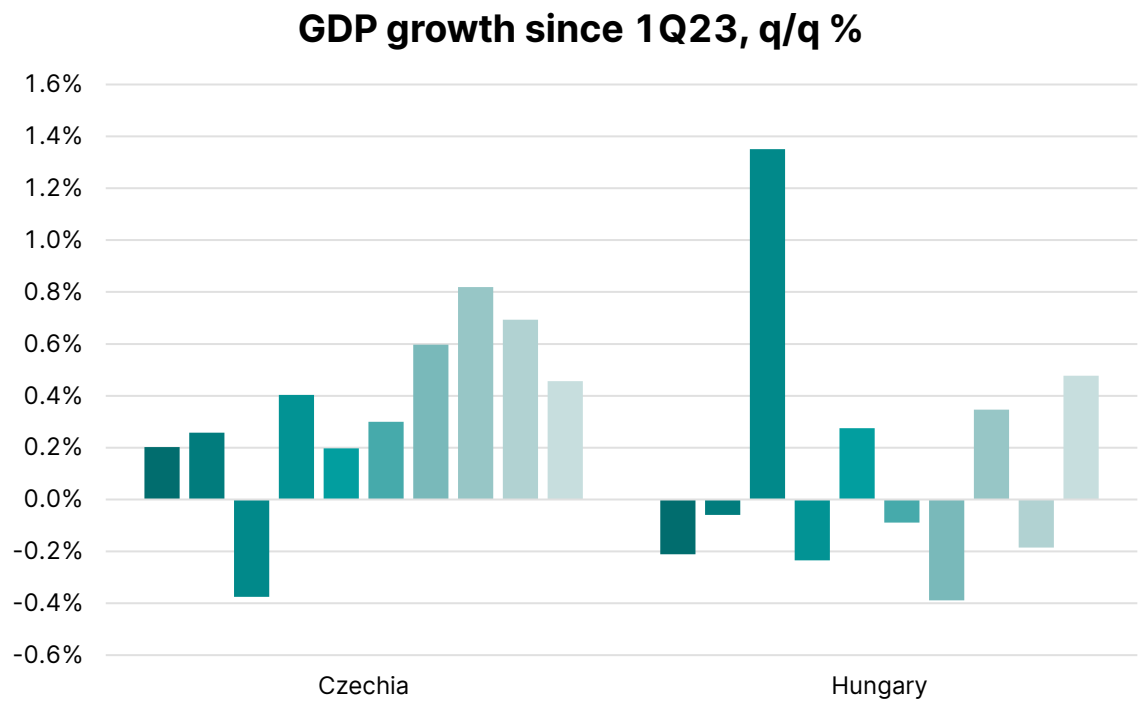
Czechia's economy has regained strength lately

Although the GDP growth level in Czechia is still below that of Hungary (if compared to the pre-pandemic level in 4Q19), recent growth dynamics in Czechia are very encouraging. The GDP level has been gradually converging toward the Eurozone level. The acceleration of the catching up process since 2024 has been pretty apparent.

Source: Erste Group Research
November 25, 2025

Czechia vs. Hungary growth dynamics since 2022





The strong momentum of the Czech economy, with solid growth dynamics in q/q terms, translates into y/y GDP growth above 2% in recent quarters and a clear upward trajectory of the annual growth dynamics. In Hungary, on the other hand, q/q growth has been zigzagging and in annual terms the growth has been close to zero for roughly a year. In 2025, the Hungarian economy is likely to stagnate again, after a very weak 2024.

Source: Erste Group Research
November 25, 2025

Economic structure is similar in both countries

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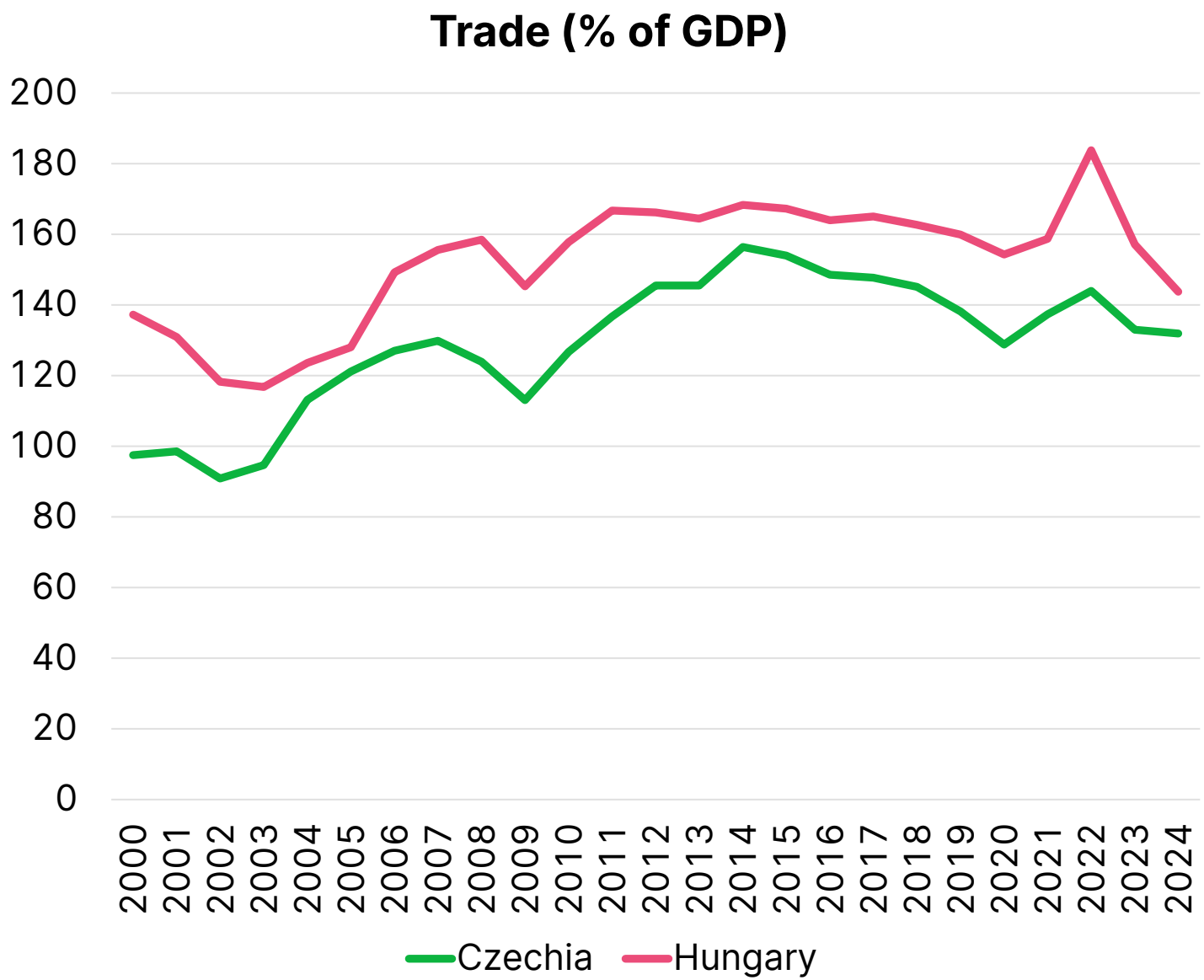
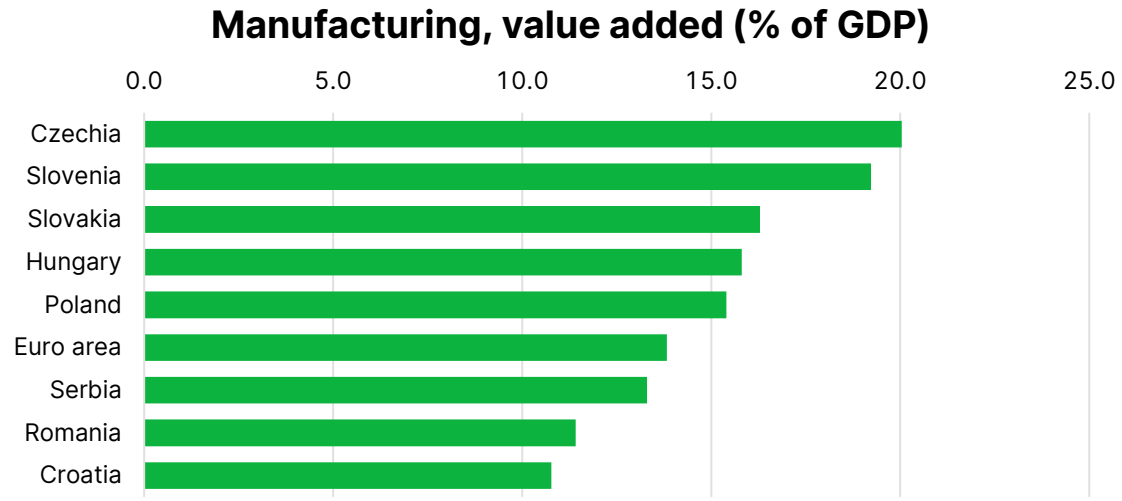
Export and import as % of GDP

