# National Bank of Hungary Review: Normalisation remains a function of market stability

The National Bank of Hungary felt comfortable in continuing to cut interest rates. The 100bp cut to the effective rate is in line with consensus. The emphasis remains on cautiousness and graduality as ongoing easing remains a function of market stability

The National Bank of Hungary in Budapest

## Normalisation has continued in line with expectations

The National Bank of Hungary decided to repeat the move it made in May and cut the overnight collateralised lending rate (top-end of the rate corridor) by 100bp to 18.5% in June. More importantly, the central bank announced that from 21 June, the interest rate of the overnight quick deposit tender will be lowered to 16%. This means a 100bp effective rate cut. A similar change is coming to the interest rate of the overnight FX swap tender. This outcome was not a surprise.

The determining factor of the monetary policy normalisation remains market stability, which was emphasised several times during the press conference and in the statement. The Monetary Council remains cautious, and easing will be gradual as not all the risk-related hurdles have been cleared yet. A highlighted example of this was the recent volatility of global energy prices.

However, the NBH in general sees a continued improvement in the risk environment. Regarding the external developments, it sees an improving current account balance along with better terms-of-trade. Stability of FX, bond and swap markets is a welcome development as well. However, a key issue that the NBH emphasised as well is the energy (especially natural gas) price-related risks, which could result in volatility and uncertainty. When it comes to the general risk environment, risk aversion is reducing globally, but there is somewhat increased uncertainty regarding major central banks' monetary policies. Meanwhile, the Hungarian central bank sees the ongoing war in Ukraine as an unresolved risk factor, understandably.

With these remarks in mind, it is worth noting that the NBH made a slight rebalancing in the order of factors which are affecting the monetary policy. The updated forward guidance now puts the effects of international financial market developments on the domestic risk environment in first place, followed by incoming macroeconomic data and developments in the outlook for inflation. The inflation-related remark was also in third place in May, in line with the central bank's communication, which separates market and price stability issues.

## Minor tweak to the forward guidance

There is yet another minor, though maybe telling change in the forward guidance, in our view. In the Monetary Council's assessment, maintaining the current level of the base rate will ensure price stability, based on the June statement. In contrast, the May press release put it this way: "it is necessary to maintain the current level of the base rate over a prolonged period" to ensure price stability. This is a tiny shift, though this might be the first hint that after the expected merger of the effective rate with the base rate in September (which is only three months from now), easing will continue without a pause. In our assessment, this would be roughly in line with recent market pricing.

This change also aligns with the central bank's new balance-of-risk assessment. The Monetary Council identified three major alternative scenarios, where two contain disinflationary risks (quicker ease of supply constraints, lower-than-expected consumption) and one is pro-inflationary (stronger second-round effects in inflation). With this, the balance of risks is now tilted to the downside when it comes to the inflation outlook.

In general, we still see a central bank which is extremely measured in its decisions and trying to keep market stability in check despite an ongoing series of rate cuts. So far so good.

## The updated GDP & CPI forecasts of the NBH

The full macroeconomic assessment and outlook will be released with the June Inflation Report on 22 June. The GDP growth outlook remained unchanged compared to the March forecast for the entire time horizon. This is fully in line with what we were suggesting in our preview note. The forecast range of inflation in 2023 was narrowed to 16.5-18.5% (roughly matching our expectations). There is a 0.5ppt upshift in the forecast range in 2024 to 3.5-5.5%, reflecting the upcoming excise duty hike in fuel. This suggests that there is no structural or underlying change here, as according to our own calculation, the change in excise duty will boost average inflation by an additional 0.5ppt in 2024.

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