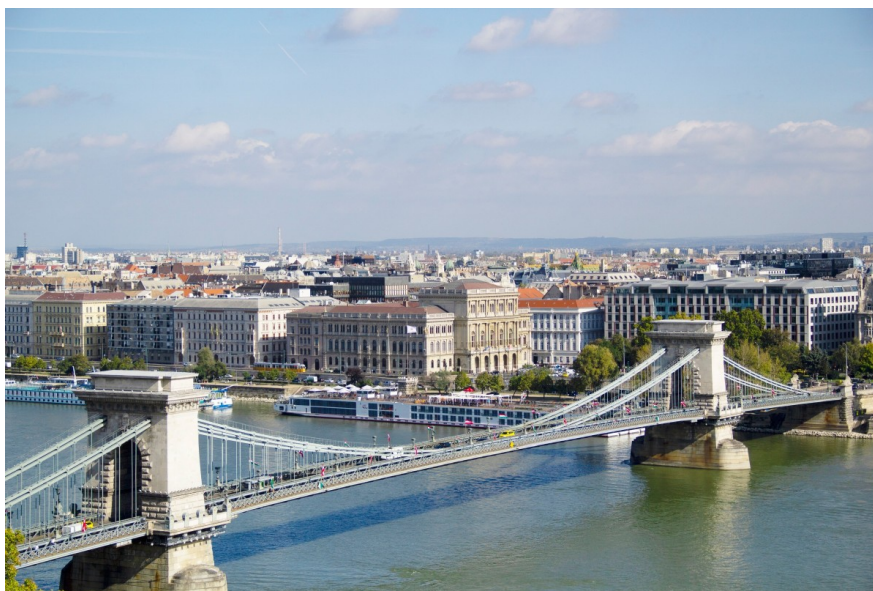


Monitoring Hungary: Improved growth is contingent on confidence

We're reassessing our Hungarian economic and market forecasts as subdued economic sentiment is again proving to be a growth headwind. We're maintaining our pessimistic growth outlook for 2024, but there are some more positive factors that balance the overall long-term picture



Hungary: At a glance

- High-frequency data since the first estimate of the second-quarter GDP data confirm our pessimistic view, therefore we still maintain our full-year GDP forecast for 2024 at 1.5%.
- Despite the recent (possibly temporary) positive monthly momentum in the industrial sector, both retail sales and construction output were major disappointments, casting a shadow over the year as a whole.
- The resilience of the labour market is remarkable, but we may need to see a decisive rise in consumer confidence to trigger a positive consumption impulse.
- As the external balance seems to remain intact on the back of weak domestic demand, we have increased our year-end current account forecast to 2.2% from 0.8%.
- A range of underlying inflation indicators have started to move higher, with services

inflation proving particularly sticky. We still expect inflation to move markedly above 5% by year-end.

- Though key interest rates remained on hold in August, we expect the National Bank of Hungary to deliver two more rate cuts in 2024, most likely in September and December.
- The fiscal picture has improved significantly in recent months, but unfortunately, this is more due to technical factors than a steady improvement in economic activity.
- We expect EUR/HUF to trade in the range of 390-400 for the rest of the year, with the lower end giving room for speculation for a more dovish NBH, while the upper end is proving to be a well-known hard resistance level.
- The short end of the FRA curve roughly aligns with our view. The long end of the IRS curve still offers good value supported by a synchronised global and local easing cycle, combined with an improvement on the fiscal side.

Quarterly forecasts

	2Q24	3Q24F	4Q24F	1Q25F	2Q25F	3Q25F	4Q25F	1Q26F
Real GDP (%YoY)	1.5	1.3	2.2	2.4	3.3	4.0	4.8	4.6
CPI (eop, %YoY)	3.7	3.6	5.5	4.4	5.1	4.2	3.7	3.5
Central bank key rate (eop, %)	7.00	6.50	6.25	6.25	6.00	5.75	5.25	5.00
3m interest rate (eop, %)	6.89	6.35	6.10	6.00	5.85	5.60	5.10	4.85
10yr yield (eop, %)	6.82	6.35	6.40	6.60	6.80	6.95	7.10	7.10
EUR/HUF exchange rate (eop)	395.2	393.0	395.0	400.0	408.0	400.0	405.0	408.0
USD/HUF exchange rate (eop)	369.4	350.9	359.1	363.6	370.9	363.6	368.2	370.9

