MINUTES
OF THE MONETARY COUNCIL MEETING
27 AUGUST 2019

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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

The Magyar Nemzeti Bank’s (MNB) single anchor was inflation, its primary objective was to achieve and maintain price stability. The factors determining inflation continued to show volatility. Therefore, in assessing the outlook, the Monetary Council paid more attention to the measures of underlying inflation capturing persistent trends.

Consistent with the MNB’s expectations, the annual consumer price index had started to decline in the summer months. In July 2019, inflation, core inflation and core inflation excluding indirect tax effects had fallen to 3.3 percent, 3.7 percent and 3.2 percent, respectively. Both industrial goods and services inflation had slowed compared to the previous month. Persistent inflation developments had been overall lower even than expected.

A dichotomy remained between the factors determining likely developments in inflation. Buoyant domestic demand was boosting, and weakening external activity was increasingly restraining the pace of inflation. Due to a strengthening of external disinflationary effects, core inflation excluding indirect tax effects was likely to decline gradually to 3 percent from the end of 2019. The increase of excise duty on tobacco products on a six-monthly basis, which was outside the scope of monetary policy, was likely to raise the consumer price index over the entire forecast horizon. This measure did not cause any second-round effects, consequently, did not influence changes in core inflation excluding indirect tax effects. Lower-than-expected underlying inflation data for recent months and the ongoing deterioration in external activity indicated strengthening in downside risks to the longer-term inflation outlook.

The Hungarian economy had grown by 4.9 percent in the second quarter of 2019, mainly driven by market services, industry and construction. On the expenditure side, domestic demand might have continued to grow. Labour demand had remained strong, and the unemployment rate had been close to its historically low level. The current account had remained in surplus in the first quarter of 2019. Due mainly to dynamic growth in imports, the trade surplus had declined in recent quarters, primarily reflecting strong investment activity in the corporate sector.

Economic growth was expected to slow gradually from the middle of the year, but to remain strong. Subdued economic activity in Europe from the second half of the year was also reflected in the slowdown of growth in Hungary. The Hungarian economy was expected to grow by 4.3 percent in 2019 and by 3.3 percent in 2020. As a result of further dynamic growth in credit markets, the investment rate was likely to continue to rise and stabilise at high levels in the coming years. Regarding long-term, sustainable economic growth, the improvement in competitiveness by structural measures would be given increasing emphasis.

In addition to monetary policy, the new retail government security strategy, the 2020 Budget Act and the provisions of the Economy Protection Action Plan to improve competitiveness, were aimed at further strengthening macroeconomic stability and sustainable convergence. The Hungarian Government Security Plus, introduced in June, was expected to raise households’ savings rate, in addition to the structural change of their financial assets. Consequently, an increasing share of rapid wage growth was converted into savings instead of consumption, while the promotion of self-financing also helped to reduce Hungary's external vulnerability.

Since its launch, more than HUF 1,650 billion of Hungarian Government Security Plus had been purchased. More than half of the purchases had been registered as a new source of financing for the government sector. Based on the 2020 Budget Act, the budget deficit-to-GDP ratio was likely to decline to 1 percent, with the maintenance of a significant amount of reserves. After 2019, fiscal policy would remain counter-cyclical in 2020 as well. The announced Economy Protection Action Plan was expected to gradually improve the competitiveness of the domestic economy. The above measures jointly strengthened macroeconomic stability, reduced external vulnerability, and contributed to maintain a sustainable convergence path.

Due to the deteriorating outlook for global economic growth, monetary policy stances of the world's leading central banks had become increasingly looser recently. Consistent with unfavourable European activity data and continued moderate inflation developments, the possibility of an interest rate cut had appeared in the European Central Bank's July forward guidance. In line with this, market participants expected an easing of monetary policy already in September. In July, the Federal Reserve had reduced the policy rate for the first time since 2008. Meanwhile, market participants expected further loosening measures over the remainder of the year. In its forward guidance, the Bank of Japan had signalled that, if necessary, it was ready to ease policy further.

Sentiment in international financial markets had deteriorated since the Council's previous interest rate decision. Risk appetite had been influenced by developments in international trade policies, measures taken by the world's leading central banks and expectations of their future policy measures, domestic political tensions in Italy and news relating to Brexit. Oil prices had fallen recently.