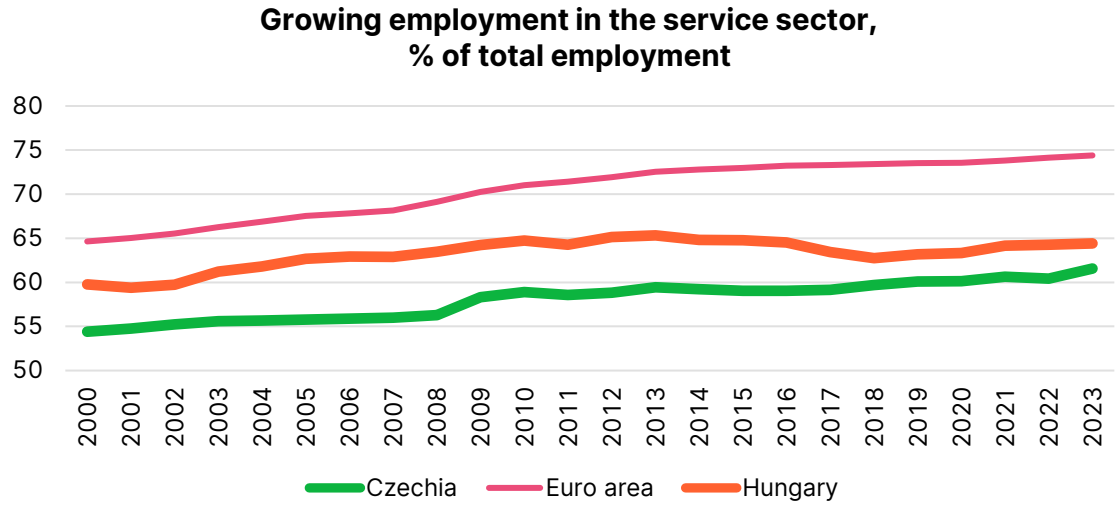
Hungary and Czechia are two small open economies with trade-to-GDP ratios close to 140%. Such a high ratio highlights the critical role of trade in their economic development. For small open economies, international trade tends to be a key driver of growth, allowing them to access larger markets, diversify production, and benefit from comparative advantages. High trade integration supports industrial specialization and attracts foreign investment. On the other hand, it makes these economies more sensitive to global demand fluctuations and external shocks.



Source: Erste Group Research
November 25, 2025

Key role of manufacturing sector, but importance of services has been growing



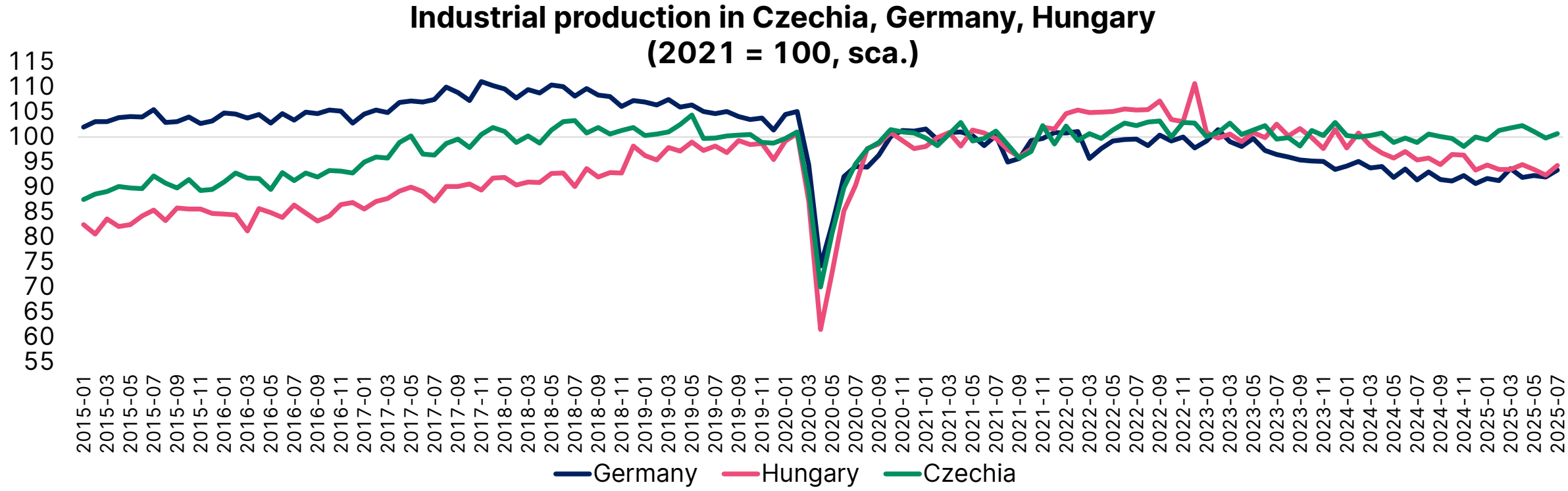


The manufacturing sector plays an important role in the economic development in Czechia and Hungary. Within the manufacturing sector, automotive is the largest sub-sector in Hungary's manufacturing industry. Czechia hosts major players like Škoda Auto, TCPA and Hyundai, while Hungary is home to large production facilities for Audi, Mercedes-Benz and Suzuki. Manufacturing underpins export competitiveness. In Czechia, we have recently observed a difference between strong exports of finished cars and auto parts, primarily for German companies. The weaker demand for auto parts is being offset by the growing production of the Czech defense industry. However, the share of services in GDP has been increasing, while the share of industry, although still considerable, decreased slightly over the last few years in both Czechia and Hungary.

