MINUTES

OF THE MONETARY COUNCIL MEETING

15 DECEMBER 2015

Time of publication: 2 pm on 23 December 2015

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

The Magyar Nemzeti Bank's Monetary Council decided that, beginning from December 2015, it would issue shorter-form press releases following its policy meetings in the months of publication of the Inflation Report, in order to facilitate comparison of monthly press releases. The press releases would have the same format as those issued monthly between Inflation Reports.

In parallel, the Council's statements published previously in the Inflation Reports' months would be transformed into an introductory chapter of the Inflation Report, describing the Council's assessment of macroeconomic conditions entitled 'The Monetary Council's key findings'.

At its meeting on 15 December, the Monetary Council discussed the December 2015 Inflation Report. If the assumptions underlying the Bank's projections held, the current level of the base rate and maintaining loose monetary conditions for an extended period, over the entire forecast horizon, were consistent with the medium-term achievement of the inflation target and a corresponding degree of support to the economy.

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 substantially below the Bank's target.

The annual inflation rate had increased slightly and core inflation had been broadly unchanged in November 2015. The Bank's measures of underlying inflation continued to indicate moderate inflationary pressures in the economy. Core inflation had been rising gradually as a result of an expansion in household consumption and an acceleration in wage growth, but the persistently low global inflationary environment contained the increase in the domestic consumer price index. Inflation expectations had fallen to a historic low. Inflation was expected to remain below the 3 per cent target over the forecast period, and was only likely to approach it by the end of the forecast horizon.

Hungarian economic growth had continued at a weaker-than-expected rate in the third quarter of 2015. The decline in agricultural production and the moderation in industrial production dynamics had been the main contributing factors to the deceleration. As in previous months, retail sales had been stable in October, with their volume increasing across a wide range of products. Employment and unemployment had been broadly unchanged. The deceleration in external demand and in funding from the EU would lead to a significant slowdown in growth in 2016. Recovery was expected from the second half of 2016, mainly reflecting the strengthening performance of Hungary's export markets as well as the Bank's and the Government's policy measures. In the Council's assessment, the Bank's Growth Supporting Programme and the recent steps taken by the Government to encourage home building were expected to dampen the slowdown in the rate of growth. In addition to these factors, rising household consumption was likely to support the economic expansion in the coming years.

Sentiment in global financial markets had been volatile in the past month, deteriorating significantly during the last week. Over the period, the main factors affecting appetite for risk had been the ECB's communication suggesting that it would adopt a looser monetary policy stance and its policy decision, continued uncertainty about an interest rate increase by the Fed, and concerns over growth prospects in emerging economies. Conditions in Hungarian financial markets had been mostly influenced by international factors. The forint exchange rate had weakened and Hungary's CDS spread had been broadly unchanged in the period since the previous policy decision. Hungary's persistently 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 cautious approach to monetary policy was still warranted due to uncertainty in the global financial environment.

Market yield expectations had been in line with the Bank's forward guidance that the base rate would be held constant over an extended period. The unconventional, targeted monetary policy instruments introduced by the Bank also facilitated a decline in long-term yields and, consequently, a loosening in monetary conditions. Forward-looking money market real interest rates were in negative territory and were declining even further as inflation rose.

In view of the December Inflation Report, the Council judged that the reduction in unused capacity temporarily stopped as economic growth slowed, and therefore the negative output gap would close only at the end of the policy horizon. In line with this, inflationary pressures would remain moderate over a sustained period and inflation was expected to approach the inflation target by the end of the forecast horizon. Several members noted that for them the sustainable achievement of the target meant that inflation approached the target not just for a short period, but, looking forward, moved around the price stability objective over an extended period. To this end, solid economic growth and maintaining loose – if necessary looser than that of the current – monetary conditions, over an extended period were required. Some members pointed out that, in the macroeconomic environment following the crisis, the risk of undershooting the inflation target was greater than that of overshooting it, due to economic agents' historically low inflation expectations. If the assumptions underlying the Bank's projections held, the current level of the base rate and maintaining loose monetary conditions for an extended period, over the entire forecast horizon, were consistent with the medium-term achievement of the inflation target and a corresponding degree of support to the economy. In view of this, members voted unanimously in favour of leaving the base rate unchanged.

Members agreed that the inflation target could be achieved in a sustainable way by holding the base rate unchanged for an extended period and by using unconventional, targeted monetary policy instruments. Some members added that an advantage of these programmes was that they were targeted, as they contributed efficiently to the further loosening in monetary conditions, particularly to the decline in long-term yields. One member noted that in some cases the unconventional tools also supported the achievement of the Bank's other objectives. In this spirit, Council members examined thoroughly the range of potentially applicable tools. In the Council's view, the current decision was consistent with the Bank's past behaviour and previous communication as well as with market expectations, and therefore it strengthened the Bank's credibility and predictability.

Votes cast by individual members of the Council:

In favour of maintaining the base rate at 1.35%	**9**	Gusztáv Báger, Andrea Bártfai-Mager, János Cinkotai, Ferenc Gerhardt, György Kocziszky, György Matolcsy, Márton Nagy, Gyula Pleschinger, László Windisch

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 26 January 2016. The minutes of that meeting will be published at 2 pm on 10 February 2016.