MINUTES
OF THE MONETARY COUNCIL MEETING OF
19 SEPTEMBER 2017

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Article 3 (1) of the MNB Act (Act CXXXIX of 2013 on the Magyar Nemzeti Bank) defines achieving and maintaining price stability as the primary objective of the Magyar Nemzeti Bank. The MNB's supreme decision-making body is the Monetary Council. The Council convenes as required by circumstances, usually twice a month, according to a pre-announced schedule. At the second scheduled meeting each month, members consider issues relevant to immediate policy decisions. Abridged minutes of the Council's rate-setting meetings are released regularly, before the next policy meeting takes place. The minutes present the decision-makers' assessment of current economic conditions and the factors they consider when deciding on the base rate. Until December 2013, the Monetary Council presented the information underlying its assessments as part of the abridged minutes. In order to provide more detailed information, background materials will henceforth appear as a separate publication with enhanced content under the title 'Macroeconomic and financial market developments', at the same time as the abridged minutes.

The minutes are available on the MNB's website at:
http://www.mnb.hu/en/monetary-policy/the-monetary-council/minutes

THE COUNCIL’S ASSESSMENT AND INTEREST RATE DECISION

In the Council’s assessment, Hungarian economic growth picked up over the forecast horizon. Some degree of unused capacity had remained in the economy, but this was likely to be gradually absorbed as output grew dynamically. In the September projection, the inflation target was expected to be achieved in a sustainable manner one additional quarter later, i.e. by the middle of 2019, following a delay of half a year indicated in the June projection.

In August 2017, inflation had risen to 2.6 percent and core inflation to 2.8 percent. The increase in core inflation had mainly reflected base effects and temporary effects, such as changes in the prices of tobacco and dairy products. In line with the Bank’s expectations, measures of underlying inflation were around 2 percent, significantly below the level of core inflation. The expansion in domestic employment, the tight labour market as well as increases in the minimum wage and the guaranteed minimum wage had led to a general, dynamic rise in whole-economy wages. The upward effect of this on costs was being offset by the reduction in employers’ social contributions and in the corporate income tax rate early this year. In line with the Bank’s expectations, there had not yet been any significant upward pressure on inflation from wages. The rise in global inflation which had started at the beginning of the year had stalled, and consumer price indices in some economies had fallen. The European Central Bank revised down its projection for euro-area inflation again. External inflation, particularly in the euro area, was likely to remain low for a prolonged period.

In the coming months, the consumer price index was likely to decline again from its current level to the bottom of the tolerance band by the end of 2017. Core inflation was expected to decrease in the second half of next year as the temporary effects waned. Looking ahead, the Bank’s measures of underlying inflation were expected to be around 2 percent. Moderate imported inflation and historically low inflation expectations as well as the VAT rate cuts, announced for next year, had been slowing the rise in domestic prices. According to the projection in the September Inflation Report, the price stability target could be achieved sustainably one quarter later, i.e. by the middle of 2019.

Growth of the Hungarian economy had continued in the second quarter of 2017. Industrial production had stagnated in July due to factory shutdowns in the summer. A reversal and gradual pick-up in industrial production was expected towards the end of the year. Robust growth in construction and the expansion in the performance of the service sector were likely to continue in the coming months. Retail sales growth had slowed somewhat in July. Labour demand had remained strong: employment had been at historically high levels in the second quarter of 2017. The unemployment rate had remained at a low level. The general increase in domestic demand would continue to play a central role in economic growth. Hungary’s current account surplus was expected to fall over the forecast horizon in response to rising domestic demand. Economic growth this year would also be supported by the fiscal budget and the stimulating effects on investment of EU funding. The Monetary Council expected annual economic growth of 3.6 percent in 2017 and stable growth of between 3-4 percent over the coming years. The Bank's and the Government's stimulating measures contributed substantially to economic growth.

Sentiment in international financial markets had, on the whole, improved in the period since the Council's previous interest rate decision. Besides an escalation in geopolitical risks, favourable macroeconomic data and negotiations about Brexit also had had an effect on risk appetite. Investors' perceptions about the Central and Eastern European region had continued to be positive. Due to the different inflation paths expected in the countries of the region and the different characteristics of inflation targeting regimes, market pricing suggested that the timing of central bank actions would differ. The amount of liquidity crowded out due to the introduction of an upper limit on the stock of three-month deposits had continued to have a marked influence on domestic money market rates. The three-month BUBOR had fallen to a new historic low. The yield curves for the interbank and government securities markets had shifted downwards. Three and five-year yields on government securities were at their historical lows.