To improve the effectiveness of monetary policy transmission, the Monetary Council had launched its corporate bond purchasing programme with a total amount of HUF 300 billion on 1 July 2019. By introducing the Bond Funding for Growth Scheme (BGS), the Council's specific objective was to promote the diversification of funding to the domestic corporate sector. Corporate bond issuances were expected to pick up in the fourth quarter. The MNB would neutralise excess liquidity arising from bond purchases by using the preferential deposit facility bearing interest at the central bank base rate. The programme complemented the Funding for Growth Scheme Fix launched at the beginning of 2019 to build a healthier lending structure. Under the scheme, participating credit institutions had concluded loan contracts with domestic SMEs totalling HUF 219 billion until end of July.

Following the review of macroeconomic and money market developments, the Monetary Council discussed the details of the monetary policy decision. Council members pointed out that, consistent with the baseline projection in the June Inflation Report, inflation had started to decline in the summer months. Council members confirmed that the factors determining inflation had continued to show volatility; therefore, in assessing the outlook, special attention still had to be paid to the measures capturing persistent trends. Members stressed that more persistent inflation developments had been even lower than expected. In this context, members emphasised that lower-than-expected underlying inflation and weakening external activity might jointly indicate a strengthening in downside risks to longer-term inflation outlook.

Council members were unanimous in pointing out that several factors were likely to exert their effects in the second half of 2019, which would fundamentally influence the macroeconomic environment of Hungarian monetary policy. Several members noted that due to the deteriorating outlook for global economic growth, monetary policy stances of the world's leading central banks had become looser recently. On this point, decision-makers agreed that the possible disinflationary effects of weakening economic activity, especially in Europe, and changes in the external monetary policy environment would have to be closely monitored in the coming period. Regarding developments in Hungary, members emphasised that assessing the persistent effects of the Hungarian Government Security Plus programme on savings would become a key factor in the coming months. Several members stressed that the outstanding amount of the new retail government security had risen by over HUF 1,650 billion since it had been issued in June. More than half of the purchases had been registered as a new source of financing for the government sector. The programme helped to reduce Hungary's external vulnerability by promoting self-financing. In addition, they also pointed out that the Hungarian Government Security Plus programme might influence inflation developments as a result of its effects on saving and consumption decisions. In conclusion, fiscal policy becoming counter-cyclical was likely to influence economic growth and the outlook for inflation, hence monitoring this was also of key importance.

Taking account of incoming data and the risks related to the outlook for inflation and the macroeconomy, Council members agreed that the projection in the June Inflation Report and data received since the Council's previous interest rate decision as well as domestic and international financial market developments had not warranted a change in monetary conditions in August. Regarding persistent inflation trends, downside risks had strengthened. In assessing their extent, data to be received in the second half of the year would be decisive. Accordingly, a cautious approach was still warranted in monetary policy.

The Monetary Council left 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 -0.05 percent unchanged. In addition, in June, the Council had set the average amount of liquidity, to be crowded out for the third quarter, at least at HUF 200-400 billion and would take this into account in setting the stock of central bank swap instruments. The MNB changed the stock of the FX swap instrument in a flexible manner to ensure that the interest rate transmission changes were in line with the decisions by the Monetary Council, and the volatility of interbank rates remained at low levels. Accordingly, the stock of FX swaps providing forint liquidity had increased recently in order to achieve the average amount of liquidity to be crowded out.

In its decisions, the Monetary Council focused on the maintenance of price stability. The monetary policy stance would continue to be accommodative, economic agents' financing costs would remain favourable. A dichotomy remained between the factors determining likely developments in inflation. Buoyant domestic demand was boosting, and weakening external activity was increasingly restraining the pace of inflation. Regarding the persistent inflation trends, downside risks had strengthened. In assessing their extent, data to be received in the second half of the year would be decisive. Of these, the following were of key importance: the spillover of disinflationary effects of slowing European economic activity, changes in monetary policies of the world's leading central banks, the effect of the new retail government security on savings, and the economic consequences of counter-cyclical fiscal policy. The Monetary Council would assess their effects on the maintenance of price stability over the 5-8 quarter horizon of monetary policy. In its monetary policy decisions, the Council applied a cautious approach, relying mainly on the comprehensive projections for the macroeconomy and inflation of the quarterly published Inflation Report. The future developments in the outlook for inflation would be a decisive factor in the necessity of further measures.

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 -0.05 percent:**	9	Gusztáv Báger, Kolos Kardkovács, György Kocziszky, György Matolcsy, Márton Nagy, Bianka Parragh, Mihály Patai, Gyula Pleschinger, László Windisch
Vote against:	0	

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

Gusztáv Báger

Kolos Kardkovács

György Kocziszky

György Matolcsy

Márton Nagy

Bianka Parragh

Mihály Patai

Gyula Pleschinger

László Windisch

The Council will hold its next policy meeting on 24 September 2019. The minutes of that meeting will be published at 2 p.m. on 9 October 2019.