MAGYAR NEMZETI BANK

ABRIDGED MINUTES

OF THE MONETARY COUNCIL MEETING OF 23 APRIL 2007

Pursuant to Article 3 (1) of the Central Bank Act (Act LVIII of 2001 on the Magyar Nemzeti Bank, as amended), the primary objective of the Magyar Nemzeti Bank is to achieve and maintain price stability. The MNB's supreme decision-making body is the Monetary Council. The Council is convened as required, at least twice a month, according to a pre-announced schedule. Each month, the agenda of the second meeting includes the potential modification of the base rate of interest. The abridged minutes of these meetings are published before the scheduled date of the next rate-setting meeting of the Monetary Council. The abridged minutes are divided into two parts. As a summary of the analyses drawn up by the experts of the MNB for the Monetary Council, the first part contains an overview of economic and financial trends as well as new information, which has become available since the previous meeting. Based on this information, the second part discusses the decision-makers' situation assessment and the debate concerning the decision.

The abridged minutes are available on the MNB's website at:
http://www.mnb.hu/engine.aspx?page=mnbhu_mt_jegyzokonyv

I. Macroeconomic and financial trends

While the data for the first two months of 2007 reflected a favourable inflationary trend, the latest (March) data have been more ambiguous. While the 9-percent annual inflation and 6-percent core inflation rates did not come as a surprise, the trend inflation indicator (the quarterly core inflation index, eliminating the impact of the VAT increase) declined at a rate lower than expected. The assessment of last month's inflation data is complicated by the fact that, in comparison with the previous month, the acceleration of inflation was associated with non-durable consumer goods and processed food products. More specifically, the price of outerwear products increased at a relatively high rate, which may partly be justified if shops began to sell spring collections earlier than usual. That, however, can only be determined on the basis of the data for the forthcoming months. At the same time, the inflation of services was similar to those of last year, which is an indication that the relatively high rate of wage increase in the sector has so far not resulted in a price pressure.

Wage and labour market data show an unfavourable picture. The more than 12 percent increase, during January, of the regular payments of the competitive sector was probably only partly the result of the 'whitening' of certain industries; the high wage data may thus also be an indication of an actual cost-side wage inflation pressure. While the February data show a slight decline of the rate of increase of wages, the over 10-percent increase of gross average wages, net of bonuses, of the competitive sector is a historical high.

According to the data of the latest labour market survey, unemployment is declining coupled with a sluggish rate of employment, which may also increase wage inflation pressure on an increasingly tight labour market.

There was no significant change in the economic trends during the past month. In 2006, domestic demand decelerated at a rate higher than expected, while net export increased dynamically as a result of external prosperity. However, foreign trade data for the beginning of this year show an increase of import, an indication that the improving trend of the trade balance came to a halt. A methodological uncertainty, i.e. the considerable gap between households' income and expenditure, hampers the assessment of domestic demand. In summary, there are no indications of the emergence of additional disinflation factors in the economic activity.

Since the March meeting of the Council, the external investment environment has changed favourably; in April, investors' risk appetite increased. Despite the repeated rise of oil prices, the markets tend to have a more favourable view of the outlooks of the global economy. Long-term yields increased on the major markets, reflecting the rearrangement of investments into higher-risk instruments, this time primarily into shares. As a result of bullish share markets, stock exchanges have adjusted the significant drop in prices during the February and March volatility shocks. Emerging markets premiums have also declined, the EMBI spread falling to a historical low.

Heterogeneous macro-economic data were published in the United States; however, the markets have preferred to respond to positive data during the past few months, which may be an indication of subsiding recession concerns. This was confirmed by the minutes of Fed's rate-setting policy committee meeting in March, putting the main emphasis on inflation-related risks. These have caused expectations concerning a possible interest cut in the US to abate, i.e. as compared to 50 basis points in March, markets have now priced a slackening of only 25 basis points for the year. At the same time, there have been growing expectations for an interest increase in the Euro region. In addition to the 25 basis-point tightening priced for June, the markets do not rule out a further interest rate increase on the longer run. Consequently, the Euro has continued to gain strength against the US dollar and the yen.

The Central European region is also seen positively; with the exception of the lowest interest-bearing Czech crown, Visegrad currencies have strengthened. In order to moderate the revaluation pressure on the exchange rate, the central bank of Slovakia cut the interest rate by 25 basis points, asymmetrically widened the interest rate corridor, maintained surplus inter-bank liquidity and intervened on the foreign exchange market. Beyond the expectations about an interest increase, the fact that the S&P improved Poland's debt rating (to A-) has contributed to the strengthening of the Polish zloty.

