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Deputy Governor | Magyar Nemzeti Bank

Analyst background discussion
28 January 2025

BACKGROUND DISCUSSION FOLLOWING THE MONETARY COUNCIL'S 28 JANUARY 2025 DECISION

MAIN MESSAGES:
MACROECONOMIC AND FINANCIAL MARKET ASSESSMENT

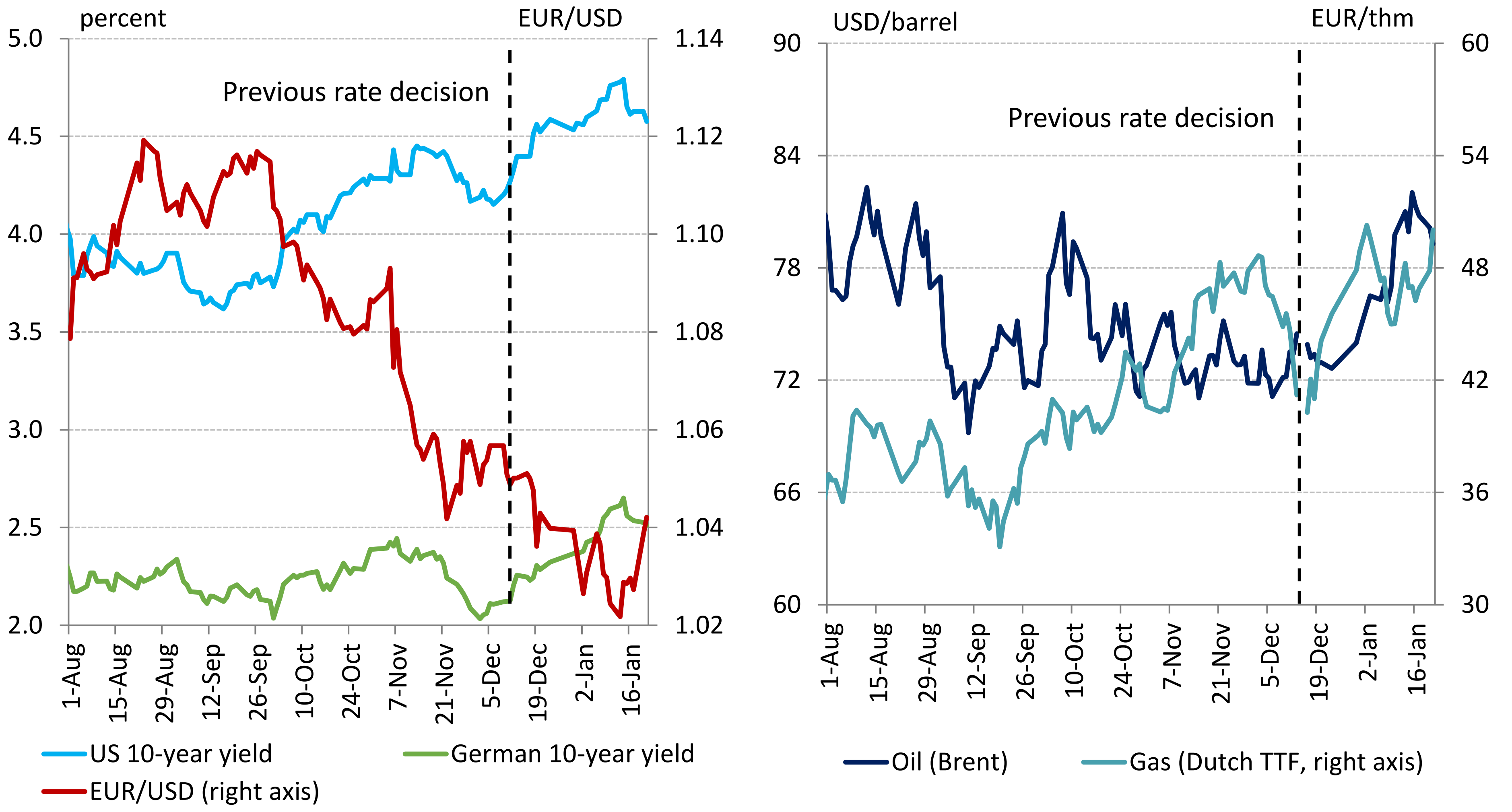
- **Global investor sentiment has been characterised by a high degree of volatility since the December interest rate decision.** The prices of crude oil and natural gas have risen since the last interest rate decision.
- **A divergence between the monetary policies of the Federal Reserve and the European Central Bank is expected in 2025**, which could lead to increased risk aversion in emerging markets.
- **In December, the increase in domestic inflation and core inflation has exceeded analysts' expectations.**
- **Increasing risk aversion, ongoing geopolitical tensions and rising inflation expectations are warning signs in terms of the inflation outlook. Looking ahead, a disciplined anti-inflationary stance remains necessary.**
- **The fundamentals of the Hungarian economy are generally improving. Disinflation will resume from February onwards.**
- **From 2025 onwards, economic growth will be increasingly broad-based. The Hungarian economy may gradually return to a balanced growth path.**

MAIN MESSAGES:
THE MONETARY POLICY DECISION IN JANUARY

- **A stable, predictable economic environment fundamentally defines the entire macroeconomic trajectory** through strengthening confidence.
- **The Monetary Council has kept the base rate at 6.50 percent at today's meeting.**
- To reach the inflation target again and to maintain financial market stability, **the effective transmission of monetary policy remains crucial.**
- Since late December, the MNB has been **announcing daily FX swap tenders at a 50 basis points higher implied interest rate.** In the Council's assessment, **an FX swap interest rate of 6 percent remains warranted.**
- Given the risk aversion towards emerging markets and the current outlook for inflation risks, **the base rate may remain at the current level for an extended period.**
- **The Monetary Council's forward guidance has changed:** *„(…) geopolitical tensions, a volatile financial market environment, and risks to the outlook for inflation* ***warrant the maintenance of tight monetary conditions."***

