MINUTES

OF THE MONETARY COUNCIL MEETING

20 SEPTEMBER 2016

Time of publication: 2 p.m. on 12 October 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 would continue to pick up in the remaining part of the year following the temporary slowdown at the beginning of the year. There continued to be a degree of unused capacity in the economy and inflation remained persistently below the Bank's target. Looking ahead, the disinflationary impact of the domestic real economic environment was gradually decreasing.

In August 2016, consumer prices had been slightly lower than a year earlier. Core inflation had decreased somewhat relative to the previous month. The Bank's measures of underlying inflation continued to indicate a moderate inflationary environment in the economy. Inflation was expected to rise gradually into positive range in the coming months. Persistently low global inflation was restraining the pace of increase in domestic consumer prices. Inflation expectations were at historically low levels. Whole-economy wage growth remained strong, which was likely to raise core inflation gradually through rising household consumption. Inflation remained below the 3 per cent target over the forecast period, and only got close to it by the middle of 2018.

Hungarian economic growth had picked up again in the second quarter of 2016, in line with the Bank's expectations. Growth had been supported primarily by final consumption and net exports and, on the output side, by growing services driven by the pick-up in domestic demand as well as by the correction in industrial and agricultural performance. Whole-economy investment had continued to decrease relative to the same period a year earlier, mainly as a consequence of the decline in government investment financed by EU funds. Retail sales had expanded in July also. Household consumption was expected to grow further in the coming quarters. Industrial production had fallen in July relative to the same period a year earlier, caused by the longer factory shutdowns in the summer in various manufacturing sub-sectors. Labour demand had remained strong, and therefore the number of employees had increased again, while the unemployment rate had remained at a low level. The time profile of this year's economic growth was characterised by duality. The economy had picked up following temporary slow growth at the beginning of the year, mainly supported by domestic demand. Economic growth of around 3 per cent could be achieved overall by the extension of the Funding for Growth Scheme, the Growth Supporting Programme, the easing steps of monetary policy as well as the Government's measures.

Moderate growth early this year had resulted in a more negative output gap temporarily; however, the acceleration in growth and the expansionary impact on demand of next year's fiscal budget contributed to the closure of the gap. Rising incomes and the pick-up in lending were contributing to the expansion in household consumption, which in turn strongly promoted economic growth in the coming years.

Sentiment in global financial markets had been volatile since the Council's latest interest rate-setting decision, mainly driven by the release of macroeconomic data in the US and the euro area as well as by expectations about further actions by the world's leading central banks. Short- and medium-term domestic government securities yields and interbank rates had fallen sharply since July in response to the Council's earlier announcement about the change to monetary policy instruments. But they had remained broadly unchanged in the weeks since the previous policy decision, while the forint exchange rate had remained stable. 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. These factors had also contributed significantly to the fact that the S&P – as the second of the large credit rating agencies – had upgraded Hungary's debt rating back to investment grade. Forward-looking domestic money market real interest rates were in negative range and were declining even further as inflation rose. However, 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, there continued to be a degree of unused capacity in the economy and inflation remained moderate for an extended period. The disinflationary impact of the real economy was gradually decreasing over the policy horizon.

In discussing the current decision, Council members reviewed recent macroeconomic developments based on the September Inflation Report and agreed that no event had occurred since the previous policy decision, which would warrant a change to the current interest rate level with respect to the fundamentals of the Hungarian economy as well as the sustainable achievement of the inflation target. The low global interest rate and inflation environment also underlined maintaining the base rate. Several members noted that leaving the base rate unchanged was consistent with the previous communication of the Monetary Council and market expectations as well as the latest upgrade of Hungarian government debt. Council members agreed that due to the transformation of monetary policy instruments an opportunity would present itself for the targeted adjustment of monetary conditions through the limitation of the three-month deposit facility. Taking these factors into account, all members present voted to leave the base rate and the interest rate corridor unchanged.

If the assumptions underlying the Bank's projections held, maintaining the current level of the base rate for an extended period, and the loosening of monetary conditions by the limitation of the deposit facility were consistent with the medium-term achievement of the inflation target and a corresponding degree of support to the economy. If subsequently it was warranted to loosen the monetary conditions further to meet the inflation target, the Monetary Council would stand ready to apply a stronger limitation to three-month deposits.

Votes cast by individual members of the Council:

In favour of maintaining the base rate at 0.90%:	**8**	Gusztáv Báger, János Cinkotai, Kolos Kardkovács, György Kocziszky, György Matolcsy, Márton Nagy, Gyula Pleschinger, László Windisch
In favour of maintaining the overnight collateralised loan rate at 1.15% and the overnight central bank deposit rate at -0.05%:	**8**	Gusztáv Báger, János Cinkotai, Kolos Kardkovács, György Kocziszky, György Matolcsy, Márton Nagy, Gyula Pleschinger, László Windisch
Vote against:	**0**	

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

Gusztáv Báger

János Cinkotai

Kolos Kardkovács

György Kocziszky

György Matolcsy

Márton Nagy

Gyula Pleschinger

László Windisch

The Council will hold its next policy meeting on 25 October 2016. The minutes of that meeting will be published at 2 p.m. on 9 November 2016.