MINUTES

OF THE MONETARY COUNCIL MEETING

26 APRIL 2016

Time of publication: 2 pm on 11 May 2016

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 continued. A degree of unused capacity remained in the economy, and therefore the domestic real economic environment continued to have a disinflationary impact. Inflation remained persistently below the Bank's target.

The annual inflation rate and core inflation both had decreased in March 2016 relative to the previous month. The Bank's measures of underlying inflation continued to indicate moderate inflationary environment in the economy. Persistently low global inflation contained the increase in domestic consumer price inflation. Core inflation was rising gradually as a result of the recovery in household consumption and the pick-up in wages. Inflation expectations remained at historically low levels. Inflation remained below the 3 per cent target over the forecast period, and only approached it in the first half of 2018.

The Hungarian economy had grown dynamically again in the fourth quarter of 2015. Over the last year as a whole, the economy had grown at a rate close to 3 per cent. Based on monthly indicators, economic activity had slowed in the first quarter of 2016. Annual growth in industrial output in February had been lower than the high levels recorded at the end of 2015, and the volume of construction output also had fallen relative to the same period of the previous year. However, according to February data, retail sales had grown at a faster pace than in previous months. The employment rate had risen and the unemployment rate had fallen further. The deceleration in funding inflows from the EU led to a slowdown in growth, but the Bank's and with a growing significance the Government's policy measures were making an increasing contribution to the economic recovery. In the Council's assessment, economic growth accelerated again from the middle of the year and a growth rate of around 3 per cent could be maintained through the Bank's Growth Supporting Programme as well as the steps taken by the Government to encourage home construction and to facilitate the faster draw-down of EU transfers. Rising incomes, the pick-up in lending and the gradual decline in households' precautionary considerations contributed to the expansion in consumption, which in turn provided considerable support for economic growth in the coming years.

Sentiment in global financial markets had been volatile since the Council's latest policy decision, mainly driven by expectations related to the monetary policy stance of the world's leading central banks and news coming from oil markets. Short-term interbank yields and government bond yields had declined since the previous policy decision. Hungary's strong external financing capacity and the resulting decline in external debt were contributing to the sustained reduction in the vulnerability of the economy. In the Council's assessment, a watchful approach to monetary policy was still warranted due to uncertainty in the global financial environment.

The unconventional, targeted monetary policy instruments introduced by the Bank facilitated a decline in long-term yields and, consequently, an easing in monetary conditions. Forward-looking money market real interest rates were in negative territory and were declining even further as inflation rose.

In the Council's assessment, there continued to be a degree of unused capacity in the economy and inflationary pressures remained moderate for an extended period. The real economy had a disinflationary impact over the policy horizon. If the assumptions underlying the March Inflation Report projection held, inflation would approach the 3 per cent target only in the first half of 2018.

In discussing the current decision, members advanced various arguments for continuing the interest rate cutting cycle; however, several members emphasised the need for caution in relation to the extent of the continuation of the cycle. Members agreed that both international and domestic factors pointed to monetary easing. Low inflation and interest rate environment abroad, and in particular the monetary policy of the European Central Bank, supported the MNB's easing cycle. Of the domestic macroeconomic factors, it was moderate inflation and inflation expectations as well as the existence of unused capacities that warranted the continuation of the interest rate cutting cycle. However, several members drew attention to the stronger-than-expected increase in whole-economy wages at the beginning of the year, which was likely to warrant a more cautious monetary policy approach. In addition, some members noted that next year's draft budget contained important new information also from a monetary policy perspective. Greater focus in the budget on the stimulation of demand than previously thought might play an increasing role in the closure of the output gap. Several members expressed that they did not support a further reduction in the overnight deposit rate in the negative territory. Using negative interest rates is still a new phenomenon in monetary policy, and therefore it was useful to wait for international experience in this field. Another member thought that narrowing the interest rate corridor was in line with the MNB's long-term objectives.

Taking these factors into account, all members supported the reduction in the base rate; however, one member proposed a smaller, 10 basis points reduction. In that member's opinion, before making a larger reduction in the central bank base rate, members should wait patiently to see whether the policy easing by the ECB announced recently would have a material impact on corporate lending. One member noted that market participants' expectations about the bottom of the interest rate path were excessively low, and it was therefore proposed to provide a stronger signal to the public in the press release about where the MNB thought the interest rate cutting cycle would end. Another member argued that the room for interest rate cuts was narrowing. In the Council's assessment, the sustainable achievement of the inflation target pointed to a further slight reduction in the policy rate.

Phase 3 of the Self-Financing Programme had contributed to a decline in long-term government securities yields. The risks of second-round effects resulting in below-target inflation over a sustained period remained, due to persistently low cost-side inflationary pressure, the slowdown in global growth and the historically low level of inflation expectations. The Monetary Council continued its interest rate cutting cycle in order to mitigate these risks and decided to reduce the central bank base rate by 15 basis points. The Council left the overnight deposit rate unchanged at -0.05 per cent and lowered the overnight lending rate by 15 basis points to 1.3 per cent. The Monetary Council remained ready to use every instrument at its disposal to contain second-round inflationary effects. In the Council's assessment, the sustainable achievement of the inflation target pointed to a further slight reduction in the policy rate.

Votes cast by individual members of the Council:

In favour of reducing the base rate to 1.05%:	**8**	Gusztáv Báger, Andrea Bártfai-Mager, Ferenc Gerhardt, György Kocziszky, György Matolcsy, Márton Nagy, Gyula Pleschinger, László Windisch
In favour of reducing the base rate to 1.10%:	**1**	János Cinkotai
In favour of reducing the overnight collateralised loan rate to 1.3% and maintaining the overnight central bank deposit rate at -0.05%:	**8**	Gusztáv Báger, Andrea Bártfai-Mager, Ferenc Gerhardt, György Kocziszky, György Matolcsy, Márton Nagy, Gyula Pleschinger, László Windisch
Vote against:	**1**	János Cinkotai

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

Gusztáv Báger

Andrea Bártfai-Mager

János Cinkotai

Ferenc Gerhardt

György Kocziszky

György Matolcsy

Márton Nagy

Gyula Pleschinger

László Windisch

The Council will hold its next policy meeting on 24 May 2016. The minutes of that meeting will be published at 2 pm on 8 June 2016.