In the Council's assessment, some degree of unused capacity had remained in the economy, but this was likely to be absorbed gradually as output grew dynamically. The inflation target was expected to be achieved in a sustainable manner one additional quarter later, i.e. by the middle of 2019, following a delay of half a year indicated in the June projection.

In discussing the current decision, several members noted that the external environment continued to pose a downside risk to inflation, which was also indicated by incoming data and by repeated downward revision to the projection by the European Central Bank. In addition, several members emphasised that, on the whole, monetary conditions had become tighter in recent months. Members noted that, as a result, the date of the sustainable achievement of the inflation target had been delayed by one quarter based on the September Inflation Report projection. The date of the sustainable achievement of the inflation target had already been delayed by half a year in the June projection; therefore, there had been a delay of three quarters in a short period, to the middle of 2019. Members agreed that the easing in monetary conditions was in accordance with the Council's commitment to maintaining loose monetary conditions as well as its September projection. Several members noted that the decision to ease monetary conditions was supported by earlier communications by the Bank. In conclusion, members argued unanimously that the sustainable, medium-term achievement of the inflation target and maintaining loose monetary conditions warranted monetary easing. Members agreed that such an easing should be achieved through harmonised measures. It was an important objective to implement monetary easing through a reduction in the overnight deposit rate over the longest possible section of the yield curve. This could be achieved in an effective manner with the use of swap instruments. In the course of the discussion, it was noted that it was of key importance to monitor the measures taken by the European Central Bank, as they had an effect on relative monetary conditions on their own. Members emphasised that the Monetary Council would continue to monitor closely the risks to inflation and developments in monetary conditions, and would stand ready to ease them further using additional unconventional, targeted instruments.

Achieved through the change in monetary policy instruments, the earlier loose monetary conditions, necessary to meet the inflation target in a sustainable manner, had, on the whole, become tighter in recent months. The repeated delay in the date of meeting the inflation target also warranted monetary easing. The Monetary Council decided on harmonised measures to ensure the adequate monetary conditions. In particular, the Council reduced the interest rate on the overnight central bank deposit by 10 basis points. In addition, the Monetary Council made a unanimous decision on a HUF 75 billion upper limit on the stock of three-month central bank deposits outstanding from the end of 2017. The stock of swap instruments would be increased in the coming period. The objective of the latter was to provide the loosening effect up to the longest possible section of the yield curve as soon as possible.

In the Council's assessment, the limitation on the stock of three-month deposits had fulfilled its role and the HUF 75 billion year-end upper limit on the stock would not be reduced further. The importance of the stock and maturity structure of swap instruments providing forint liquidity would increase in the future.

The Council lowered the overnight deposit rate by 10 basis points to -0.15 percent and left the base rate, the overnight and one-week lending rates unchanged by a unanimous vote. The Council considered that the external environment continued to pose a downside risk to inflation. In the Council's assessment, maintaining the base rate and loose monetary conditions for an extended period were necessary to achieve the inflation target in a sustainable manner. The Monetary Council would continue to monitor closely the risks to inflation and developments in monetary conditions, and would stand ready to ease them further using additional unconventional, targeted instruments.

Votes cast by individual members of the Council:

In favour of maintaining the base rate, the overnight collateralised lending rate, the one-week collateralised lending rate at 0.9 percent **and** **the reduction of the interest rate on the overnight central bank deposit by 10 basis points to -0.15 percent:**	9	Gusztáv Báger, Ferenc Gerhardt, Kolos Kardkovács, György Kocziszky, György Matolcsy, Márton Nagy, Bianka Parragh, Gyula Pleschinger, László Windisch
Vote against:	0	

The following members of the Council were present at the meeting:

Gusztáv Báger

Ferenc Gerhardt

Kolos Kardkovács

György Kocziszky

György Matolcsy

Márton Nagy

Bianka Parragh

Gyula Pleschinger

László Windisch

The Council will hold its next policy meeting on 24 October 2017. The minutes of that meeting will be published at 2 pm on 8 November 2017.