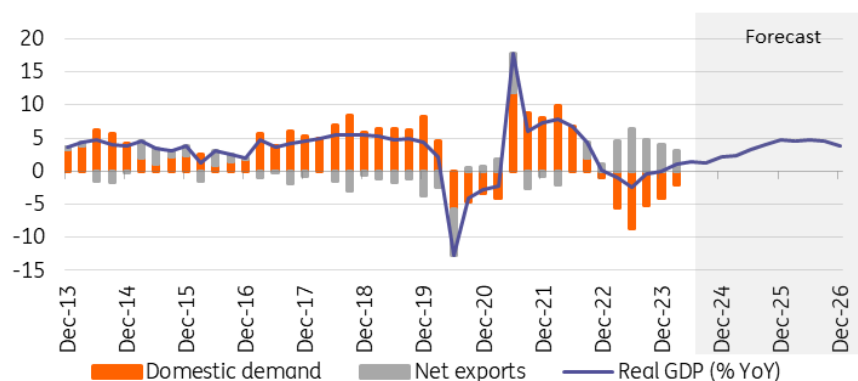
Source: National source, ING estimates

2024 outlook remains downbeat, but there are tailwinds for 2025

The Hungarian economy crawled out of stagnation in the first quarter of 2024, but the recovery was short-lived, as evidenced by the 0.2% quarterly contraction in the [second quarter](#) on a seasonally and calendar-adjusted basis. We are still waiting for the details, which are due on 3 September, but based on recent high-frequency data, domestic demand may have disappointed once again. So, we are maintaining our full-year GDP forecast of 1.5% for 2024, while we expect an acceleration in the growth rate to around 3.6% in 2025.

There are a number of factors that could prove to be tailwinds as we move into next year, such as an increase in both consumer confidence and household propensity to consume. In addition, the expected large retail coupon outflow in the first quarter of 2025 could also provide a further boost to consumption momentum.

Real GDP (% YoY) and contributions (ppt)



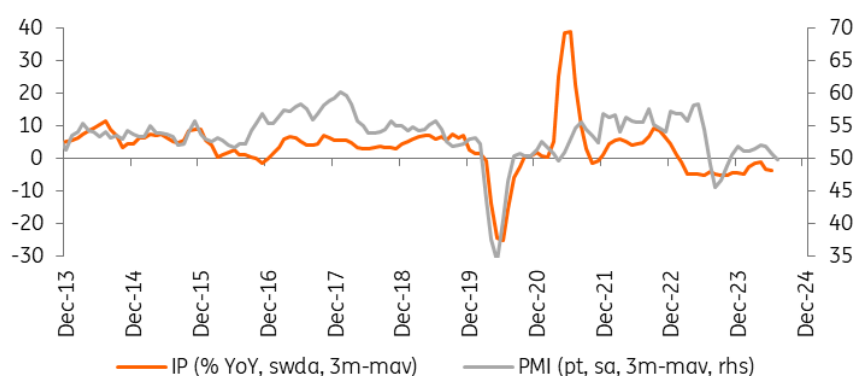
Source: HCSO, ING

Without a turnaround in external demand, industry will suffer

Industrial production surprised to the upside in [June](#), as production volumes rose by 0.5% month-on-month (MoM), contributing to a 3.7% year-on-year (YoY) decline in output on a working day basis. Compared with the average monthly volume in 2021, industrial production is 3.4% below the 2021 average level. The general industrial performance remains rather weak, which is not surprising given the state of external demand. In this regard, the export order book continued to deteriorate, falling 29.1% YoY in June.

While we expect industry to make a negative contribution to GDP growth in 2024, we are more optimistic about the outlook for 2025. We see a turnaround in the global inventory cycle, in addition to new FDI capacity, which should boost the trade surplus via the export side. Complementing the consumption boom, this could also open the door to more investment via improving business confidence.

