MINUTES
OF THE MONETARY COUNCIL MEETING
22 AUGUST 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. The inflation target was expected to be achieved in a sustainable manner from early 2019.

In July 2017, inflation had risen to 2.1 percent and core inflation to 2.6 percent. The increase in core inflation adjusted for the effects of indirect taxes had primarily reflected the change in processed food prices. Developments in the Bank's measures of underlying inflation had remained stable, in line with expectations. 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 upward pressure on inflation from wages. Global inflation had started to rise at the end of 2016, but had moderated in recent months. The external inflation environment, particularly in the euro area, was likely to remain low for a prolonged period.

The consumer price index was likely to rise temporarily in the coming months, before easing back to around current levels by the end of the year. To a smaller extent, the expansion in household consumption was expected to lead to higher core inflation and, to a greater extent, to a reduction in the trade surplus. Moderate imported inflation and historically low inflation expectations as well as the VAT rate cuts, announced for next year, were slowing the rise in domestic prices. In the baseline projection, the 3 percent inflation target was expected to be achieved in a sustainable manner from early 2019.

The GDP data for the second quarter of 2017 had shown that Hungarian economic output growth had continued. Industrial production had risen again in June; and the sector's performance was expected to be buoyant in 2017 as a whole. Robust growth in construction was likely to continue in the coming months. In June, the volume of retail sales had risen. Labour demand had remained strong: employment had grown further in the second quarter of 2017 and the unemployment rate had remained at historically low levels. Driven mainly by strong growth in investment alongside continued expansion in household consumption, the 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 stable annual economic growth of between 3–4 percent over the coming years, to which the Bank's and the Government's measures to stimulate economic growth contributed substantially.

The Funding for Growth Scheme had ended at the end of March 2017. After it had been phased out, the transition to lending under market conditions was ensured by the Bank's Market-Based

Lending Scheme introduced in early 2016 and extended in 2017. At the tender held in the second phase of the Scheme in July, commercial banks had raised their lending commitment by one-third. This would ensure that growth in lending to SMEs was maintained in the upper half of the 5–10 percent range, deemed necessary by the MNB for sustainable economic growth.

Sentiment in international financial markets had been mixed in the period since the Council's previous interest rate decision. Risk appetite had been influenced mainly by the release of macroeconomic data and expectations related to the monetary policy of the world's leading central banks. Market expectations for the timing of policy tightening by the ECB had shifted out. Investors' perceptions about the Central and Eastern European region had improved, which had led to an appreciation of local currencies. However, there were significant differences among the countries of the region, and therefore it was useful to distinguish between them. Those differences included macroeconomic developments and the specific characteristics of central banks' inflation targeting regimes. Consequently, although inflation was rising in every country of the region, taking account of the changed monetary conditions and the different inflation targets, market pricing suggested that the timing of central bank actions would differ.

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. Over the forecast period, the inflation target was expected to be achieved in a sustainable manner from early 2019.

In discussing the current decision, the Council assessed that no event had occurred since the previous rate decision 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.

All members pointed out that it was the maintenance for an extended period of the unchanged base rate and the loose monetary conditions achieved through the change in monetary policy instruments earlier, which was consistent with the baseline projection in the June Inflation Report. The recent inflation and GDP data had been in line with the Council's expectation; and there had been a general improvement in investor sentiment about the region. Several members added that recent data on the external environment had underlined the downside risks to inflation identified in the June projection. For one member, it was important to point out that changes in the prices of tobacco products contributed significantly to the rise in core inflation; however, measures of underlying inflation continued to be stable. Members stressed that the Council should continue to pay close attention to global inflation and financial market developments, as well as to current and expected future monetary policy of developed country central banks, in particular the ECB and the Fed. In addition, members attached great importance to the continuous analysis of monetary conditions, to assess whether they ensure the sustainable achievement of the 3 percent inflation target. Members agreed that, in the light of recent information, it was useful to send a stronger monetary policy message than previously by abandoning the conditionality of the forward guidance. Consistent with this, they stressed that the Monetary Council would stand ready to ease monetary conditions further using unconventional, targeted instruments to ensure the monetary conditions necessary to meet the inflation target in a sustainable manner.

At its meeting in June 2017, the Council had set a HUF 300 billion upper limit on the stock of three-month central bank deposits as at the end of the third quarter of 2017, in order to preserve the amount of liquidity crowded out of the deposit facility, and thereby to maintain the loose monetary conditions achieved. The MNB had managed uncertainties related to liquidity developments in the banking sector using fine-tuning operations introduced in October 2016 and extended with longer maturities in March 2017. The additional liquidity provided by the MNB to the banking system rose to HUF 950 billion by early August. Members of the Monetary Council agreed that the use of instruments with a maturity of 6 and 12 months has successfully contributed to the maintenance of loose monetary conditions for an extended period. The limit set on the three-month deposit stock and its potential future change were considered to be integral parts of instruments. The Bank continued to aim to maintain loose monetary conditions and provide a corresponding degree of support to the economy through money market rates. The Monetary Council intended to ensure that the limit imposed on the stock of three-month deposits exerted its expected effect on monetary conditions efficiently. The limit was set quarterly. On the next occasion, a decision on its level as at end of the fourth quarter of 2017 would be made in September 2017. Taking all 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, it was the maintenance for an extended period of the current level of the base rate and the loose monetary conditions achieved through the change in monetary policy instruments earlier, which was consistent with the medium-term achievement of the inflation target and a corresponding degree of support to the economy. In the Council's assessment, the external environment continued to pose a downside risk to inflation. The Council would stand ready to ease monetary conditions further using unconventional, targeted instruments to ensure the monetary conditions necessary to meet the inflation target in a sustainable manner.

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%:**	8	Gusztáv Báger, Ferenc Gerhardt, Kolos Kardkovács, György Kocziszky, 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

Márton Nagy

Bianka Parragh

Gyula Pleschinger

László Windisch

The Council will hold its next policy meeting on 19 September 2017. The minutes of that meeting will be published at 2 p.m. on 4 October 2017.