

CIB WEEKLY REPORT



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What to watch next week

Local market movers

The key event of the forthcoming week is going to be the NBH's rate-setting meeting. Rate changes are only expected in June, but the statement is likely to repeat the hawkish statements of vice governor Virág. CSO is going to publish the most recent wage and unemployment statistics. Wage growth is likely to remain high in March (driven by public sector wage adjustments), and the labor market recovery is likely to continue mirroring the gradual reopening of the economy.

External developments

The ESI and the German Ifo indices are likely to edge higher, confirming the positive growth outlook in the euro zone. US regional manufacturing indices may retreat in May, and the consolidation on the housing market is set to continue, too. The core PCE index is expected to jump from 1.8% to 2.4%, US confirming that inflationary pressures are on the rise.

Summary of recent macro and market developments

GDP surprised at the strong side, NBH flags rate hikes

Flash Q1 GDP figures surpassed even the most optimistic expectations. GDP grew by 1.9% q-o-q and were only 2.3% lower compared to the same period of 2021. (The consensus and the most optimistic forecast were -3-7% and -3.2% respectively). The swda y-o-y data was -1.8%. Details are not available yet, but CSO said that at the production side, the industry, financial and ICT services contributed the most to growth, which suggests that the strong performance of the above sectors could offset the weakness in the pandemic-hit sectors more than had been expected.

Although Hungarian figures were much better than expected, it is generally true, that European economies fared much better during the current wave of the pandemic compared to the first wave.

The recovery will gain further momentum from Q2 in line with the full reopening of the economy. In light of the strong Q1 reading, it is no surprise that FY growth expectations shifted up. Our macro scenario is under revision (the updated forecasts will be published in mid-June), but we will certainly revise up our March GDP forecast, and even a conservative estimate would put FY GDP growth to around 5.5%.

Not only the GDP release came as a surprise this week, the NBH also managed to shock the market when vice governor Virag had flagged rate hikes on Monday.

In an interview with Reuters, the vice governor said that

- In tandem with the full reopening of the economy, monetary policy will enter a new phase.
- Reacting to upside inflation risks, the central bank plans a pre-emptive policy rate hike in June.
- It is not going to be a one-off, but rather the start

of a cycle.

- The NBH switches to a “data-driven” mode.
- The rate hike will precede the withdrawal of other non-conventional support measures, but the latter will also happen in the upcoming period.
- QE will remain in place yet.

The central bank has already altered its communication during the last couple of months and has adopted a more hawkish bias. “Risk aversion vis-à-vis emerging markets” and “second round inflation impacts” have been repeatedly mentioned as the key risks to the inflation outlook. The shift in communication was followed by a de facto rate hike announcement on Monday (just a week ahead of the next scheduled MC meeting).

Flagging a rate hike can well be explained by incoming new information:

- Q1 GDP came out much stronger than expected, FY GDP forecasts moved further up. (The central bank itself now expects GDP growth close to 6% compared to the 4-6% March projection).
- Fiscal policy will be more expansionary than expected not only this year, but also in 2022.
- Overheating risks are clearly on the rise.
- April CPI was already above 5%, the 2021 inflation trajectory moved higher, and so did inflation expectations (not alarmingly fast, though).
- Upside inflation risks have strengthened.

To sum it up, everything is in place for an overheating economy which -in tandem with supply side bottlenecks- may result in inflation stuck at high levels, and inflation expectations may also shift permanently higher, endangering price stability. The central bank is trying to

tackle these risks with a proactive move.

Virág Barnabás failed to give any concrete guidance about the size of the hike. Our calculations show inflation peaking closer to 5.5% (as opposed to 5%) in May, and the retreat from the peak will be also slower than previously expected. December y-o-y CPI may be above 4% and the same stands for average 2021 CPI. Nonetheless, we think that both demand- and supply-side pressures will slowly and gradually ease during the next 6-9 months, therefore CPI may return to the target band in 2022. If our expectations are valid, it suggests that no aggressive hikes are needed at this stage to prevent inflation spiraling out of control; the market pricing (~80-90 bps tightening within the next 12 months) seems to be too aggressive to us.

