

REPORT ON INFLATION

12 May 2025

Inflation hit a higher-than-expected low in April. We expect a gradual acceleration for the rest of the year. Underlying inflation remains a cause for concern.

- Hungary's headline inflation decelerated to 4.2% year-on-year (YoY) in April, down from 4.7% YoY in March. This figure was higher than the market consensus of 4.0% and significantly exceeded our forecast of 3.6%. The unprecedented substantial difference between our forecast and the actual data is primarily due to unexpected price increases for several specific items and a smaller-than-expected impact from retailers' profit margin cap.
- In April:
 1. Pharmaceutical prices increased by 3% month-on-month (MoM). The last time there was a one-month price increase of this magnitude was in early 2007, when subsidies for medicines were cut.
 2. Natural gas prices rose by 8% MoM. This is a consequence of the difficult-to-understand gas price accounting methodology of the KSH, as the weight of subsidised and non-subsidised gas varies from month to month, rather than being recorded once a year. For this reason, there are unpredictable movements in the 'composite' gas price, even though neither the subsidised nor the non-subsidised gas price has changed. We think that (at least part of) the surprise in gas prices will be corrected in the coming month(s).
 3. Banking and telecom service charges also rose, albeit to a lesser extent compared to traditional backward-looking inflation-linked repricing. However, the price increase is a surprise, as these providers had committed themselves to the government not to raise prices until mid-2026. It is possible that this commitment does not apply to all representative items used in the inflation calculation. For example, banks have pledged to freeze account maintenance fees, whereas the KSH uses six to seven different representative items for calculating banking service charges.
 4. Tobacco prices grew by 2.5% MoM, while we had expected stagnation.
 5. Overall food inflation was 0.6 percentage points higher than we had expected. It is likely that retailer's profit margin cap had a smaller effect on food inflation than anticipated.
- Despite the significant decline in the headline CPI, underlying inflation developments remain a cause for concern. The closely watched constant tax core inflation decelerated to 4.7% YoY from 5.4% YoY; however, since this indicator includes processed food, the announced profit margin caps also affected it, reducing it by 0.5-0.6 percentage points in our estimate. Sticky price inflation decelerated to 5.4% YoY from 5.9% YoY. In the latter, the modest repricing of banking and telecom service providers played a significant role. However, the annualized month-on-month change of our trend inflation indicator, which excludes mainly backward-looking pricing items (such as telecom and financial fees), remained unchanged at 6.2% (in the third consecutive month). The stagnation of this figure highlighted our long-held view that the underlying inflationary processes are not in line with the MNB's 3% target, and exceed not only the average of the first nine months of 2024 (4.4%) but also the average of the last quarter of 2024 (5.4%).

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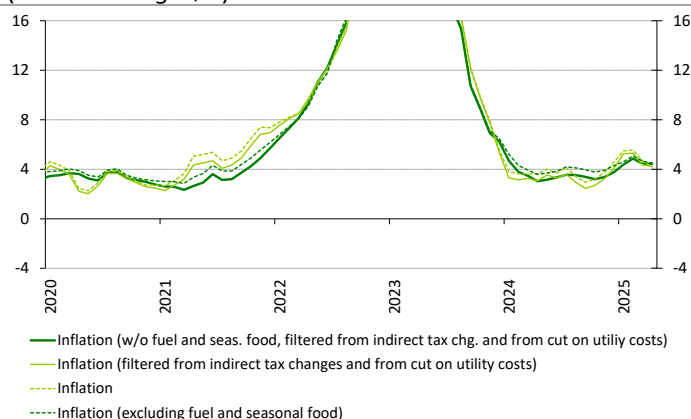
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- The data indicate that the recently introduced measure to cut retailers' profit margins has reduced food inflation, at least in the short term. The government has also announced similar measures for drugstores: they will have to cut margins in 30 product categories. The measure will enter into force in mid-May. As the price data collection of the KSH lasts until the 20th of the month, the impact will be reflected to a greater extent in the June inflation data.
- A much higher-than-expected April figure in itself would have raised our previous inflation forecast to 4.5%, as we believe most of the surprise factors will have permanent effect on inflation. However, we have left our forecast unchanged for the time being due to the rapid decline in oil prices and the new profit margin cut measure for drugstores. It is important to underline that, while margin freezes and voluntary price freezes by service providers help disinflation in the short run, in the longer run such measures tend to cause excess inflation, especially given the number of government stimulus measures that will be in place from the second half of the year onwards. There is therefore a significant risk that inflation will not fall further in 2026.
- Due to the above, we believe that the central bank has limited room for manoeuvre in terms of interest rate cuts, and we expect that it will have to offset the loosening fiscal policy by maintaining tight monetary conditions. For this reason, we do not expect interest rate cuts either this year or next.