MACROECONOMIC AND FINANCIAL MARKET ASSESSMENT AND OUTLOOK

GLOBAL INVESTOR SENTIMENT IS VOLATILE, GAS AND OIL PRICES HAVE INCREASED

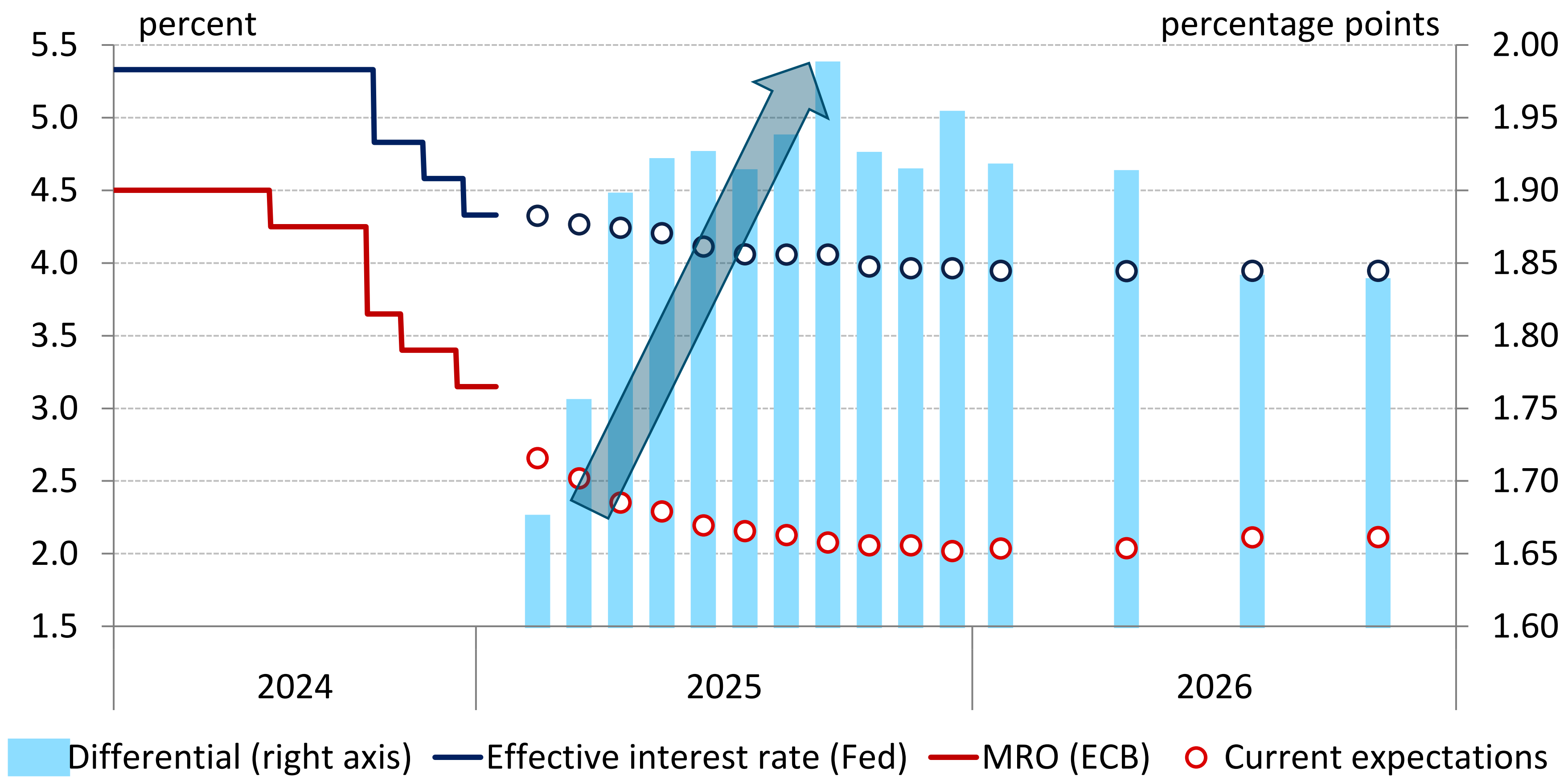


DEVELOPED MARKET 10-YEAR GOVERNMENT BOND YIELDS AND THE DOLLAR-EURO EXCHANGE RATE (LEFT PANEL); OIL AND GAS PRICES (RIGHT PANEL)

Source | Bloomberg

DIVERGENCE BETWEEN THE MONETARY POLICIES OF THE FED AND THE ECB IN 2025

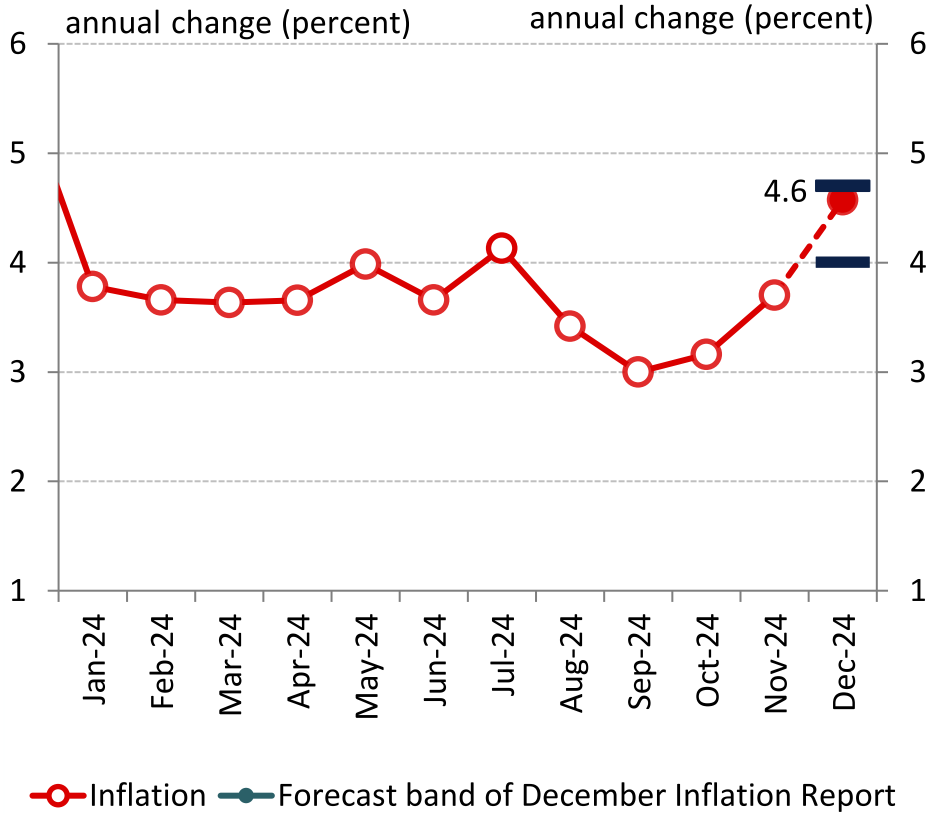
Risk aversion towards emerging markets continues to be high.