Industrial production (IP) and Purchasing Manager Index (PMI)



Source: HALPIM, HCSO, ING

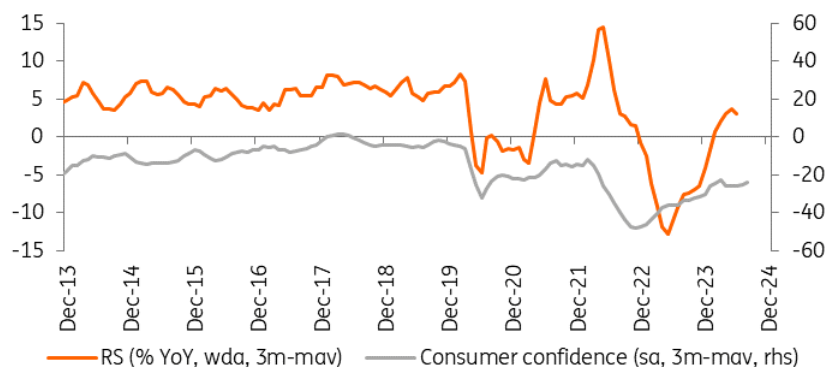
Stagnating consumer confidence limits the upside in retail sales

Retail sales volumes dropped by 0.1% MoM in [June](#), bringing the YoY figure to 2.6%, adjusted for seasonal and working day effects. At the component level, food retailing posted a 0.9% decline on

a monthly basis, which has been the largest monthly decline so far in 2024. In contrast, non-food and fuel sales rose by 1% and 0.5%, respectively, underlining the fact that consumption isn't particularly lacklustre in every segment.

Remarkably strong wage growth so far hasn't translated into a sustained boost to retail sales, as the recovery in consumer confidence is proving to be very gradual. However, if that confidence were to improve further, this would likely lead to an increase in households' propensity to consume, which is the catalyst for next year's growth prospects.

Retail sales (RS) and consumer confidence



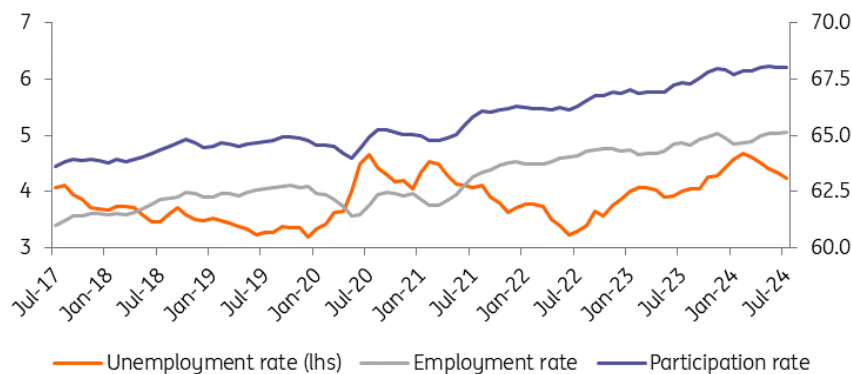
Source: Eurostat, HCSO, ING

Labour market strength without improved confidence remains barren

The recent improvement in labour market statistics continued in July, as the 3-month (May-July) unemployment rate moved to 4.2%, marking the fifth month of continuous decline; the loosening of the labour market has stalled as the increase in the number of full-time employees confirms. This may be one of the reasons for the exceptionally strong wage outflow data we saw in the first half of the year.

Even though the latest wage growth figure indicated a slowdown to 13.3% YoY in [June](#), the pace of real wage growth has remained above 9% for a seventh consecutive month. In our view, households are in a relatively good position from an accrued income perspective, but we may need to see a decisive rise in consumer confidence to trigger a shift from savings to consumption.

Historical trends in the Hungarian labour market (%)