Chart 1: Summary chart of inflationary processes*

(annual changes, %)

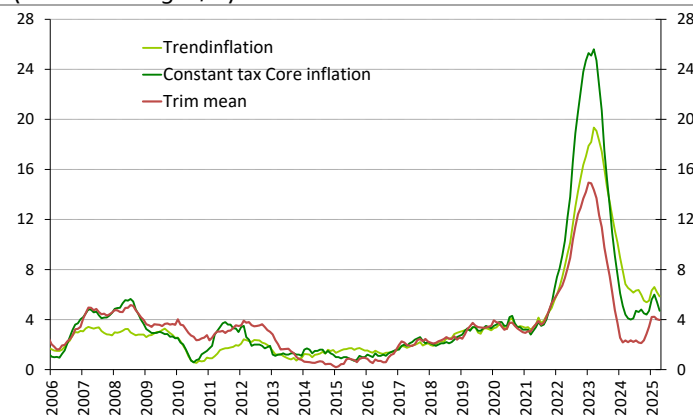


Sources: KSH, OTP Research

*: our filtered inflation indicator corrected with the price-cap effects on certain food items

Chart 2: Core, trend* and trimmed mean inflation

(annual changes, %)

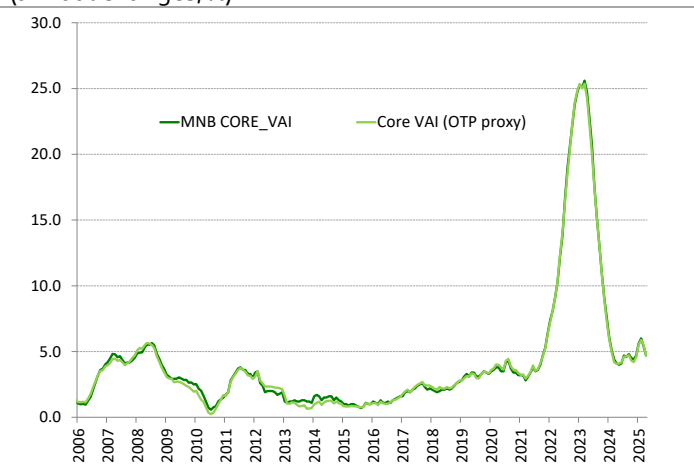


Sources: KSH, OTP Research

*Filtered from indirect tax and visit fee changes, and one-off items and w/o second-hand car prices

Chart 3: Constant tax core inflation and our proxy*

(annual changes, %)



Sources: KSH, OTP Research

* We cannot reproduce exactly the tax-filtered core inflation because (1) the MNB has its own methodology for the calculation of tax changes, which is not known to us. (2) In addition, core inflation cannot be calculated exactly from the KSH's 160 CPI items. So, our calculation tries to proxy the MNB's core vai indicator.

Chart 4: Trend inflation*

(3M/3M annualized change, %)

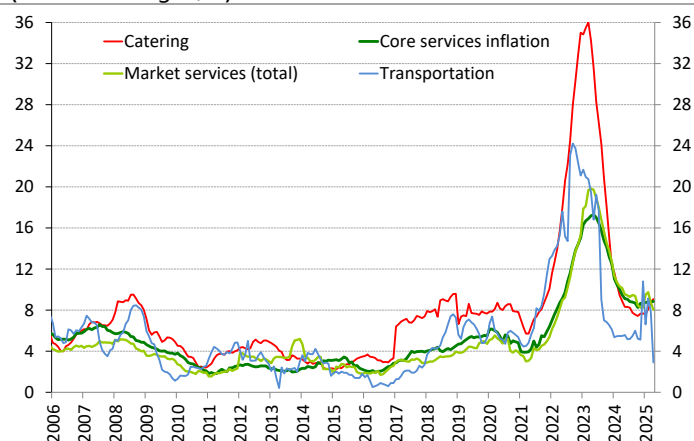


Sources: KSH, OTP Research

* Filtered from indirect tax (including the financial transaction tax) and visit fee changes

