

## Hungary: Central bank to begin cautious normalisation

In Hungary, all the main inflation indicators are now above the central bank's target. The central bank has reached the point of no return and tightening is set to begin. However, we see a rather dovish hike and no pre-commitment to further action



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### What to expect from the NBH meeting

- The latest press release from the National Bank of Hungary delivered a clear signal that policy normalisation is around the corner. Core inflation, excluding indirect taxes, rose above the 3% target in February, which was highlighted as a trigger for the start of policy normalisation.
- This normalisation will consist of two components simultaneously: a 10 basis point hike in the overnight deposit rate to -0.05% and a HUF200-300 billion reduction in the outstanding amount of FX swaps, which will decrease the squeezed-out liquidity.
- The NBH will also reveal its updated GDP and CPI forecasts, but the full Inflation Report will be released two days after the rate setting meeting. We don't expect any material change in the figures, but we do look for the MPC to highlight risks to the forecasts. Due to the rather gloomy outlook in the external environment (including a more dovish European Central Bank and downgraded eurozone GDP forecast), we expect the NBH to emphasise

downside risks to the outlook for domestic inflation in the monetary policy horizon (five to eight quarters) and highlight its cautious and gradual approach once again.

- Looking forward, the most important meetings should be those associated with the release of new inflation reports. After March, we see hardly any material change in monetary policy until June. In the meantime, we expect core inflation to edge higher to 3.6-3.7% in 2Q19, which could fuel expectations of further hikes. But the NBH will overlook the short-term overshoot if it sees a significant domestic deceleration in 2020-21 accompanied by a gloomy global outlook.

## Impact on the forint

While the NBH may sound cautious and is unlikely to pre-commit to an aggressive tightening cycle, we don't look for a repeat of the 2Q18 price action when the forint sold off aggressively. Back in 2Q18, the market questioned the NBH's credibility. This time round, the NBH is regaining its credibility via the start of Bubor normalisation (albeit cautiously). This, coupled with speculators still being net short HUF, and HUF benefiting from a current account surplus, should mean we avoid an excessive sell-off in the forint.

## Impact on rates

Given the expected cautious NBH message and the fairly aggressive market pricing vs the likely ex post Bubor path, we expect HUF rates to grind lower across the curve with a flattening bias, the latter also being a function of the dovish stance of global central banks – the Fed and ECB – which should keep long-end yields in check.