Source: Erste Group Research
November 25, 2025

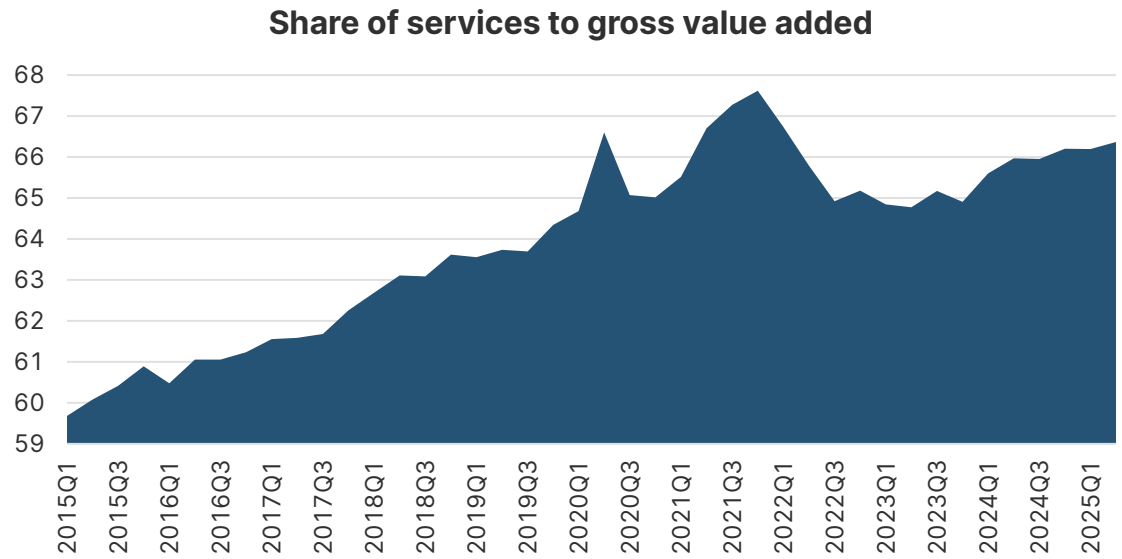
Pre-pandemic decoupling with Germany disappeared and correlation became strong again with Hungary

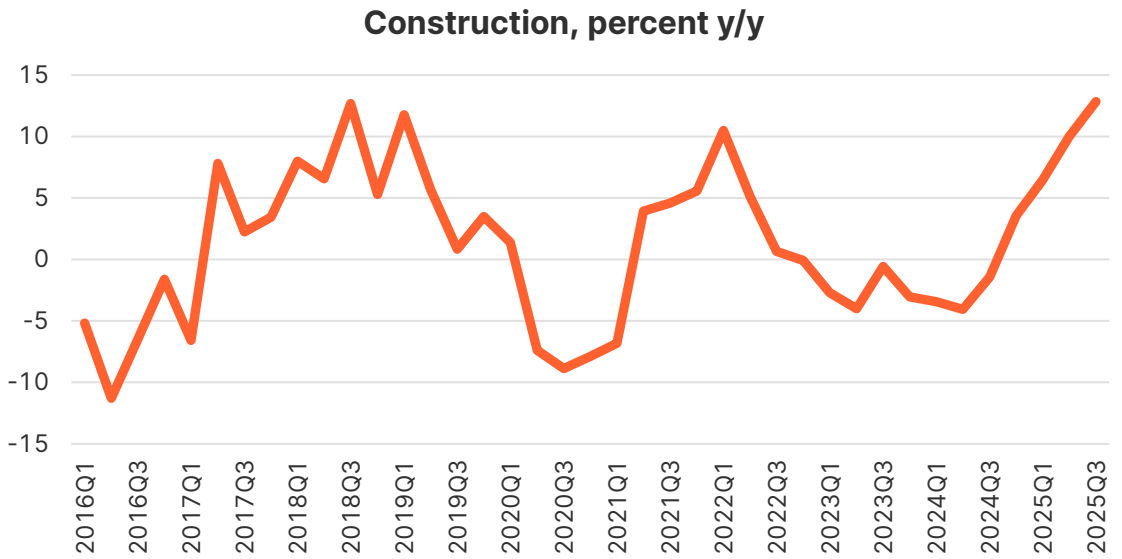
We see an industrial downturn for the third consecutive year in Hungary, mainly due to the prolonged stagnation of the German economy. Germany remains Hungary's most important foreign trade partner, serving as a key market for automotive products and batteries. It is also the most important partner for the Czech economy, but its overall share has been declining.