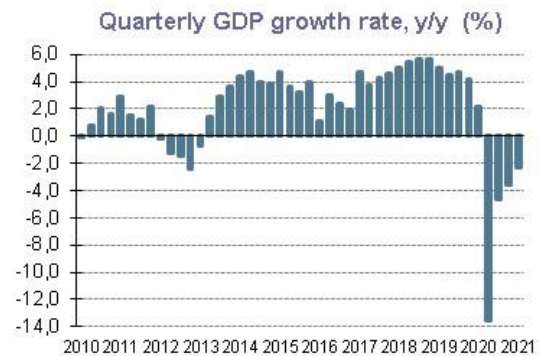
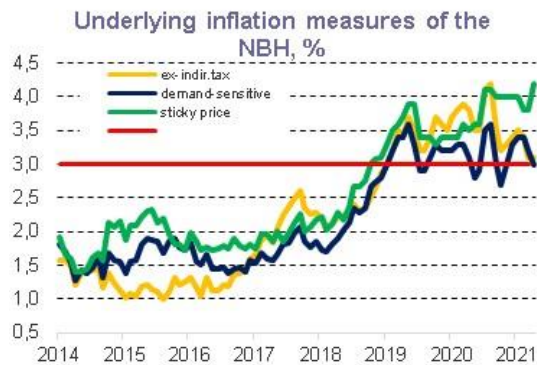
The Monetary Council will have many options to consider in June:

- Raising the policy rate (0.6%) to the level of the 1W depo rate (0.75%). It would rather be a symbolic move than effective tightening.
- Increasing both the policy rate and the 1W depo rate close to market rates (0.85%)
- Changing the interest rate corridor simultaneously

Following the pre-announced June rate hike, the data driven central bank will make moves taking into account incoming new information. If our inflation scenario holds, we think that one or two moderate rate increases will be enough, and the policy rate will not be raised markedly above 1% in 2021.

The hawkish monetary policy turn and higher rates point to lower EUR/HUF, and Monday's announcements suggest that the central bank's preference is now for a stronger FX rate, which could help to mitigate inflation risks. We do not believe, however, that a lasting period of strong HUF appreciation is to come. If the rate increases

of the upcoming period will not be much bigger than our current forecast, EUR/HUF may establish a new trading range in the 345-355 band (down from 355-365 previously).



Source: CSO, NBH

EUR/HUF below 350

The steady appreciation trend of the forint continued this week, EUR/HUF has been fluctuating around levels not seen since the late summer 2020 after the NBH positioned itself as one of the first in the EU to tighten monetary policy. On Monday the forint's market was dominated by the central bank vice president's statement who flagged a possible base rate hike as soon as next month, which triggered a fast strengthening. At the beginning of the week the EUR/HUF fell close to 350 and was trading below that level even in the first part of the Friday trading session. The space for further appreciation depends on the NBH's decision, but we expect EUR/HUF

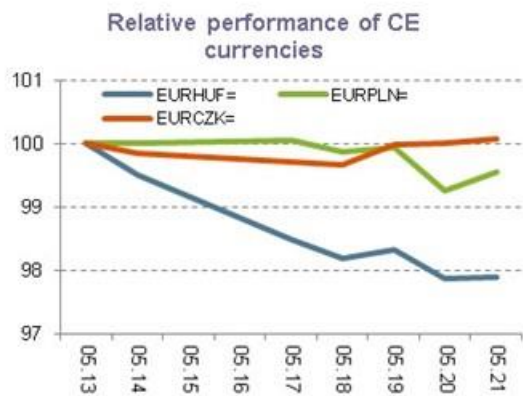
to trade in the 345-355 range in the upcoming period. During the last couple of days, the strengthening against the dollar was more significant in line with the international movement of the US currency, USD/HUF dropped to lowest level (around 285) since late June 2019, this meant a 2.5% appreciation on a weekly basis.

Interest rate movements in the whole BUBOR maturities reflected an adjustment of 5 to 10 bps directly after the NBH's comment, while the yield curve of the government securities market has become flatter thanks to the significant jumps (15-30 bps) up to the 5-year maturity.



CE3 GOVERNMENT BOND YIELDS							
SPOT (bid)	HU		PL		CZ		EU
	yield (%)	spread (bp)	yield (%)	spread (bp)	yield (%)	spread (bp)	yield (%)
1Y	0,90	153	0,20	82	0,60	122	-0,63
3Y	1,83	248	0,54	119	1,12	178	-0,65
5Y	2,16	266	1,24	174	1,51	201	-0,50
10Y	3,18	329	1,91	201	1,82	192	-0,11
60-DAY AVG	yield (%)	spread (bp)	yield (%)	spread (bp)	yield (%)	spread (bp)	yield (%)
1Y	0,72	135	0,12	75	0,05	69	-0,63
3Y	1,49	219	0,41	112	1,04	175	-0,71
5Y	1,91	251	0,94	154	1,41	201	-0,60
10Y	2,81	307	1,54	180	1,82	208	-0,26

