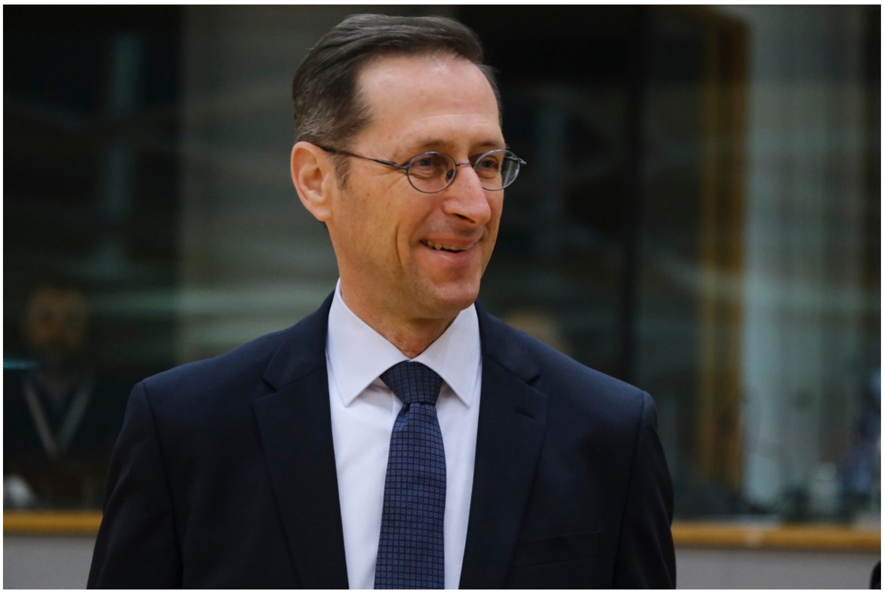
National Bank of Hungary review: Worsening macroeconomic outlook

The first rate-setting meeting under Governor Varga brought little excitement, as interest rates were left unchanged. Due to the hawkish rhetoric, we expect rates to remain steady throughout the year. Meanwhile, the updated staff projections reveal a deteriorating economic outlook



National Bank of Hungary Governor Mihaly Varga

6.50%

Key interest rate

Unchanged

We expect rates to remain on hold

The latest upwardly revised staff projection of the central bank is getting closer to our very own inflation forecast, yet we see inflation being even stronger. While price curbs can provide a temporary relief, loosely anchored price expectations and the looming tariff war point to further upside risks to inflation. In this environment, it is really hard to argue for monetary easing.

When it comes to possible rate hikes, based on the updated forward guidance and Mr Varga's messages during the press conference, the central bank doesn't feel the urgency to put rate hikes back on the table. And while all options are on the table should the need arise, we believe that the Monetary Council will rather wait for more clarity on the risk factors mentioned above.

Against this backdrop, we think it is safest to assume that the policy rate will remain at 6.50% for the rest of the year. We do not completely rule out the possibility of a deviation from this towards the end of the year, but the chances of this happening are rather low, given the inflation risks.

On the contrary, with a significant tightening of liquidity (about HUF3,000bn of the HUF10,000bn of excess liquidity in the banking sector) in the rest of the year, we could see more room for some unconventional easing via balance sheet measures (another iteration of the Funding for Growth Scheme, the Bond Funding for Growth Scheme and/or an asset purchase programme for government bonds, all with some green flavour).

New governor, same decision

In our NBH preview, we argued that despite the recent relative strength of the Hungarian forint, the deteriorating overall inflation picture would lead to a no change decision. The outcome of the March meeting – the first under the new regime led by Governor Varga – therefore came as no surprise.

The National Bank of Hungary left its key interest rate unchanged at 6.50% on 25 March. This was the sixth consecutive decision in which the policy rate and the interest rate corridor (+/- 100bp) remained unchanged.

Inflation remains the No. 1 enemy

The central bank's main message is loud and clear and virtually unchanged from previous months: the inflation outlook has worsened compared with previous expectations and the NBH's main objective remains to fight inflation. The central bank's task has not become any easier in recent months, given the upside surprises in price pressures, the further rise in households' and firms' price expectations and the increasing upside risks.

Governor Varga used the same wording as Deputy Governor Virág: a stability-orientated, cautious and patient monetary policy is needed. Tight monetary conditions, i.e. sustained positive real interest rates, are necessary to achieve price stability over the monetary policy horizon. Speaking of which, the NBH now expects inflation to reach the 3% inflation target only by the end of 2026.

Forward guidance points to unchanged rates in the foreseeable future

The Monetary Council statement and Varga’s press conference can be considered hawkish. However, based on the immediate market reaction, not hawkish enough. In our view, market expectations and pricing of the possibility of future rate hikes were exaggerated. The press conference was a reality check in this regard.

Governor Varga made it clear that while the Monetary Council is ready to change its stance if necessary (even by holding an ad-hoc meeting), based on the information currently available, the Monetary Council was unanimous in its decision at the March meeting and there was only one option on the table: to keep rates on hold. The new governor also reiterated what we have been hearing lately: the central bank is prepared to keep the interest rate at its recent level for the foreseeable future.

Updated GDP and CPI forecasts of the NBH (% YoY)

	2025	2026	2027
Change in real GDP - March projection	**1.9 – 2.9**	**3.7 – 4.7**	**2.8 – 3.8**
Previous NBH projection	2.6 – 3.6	3.5 – 4.5	2.5 – 3.5
Change in consumer prices - March projection	**4.5 – 5.1**	**2.9 – 3.9**	**2.5 – 3.5**
Previous NBH projection	3.3 – 4.1	2.5 – 3.5	2.5 – 3.5

Source: NBH, ING

The updated GDP and CPI forecasts

The full macroeconomic assessment and outlook will be published with the March Inflation Report on 27 March. In general, based on the latest GDP and inflation forecasts, the NBH's view has become gloomier. This implies a worsening outlook for GDP growth in 2025 and higher inflation in 2025 and 2026.

In contrast to previous press conferences with Deputy Governor Virág, Governor Varga did not shed too much light on the drivers behind the updated outlook. Reading between the lines, the inflation surprises and the higher-than-usual repricing at the beginning of the year could be behind the change in inflation forecasts. The weaker economic outlook could be due to the lack of external demand, weaker consumer and business confidence and further delays in new export capacity coming on stream.

Regarding the alternative scenarios, the Monetary Council highlighted four main scenarios: rising trade tensions, deterioration in emerging market sentiment, easing of geopolitical tensions and fiscal stimulus in Europe. In our view, the balance of these alternative scenarios points to upside risks to inflation and balanced risks to growth.

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