



MINUTES
OF THE MONETARY COUNCIL MEETING
26 MAY 2015

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 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://english.mnb.hu/Monetaris_politika/decision-making/mnben_mt_jegyzokonyv

THE COUNCIL'S ASSESSMENT AND INTEREST RATE DECISION

In the Council's judgement, Hungarian economic growth was likely to continue. While the pace of economic activity was strengthening, output remained below potential and the domestic real economy was expected to continue to have a disinflationary impact, albeit to a diminishing extent. Despite the pick-up in the components of domestic demand, capacity utilisation was expected to improve only gradually due to the protracted recovery in Hungary's export markets. With employment rising, unemployment continued to exceed its long-term level determined by structural factors. Inflationary pressures were likely to remain moderate for an extended period.

Based on the inflation data for April, consumer prices showed historically low dynamics; however, the rate of decline in prices had slowed further. The April inflation data had been slightly higher than both the projection in the March issue of the *Inflation Report* and market expectations; however, the Bank's measures of underlying inflation capturing the short-term outlook still indicated moderate inflationary pressures in the economy, reflecting persistently low inflation in external markets, subdued imported inflation, the degree of unused capacity in the economy and the moderation in inflation expectations. Rises in fuel prices as well as in the price indices for market services and unprocessed food had been the main factors contributing to the increase in inflation. Core inflation had been up slightly compared to the previous month. With the pick-up in domestic demand and owing to the increase in wages, core inflation was likely to rise gradually; however, this process might slow due to the second-round effects of low commodity prices. Domestic real economic and labour market factors continued to have a disinflationary impact and low inflation was likely to persist for a sustained period. Overall, moderate underlying inflation developments continued to point in the direction of a low inflation environment, and therefore inflation was expected to approach levels around 3 per cent towards the end of the forecast period.

In the Council's judgement, Hungarian economic growth was likely to continue at a rapid pace. Robust growth was supported by both domestic and external demand. This was underpinned by the preliminary GDP data for the first quarter of 2015, which showed that the Hungarian economy continued to grow dynamically, mainly driven by the performance of industry and the expansion in retail sales. On the expenditure side, domestic demand growth may have continued. According to preliminary data, the trade surplus had been higher in March than a year previously. The dynamics of retail sales had been stable and increased slightly in recent months, with the volume of sales increasing across a wide range of products. Rising household real income as a result of low inflation, the reduced need for deleveraging and increasing employment were expected to contribute to the increase in household consumption. Investment was expected to pick up gradually, owing to the recovery in activity, the Funding for Growth Scheme and its extension. Employment had grown further in the first quarter as activity picked up.

International investor sentiment had been mostly unfavourable in the period since the Council's latest interest rate decision. The downgrade of Greek government debt as well as tensions surrounding its financing and weak incoming macroeconomic data from the

US had negatively affected international investor sentiment. In addition, the reduction in risks associated with deflation in the euro-area economy may also have contributed to rises in long-term yields in developed and emerging markets. Accompanied by noticeable fluctuations, the forint had depreciated against the euro, mainly driven by international factors. The domestic CDS spread had remained broadly unchanged, while long-term government bond yields had risen in line with rising euro area yields in the period since the latest policy decision. Hungary's persistently high external financing capacity and the resulting decline in external debt had contributed to the reduction in its vulnerability. In the Council's judgement, a cautious approach to monetary policy was warranted due to uncertainty in the global financial environment.

In the Council's judgement, there was a degree of unused capacity in the economy and inflationary pressures were likely to remain moderate for a sustained period. The real economy was likely to have a disinflationary impact at the policy horizon and the negative output gap was expected to close only gradually. Based on data becoming available previously, the risk of second-round effects taking hold in the wake of the change in inflation expectations still remained after increasing in recent months.

In the Council's judgement, the assumptions underlying the projections in the March *Inflation Report* continued to hold, under which the outlook for inflation and the cyclical position of the real economy pointed in the direction of a further reduction in the policy rate and loose monetary conditions for an extended period. The Monetary Council unanimously voted in favour of a 15 basis point reduction in the base rate. In the Council's judgement, the decision was consistent with the Bank's earlier approach and market expectations, thereby strengthening the Bank's credibility and predictability and, looking forward, it provided adequate room to continue the easing cycle. Several members noted that the inflation and real economic data becoming available in the period since the latest policy decision had been consistent with their expectations, which was in favour of a further reduction in the base rate. Taking into account that developments in the macroeconomy and financial markets had been generally in line with the assumptions underlying the projection since the latest policy decision, the overwhelming majority of decision-makers did not see a case for a change to the forward guidance. One member proposed to draft a more cautious forward guidance than previously used, with reference to the impending interest rate increase by the US Fed.

After the discussion, the Chairman invited members to vote on the propositions put to the Council. Members voted unanimously in favour of reducing the base rate by 15 basis points. The overwhelming majority of decision-makers judged it necessary to maintain the previous forward guidance and agreed that cautious easing of monetary conditions might continue as long as it supports the achievement of the medium-term inflation target.

Votes cast by individual members of the Council:

In favour of reducing the base rate to 1.65%	9	Ádám Balog, Andrea Bártfai-Mager, János Cinkotai, Ferenc Gerhardt, Csaba Kandrács, György Kocziszky, György Matolcsy, Gyula Pleschinger, László Windisch
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The following members of the Council were present at the meeting:

Ádám Balog

Andrea Bártfai-Mager

János Cinkotai

Ferenc Gerhardt

Csaba Kandrács

György Kocziszky

György Matolcsy

Gyula Pleschinger

László Windisch

The Council will hold its next policy meeting on 23 June 2015. The minutes of that meeting will be published at 2 p.m. on 8 July 2015.