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Opinion

Hungary: A close call on Fitch review

Despite pros outweighing the cons, S&P only affirmed the Hungarian sovereign debt rating. This time we have a chance with Fitch, but don't hold your breath

The factors

After a bit of a disappointing decision by S&P, we see it as more likely that Fitch will join the club, affirming Hungary's 'BBB-' sovereign credit rating, and keeping the positive outlook. Given the fact Fitch gave Hungary an outlook upgrade in November 2017 and affirmed that in March 2018, we don't see the elapsed time as being long enough to justify an upgrade. Moreover, we see it probable that Fitch will just skip the review.

> Fitch gave Hungary an outlook upgrade in November 2017

Regarding Fitch Ratings' latest comment about a possible upgrade, they pointed out: "the main factors that could lead to a ratings upgrade include a continued reduction in external indebtedness and improved external liquidity supported by current account surpluses; increased confidence in the economic policy framework and improved business environment; and a sustained decline in state debt as a percentage of GDP."

> The decrease in net external debt and the strong growth are supporting the upgrade...

Taking into consideration the above-mentioned factors, and first of all, the pros, we saw the latest net external debt reading decreasing further to 11% of GDP in 1Q18. Besides this, the economy posted 4.5% YoY growth in 1H18, exceeding the rating agency's forecast of "around 4%" YoY GDP growth. Another important factor to consider is that S&P is more sensitive to politics, so if Fitch only relies on hard data, that would be supportive.

> The lack of improvement in potential growth and demographics are dampen our chances

However, there are still some cons supporting the non-action by Fitch even when it comes to hard data. The current account surplus decreased to 3.1% of GDP in 1Q18, which is the latest available data for Fitch to consider. Moreover, EM geopolitical risks are still affecting Hungary, and the financing need of the budget threatens the debt reduction path too. In line with S&P, Fitch also emphasized the potential growth as a decisive factor in a rating upgrade, pointing to the unfavourable demographics and labour shortages, which have already pulled back the economic expansion, a non-action is more likely, in our view.

The verdict

We rather call a wait-and-see decision (or skipped review) by Fitch, especially in light of the S&P decision. When it comes to the rest of 2018, Moody's still has one more review, although an upgrade would be a huge surprise from the agency, as the outlook is only stable. If anything, an outlook upgrade is the best that Hungary can achieve. As for market moves, we maintain our earlier opinion that the market won't consider any scenario as a game changer since Hungary has already been priced as a 'BBB' category sovereign.

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