Source: Eurostat, Erste Research

Czech economy's ties to Germany reduced



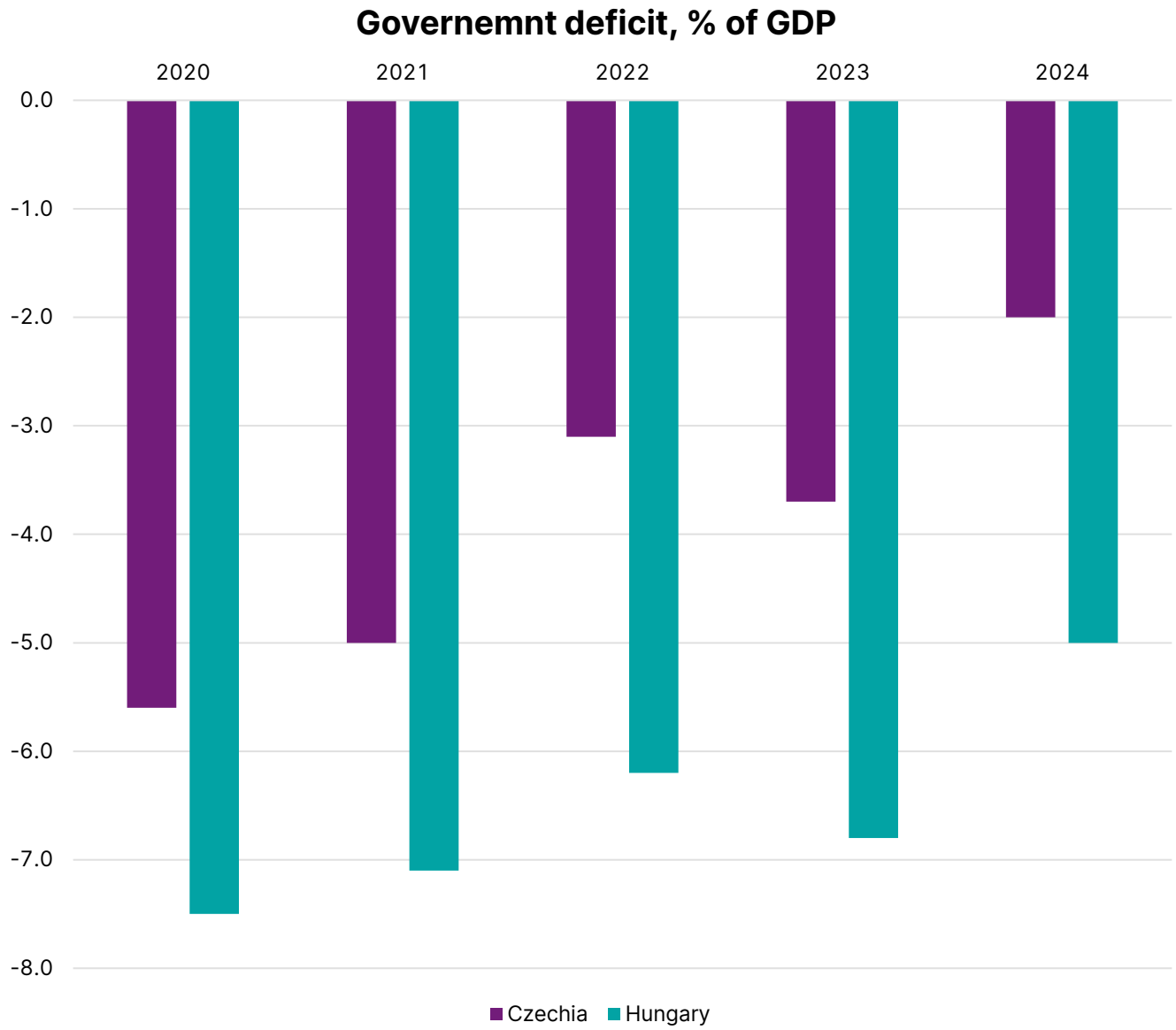


Firstly, Czech exporters have succeeded in compensating for weaker demand from Germany by exporting to other countries. The share of exports to Germany in total exports decreased from nearly 33% in 2023 to approx. 31.5% in the first three quarters of 2025. The share remains sensitive to recovery in Germany, however. Secondly, the share of services in GDP is gradually increasing. Recently, households are likely consuming more domestic services at the expense of imports. Finally, the construction sector significantly contributes to the growth, influenced by both the economic recovery and the preparation for projects that had stalled for many years.

Fiscal consolidation could have slowed recovery in Czechia

In Hungary, fiscal policy tends to be pro-cyclical and strongly influenced by election cycles. Following a consolidation amounting to 2% of GDP in 2024, the primary balance is expected to deteriorate in 2025 and 2026, while the ESA-based deficit is projected to remain around 5% of GDP for longer, increasing the likelihood of a rising public debt trajectory.

In Czechia, the government deficit remains relatively low, supported by fiscal consolidation from January 2024 and ongoing surpluses in local government budgets. However, with the new government taking office, an increase in the deficit is generally expected. Its share of GDP could increase to 2.4% with upside risk.



Source: Erste Group Research
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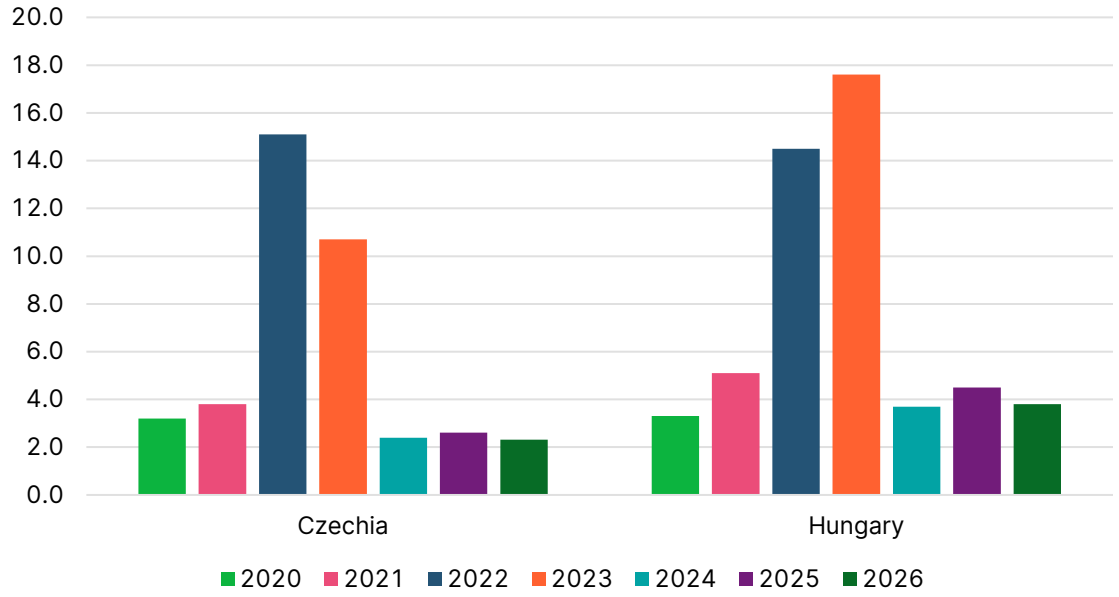
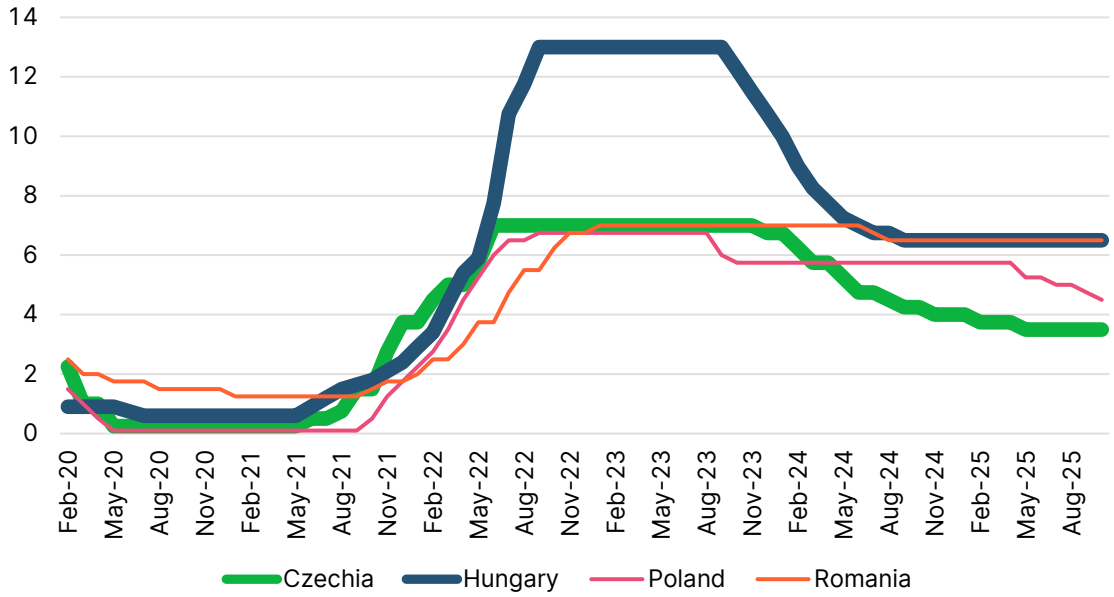
Different policy paths behind divergent performance

Easing inflation and monetary easing cycle

Inflation development, %



Key policy rate development, %



Inflation peaked in Czechia in 2022 , while in Hungary inflation was the highest in 2023. While in Czechia, inflation returned toward the target of 2% in 2024, in Hungary, it remains elevated. The monetary response to the inflation shock has also been quite different. In Czechia, the key policy rate reached 7% at the peak, while in Hungary, the key policy rate was at 13%, with the effective interest rate much higher at 18% (one-day deposit rate was set at 18% in October 2022 in response to weakening of Hungarian forint). The monetary easing cycle, which was disrupted in Hungary due to volatility on the FX market, puts Czechia in a more favorable position as far as economic recovery is concerned.