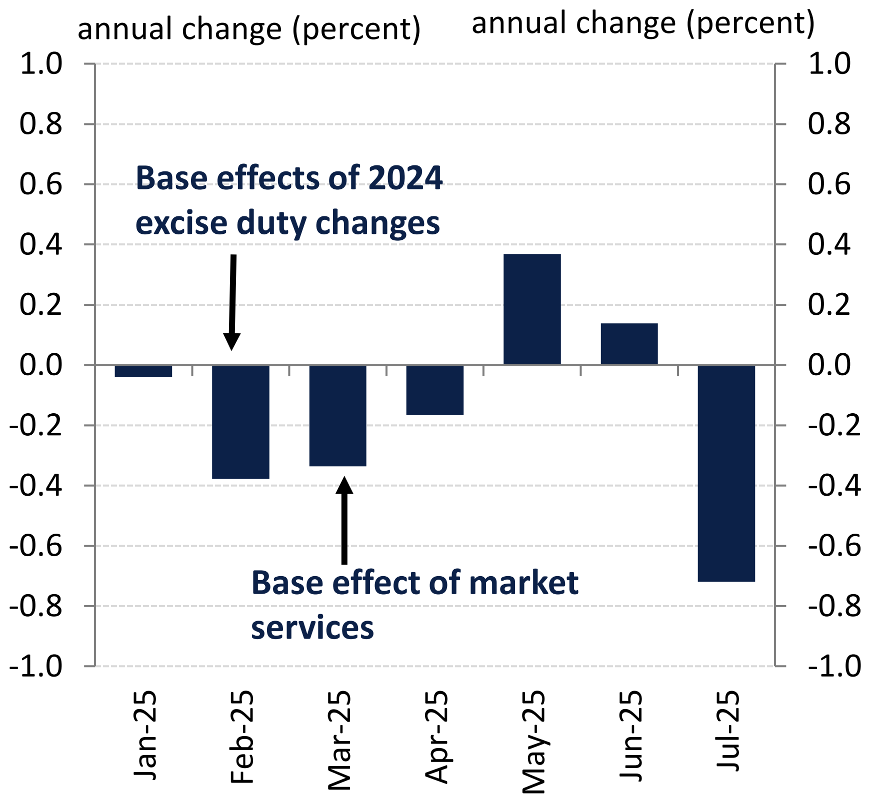


EXPECTED INTEREST RATE PATHS OF THE FED AND THE ECB BASED ON MARKET PRICING

Source | Bloomberg

INFLATION WAS AT THE UPPER EDGE OF THE FORECAST BAND IN DECEMBER 2024





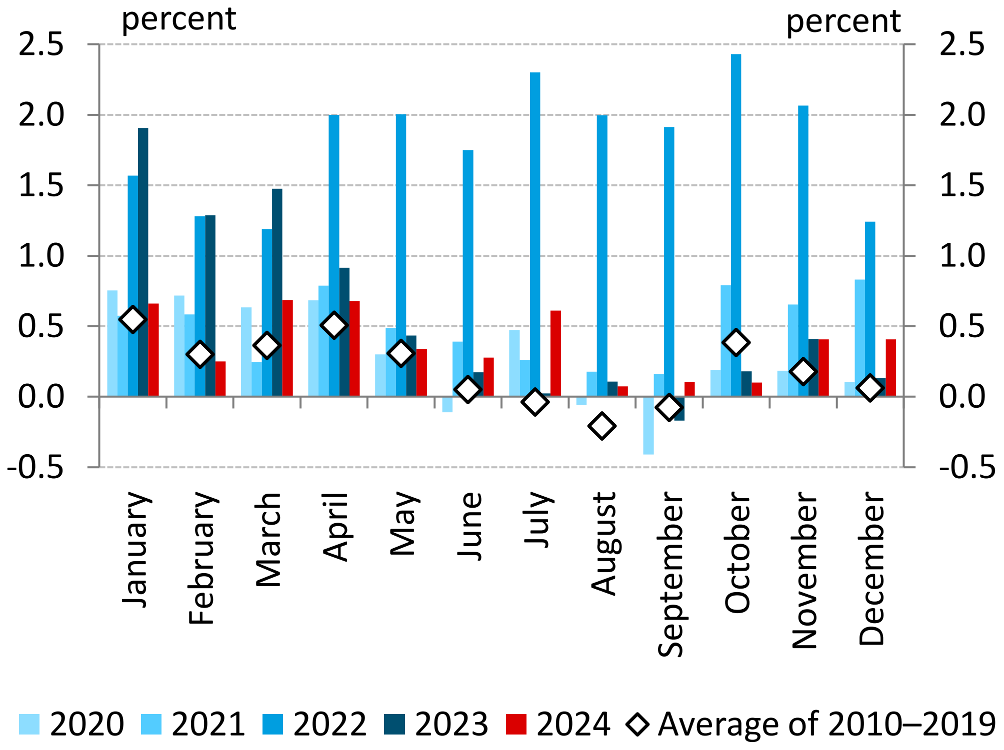
INFLATION DEVELOPMENTS (LEFT PANEL) AND THE SHORT-TERM FORECAST OF BASE EFFECTS (RIGHT PANEL)

Note | Base effects are compared to month-on-month changes between 2010-2019. Based on the forecast of the December Inflation Report.

Source | HCSO, MNB

THE COMBINED EFFECT OF THE RISE IN GLOBAL COMMODITY PRICES AND MOVEMENTS IN THE FORINT MARKET WAS REFLECTED IN THE PRICES OF IMPORTED GOODS

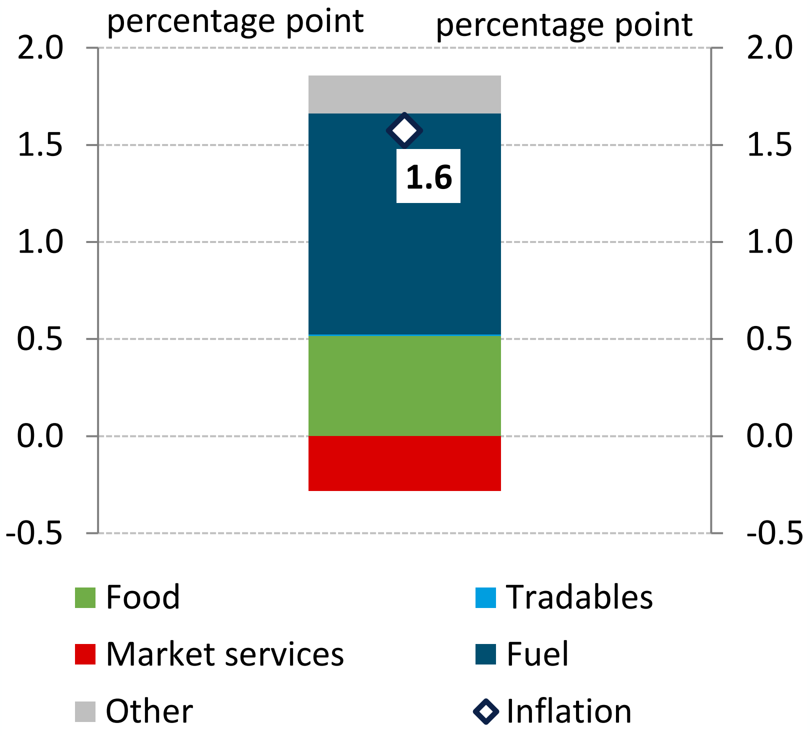
Repricing at the beginning of the year is key.



