National Bank of Hungary review: The easing continues

The National Bank of Hungary cut its base rate by another 75bp, repeating last month's decision. The Monetary Council did a balancing act, while making the closest thing to a pre-commitment. We therefore expect the central bank to maintain this pace of easing in the coming meetings

The National Bank of Hungary in Budapest

11.50%

Key interest rate

ING forecast 11.50% / Previous 12.25%

As expected

No surprise in November

The National Bank of Hungary (NBH) reduced its base rate by 75bp to 11.50% at its November rate setting meeting. At the same time, the entire interest rate corridor was lowered by 75bp, maintaining the symmetry of the +/- 100bp range.

Although this was again a unanimous decision, the menu seen in October was also present at this rate-setting meeting. That is, the Monetary Council decided between a 50, 75 or 100bp cut. The statement and press conference made it clear what the reasoning was for sticking with the proverbial golden mean.

The pros and cons canceled each other out

A hawkish shift compared to the October meeting was dropped due to favourable incoming macroeconomic data. Hungarian inflation returned to single-digit territory, with the underlying monthly repricing pattern showing similarities to 2019-2020 (pre-shock pattern). The improvement in the external balance continued on the back of rising export capacity, supported by shrinking domestic demand, which reduced import needs and the energy balance also improved. Last but not least, together with the ongoing disinflation, the Hungarian economy exited the recession and the incoming high-frequency data suggest that the year-on-year print could return to positive territory from the fourth quarter of 2023.

However, all these positive changes have been accompanied by significant external risks. Geopolitical tensions and sanctions are still with us, and we can't rule out another shock to energy and commodity markets as a result. The armed conflicts in Ukraine and Gaza keep the economic landscape highly unpredictable. On the macroeconomic side, there are ongoing labour market tensions and recessionary fears in the international environment. Against this background, the Monetary Council decided to maintain its cautious approach and closed the door on the dovish 100bp easing option.

Steady as she goes

Even before today's official and explicit forward guidance, we expected the National Bank of Hungary to stick to the recent step size as the baseline pace of further rate cuts. During the background discussion, Deputy Governor Virág made it clear that – based on the latest information – the policy rate could fall below 11% by the end of the year and reach single digits in February 2024. We wouldn't go so far as to say that this is a pre-commitment, but it's certainly the closest thing to it. Such a rate path would imply a continuation of 75bp rate cuts up to (and including) the February rate-setting meeting.

In general, the statement and the press conference did not bring any changes either in the tone of monetary policy or in the main functions that influence monetary policy decisions. As a result, today's rate-setting meeting can be described as a well-managed non-event.

Our market views

After the NBH meeting, everything seems to be in line with market expectations and rates have not moved much. This is good news for the HUF, which has re-established a relationship with rates over the last three days and has weakened to 380 EUR/HUF before the meeting. Still, the recent rally in rates points to weaker HUF levels, but this will probably not be the case for now. A stable NBH and higher EUR/USD could offset this, plus we could see some progress in negotiations with the EU in the near term. Overall, today's meeting thus seems to be positive for HUF, which will halt the weakening from recent days. In the short term we probably need to see some catalysts for new gains, e.g. the EU story, but overall we remain positive on the HUF. If everything goes in a positive direction, then we believe EUR/HUF will move into the 370-375 range before the year ends. On the other hand, the current weakness probably hasn't changed the market's long positioning much and we should still keep that in mind if bad news comes.

Rates have rallied a lot in recent weeks and have closed the biggest gaps between market pricing and our forecast. But something is still missing to perfection and we still see the whole curve lower but rather flatter later. At the short end of the curve, we think the market needs to accommodate the set pace of 75bp rate cuts as the central bank confirmed today, while the long end remains significantly elevated also because of high core rates. Thus, as we mentioned earlier, the long end in our view has more potential to rally further and the curve has steepened too early and too quickly, closing the gap with the region.

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