Source: Erste Group Research
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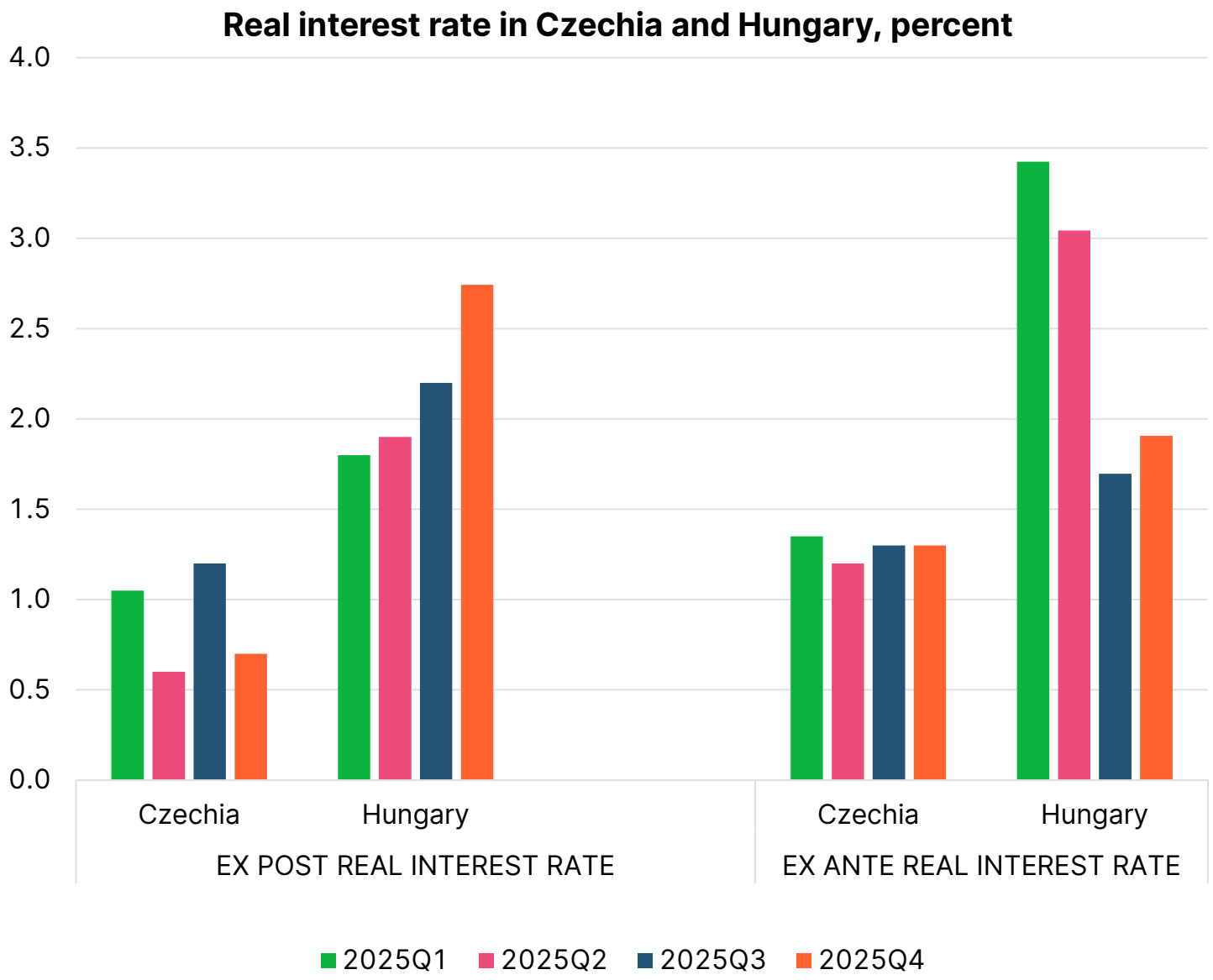


Real interest rate

The lower real interest rate in Czechia may also be considered a growth-positive impulse, when we try to look at the difference between countries that could possibly account for divergent development.

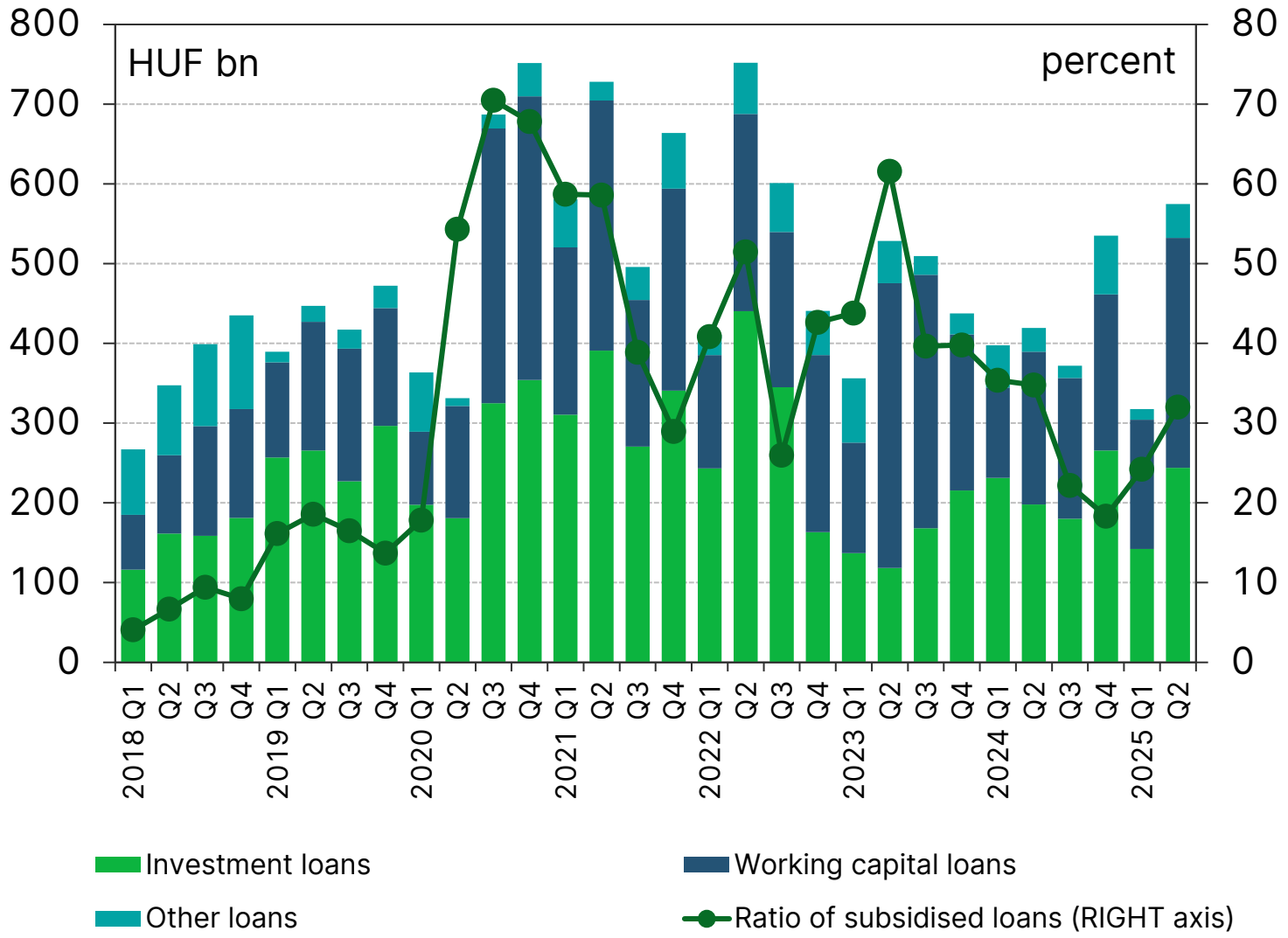
In general, both the ex-post real interest rate (central bank rate and inflation rate at the same period) and ex-ante real interest rate (central bank rate and expected inflation rate in one-year) are positive in most CEE countries. In Czechia, both ex-ante and ex-post real interest rates are much lower compared to Hungary.