MONTHLY PRICE CHANGES OF CONSUMER PRICES EXCLUDING FUEL PRICES AND REGULATED PRICES

Note | Tax-adjusted, seasonally unadjusted monthly change.
Source | HCSO, MNB

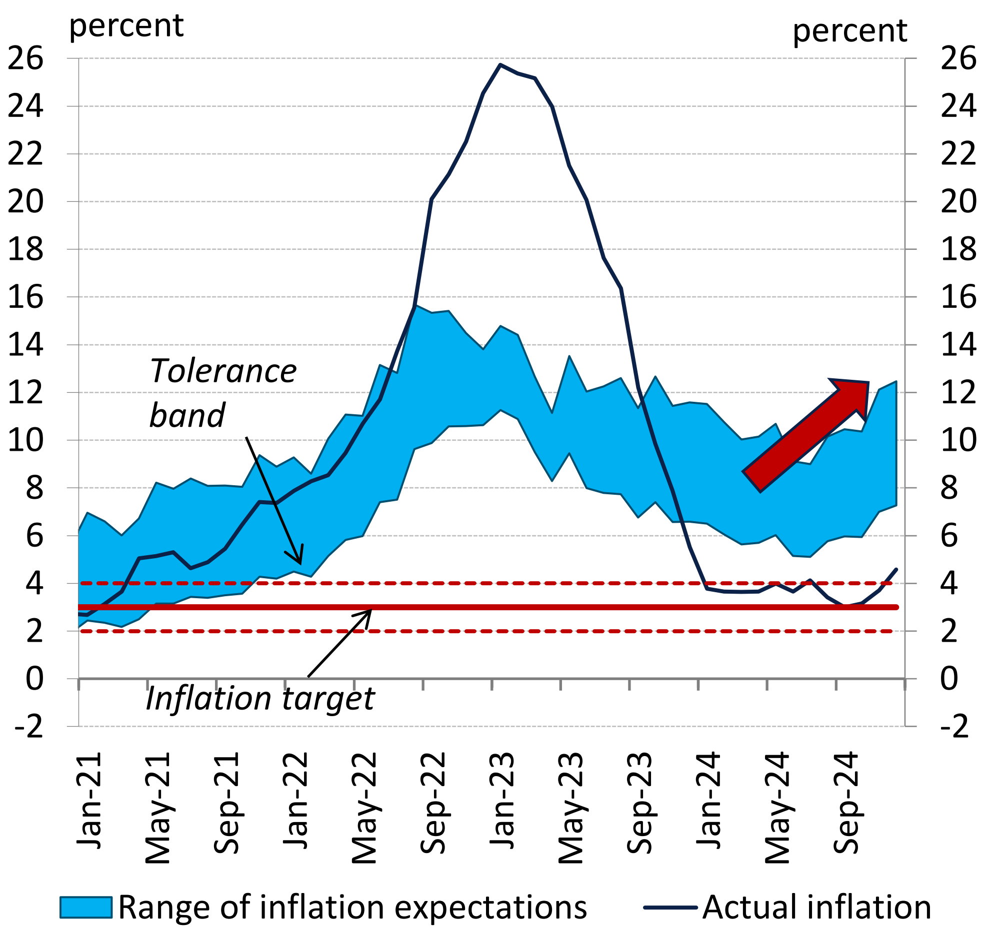
The rise in CPI inflation between September and December 2024 was mainly driven by increases in food and fuel prices.



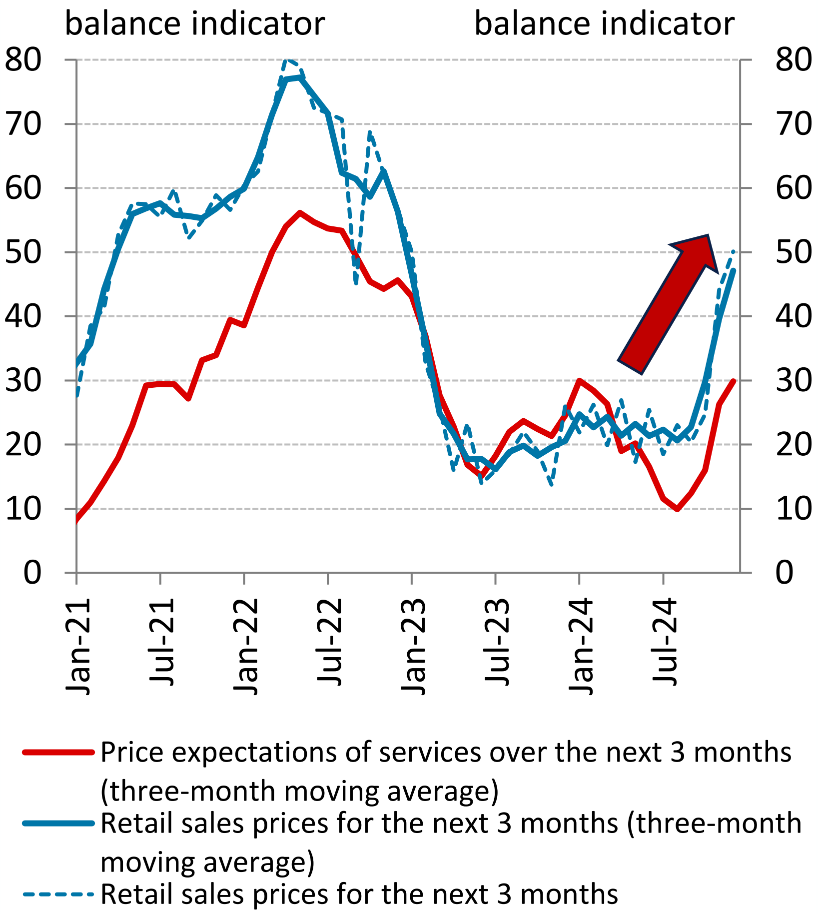
DECOMPOSITION OF THE CHANGE IN INFLATION BETWEEN SEPTEMBER AND DECEMBER 2024

Source | HCSO, MNB-calculation

INFLATION EXPECTATIONS HAVE INCREASED



EVOLUTION OF HOUSEHOLD INFLATION EXPECTATIONS



CHANGES IN EXPECTATIONS FOR RETAIL SALES AND SERVICES PRICES IN HUNGARY

Source | MNB-calculations based on data from the European Commission and the HCSO

THE RISKS SURROUNDING THE OUTLOOK FOR INFLATION HAVE SHIFTED UPWARDS

In December, consumer prices rose at a pace exceeding analysts' expectations.

