

National Bank of Hungary Review: Flexible does not mean less hawkish

The National Bank of Hungary raised the base rate by 100bp and remains hawkish with its forward guidance. We maintain our above 8.25% terminal rate call. For FX & rates, fiscal policy will be more decisive than the monetary policy path as the central bank urged for fiscal rebalancing as well



The National Bank of Hungary in Budapest

5.40%

Hungary's base rate

ING forecast 5.40% / Previous 4.40%

As expected

Hawkishness remains, but uncertainty screams for flexibility

The Hungarian central bank raised the base rate and the whole interest rate corridor by 100bp at its April meeting, surprising no one. Now the base rate sits at 5.40%. Neither the briefing nor the press release contained any reference to the size of the 1-week deposit rate hike this Thursday.

We assume that another +30bp move to 6.45% will come.

The tone of the monetary policy message and the forward guidance has remained the same and points towards continued tightening. However, Governor Gyorgy Matolcsy made it clear that Hungary is facing a triple challenge: rising inflation, a deteriorating fiscal balance, and worsening external balance. And although the central bank is ready to do everything it can, fiscal policy needs to support this fight to be successful.

When it comes to the macroeconomic outlook, not much has changed. The central bank sees both headline and core inflation rising in the coming months. Inflation is expected to return to the central bank tolerance band in the second half of 2023 before reaching the central bank target of 3% in the first half of 2024. We see this forecast as realistic as we also agree with the central bank's latest view on first-quarter GDP growth at around 7-8% year-on-year.

The biggest change in April is that the central bank will give itself a bit more flexibility. Instead of signalling that April's rate decision is indicative of the coming months, decision-makers emphasised that step sizes will be decided monthly. Decisions will be affected by changes in actual inflation and the inflation outlook as well as the outcome of risk events. The uncertainties and risks are plenty: the war and its implications, the approaching fiscal rebalancing, the impact of energy prices on the external balance and the outcome of the rule-of-law procedure.

Even one of the above should justify more flexibility in monetary policy. Thus, in our view, this simply means that the NBH switches to a more data- and event-driven mode as uncertainties mount, and we don't see this as a shift on the dovish-hawkish scale. We maintain our view as of now that May will bring the same 100bp hike in the base rate.

FX and rates markets to resonate more on fiscal shifts

We believe that the central bank is committed to tackling inflation with tighter monetary conditions. The fact that the NBH envisions a constant improvement in the real interest rate environment in coming quarters is also supportive for the forint. However, all the risks emphasised by the NBH (war, fiscal and external imbalances, rule-of-law debate) will keep investors on alert. We see EUR/HUF around 370 in the short run with a possible quick move to 355-360 should we see a sudden de-escalation in geopolitics or a pledge on strong fiscal rebalancing which would improve the external balance as well.

Considering recent market volatility and the current environment of rising core rates, we see room for rates to move higher, especially as we see an 8.25% terminal rate. On the FRA curve, we see the juiciest spot within six months. On the longer horizon (especially over one-year), the market is still pricing in higher levels than our rate forecast, but we don't expect the market to have a reason to lower its expectations in light of uncertainties and accelerating inflation.

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