Source: Erste Group Research
November 25, 2025

Monetary policy transmission

Not only does the level of real interest rate matter, monetary policy transmission channels are of importance as well in terms of the growth impulse. In Hungary, many subsidized lending programs offering lower rates for both households and corporates may weaken monetary transmission compared to Czechia and other CEE countries. On the other hand, in Czechia, the monetary transmission mechanism may be affected by increased borrowing in foreign currency. Such a development is a result of the recent tight CNB rate settings and the strong ties of Czech export sectors to the Eurozone.

New disbursements of SME loans by loan purpose and the ratio of subsidised loans



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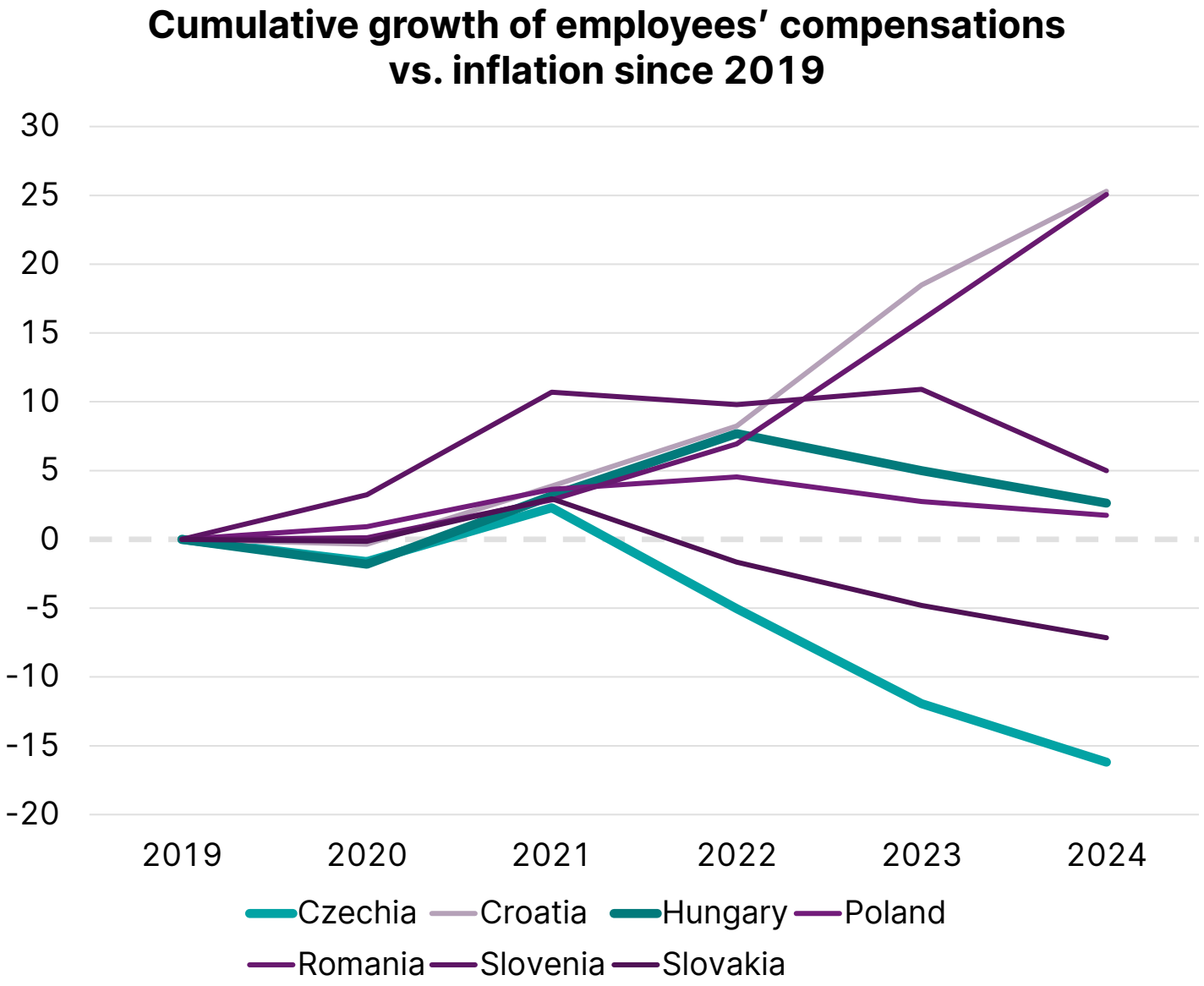
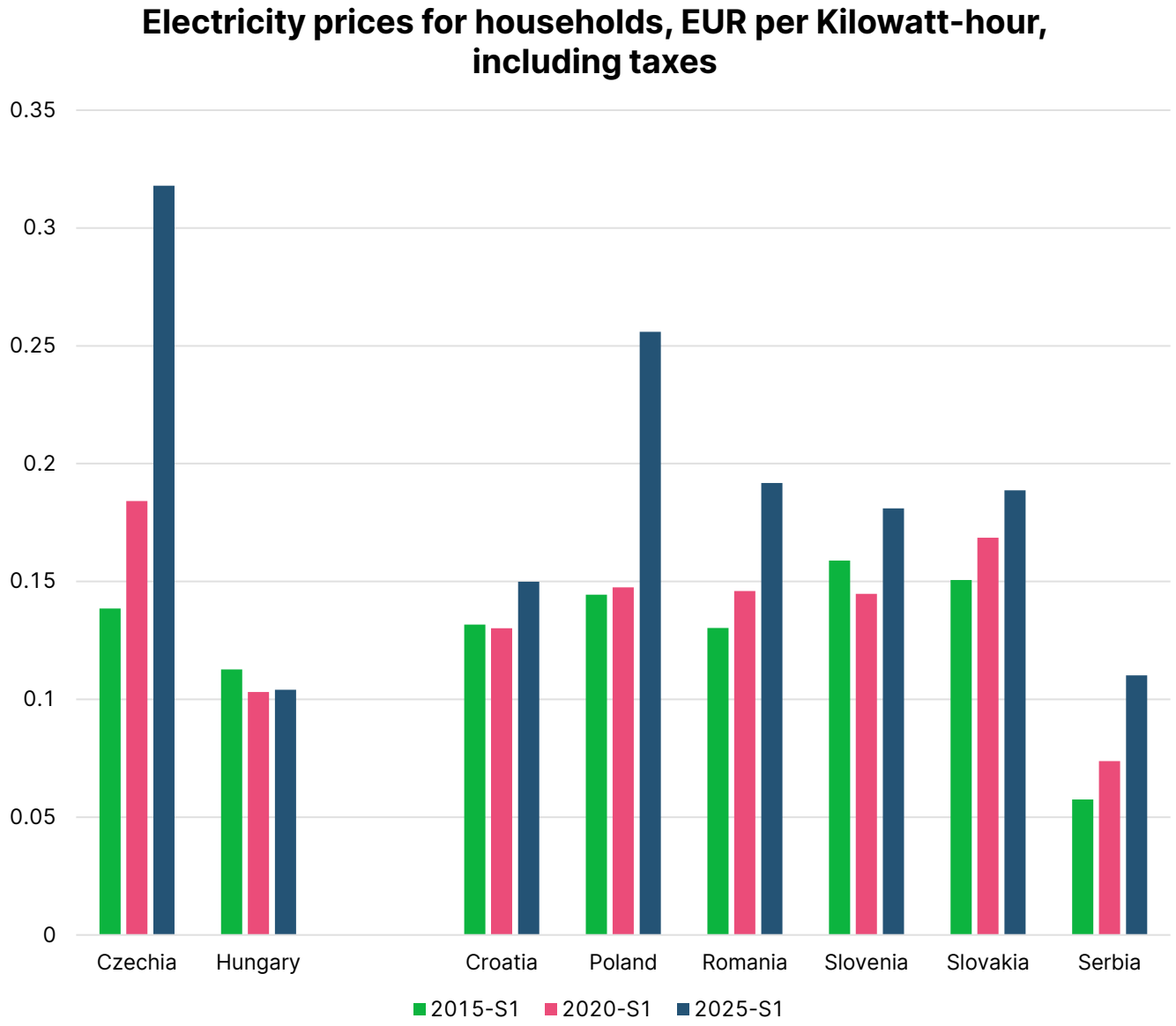