Chart 5: Services inflation*

(annual changes, %)

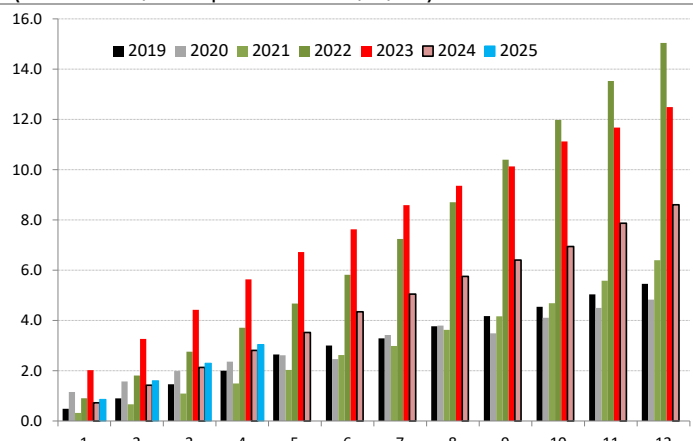


Sources: KSH, OTP Research

* Filtered from indirect tax (including the financial transaction tax) and visit fee changes

Chart 6: Intra-year price setting in core services*

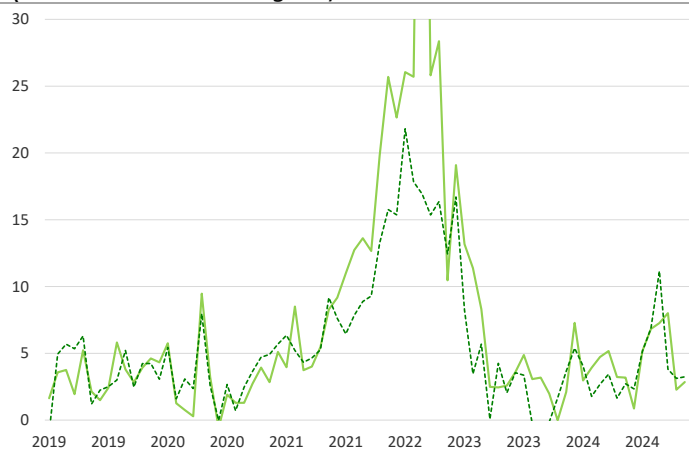
(cumulated, over previous Dec, %, SA)



Sources: KSH, OTP Research

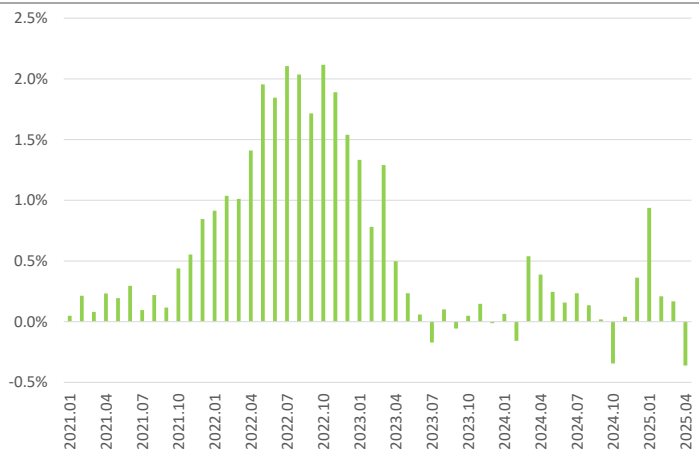
* Aggregation of the most demand-sensitive and labour-intensive services, filtered from indirect tax and visit fee changes

Chart 7: Filtered and trim mean inflation
(annualized MoM change, %)



Sources: KSH, OTP Research

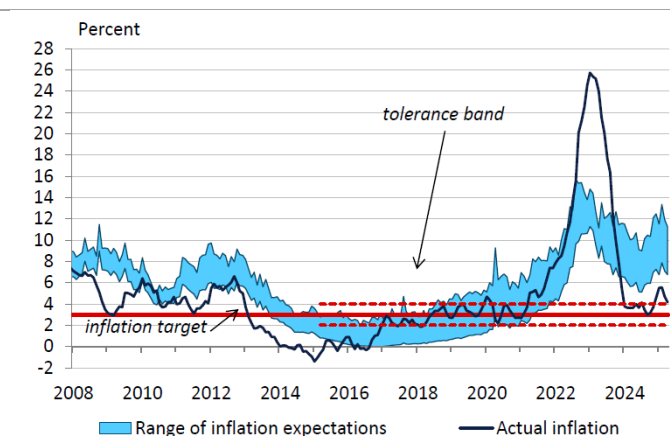
Chart 8: Extra re-pricing* in the constant tax core inflation
(%point)



