



## ***No surprise: the MNB cut the base by 75 basis points, to 11.5% in November, and will keep this pace at least until February***

**The decision:** As expected, at the November meeting of the MNB's Monetary Council, the easing cycle continued with a 75-basis-point cut, which brings the base rate down to 11.5%.

### ***The MNB's key messages:***

- The decline in inflation remained broad-based. The strong moderation in inflation will continue until the end of the year, when it could be around 7%. With unchanged oil prices, it could be below 7%.
- The base rate could fall below 11% by the end of the year and be in single-digit territory by February 2024.
- The Monetary Council also discussed the possibility of another 100-basis-point and 50-basispoint cuts at their November meeting.
- The fight against inflation is not over, disinflation must continue in 2024, so monetary policy must remain cautious.
- In Q3, the Hungarian economy emerged from recession. Economic activity continues to pick up for the rest of the year and the YoY growth rate is turning positive in Q4.
- Hungary's external position is showing a rapid and significant improvement.
- International investor sentiment has improved, but external risks remain significant.
- The MNB uses a data-driven approach, taking decisions depending on the inflation path and the evolution of the risk environment.

### ***Market reactions:***

- When Mr. Barnabas Virág announced last Thursday that the MNB would likely go on with 75 bps rate cuts till February, the announcement contributed to a sharp fall in bond yields and to unprecedented bid-to-cover and sales figures at the bond auction.
- On Tuesday, the benchmark bond yields also dropped by 15-20 bps in the morning, but that totally reversed by late afternoon. We think that this move should be seen as a technical one, and likely it had nothing to do with the rate decision.
- Short-term FRA rates dropped by 10-20 bps around the decision, but longer maturities did not budge.
- However, the HUF depreciated against the EUR from 379 to 381, so the weakening that started after the announcement on 75 bps cuts till February went on.

### ***Before the decision: we expected 75 bps cut, just like the consensus, the market priced 75 bps***

- The Council's five 100-basis-point cuts brought down the key rate to 13% by September, from the peak of 18% in May; then the MNB shifted into lower gear, trimming the base rate by 75 basis points in October. Although the MNB often emphasized that its interest rate policy was not on autopilot –instead, inflation and market processes (the EUR/HUF) determined the pace of interest rate cuts each month–, the baseline scenario was that, in the absence of unfavourable developments, the 75-basis-point pace may persist in the coming months.
- However, in recent months, many factors have changed in the direction that would have allowed a stronger interest rate cut. America's economy and labour market began to lose speed, the wild rise in dollar yields (the 10Y yield peaked at 5%) reversed, which was supported by October's lower-than-expected inflation data. In Hungary, the third-quarter GDP data turned out weaker than expected, inflation slowed to the single-digit territory sooner than had been thought, the current account surplus is nearing 2% of GDP, and the forint strengthened to multi-month

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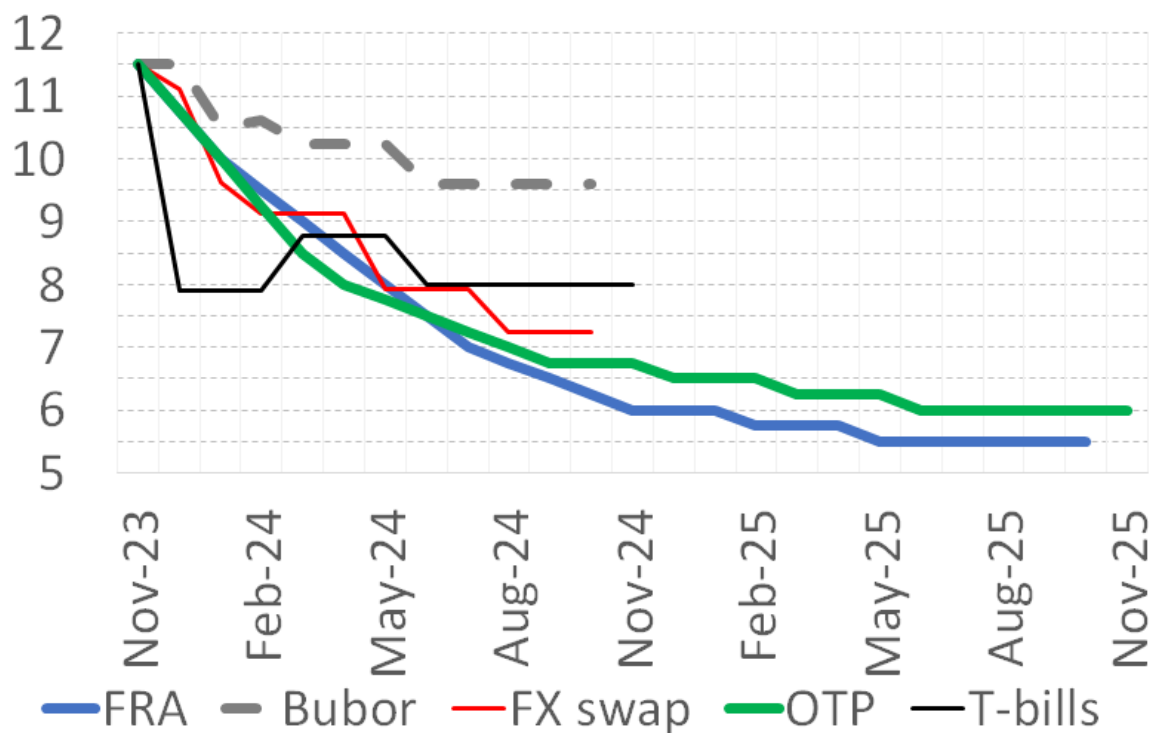
high: the EUR/HUF was once again trading below 380. This sparked market rumours about an interest rate cut of up to 100 basis points. But deputy governor Barnabás Virág dispelled the uncertainty by announcing that the interest rate may drop by 75 basis points in November, and this pace may remain in place until February. This conveyed new information because the market had priced in 75-basis-point reduction for November, and increasingly for December as well, but expected only 50-basis-point cuts for the first quarter of 2024.