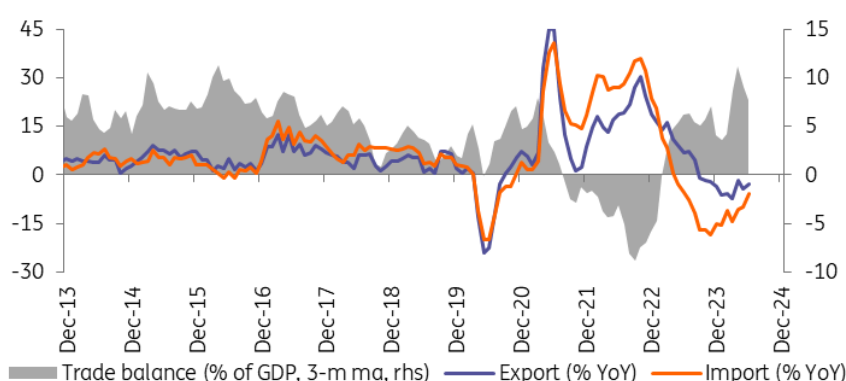
Source: HCSO, ING

We're raising our forecast for the current account balance in 2024 to 2.2%

While the value of exports fell by 5.8% in the first half of 2024, the value of imports fell by a significant 10.8%, hence the persistent trade surplus despite continued weakness in industrial export sales. The latest June figure shows a change in direction, with exports falling more sharply than imports. Nevertheless, June still brought a large trade surplus of EUR1.1bn, as exports were still higher than imports in nominal terms.

We believe that the general trend we've seen so far will continue throughout 2024, leaving the country's external balance intact. As a result, we raise our forecast for the current account balance, which we expect to be around 2.2% of GDP in 2024, followed by a surplus of 2.3% next year.

Trade balance (3-month moving average)



Source: HCSO, ING

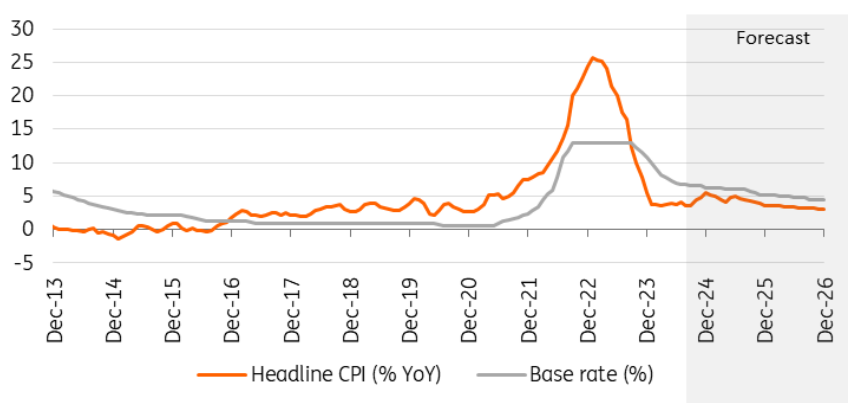
We still expect inflation to move markedly above 5% by year-end

Headline inflation increased, with the year-on-year rate rising to 4.1% in [July](#), while the monthly repricing was 0.7%, which means that the increase in the headline rate was mainly due to the

significant monthly repricing. In addition, a range of underlying indicators has risen further, signalling that Hungary still has an inflation problem. Going forward, we expect inflation to remain on an upward trend, with monthly repricing remaining above historical norms.

As a result, we expect both headline and core rates to creep back firmly above 5% by December 2024, while average inflation for 2024 could hover around 4%. Looking ahead to next year, a rise in consumer confidence could provide a positive consumption stimulus, which, in addition to the pass-through of tax increases, could revive corporate pricing power. As a result, we expect an uptick to 4.5% in average inflation for 2025 as a whole.

Inflation and policy rate



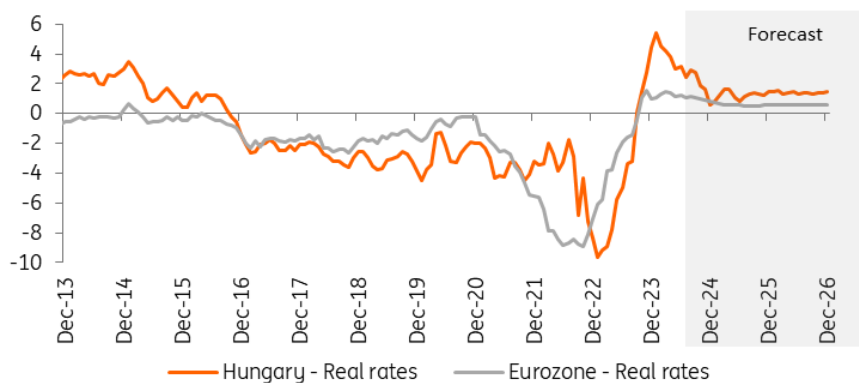
Source: NBH, ING

We expect two more rate cuts from the NBH in 2024

At its [August](#) meeting, the National Bank of Hungary (NBH) kept its key interest rate unchanged at 6.75% while maintaining the +/- 100bp symmetric interest rate corridor around the key rate. Although the central bank introduced a new buzzphrase, the stability-orientated approach, in practice, we expect the Monetary Council to make its decisions according to the same playbook. In this regard, we continue to focus on inflation, Fed/ECB moves and the country's risk perception.

