MINUTES
OF THE MONETARY COUNCIL MEETING
24 APRIL 2018

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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, but at least twice a month, according to a pre-announced schedule. At the second scheduled meeting each month, members consider issues relevant to decisions on interest rates. 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

Before taking its policy decision on 24 April, the Council reviewed recent developments in inflation and the macroeconomy. In the Council's assessment, in parallel with the pick-up in domestic demand Hungarian economic output was close to its potential level. Growth of the Hungarian economy would pick up further in 2018, then, if the assumptions of the current projection hold, it would slow down gradually from 2019. The inflation target was expected to be achieved in a sustainable manner by the middle of 2019.

In March 2018, inflation had stood at 2.0 percent and core inflation at 2.4 percent. Inflation and core inflation had been in line with the Bank's expectations. The Bank's measures of underlying inflation had remained unchanged and had continued to be below core inflation. 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, which had continued into early 2018. The upward effects of this on costs was being offset by the reduction in employers' social contributions at the beginning of the year and in the corporate tax rate in 2017. In the first quarter of 2018, services prices had risen somewhat faster than last year, though still at a moderate pace. Consequently, in line with the Bank's expectations, there had not yet been any significant upward pressure on inflation from wages. Oil prices had increased over the past month. According to the ECB's projections, underlying inflation would continue to be moderate in the euro area in the coming years as well.

If the assumptions in the March projection held, the consumer price index would remain in the lower half of the tolerance band in the coming months. Over the medium term, buoyant domestic demand and the increase in wage costs would point to an increase in domestic core inflation. However, moderate external inflation and inflation expectations stabilising at historically low levels, as well as subsequent reductions in employers' social contributions and the VAT rate cuts this year, were slowing the rise in prices. If the assumptions of the current central bank projection held, the inflation target could be achieved sustainably by the middle of 2019.

The Hungarian economy had grown by 4.4 percent in the fourth quarter of 2017. Industrial production and the volume of retail sales had continued to grow in February. Labour demand had remained strong. The unemployment rate had been at its historical low. Strong credit growth had continued in February. Outstanding lending to the corporate sector had increased by nearly 10 percent relative to a year earlier. In the household sector, annual growth in lending had been 2.5 percent. A significant part of this had been related to the expansion in housing loans.

Looking ahead, the general strengthening of domestic demand would continue to play a central role in economic growth. Robust growth in construction and the expansion in the performance of the service sector were likely to continue in the coming months. From a historically high level of 6 percent in 2016, Hungary's current account surplus relative to GDP was expected to fall to below 2 percent in 2018, driven by rising domestic demand. However, it was expected to remain in positive territory over the longer term. Economic growth this year would also be supported by the fiscal budget and the stimulating effects on investment of European Union funding. In the Council's assessment, GDP growth would be above 4 percent in 2018, higher than last year, then, according to the current projection, it would slow down gradually from 2019. The Bank's and the Government's measures contributed substantially to this year's economic growth.

Sentiment in international financial markets had been volatile in the period since the Council's previous interest rate decision. Developments related to trade policy measures by the US and China had been the main factors influencing investors' appetite for risk. Market participants expected the Fed to continue raising interest rates. The ECB was likely to maintain loose monetary conditions. Investors' perceptions about the Central and Eastern European region continued to be positive. Expectations related to interest rate increases had moderated in several countries of the region. Due to the different inflation paths expected in the countries of the region and the different characteristics of inflation targeting regimes, market prices suggested that monetary policy stances by regional central banks would continue to differ.

The short end of the market yield curve had shifted upwards in recent months, while the Bank's guidance about the maintenance of loose monetary conditions over an extended period had remained unchanged. Hungarian long-term spreads over yields in the euro area and the region had fallen during the spring months following an increase earlier in the year and had decreased significantly over a longer horizon as well.