Median expectation	Actual
4.4	4.6

Global commodity prices (food, oil, gas) have increased.

Inflation expectations have increased.

THIS YEAR'S GROWTH IS BASED ON INCREASINGLY BROAD FOUNDATIONS

Incomes

4.7-5.7% real wage growth (2025)

2X increase in family tax allowance (from 2025)

HUF 1060 billion interest on Premium Government Bonds (2025 Q1)

Credit

13.5-15% household credit expansion (2025)

3.7 percentage point boost from the Worker's Credit Programme (2025)

8.3-9.7% corporate credit expansion (2025)

Construction

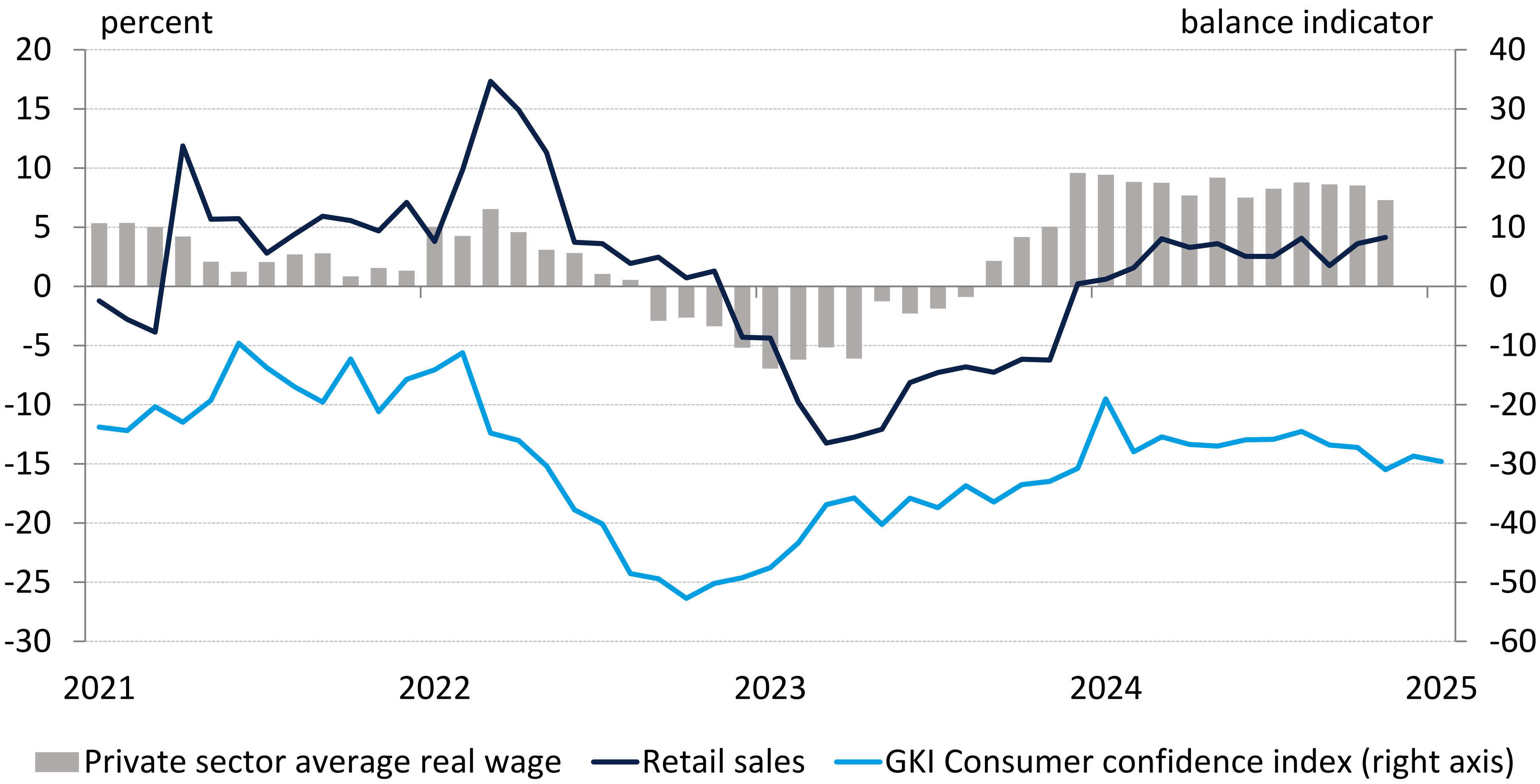
32% growth in the stock of contracts (November 2024)

Housing

28% rise in housing market turnover (2024)

In the current macroeconomic environment, the Bank's most effective contribution to restarting economic growth is strengthening confidence by maintaining price stability and financial market stability.

