MINUTES

OF THE MONETARY COUNCIL MEETING

28 MARCH 2017

Time of publication: 2 p.m. on 12 April 2017

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 following the temporary slowdown last year, but this was likely to be gradually absorbed as the economy grew. Inflation reached the target sustainably from the first half of 2018.

The increase in inflation, mainly driven by base effects, had continued in February 2017. However, the Bank's measures of underlying inflation had remained stable, in line with expectations. The price index was likely to rise temporarily further slightly over the next month, and then to fall below the target from the spring months as the base effects at the beginning of the year faded. Whole-economy wage growth was likely to pick up further, reflecting the dynamic expansion in employment, the tight labour market and the wage agreement at the end of last year. The upward effect of this on costs was likely to be offset by the reduction in employers' social contributions and in the corporate income tax rate. To a smaller extent, this was expected to lead to higher core inflation and, to a greater extent, to a reduction in the trade surplus through an expansion in household consumption. In the baseline projection, inflation reached the 3 per cent level consistent with price stability in a sustainable manner from the first half of 2018.

Hungarian economic growth had continued in the fourth quarter of 2016. In January 2017, the volume of retail sales had picked up and industrial production had risen relative to the same period a year earlier. Construction output had grown strongly in January following the sharp decline in the previous year; and output growth was expected to continue in the coming months. Labour demand had remained strong. Employment had continued to increase and the unemployment rate had fallen to a historic low. In parallel with strong wage growth, household consumption was likely to grow dynamically, which would be supported by the compensation of consumption deferred from previous years as well. Hungary's current account surplus was expected to fall significantly over the forecast horizon, driven by rising domestic demand.

The Funding for Growth Scheme, which had been launched in June 2013, would close at the end of March 2017. The programme had achieved its goal, by facilitating financing for nearly 40,000 companies, it had contributed greatly to the dynamic growth in SME borrowing which had amounted to 12 per cent last year. The transition to lending under market conditions was assisted by the Bank's Market-Based Lending Scheme. Under this programme, credit institutions had committed to expanding their lending by HUF 170 billion this year. As a result, growth of between 5–10 per cent in lending to SMEs was expected to be maintained. Economic growth this year would also be supported by the budget and the stimulating effects on investment of EU funding. The Monetary Council expected stable annual economic growth of between 3–4 per cent over the coming years, to which the Bank's and the Government's measures to stimulate economic growth contributed substantially.

The divergence of monetary policies across the world's major central banks had continued since the Council's latest interest rate-setting meeting. The US Fed had continued its tightening cycle, in line with expectations, while the ECB, being the most relevant for Hungarian monetary policy, continued to maintain its loose monetary policy conditions. The majority of developed market equity indices and yields on long-term government securities had risen. The amount of liquidity crowded out following 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. As a consequence, the three-month BUBOR had remained at a historically low level and short-term yields in the government securities market had fallen slightly. Domestic long-term yields had risen somewhat, in line with global trends.

Hungary's strong external financing capacity and the decline in external debt were contributing to the sustained reduction in the vulnerability of the economy. Forward-looking domestic money market real interest rates had fallen substantially over recent years and were expected to remain in negative territory for a prolonged period. In the Council's assessment, a watchful approach to monetary policy was still warranted due to uncertainty in the global financial environment.

In the Council's assessment, some degree of unused capacity had remained in the economy following the temporary slowdown last year, but this was likely to be absorbed gradually as the economy grew. Over the forecast period, inflation reached the target sustainably from the first half of 2018.

In discussing the current decision, Council members noted that the March Inflation Report provided an opportunity for an overall assessment of recent developments in inflation, the real economy and the external monetary environment. In view of the March Report projection, the Council assessed that no event had occurred in terms of Hungarian economic fundamentals and the sustainable achievement of the inflation target which would warrant a change to the current level of the base rate or the interest rate corridor. Members noted that leaving the base rate unchanged was consistent with the baseline projection in the March Inflation Report, the Monetary Council's previous communications and market expectations. Several members concluded that underlying inflation had been unchanged and the rise in inflation mainly reflected base effects and was judged to be temporary. Members noted that potential inflationary effects of the tight labour market and the global environment should be monitored closely. Several members noted that the macroeconomic outlook was surrounded by both upside and downside risks, although those risks were balanced.

The Bank continued to aim to maintain loose monetary conditions and provide a corresponding degree of support to the economy through money market rates. Members agreed that the HUF 500 billion upper limit set on the stock of three-month central bank deposits as at the end of the second quarter of 2017 would ensure that the amount of liquidity crowded out over the past two quarters was preserved and, consequently, that the loose monetary conditions achieved were maintained. In addition, the extension of the existing range of swap instruments providing forint liquidity with 6 and 12-month facilities also supported the efficient functioning of the quantitative limits. Taking these factors into account, all members voted unanimously in favour of leaving the base rate, the overnight deposit rate, the overnight lending rate and the one-week lending rate unchanged.

If the assumptions underlying the Bank's projections held, maintaining the current level of the base rate and loose monetary conditions achieved through the change in monetary policy instruments for an extended period was consistent with the medium-term achievement of the inflation target and a corresponding degree of support to the economy. The Monetary Council monitored developments in monetary conditions and markets. If inflation remained persistently below the target, the Council would stand ready to ease monetary conditions further using unconventional, targeted instruments.

Votes cast by individual members of the Council:

In favour of maintaining the base rate, the overnight central bank lending rate and the one-week collateralised central bank lending rate at 0.90% and maintaininging the overnight central bank deposit rate at -0.05%:	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 25 April 2017. The minutes of that meeting will be published at 2 p.m. on 10 May 2017.