***Our assessment has not changed: we expect the base rate to moderate to 10.75% by December 2023, to 8.5% in March, and to 6.5% in December 2024.***

Just like before, we still believe that the trajectory of domestic inflation and growth would support the interest rate path we had indicated.

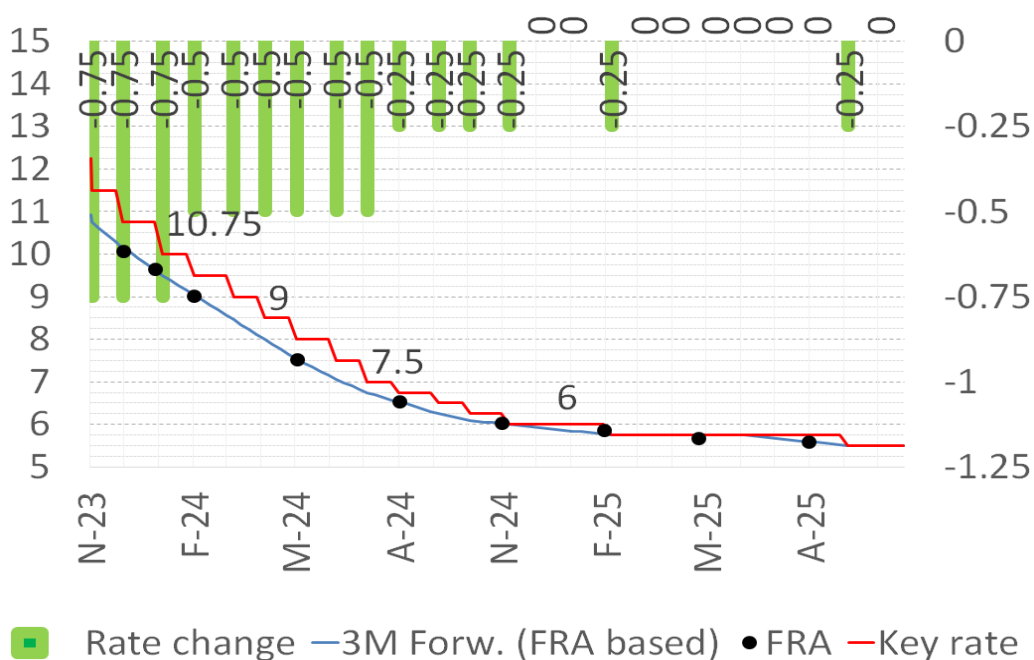
- As deputy governor Barnabás Virág previously indicated, the rate-cutting cycle can continue with 75-basis-point cuts till February 2024, which could bring the base rate down to 10.75% by the end of 2023 and to 9.25 by February 2024.
- Since the MNB wants to maintain the highest real interest rate in the CEE region, the pace of interest rate cuts may slow down to 50 basis points from March 2024. By next December, the base rate could reach 6.5% in our view.
- Inflation risks are on the upside in the medium term, which could slow the pace of disinflation and hence the pace of interest rate cuts. As the government's most important economic policy goal for next year is to restart growth, this may further complicate the continuation of disinflation. We think that the announced minimum wage hike may pose upside risk to wage growth, and thereby to inflation, but the MNB does not find that a significant risk.

• Expectations on the key rate (%)



Sources: Bloomberg, OTP Research, MNB

Key rate trajectory based on FRA pricing (%)



Sources: Bloomberg, OTP Research

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