

The MNB is comfortable with the current monetary conditions; only persistent inflationary pressure could change its policy

At Tuesday's meeting Hungary's MNB left monetary policy conditions unchanged and neither did it change the main message of its press release. Although in the last paragraph the MNB emphasizes that 'The necessity of further measures will be determined by the **persistent** change in the outlook for inflation ...', we think this subtle change in communication reflects that January inflation is expected to rise temporarily above 4% if repricing is stronger than expected.

In line with the MNB's expectation, December inflation has accelerated to 4% since the latest meeting, due to higher fuel and foods prices. Core inflation was 3.9% while constant-tax core inflation stood at 3.5%. Although inflation touched the upper end of the MNB's tolerance band, the central bank is confident that inflation will revert to below 3% until mid-2020 as base effects stemming from higher food and fuel prices will fade. The key risk to the MNB's forecast could be the January-February repricing, which could accelerate services inflation. This risk is underlined by the fact that core services inflation stood at 5.6% in December and seems to have [stuck at a high level](#).

Looking at the real economy, incoming data remained strong in Hungary in the past couple of months, therefore annual GDP growth rates could be around 5% in 2019 and 3.7% in 2020, according to the MNB. This also means that the tight labour market conditions will persist and the strong wage growth could still pose an inflation risk as well.

Before the coronavirus outbreak, international sentiment remained cautiously optimistic as risks stemming from Brexit and the US-China trade war had eased. However, the MNB's press release noted that the outbreak of the coronavirus could deteriorate global growth expectations and increase risk aversion in emerging markets as well. Last week's HUF depreciation partly reflected this sentiment.

The EUR/HUF remained volatile in the past month and was vulnerable to changes in investor sentiment. The MNB is not worried about the HUF depreciation, which poses no financial stability threats for the real economy, but in recent weeks it used the FX swap auctions to send subtle messages to the market that it deems the current pace of the HUF depreciation excessive. Due to the decrease in FX swap outstanding, the 3M BUBOR increased from 16 bps to 22 bps.

We think the MNB may want to help anchor expectations by trying to reduce the volatility of the exchange rate. This is because in a risk scenario (a rapid HUF depreciation coupled with a robust double-digit wage growth in the private sector), inflationary processes may become less anchored, particularly as underlying inflation indicators are exceeding the target. Under these circumstances, the effect of any unexpected inflation shock (e.g. if food price shocks become persistent, oil price shock) can be stronger or last longer than otherwise.

To sum it up, despite the depreciating HUF and the 4% headline inflation in December, the MNB is comfortable with the current monetary policy conditions, largely because inflation will revert toward 3% until mid-2020. Furthermore, any material effect of the coronavirus on international markets and global growth expectations could support the current loose monetary policy conditions. Overall, we think that based on the MNB's communication, 3M BUBOR could stay around its current levels at least until the end of 2020. However, if risks to the inflation forecast materialize, the MNB could start tightening, so underlying inflation expectations in the first few months should be closely watched.

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Dates of the meetings	Dates of the minutes	Inflation report	Base rate decision*	3M BUBOR*
29 January 2019	13 February 2019, 14:00 CET		0,90	0,15
26 February 2019	13 March 2019, 14:00 CET		0,90	0,15
26 March 2019	10 April 2019, 14:00 CET	x	0,90	0,13
30 April 2019	15 May 2019, 14:00 CET		0,90	0,16
28 May 2019	12 June 2019, 14:00 CET		0,90	0,20
25 June 2019	10 July 2019, 14:00 CET	x	0,90	0,24
23 July 2019	7 August 2019, 14:00 CET		0,90	0,26
27 August 2019	11 September 2019, 14:00 CET		0,90	0,26
24 September 2019	9 October 2019, 14:00 CET	x	0,90	0,21
22 October 2019	6 November 2019, 14:00 CET		0,90	0,21
19 November 2019	4 December 2019, 14:00 CET		0,90	0,19
17 December 2019	8 January 2020, 14:00 CET	x	0,90	0,16
28 January 2020	12 February 2020, 14:00 CET		0,90	0,22
25 February 2020	11 March 2020, 14:00 CET		0,90	0,16
24 March 2020	8 April 2020, 14:00 CET	x	0,90	0,16
28 April 2020	13 May 2020, 14:00 CET		0,90	0,16
26 May 2020	10 June 2020, 14:00 CET		0,90	0,16
23 June 2020	8 July 2020, 14:00 CET	x	0,90	0,16
21 July 2020	5 August 2020, 14:00 CET		0,90	0,17
25 August 2020	9 September 2020, 14:00 CET		0,90	0,17
22 September 2020	7 October 2020, 14:00 CET	x	0,90	0,18
20 October 2020	4 November 2020, 14:00 CET		0,90	0,18
17 November 2020	2 December 2020, 14:00 CET		0,90	0,19
15 December 2020	to be specified later	x	0,90	0,19

*After 2019 October, the columns show our forecast.

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This document was prepared on 29 January 2020.