IN LINE WITH THE INCREASE IN REAL WAGES, RETAIL SALES ARE GROWING AS WELL

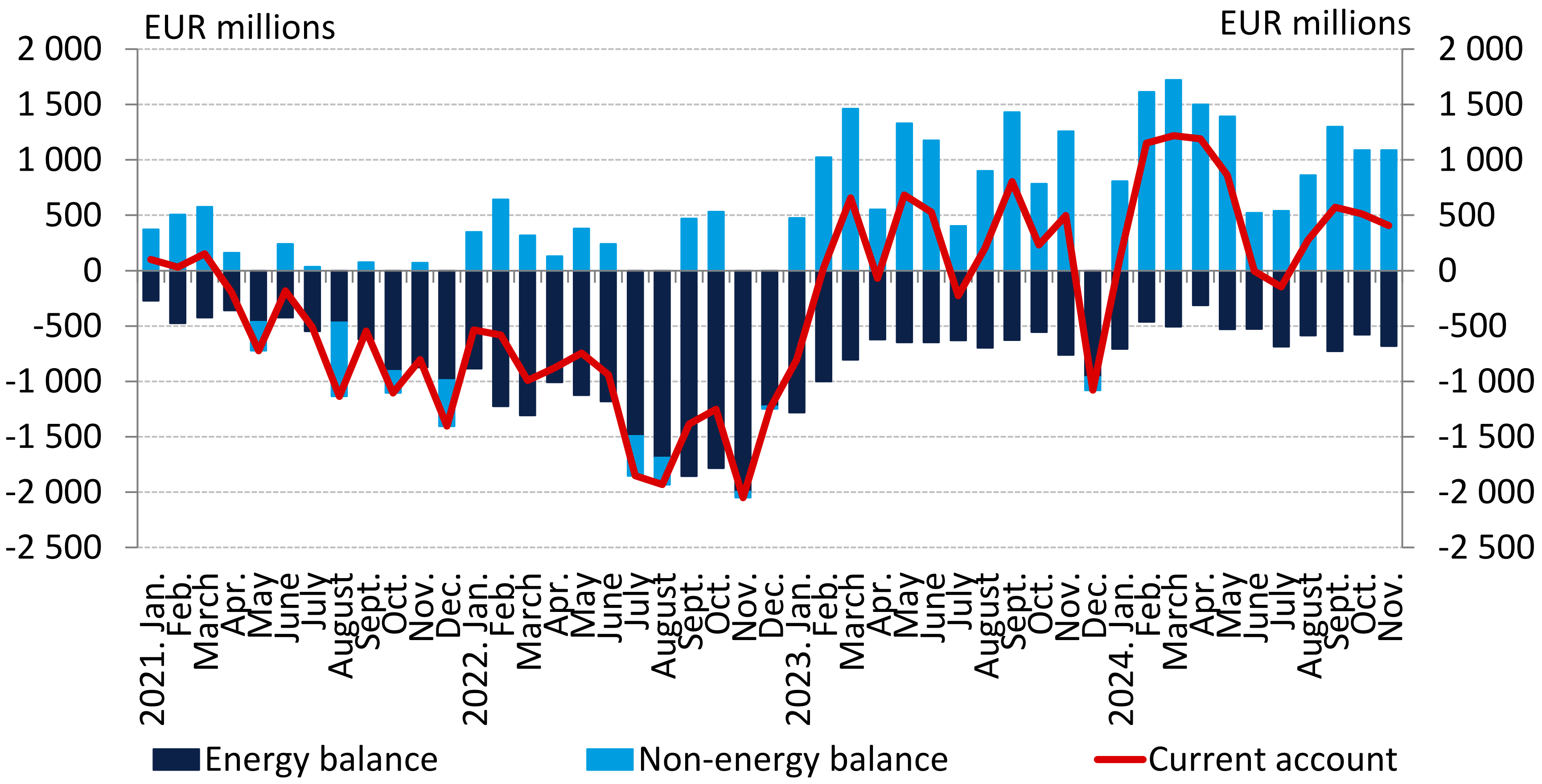


EVOLUTION OF RETAIL SALES, REAL AVERAGE WAGE IN THE PRIVATE SECTOR AND GKI CONSUMER CONFIDENCE INDEX

Source | HCSO, MNB, Economic Research Institute (GKI)

THE MONTHLY BALANCE OF THE CURRENT ACCOUNT WAS IN SIGNIFICANT SURPLUS IN NOVEMBER AS WELL

The current account showed a surplus of nearly EUR 6.1 billion in the first eleven months of 2024.

