Monthly repricing in Hungary back to elevated levels

The structure of inflation remains worrying, driven by high monthly repricing for both the headline and core baskets. In our view, the upside surprise to the central bank's forecast is likely to prompt the Monetary Council to keep rates on hold in August

Source: Shutterstock

4.1%

As expected

Headline inflation (YoY)

ING estimate 4.1% / Previous 3.7%

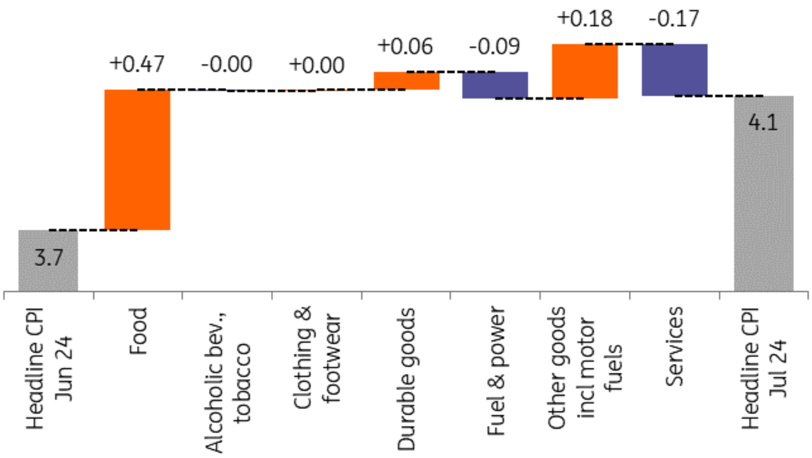
High monthly repricing similar to earlier in the year returns

The year-on-year (YoY) Hungarian inflation figure rose moderately in July, matching our own expectations but at the same time delivering an upside surprise versus the market consensus. Compared to June, headline inflation rose by 0.4ppt to 4.1% YoY, while the monthly repricing was

0.7%, which means that the increase in the headline rate was mainly due to the significant monthly repricing. At the same time, it's worth noting that after two months of stagnation in the monthly rate of price increases, we're now seeing the same dynamic pace of one-month inflation that we've seen in the first four months of the year.

What's more, the strong monthly repricing not only concerns volatile items but also elements within the core basket. This, in turn, underscores our long-held view that the structure of inflation in Hungary remains worrying. As the National Bank of Hungary had expected a headline rate of 3.8% for the July inflation print, the upside surprise relative to its forecast makes a hold on rates more likely in this risk environment than a rate cut in August.

Main drivers of the change in headline CPI (%)