Following the review of macroeconomic and financial market developments, the Council discussed the details of the current monetary policy decision. Council members agreed that incoming data in the last month had been in harmony with the March baseline projections. Decision-makers believed that maintaining the loose monetary policy stance for a prolonged period was consistent with the expectations of analysts and market participants. This was also supported by the external environment, as global inflation and the ECB's monetary policy stance had remained broadly unchanged. In the past period, several regional central banks had sent a message indicating a looser policy stance. As a result, expectations of their interest rate increase had shifted to a later date. Some decision-makers pointed out that Hungary's external financing capacity was strong in a regional comparison. The long-term persistence of this supported domestic monetary policy. Several members noted that in recent months the short end of the yield curve had risen in certain sub-markets, despite the fact that the Bank's forward guidance had remained unchanged. In the Council's assessment, in the future special attention should be given to the changes in commodity prices and long-term yield spreads, as well as the monetary policy of the ECB and the central banks in the region, in addition to short-term yields. One member pointed out that, in addition to the favourable outlook for growth, it is also important to gradually improve competitiveness, thereby stimulating potential output to ensure sustainable economic growth.

In the Council's assessment, maintaining the loose monetary conditions for an extended period was necessary to achieve the inflation target in a sustainable manner. To this end, the Monetary Council maintained the base rate, the overnight collateralised lending rate and the one-week collateralised lending rate at 0.9 percent and the overnight deposit rate at -0.15 percent. The

Council would maintain the HUF 75 billion upper limit on the stock of three-month deposits. In addition, in March, the Council had set the average amount of liquidity to be crowded-out for the second quarter of 2018 at least at HUF 400-600 billion. Furthermore, the Council had stated that the actual amount of liquidity to be crowded out must reach a level sufficient to ensure the maintenance of the loose monetary conditions for an extended period. On the next occasion, in June 2018, the Council would decide on the amount of liquidity to be crowded out and would take this into account in setting the stock of central bank swap instruments.

In March, the Monetary Council had set the maximum stock of monetary policy interest rate swaps in the first half of 2018 at HUF 600 billion. The Council's aim was that the loose monetary conditions have their effect not only at the short but also at the longer end of the yield curve. To ensure this, the Bank would continue mortgage bond purchases and the monetary policy interest rate swap facility as programmes, continuously and for a prolonged period, and therefore they constituted an integral part of the set of monetary policy instruments.

The Council considered the Bank's mortgage bond purchase programme to be successful. Under the programme, the MNB had purchased mortgage bonds with a nominal value of some HUF 150 billion up to the middle of April. Transactions in the primary market had accounted for more than one-third of total purchases. As a result of the measures, spreads of mortgage bonds over yields in the government securities market had fallen sharply and had turned negative on average. The decline in financing costs had encouraged issuance in the primary market, thereby facilitating the increase in fixed-rate lending.

In harmony with the Council's forward guidance, the new instruments contributed efficiently to the maintenance of the loose monetary conditions over a prolonged period and to an improvement in financial stability. The Monetary Council focused on the relative position of domestic long-term yields relative to international yields when evaluating the programme.

The inflation target was expected to be achieved in a sustainable manner by the middle of 2019. In the Council's assessment, maintaining the base rate and the loose monetary conditions at both the short and long ends for an extended period was necessary to achieve the inflation target in a sustainable manner. The Council would closely monitor developments in monetary conditions and would ensure the persistence of loose monetary conditions over a prolonged period by using the extended set of monetary policy instruments.

Votes cast by individual members of the Council:

In favour of maintaining the base rate, the overnight collateralised lending rate, the one-week collateralised lending rate at 0.9 percent **and** **maintaining the interest rate on the overnight central bank deposit at -0.15 percent:**	9	Gusztáv Báger, Ferenc Gerhardt, Kolos Kardkovács, György Kocziszky, György Matolcsy, Márton Nagy, Bianka Parragh, Gyula Pleschinger, László Windisch
Vote against:	0	

<u>The following members of the Council were present at the meeting:</u>

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 22 May 2018. The minutes of that meeting will be published at 2 p.m. on 6 June 2018.