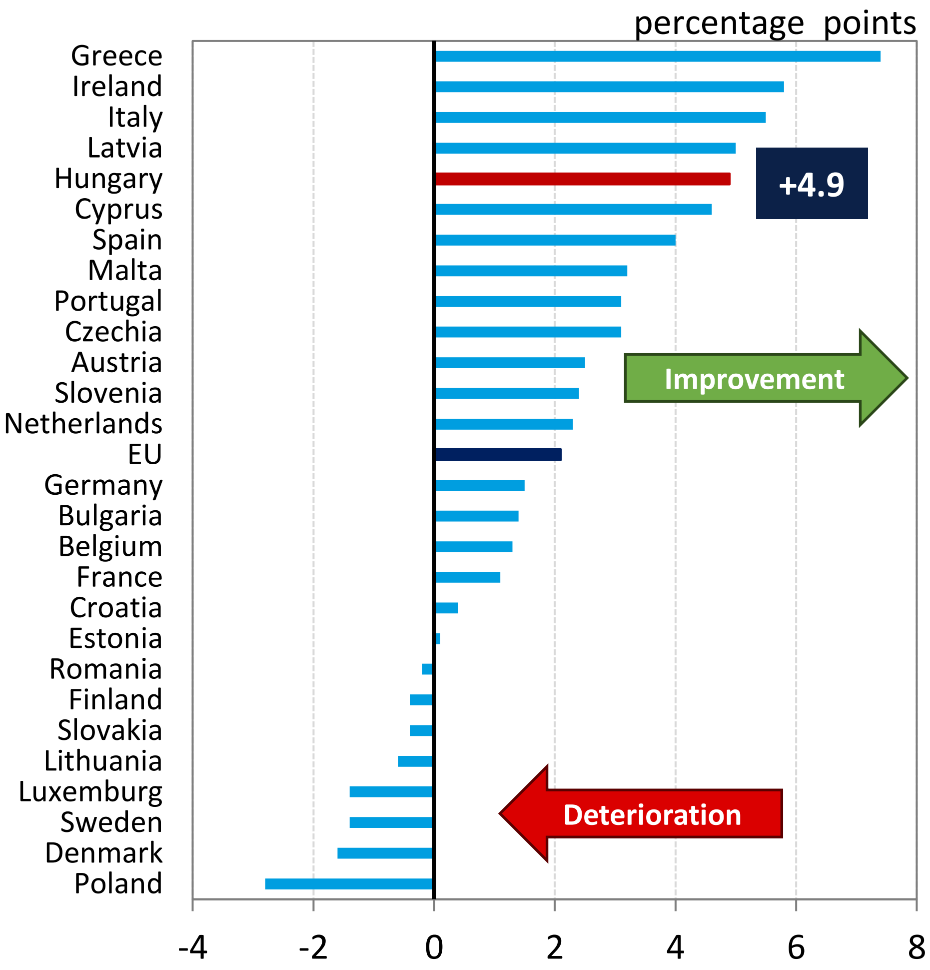


DEVELOPMENTS IN THE CURRENT ACCOUNT AND THE ENERGY BALANCE

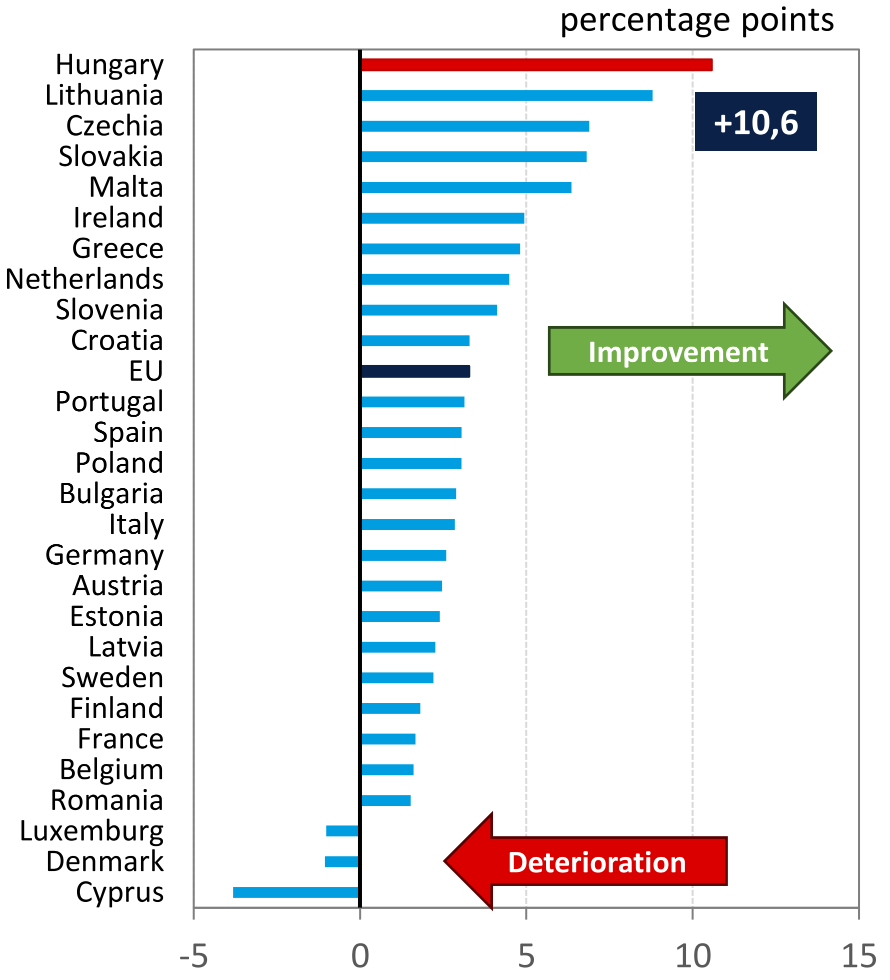
Note | Energy trade balance for the latest month is an estimate.

Source | HCSO, MNB

HUNGARY'S BALANCE INDICATORS ARE IMPROVING SIGNIFICANTLY IN AN INTERNATIONAL COMPARISON AS WELL



CHANGES IN PRIMARY BALANCE AS A PERCENTAGE OF GDP IN EU COUNTRIES BETWEEN 2021 AND 2024



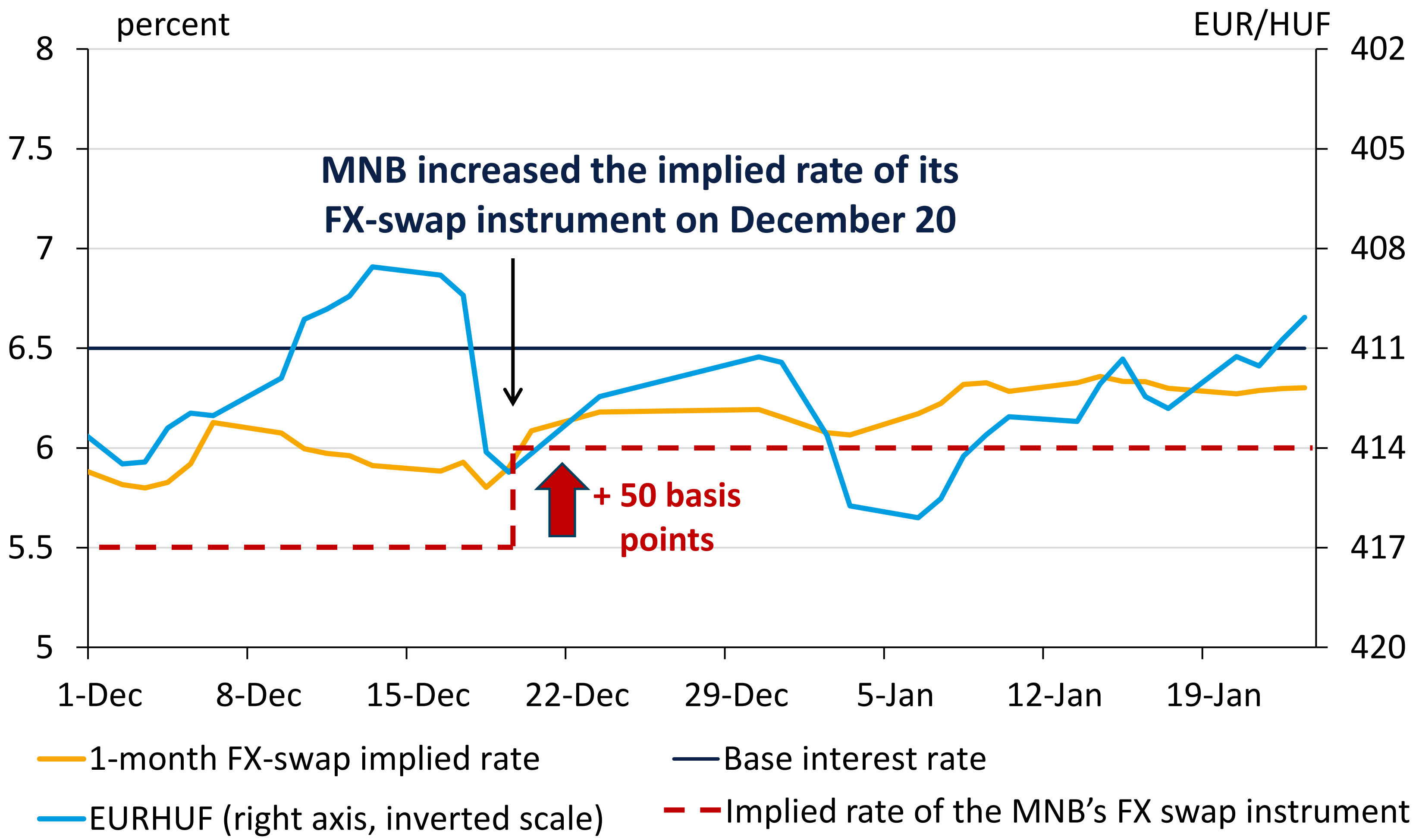
CHANGES IN CURRENT ACCOUNT BALANCE AS A PERCENTAGE OF GDP IN EU COUNTRIES BETWEEN 2022 AND 2024

Further decrease in vulnerability requires achieving price stability in a sustained manner.

Source | MNB, Eurostat, Ameco

Note | The 2024 values of current account balance are estimates.

