Hungary: Inflation drops big on services

Although we expected inflation to start falling, we didn't expect it to start as early as September. The main factors behind the disinflation are IT and recreational services

Shoppers in Budapest

3.4%

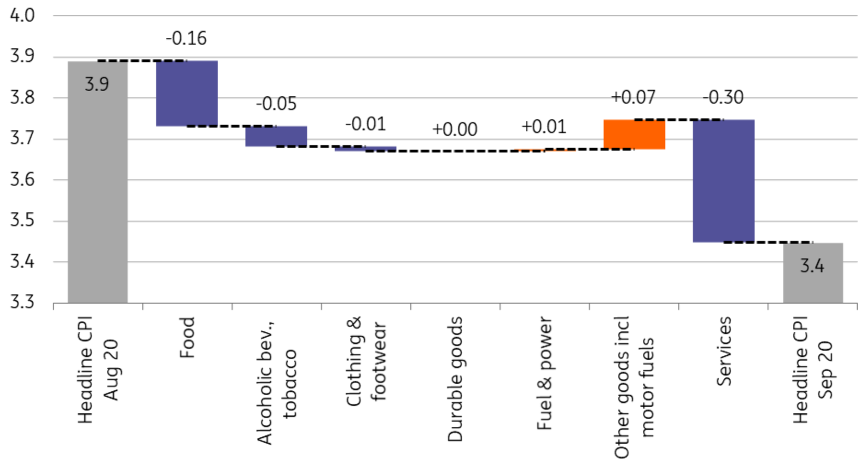
Headline CPI (YoY)

Consensus 3.9% / Previous 3.9%

Lower than expected

Headline inflation came in at 3.4% year-on-year in September, a 0.5 percentage point deceleration compared to the August reading and a major downside surprise. Although we expected something similar in the months ahead (due to the high base), we didn't expect it to start as early as September. The strong deceleration was mainly driven by services.

Main drivers of the headline CPI change (%)

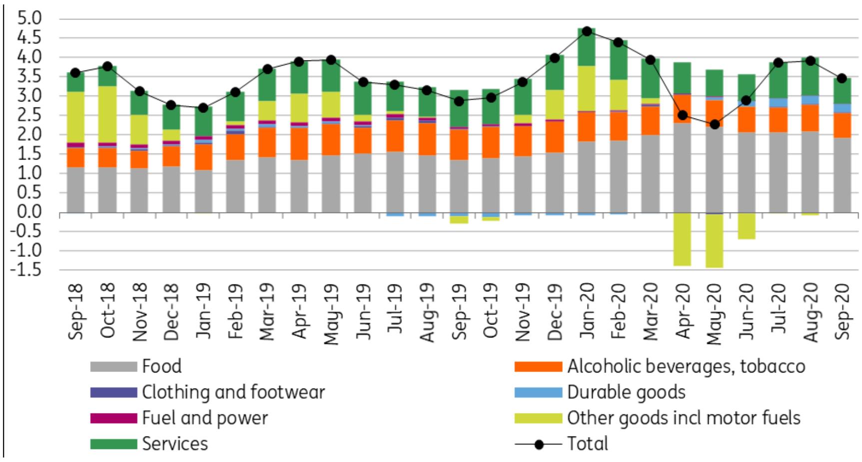


Source: HCSO, ING

The breakdown

- Inflation in services came in at 2.4% year-on-year, the lowest reading since December 2018. However, if we really want to see a long-standing record broken, the month-on-month change was -0.9%. The last time prices in services dropped so much was back in September 2009;
- Prices of recreational services dropped by almost 7% month-on-month, a surprise as we expected recreational prices to remain elevated to make up for some of the losses generated by Covid. Moreover, prices of internet and telephone services also dropped by 1.5% MoM in September, while exactly a year ago there was an extreme one-off increase of 3.1% MoM;
- Inflation in food decelerated to 7.3% YoY, mainly on meat and dairy products, while prices of seasonal fruits, vegetables and potatoes remained elevated. Meals at restaurants became 8.1% more expensive on a yearly basis;
- Prices of durables increased by 2.6% YoY, showing no easing in price pressures, while clothing prices eased somewhat. Fuel prices increased by 0.5% MoM, meaning that prices matched the levels seen last September.

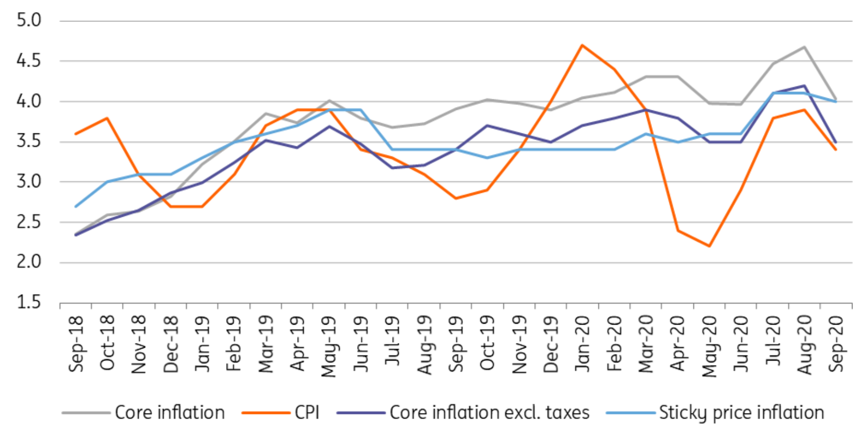
The composition of headline inflation (ppt)



Source: HCSO, ING

Against this backdrop, we can see that it was mainly core factors that were responsible for the significant easing in price pressures. Core inflation fell by 0.7ppt to 4.0% YoY, a downside surprise. It is now back at the top of the National Bank of Hungary's 2-4% target range. As part of the inflation is caused by an excise duty hike, core inflation excluding indirect taxes came in at 3.5% YoY, well within the target range.

Headline and core inflation measures (% YoY)



Source: HCSO, NBH

What's next?

All this means that the pressure has significantly eased on monetary policy as all the major inflation indicators are now in the target range. But it is not just about monetary policy. Real interest rates have also improved significantly, which also supports Hungary's forint. However, we hardly see today's data being a game changer for monetary policy. We expect the NBH to hold rates steady, and don't see a quick reversal of the last implicit rate hike.

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