The exchange rate of the forint moved within a narrow band of 245 to 250 forints/Euro. Following the March meeting of the MC, there was a temporary weakening in the exchange rate, possibly related to the communication by the central bank about refusing to abolish the exchange rate band and, consequently, to the partial closing of the positions based on the elimination of the band.

Since mid-April, expectations about an interest cut have increased. With a year-end base rate of 6.75 to 7 percent, the yield curve on the government securities market has been consistent. Forward rates indicate that the market has now priced a 50 basis-point interest cut for the forthcoming two or three months. According to a survey by Reuters, the major part of analysts and foreign exchange traders expect the base rate to remain at the April level. Most analysts expect an interest cut in May and there has been some increase in expectations about an interest cut on the medium run.

Since there has been strong investor demand on the primary government securities market, the ÁKK has continued issuing in excess of the previously targeted level. Despite the fact that foreigners purchased a significant amount of government securities at auctions, their overall volume decreased by HUF 75 billion due to maturity and sales on the secondary market. The drop in foreigners' swap portfolio is an indication of the sales of hedged government securities, which had no impact on the exchange rate. Foreigners' exposure to forint risks has essentially remained the same.

Despite net sales by foreigners and the rise of Euro returns, HUF yields have dropped, reflecting the decrease of required premiums on the medium run. Credit derivatives have reflected the reduction of the long-term default risk, while five-year forward spread has stabilised at a level lower than before, around 150 basis points.

II. Situation assessment and decision on the interest rate

Following the review of macroeconomic information and the situation of the financial market, it was proposed that the base rate of interest should be maintained while other members proposed that it should be cut by 25 basis points.

Several Council members claimed that the picture concerning the likely inflation trend has not become considerably clearer since previous month's meeting. They claimed that the wage data of the competitive sector have been the main source of uncertainty. The Council was divided about the extent the high wage inflation of the past several months has been the result of the 'whitening' of the economy and the extent it reflects growing inflationary expectations. If the former was the case, it would be a purely statistical phenomenon; in the latter situation, however, it would increase inflationary risks. Several members emphasised that the uncertainty concerning inflation will last as long as more accurate information concerning the trends on the labour market and inflation-related outlooks are not available, which requires a cautious interest rate policy.

Most members agreed that the premium expected on forint assets had declined considerably. Various members held the view that the credibility of the fiscal adjustment measures had increased and, consequently, the premium drop had substantially been due to domestic fundamentals. In theory, that could increase the Monetary Council's scope for action. It is a warning, however, that the ECB's interest rate increase has reduced the forint's spread, which makes it uncertain to what extent the central bank's base rate of interest can be accommodated to the reduction of the required premium.

Several members stressed that an improving assessment of domestic fundamentals may result in a long-term reduction of the forint's risk premium. Therefore, while the inflationary risks continue to be significant, the scope of interest rate policy for action will increase unless additional risk factors emerge. The May forecast will enable the decision to be made on the basis of a broader set of information. One of the members, however, argued that, due to the reduction of the required premium, the time had come for an immediate 25 basis-point cut.

After the discussion, the Chairman put propositions to the vote. 12 members voted in favour of leaving the level unchanged, whereas one member supported the 25 basis-point cut. The Monetary Council therefore decided to maintain the 8-percent level of the central bank's base rate of interest.

The votes:

in favour of maintaining the base rate at 8.00%:	**12**	Péter Adamecz, Henrik Auth, Péter Bihari, Vilmos Bihari, Csaba Csáki, Ilona Hardy, Ferenc Karvalits, Béla Kádár, György Kopits, Judit Neményi, Gábor Oblath, András Simor
in favour of reducing the base rate to 7.75 percent:	**1**	Tamás Bánfi

List of attending members:

András Simor, Chairman
Henrik Auth
Péter Adamecz
Tamás Bánfi
Péter Bihari
Vilmos Bihari
Csaba Csáki
Ilona Hardy
Ferenc Karvalits
Béla Kádár
György Kopits
Judit Neményi
Gábor Oblath

The Government was represented by Álmos Kovács, State Secretary of the Ministry of Finance.

The next rate-setting meeting of the Council is scheduled for 21 May 2007. The abridged minutes of the forthcoming meeting will be released at 2 p.m., 8 June 2007.