AT THE END OF DECEMBER, THE CENTRAL BANK’S MEASURES SUCCESSFULLY STABILISED THE SWAP MARKET



THE CHANGES OF THE 1-MONTH FX-SWAP IMPLIED RATE, THE EURHUF EXCHANGE RATE AND THE BASE RATE

Source | MNB, Bloomberg

MONETARY POLICY

TIGHT MONETARY CONDITIONS REMAIN WARRANTED

Consumer prices and core inflation increased at a rate above expectations in December.

Incoming data suggest an increased risk of a higher inflation trajectory this year.

Upside risks to inflation have increased in recent months due to risk aversion towards emerging markets and ongoing geopolitical conflicts.

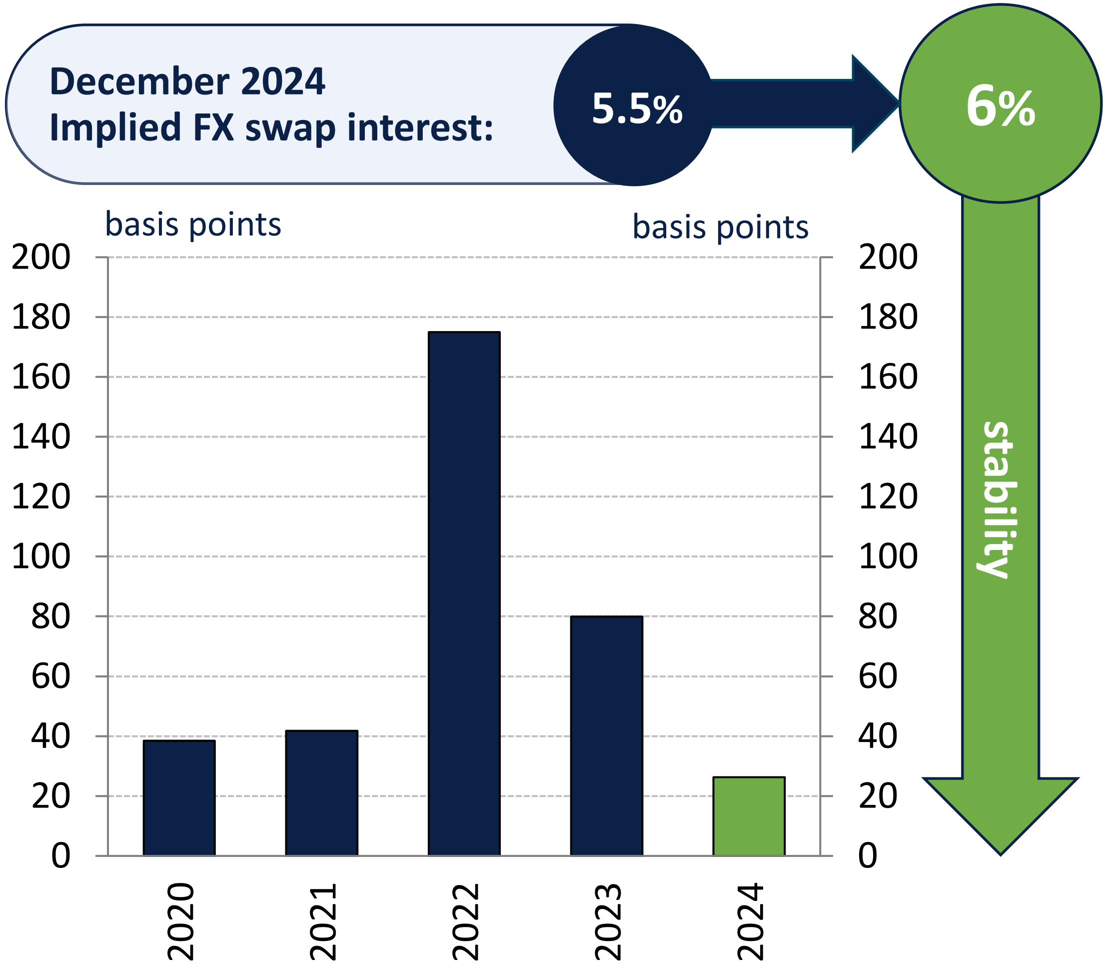
Maintaining financial market stability is crucial for the consumer price index to return to the central bank target in a sustained manner.

To reach the inflation target again and to maintain financial market stability, strengthening the effectiveness of monetary policy transmission is warranted.

THE MONETARY COUNCIL'S DECISION IN JANUARY

Central bank instrument	Interest rate	Previous interest rate (percent)	New interest rate (percent)
Central bank base rate		6.50	**6.50**
O/N deposit rate	Central bank base rate minus 1.00 percentage point	5.50	**5.50**
O/N collateralised lending rate	Central bank base rate plus 1.00 percentage point	7.50	**7.50**

IN THE COUNCIL'S ASSESSMENT, AN FX SWAP INTEREST RATE OF 6 PERCENT REMAINS WARRANTED



AVERAGE DIFFERENTIAL BETWEEN INTERBANK AND IMPLIED SWAP INTEREST RATES IN DECEMBER (WEEKLY DURATION)

Source | Bloomberg, MNB

Effective transmission of monetary policy is a precondition for achieving the price stability objective in a sustainable manner.

The Bank considers it crucial that short-term interest rates develop consistently with the level of interest rates determined by the Monetary Council in every sub-market and in every period.

THE MONETARY COUNCIL IS COMMITTED TO ACHIEVING THE INFLATION TARGET IN A SUSTAINABLE MANNER

Upside risks to inflation are being driven higher by ongoing geopolitical tensions through rising energy prices and risk aversion towards emerging markets.

Given the risk aversion towards emerging markets and the current outlook for inflation risks, the base rate may remain at the current level for an extended period.

We are closely monitoring the factors that affect the room for manoeuvre in monetary policy:

Inflation outlook

- Changes in inflation expectations
- Pass-through of exchange rate movements
- Evolution of commodity prices

Risk perception

- Developments in the external balance
- Fulfilment of fiscal targets

Financial market stability

- Evolution of country-specific risks
- Global interest rate environment and investor sentiment

Looking ahead, a careful and patient, stability-oriented approach and tight monetary conditions remain warranted.

THE MONETARY COUNCIL'S FORWARD GUIDANCE HAS CHANGED

„The expected interest rate paths of major economies are surrounded by significant uncertainty. ***Risk aversion towards emerging markets and ongoing geopolitical tensions have increased upside risks to inflation*** *in recent months. A careful and patient approach to monetary policy remains warranted. In the Council's assessment, geopolitical tensions, a volatile financial market environment, and risks to the outlook for inflation* ***warrant the maintenance of tight monetary conditions.****"*

THANK YOU FOR YOUR KIND ATTENTION!