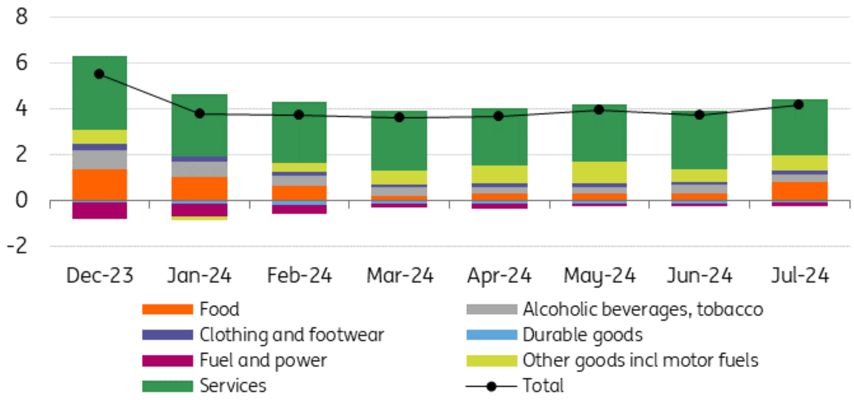


Source: HCSO, ING

The details

- Food prices rose by 0.6% month-on-month, probably as a result of the removal of price caps and mandatory in-store discounts. As a result, the annual food inflation rate rose to 2.7%, with both processed and unprocessed food prices recording monthly increases.
- Fuel prices increased by 3.8% MoM, which alone contributed to a 0.2ppt increase to the monthly repricing. We expected household energy prices to rise as a result of the high use of air conditioning due to the very warm weather, but energy prices ended up falling.
- Prices of durable goods rose by 0.3% on a monthly basis, posting the largest increase since January 2024. At the same time, prices of clothing and footwear declined by 1.2% MoM, which is also the largest decline for the past six months.
- Services inflation came in at 1.1% MoM, but due to last year's high base, the annual rate fell to 9.1%. Within services, the main increases were in recreational and postal services. In terms of annual headline inflation, the services component explains roughly 60% of total inflation.

The composition of headline inflation (ppt)



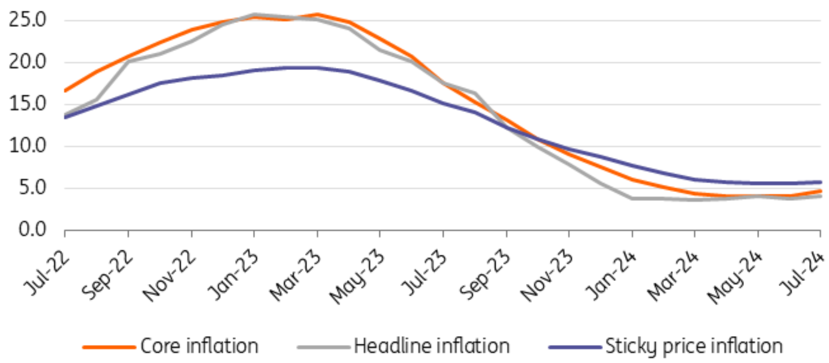
Source: HCSO, ING

A range of underlying indicators move in the wrong direction

Core inflation rose by 0.6ppt to 4.7% YoY in June, as a result of a 0.7% MoM increase in prices of core items. This is the second time in a row that this underlying indicator has risen and will continue to do so in the coming months. The monthly rate of 0.7% is almost three times the rate that would have been compatible with the 3% inflation target. In our view, the overall inflation picture has therefore deteriorated and is rather unfavourable.

This is also evidenced by the National Bank of Hungary's measure of inflation for sticky prices, which rose to 5.8% YoY in July. To put this in perspective, this is the first time since March 2023 that the measure of sticky prices has increased. Moreover, an important short-term indicator, the three-month-on-three-month annualised core inflation measure, has also increased. Therefore we can conclude that a range of underlying indicators signal that Hungary still has an inflation problem under the surface.

Headline and underlying inflation measures (% YoY)



Source: NBH, ING

The next two months might be favourable, but inflation remains in a clear upward trend

Looking ahead, the next two months may see some easing in the year-on-year inflation rate, mainly due to last year's high base, but the rate should remain close to 4%. The next big jump in inflation is expected to come in October when the figure could be well above 4%. Looking at current underlying inflation trends, we see a return to a rate of 5.0-5.5% YoY by December 2024.

According to the latest data flow, the Hungarian economy is performing weakly. As a result, significant inflationary pressures from the domestic demand side are unlikely in the short term. On the other hand, the labour market remains strong and wage outflows are higher than expected, which could put further upward pressure on services prices. Moreover, the recent tax increases announced by the government are likely to be passed on to consumers in the form of higher prices. All in all, therefore, the risks to the inflation outlook are essentially two-sided.

The structure of inflation might warrant a pause in the easing cycle

From a monetary policy perspective, the latest inflation data would clearly push the central bank towards a cautious stance when deciding on the level of the base rate. Indeed, the National Bank of Hungary's July CPI forecast was for a rate of 0.4% on a monthly basis. Of course, a lot can happen between now and the August rate decision, but at the same time, risk aversion in the financial markets has increased and the EUR/HUF is stuck in the 395-400 range. As a result, we now see a hold at the August meeting (27 August) as more likely than a cut, leaving the key rate unchanged at 6.75%.

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