The forward guidance was subtly changed. On the one hand, it suggests that this was only a temporary pause in the easing cycle, which is why we expect two further 25bp rate cuts in 2024 as the base case. On the other, it slightly alters the balance of risks in terms of the NBH's room for manoeuvre by shifting the focus a bit towards the Fed's decisions. If the Fed were to cut by 50bp in September, we think the NBH could deliver an additional 25bp of easing on top of our base case, assuming market stability prevails.

Real rates (%)



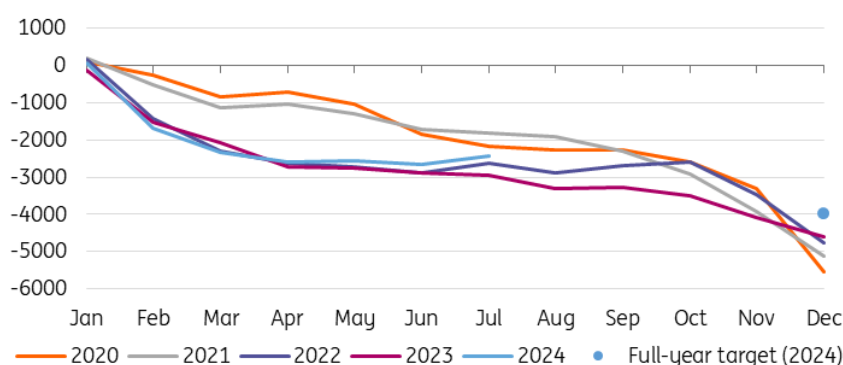
Source: ECB, NBH, ING

Fiscal landscape improves due to technical factors

The monthly budget surplus in [July](#) was HUF213bn, bringing the year-to-date general government cash flow deficit to HUF2.44 trillion. This means that the deficit has reached 61% of the planned financing needs in 2024. Underlying budgetary developments have improved, but this is more technical (the expenditure side is tightly controlled) than due to improved economic activity and, hence, better indirect tax revenues.

Recently announced measures contribute to an overall budgetary improvement of around 0.6% of GDP in 2024, increasing the chances of achieving the deficit target. However, sluggish economic activity poses a downside risk to the overall budgetary performance, and we, therefore, maintain our forecast of a year-end deficit in the range of 4.5-5.0% of GDP.

Budget performance (year-to-date, HUFbn)



Source: Ministry of Finance, ING

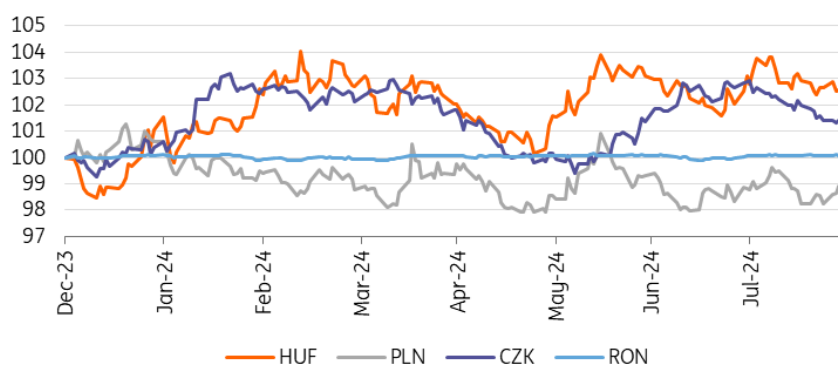
Continued easing cycle might put a floor below EUR/HUF at 390

EUR/HUF moved from just below 400 to 392 over the course of August, with the last two weeks of the month trading at the lower end of the range. Of course, the market has priced out roughly one rate cut, and at the same time, the rally in core rates has helped the forint with support from a higher EUR/USD. Overall, the external environment is supportive for the HUF, as the upcoming Fed easing cycle is almost certain, which increases the NBH's room for manoeuvre. Precisely for this

reason, we believe that the 390-392 EUR/HUF range will be a reason for an upside reversal as market players would speculate that positive FX developments would open a window of opportunity for the NBH in the face of a more dovish Fed.

