

MONETARY POLICY COMMENTARY HUNGARY

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The MNB slowed down the pace of weekly hikes from 40 bps by raising the one-week deposit rate to 3.1% from 2.9%

The decisions: The Magyar Nemzeti Bank (MNB) raised the interest rate on its one-week deposit facility by 20bps, from 2.9% to 3.1% on Thursday, halving the recent pace of weekly hikes. We found this scenario the most likely in our last [MPC Report](#), and it was also in line with market pricing: FRAs indicated altogether around 40 bps rate hike for this week and next, followed by 30 bps monthly hikes until the one-week deposit rate reaches 4.5% by March/April 2020.

It remains important to emphasise that the one-week deposit is the main instrument of the MNB, the standing facility absorbing the liquidity of the banking system, so it is the effective rate (instead of the base rate) that determines the marginal yield on banking assets. The cumulative effective tightening since the latest rate-setting meeting of the MPC has reached 130 basis points.

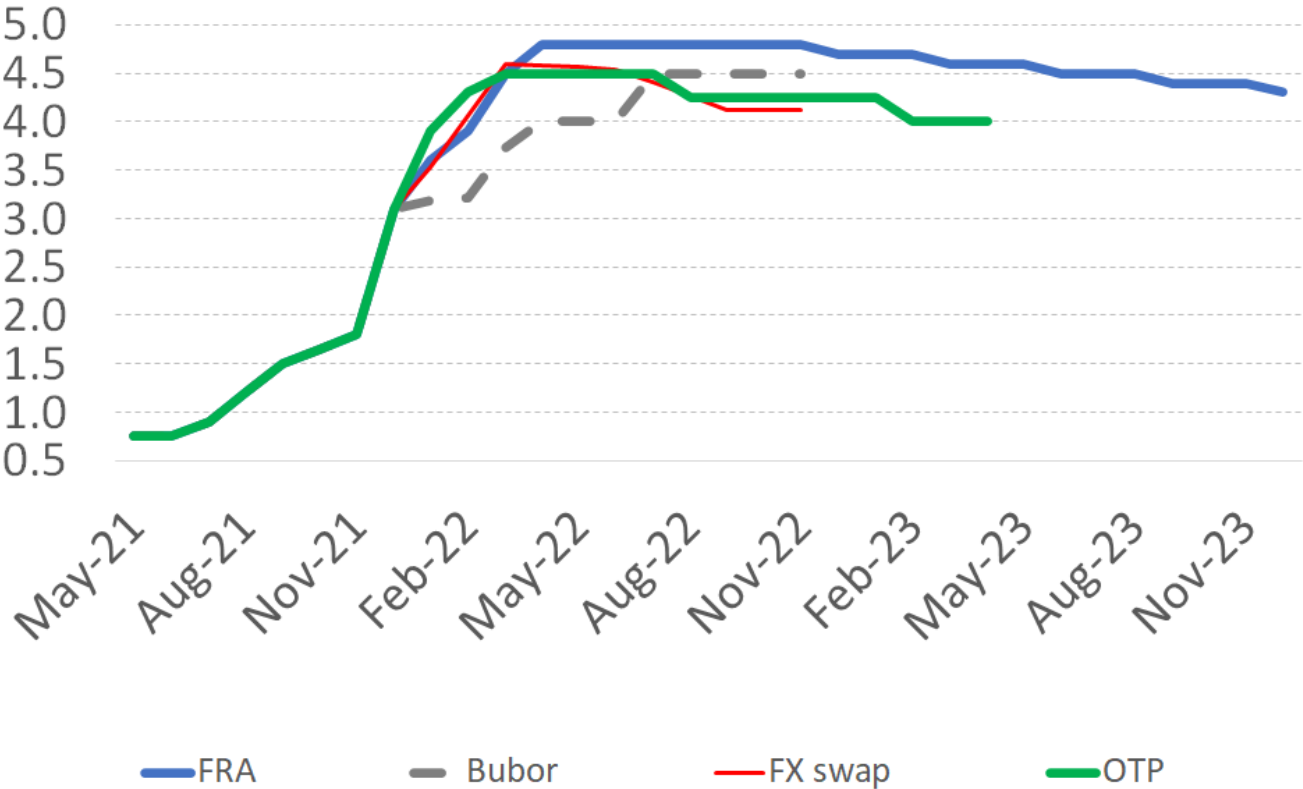
Yesterday György Matolcsy, the MNB's Governor announced in Parliament that average annual inflation could be around 5% in both 2021 and 2022, so the rate hikes will go on, and the central bank will phase out its bond purchase programme soon.

Market reactions: The HUF temporarily appreciated, pushing the EUR/HUF from 362.25 to 361 after today's decision. The immediate reaction on the fixed income market was much more modest: the FRA and the IRS curves inched down by 1-3 bps, while the bond market was hardly affected. The market reacted much stronger yesterday, when bond yields rose sharply, by 5-10 bps at the belly of the curve, and by 15-20 bps on the long end.

OTP assessment: Today's decision was in line with our expectations and market pricing. As the HUF appreciated and shifted away from historic levels against the EUR, the pace of tightening in the one-week deposit rate – dedicated to address short-term market volatility – was moderated. We expect another 20-basis-point hike next week, while from December the MNB could return to monthly rate decisions. We expect the effective rate to be hiked to around 4.5% early 2022. Therefore in our view, the tightening could be more front-loaded than what is reflected in FRA pricing. The sharp market reaction yesterday to the "Hungarian Taper" was a surprise for us, as the fast decrease in the MNB's weekly government bond purchases – from HUF 60 bn to 29 bn – had suggested that the MNB would phase out this instrument by March or April 2022.

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