Source: Reuters



Macroeconomic and market forecasts

Under revision

Week 22

MONDAY 05/24/2021

Country	Time	Data	Period	Previous	Forecast	Result
		No major data release	#N/A			

TUESDAY 05/25/2021

Country	Time	Data	Period	Previous	Forecast	Result
HU	8:00	Economic sentiment index	May	-6,8		
DE	10:00	Ifo index	May	99,5		
HU	14:00	MNB interest rate decision	May	0,6%	0,6%	
US	15:00	Case-Shiller house price index, y/y	March	11,97%		
US	16:00	New home sales, mln unit	March	1,021	0,95	

AUKCIÓK

			Amount	Previous	Forecast	Result
HU	11:30	3M T-bill	HUF 15 bln	0,60%		

WEDNESDAY 05/26/2021

Country	Time	Data	Period	Previous	Forecast	Result
		No major data release	#N/A			

AUKCIÓK

			Amount	Previous	Forecast	Result
HU	11:30	12M T-bill	HUF 10 bln	0,69%		

THURSDAY 05/27/2021

Country	Time	Data	Period	Previous	Forecast	Result
HU	9:00	Unemployment rate	April	4,0%		
US	14:30	Initial jobless claims, thousands	weekly	444		
US	14:30	Durable goods orders, m/m	April	0,8%	0,8%	
US	14:30	Personal consumption, q/q	Q1	10,7%		
US	14:30	Core PCE index, q/q	Q1	2,3%		

FRIDAY 05/28/2021

Country	Time	Data	Period	Previous	Forecast	Result
HU	9:00	Gross wages, y/y	March	9,8%		
EZ	11:00	Consumer confidence index	May			
US	14:30	Personal income, m/m	April	21,1%	-15,0%	
US	15:45	Chicago PMI	May	72,1	69,5	



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Week 21

MONDAY 05/17/2021

Country	Time	Data	Period	Previous	Forecast	Result
		No major data release	#N/A			

TUESDAY 05/18/2021

Country	Time	Data	Period	Previous	Forecast	Result
HU	9:00	GDP growth, flash, y/y	Q1	-3,6%	-3,7%	-2,3%
HU	9:00	GDP growth, flash, q/q	Q1	1,4%		1,9%
EZ	11:00	Trade balance, prelim., EUR m	March	23,1		13,0
US	14:30	Building permits, mln unit	April	1,759	1,770	1,760
US	14:30	Housing starts, mln unit	April	1,739	1,705	1,569
AUKCIÓK		#N/A	#N/A			
			Amount	Previous	Forecast	Result
HU	11:30	3M T-bill	HUF 15 bln	0,46%		0,60%

WEDNESDAY 05/19/2021

Country	Time	Data	Period	Previous	Forecast	Result
US	20:00	Fed FOMC minutes	-			

THURSDAY 05/20/2021

Country	Time	Data	Period	Previous	Forecast	Result
DE	8:00	PPI, y/y	April	3,7%		5,2%
DE	8:00	PPI, m/m	April	0,9%		0,8%
US	14:30	Initial jobless claims, thousands	weekly	473		444
US	16:00	Leading index	April	1,3%	1,2%	1,6%

AUCTIONS

HU	11:30	5Y T-bond	HUF 30 bln	1,68%		2,08%
HU	11:30	7Y T-bond	HUF 30 bln			2,51%
HU	11:30	10Y T-bond	HUF 20 bln	2,77%		3,09%

FRIDAY 05/21/2021

Country	Time	Data	Period	Previous	Forecast	Result
DE	9:30	Manufacturing PMI, flash	May	66,2	66,0	64,0
DE	9:30	Services PMI, flash	May	49,9	52,0	52,8
DE	9:30	Composite PMI, flash	May	55,8		56,2
EZ	10:00	Manufacturing PMI, flash	May	62,9	62,3	62,8
EZ	10:00	Services PMI, flash	May	50,5	52,0	55,1
EZ	10:00	Composite PMI, flash	May	53,8		56,9
US	15:45	Manufacturing PMI, flash	May	60,5	60,8	
US	15:45	Services PMI, flash	May	64,7	64,9	
US	15:45	Composite PMI, flash	May	63,5		
US	16:00	Existing home sales, mln unit	April	6,01	6,06	



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