For the rest of the year, we retain a trading range view of 390-400 EUR/HUF as we expect two additional rate cuts from the NBH and a more complicated situation with rising inflation and a weaker economy than markets currently are anticipating. In our base case (2x25bp cuts), we would see EUR/HUF more likely trade in the lower half of this range, while in our alternative scenario (3x25bp cuts), we believe the forint could more likely find support in the upper half of the range.

CEE FX performance vs EUR (29 December 2023 = 100%)

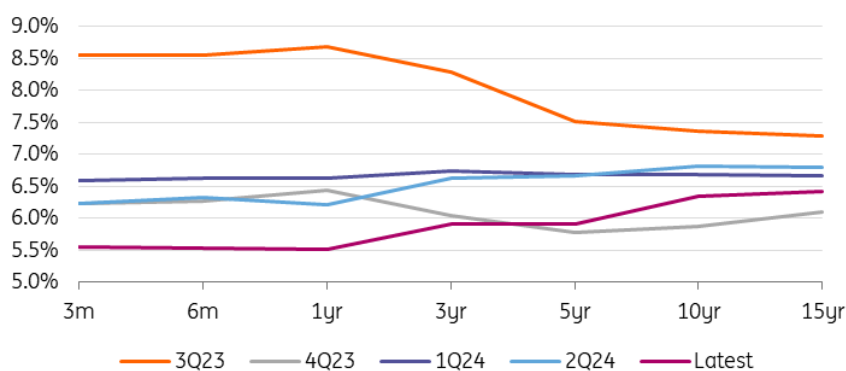


Source: NBH, ING

The long end of the curve has room to go down on dovish stance

After a correction in very dovish pricing sparked by the July inflation print, the FRA curve indicates around 47bp of additional cuts for this year, which is roughly close to our own view. The terminal rate has come back from the early August lows of 4.60% to the current 5.08%, but the slope of the IRS curve remains almost unchanged. We believe the entire curve thus has room to go lower again and may offer the best valuations within the CEE region, especially at the longer end of the curve and at a premium over core markets. Thus, if we see further signals from the Fed and ECB, we think this will attract receivers into the HUF market again, supported by NBH dovishness.

Hungarian sovereign yield curve (end of period)



Source: GDMA, ING

We are similarly positive on Hungarian government bonds (HGBs), which retain the most market interest in the CEE region. On the supply side, the debt agency has covered roughly 80% of this year's HGBs issuance, according to our calculations. Meanwhile, the latest budget data showed an improvement and raises hopes for meeting this year's fiscal deficit target of 4.5% of GDP. This would allow for a reduction of supply over the rest of the year or a focus on pre-funding next year's needs, freeing the debt agency's hands. Overall, we thus see conditions for HGBs rallying while valuations remain rather neutral versus CEE peers.

Forecast summary

	2Q24	3Q24F	4Q24F	1Q25F	2Q25F	2023	2024F	2025F
Real GDP (%YoY)	1.5	1.3	2.2	2.4	3.3	-0.9	1.5	3.6
CPI (eop, %YoY)*	3.7	3.6	5.5	4.4	5.1	17.6	4.0	4.5
Central bank key rate (eop, %)	7.00	6.50	6.25	6.25	6.00	10.75	6.25	5.25
3m interest rate (%)*	6.89	6.35	6.10	6.00	5.85	13.98	7.43	5.73
10yr yield (%)*	6.82	6.35	6.40	6.60	6.80	7.56	6.43	6.77
EUR/HUF exchange rate*	395.2	393.0	395.0	400.0	408.0	382.0	392.4	401.6
USD/HUF exchange rate*	369.4	350.9	359.1	363.6	370.9	353.3	358.6	365.1

*Quarterly data is eop, annual is avg. Source: National sources, ING estimates

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