Households in Czechia were hit hardest in terms of real wage loss

Since 2019, cumulative growth of compensation has been much lower compared to the inflation change in Czechia and Slovakia. Czechia experienced the biggest loss of purchasing power over the last couple of years. At the beginning of 2023, the average real wage reached just under 89% of the level at the end of 2019. This was one of the factors behind the weak macroeconomic developments in the period following the end of the pandemic. In Hungary employee compensation grew marginally stronger than inflation, while Croatia and Romania clearly stand out.

Source: Erste Group Research
November 25, 2025



Energy prices increased most in Czechia

In Hungary, maintaining cheap energy prices for households has been a key element of the government policy for more than 10 years. Utility costs are administratively set and disconnected from market prices. During the 2022 energy crisis, some adjustments were made, but these mainly affected gas prices.

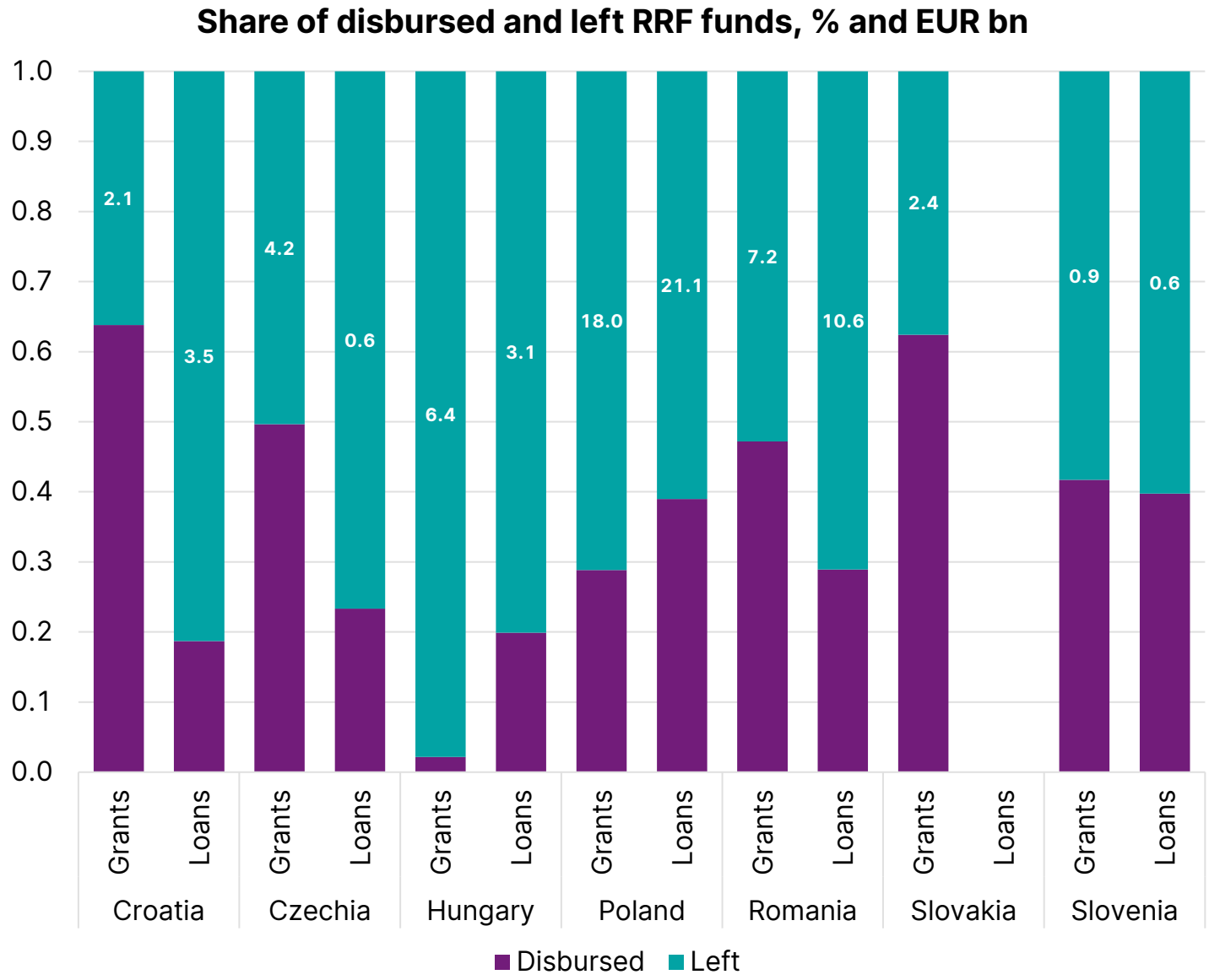
The limitation of previous electricity price support was part of the government's consolidation package from 2024. This, along with further increases in the regulated component of electricity, contributed to a significant rise in the overall price. The newly forming government plans to reduce electricity prices for both households and businesses to support the economy

Source: Erste Group Research
November 25, 2025

Hungary did not utilize RRF grants

Looking country by county, so far, only Croatia and Slovakia have had more than 50% of grants disbursed. Czechia follows with half of grants distributed as of August 2025. Hungary, on the other hand, is the only country in the region with minimal utilization of RRF funds.