Sources: KSH, OTP Research

*: %point difference of MoM changes compared to the average MoM rate of given month in the 2017-2019 period; from February 2022, data are adjusted by the effect of the price caps on vegetable oils, sugar, and milk

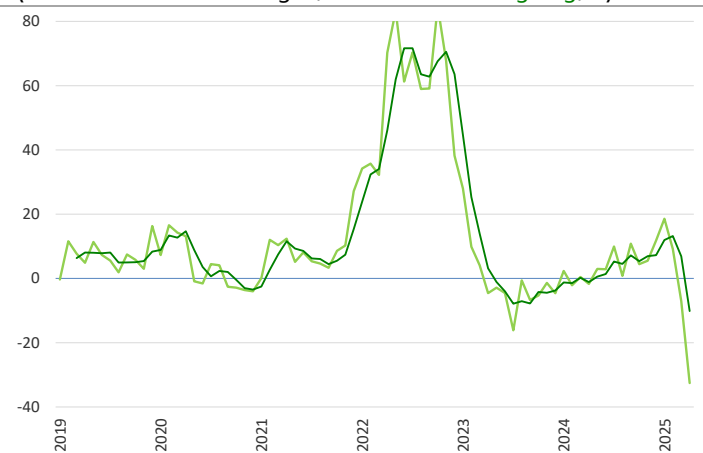
Chart 9: Inflation expectations



Sources: MNB calculations based on European Commission data; and HCSO.

Sources: MNB calculation

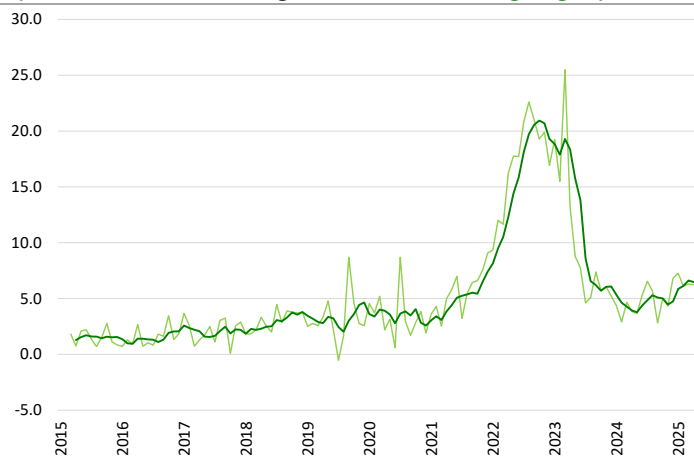
Chart 10: Food inflation*
(annualized MoM changes, and its 3M rolling avg, %)



Sources: KSH, OTP Research

*: w/o seasonal foods

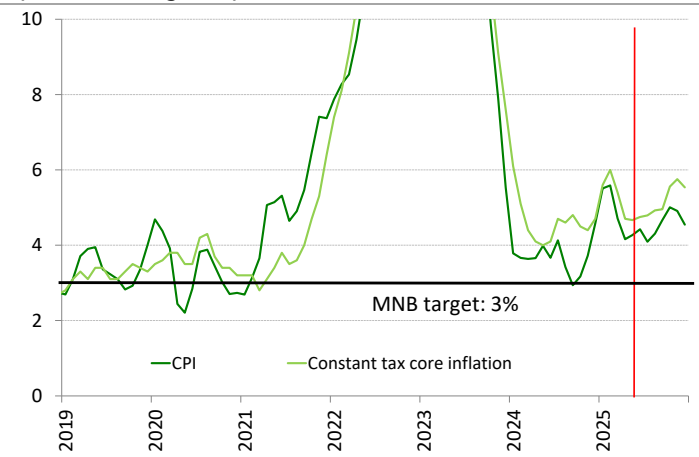
Chart 11: Trend inflation*
(annualized MoM changes, and its 4M rolling avg, %)



Sources: KSH, OTP Research

*: Filtered from the mainly backward looking pricing items (telecom, financial fees)

Chart 12: Inflation forecast
(annual changes, %)



Sources: KSH, MNB, OTP Research

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