ABRIDGED MINUTES OF THE MONETARY COUNCIL MEETING OF 30 JANUARY 2018

Time of publication: 2 pm on 14 February 2018

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

Before taking its policy decision on 30 January, the Council reviewed recent developments in inflation and the macro economy. In the Council’s assessment, in parallel with the pick-up in domestic demand, Hungarian economic output was close to its potential level. Growth of the Hungarian economy would continue to be dynamic in 2018, then it would slow down from 2019 if the assumptions underlying the current projections held. The inflation target was expected to be achieved in a sustainable manner by the middle of 2019.

In December 2017, inflation had stood at 2.1 percent and core inflation at 2.7 percent. The inflation and the core inflation had been in line with the Bank's expectations. The Bank’s measures of underlying inflation had remained unchanged overall and had continued to be significantly below 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 in 2017 and 2018. In line with the Bank’s expectations, there still had not yet been any significant upward pressure on inflation from wages. Oil prices had risen in recent months. According to the European Central Bank's projections, in the euro area, underlying inflation would continue to be moderate in the coming years as well.

According to our current projection, the consumer price index would level off at the bottom edge of the tolerance band in the first months of 2018. Over the medium term, buoyant domestic demand, increase in wage costs, as well as the second-round effects resulting from higher commodity prices would point to the increase in domestic core inflation. However, moderate external inflation and inflation expectations stabilising at historically low levels, as well as subsequent reductions in employers’ social contributions, and the VAT rate cuts, announced for this year, were slowing the rise in prices. In our projection, the inflation target could be achieved sustainably by the middle of 2019.

The Hungarian economy had grown by 3.9 percent in the third quarter of 2017. Industrial production and the volume of retail sales had continued to grow in November. Labour demand had remained strong: employment had been at historically high levels in September-November 2017. The unemployment rate had fallen further.

Looking ahead, the general strengthening of domestic demand would continue to play a central role in economic growth. Robust growth in construction and the expansion in the performance of the service sector were likely to continue in the coming months. Hungary’s current account surplus was expected to fall in 2018, driven by rising domestic demand. Economic growth this year would also be supported by the fiscal budget and the stimulating effects on investment of European Union funding. In the Council’s assessment, GDP growth would approach 4 percent after 2017, in 2018, then it would slow down from 2019 if the assumptions underlying the current projections held. The Bank’s and the Government’s stimulating measures contributed substantially to economic growth.

Sentiment in international financial markets had, on the whole, been positive in the period since the Council's previous interest rate decision. Monetary policy decisions by the world's leading central banks and the latest macroeconomic data had been the main factors influencing investors' appetite for risk. In December, the Fed had decided to further increase the base rate. As a result of the incoming macroeconomic data since then, markets expected the next interest rate increase by March. Looking ahead, the European Central Bank was likely to maintain loose monetary conditions for an extended period. Investors' perceptions about the Central and Eastern European region 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 prices suggested that the timing of central bank actions would differ.

Yields in the domestic money and capital markets had been around their historic low. Short-term yields were at a level close to or below zero. Long-term yields, with increased volatility at the end of the period, had fallen significantly overall in the past months. The decline in yields had occurred in a way that the spreads relative to the euro area and regional yields had significantly narrowed.

Following the review of macroeconomic and financial market developments, the Council discussed the details of the current monetary policy decision. Members agreed that data becoming available over the recent month had been in line with the baseline scenario of the December projection and no such real economy or financial market event had occurred that would justify a change in the monetary policy. In the members' opinion underlying inflation in the euro area had remained moderate, while the domestic underlying inflation, in accordance with the expectations, continued to fall short of core inflation. Members concluded that the upward effect of dynamic wage growth on the inflation rate continued to be moderate and inflation would rise gradually towards the target as domestic demand picked up. Some members pointed out that in relation to achieving sustainable price stability, prevailing low inflation expectations were of key importance. In terms of the external environment rising world price of oil and monetary policy of the ECB and the central banks of the region warranted special focus. Several members stressed that the global monetary policy environment was about to change. Long-term yields in the USA and in the euro area had somewhat risen, nevertheless according to market expectations loose monetary conditions were likely to stay in the euro area for an extended period. As a result of the two new unconventional instruments and the central bank's communication, since September 2017 domestic long-term yields had significantly decreased compared to the yields observed in the euro area and in the region as well. Members agreed that in the assessment of the new instruments the relative position of Hungarian yields compared to international yields should be monitored closely.

In the Council's assessment, maintaining the loose monetary conditions for an extended period was necessary to achieve the inflation target in a sustainable manner. To this end, the Monetary Council had maintained the base rate, the overnight collateralised lending rate, the one-week collateralised lending rate at 0.9 per cent, and the overnight deposit rate at -0.15 per cent. In the Council's assessment, the gradual limitation on the stock of three-month deposits had fulfilled its role and the HUF 75 billion year-end upper limit on the stock for 2017 would not be reduced further. In line with maintaining monetary conditions, the Council set a HUF 400-600 billion band for the targeted average liquidity crowded-out for the first quarter of 2018, which was equal to that of the fourth quarter of 2017. On the next occasion, in March 2018, the Council would decide on the amount of liquidity crowded out and would adjust the stock of central bank swap instruments accordingly.

The Council's aim was that the loose monetary conditions had their effect not only at the short but also at the longer end of the yield curve. To ensure this, the central bank had started targeted mortgage bond purchases in January and had held the first tender of the unconditional monetary policy interest rate swap facility. In a view of the experiences had gained from the first tender, the central bank had fine-tuned the details of the programme to achieve more effective monetary transmission. The MNB would continue the mortgage bond purchases and the monetary policy interest rate swap facility as programmes, continuously and for a prolonged period, thus they constituted integral part of the set of monetary policy instruments. In harmony with the Council's forward guidance, the new instruments contributed efficiently to the maintenance of loose monetary conditions over a prolonged period, and contributed to an increase in the share of loans with long periods of interest rate fixation, thereby improving financial stability. The Monetary Council focused on the relative position of domestic long-term yields relative to international yields when evaluating the programme.

Members were of the view that no material change was expected in the monetary policy framework; however, the Bank's set of monetary policy instruments might be fine-tuned in the future as well. Members agreed that close attention should be paid to both the operation of the extended set of monetary policy instruments and monetary conditions.

The inflation target was expected to be achieved in a sustainable manner by the middle of 2019. In the Council's assessment, maintaining the base rate and the loose monetary conditions at both short and long ends for an extended period was necessary to achieve the inflation target in a sustainable manner. The Council would closely monitor developments in monetary conditions and would ensure the persistence of loose monetary conditions over a prolonged period by using the extended set of monetary policy 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** **maintaining the interest rate on the overnight central bank deposit at -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 27 February 2018. The minutes of that meeting will be published at 2 pm on 14 March 2018.