Taking full advantage of RRF funds will be a priority next year and has the potential to support the growth in a more meaningful manner in 2026, the last year in which payments can be made.



Source: Eurostat, Erste Group Research
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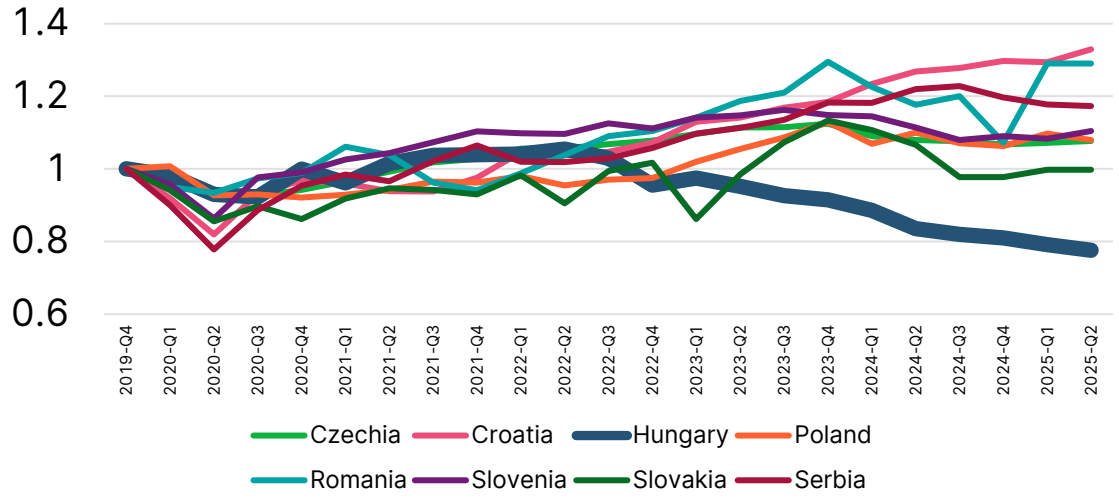
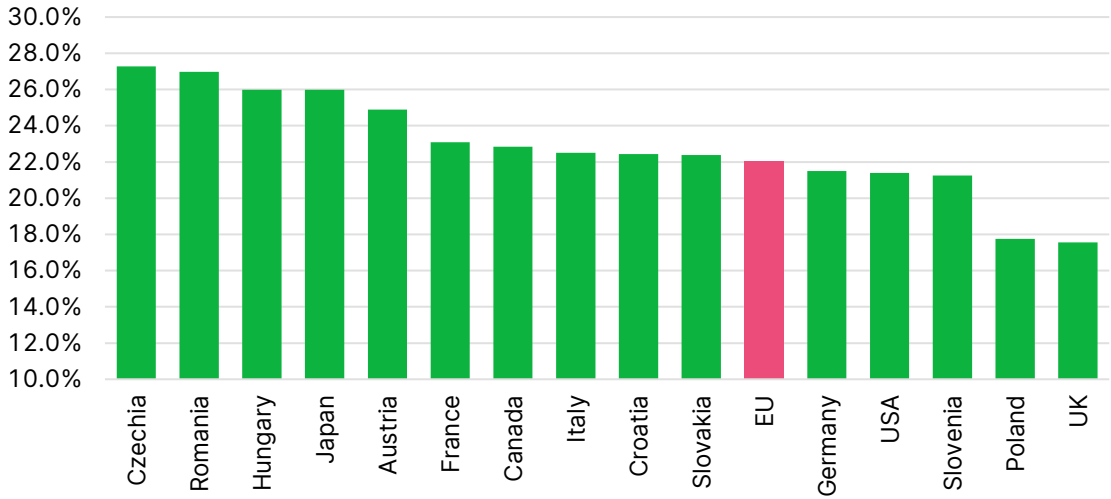
Falling investment in Hungary

Gross Fixed Capital Formation, 4Q19=1



Investment, share of GDP



One of the key developments affecting the weak economic development in Hungary is a visible fall of investment activity. It has to be noted, however, that the share of investment to GDP is one of the highest not only in the region but in Europe. It is thus falling from a high level. However, no other CEE country is in such a position as Hungary. Investment growth has been declining for three years in a row (continuous negative y/y growth since the third quarter of 2022). Hungary is also the only country that has not used the RRF funds almost at all. Disbursement of grants has been minimal (EUR 140mn out of EUR 6.1bn available) and roughly 20% of available loans have been drawn so far.

Source: Erste Group Research
November 25, 2025

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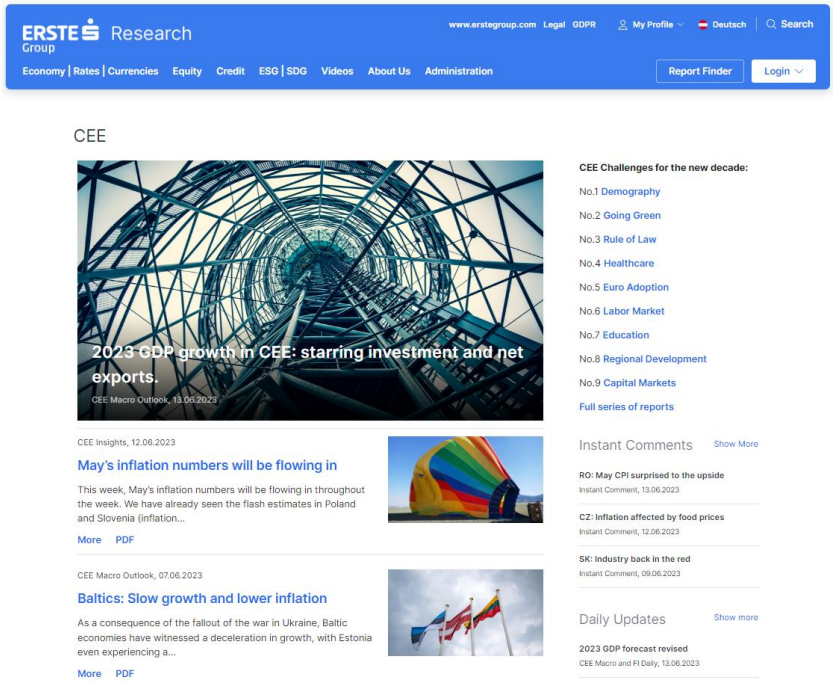

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