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Analyst background discussion

30 January 2024

BACKGROUND DISCUSSION AFTER THE MONETARY COUNCIL'S 30 JANUARY 2024 DECISION



MAIN MESSAGES: MACROECONOMIC ASSESSMENT AND OUTLOOK



- **Disinflation has been widespread and persistent in the Hungarian economy.** Across Europe, inflation fell to the greatest extent in Hungary last year.
- **Consumer prices rose by 5.5 percent in annual terms. Domestic inflation was one of the lowest** in the region at the end of the year.
- **The trend-like slowdown in underlying inflation** is indicated by the fact that the annualised three-month change in core inflation has been around 3 percent since September. **Strong disinflation continues at the beginning of the year.**
- Incoming data suggest that **domestic growth was subdued in Q4 2023.** However, **the labour market remains tight** and the unemployment rate is low even by EU standards.
- **In November 2023, the monthly current account balance was in a significant surplus.** The incoming data was above expectations and thus the current account balance in 2023 and 2024 may be more favourable than the surplus projected in the December Inflation Report.
- The inflow of **EU funds** starting in December has been a **favourable development.** However, uncertainty surrounding funds has increased recently.
- **Sentiment in global financial markets was significantly influenced by the escalation of the conflicts in the Middle East.**

MAIN MESSAGES: MONETARY POLICY DECISIONS

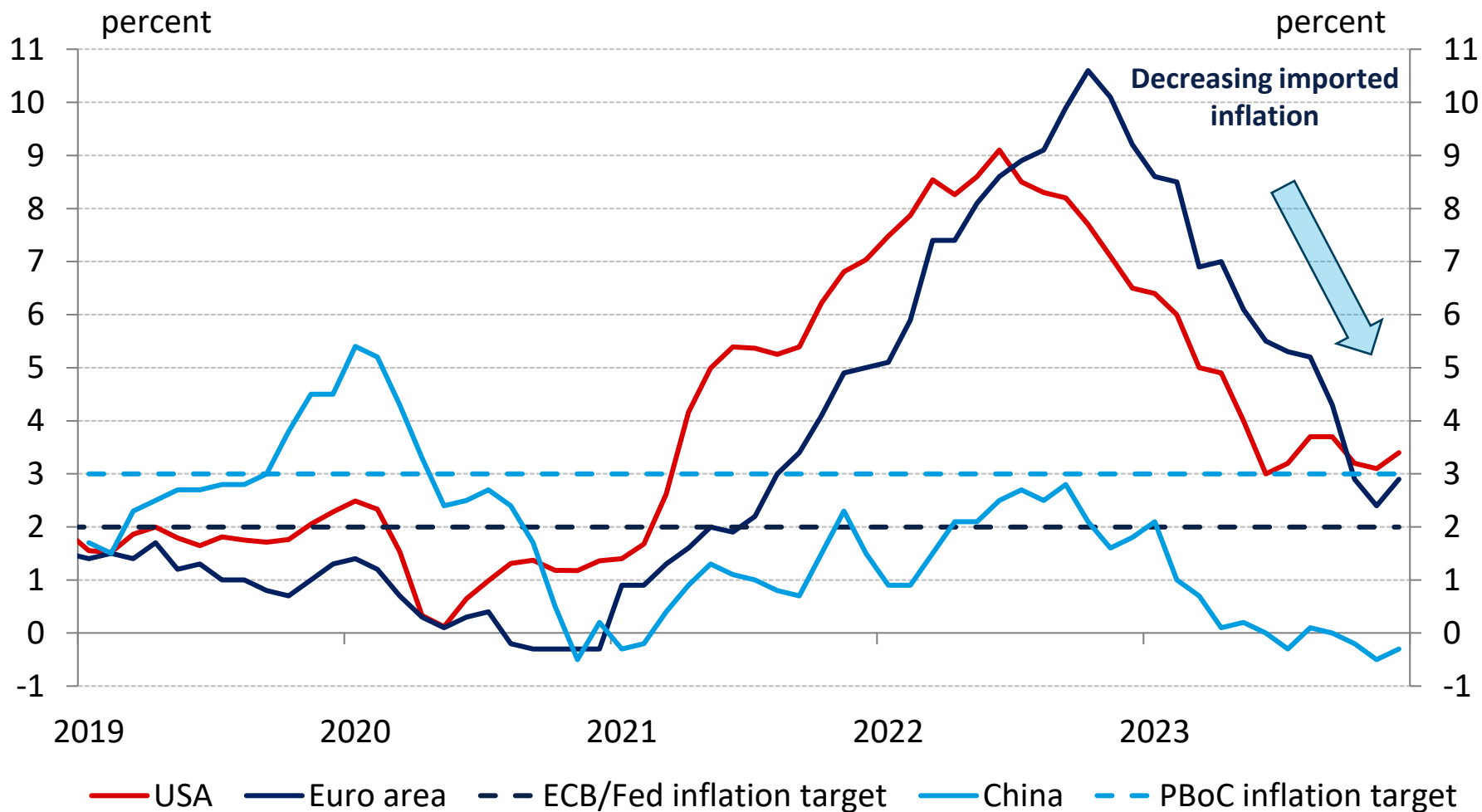


- **Disinflation must continue in 2024! It is necessary to maintain a disciplined and careful monetary policy** in order to achieve price stability.
- **At its meeting today, the Council reduced the base rate by 75 basis points to 10 percent.**
- **Developments in macroeconomic fundamentals** (larger-than-expected decrease in inflation, significant improvement in the current account and low external and internal demand pressures) **would have made possible** a larger increase in the base rate. However, **due to recent developments in the domestic risk environment, the Council supported the unchanged pace of rate decreases.**
- **Positive real interest rate will help to continue disinflation and achieve the inflation target.**
- **The MNB will discontinue the use of the long-term deposit facility with effect from 31 January.** With this, the Bank continues the simplification of the central bank monetary policy toolkit.
- The use of the **swap facility providing foreign currency liquidity** in December 2023 contributed to the maintenance of stability in the swap market, and therefore the MNB will continue to use the facility. **The ECB extended its repo line agreement with the MNB.**
- **In the coming months, decisions on any further reductions in the base rate and their optimal pace will be made in a data-driven manner.**



MACROECONOMIC ASSESSMENT AND OUTLOOK

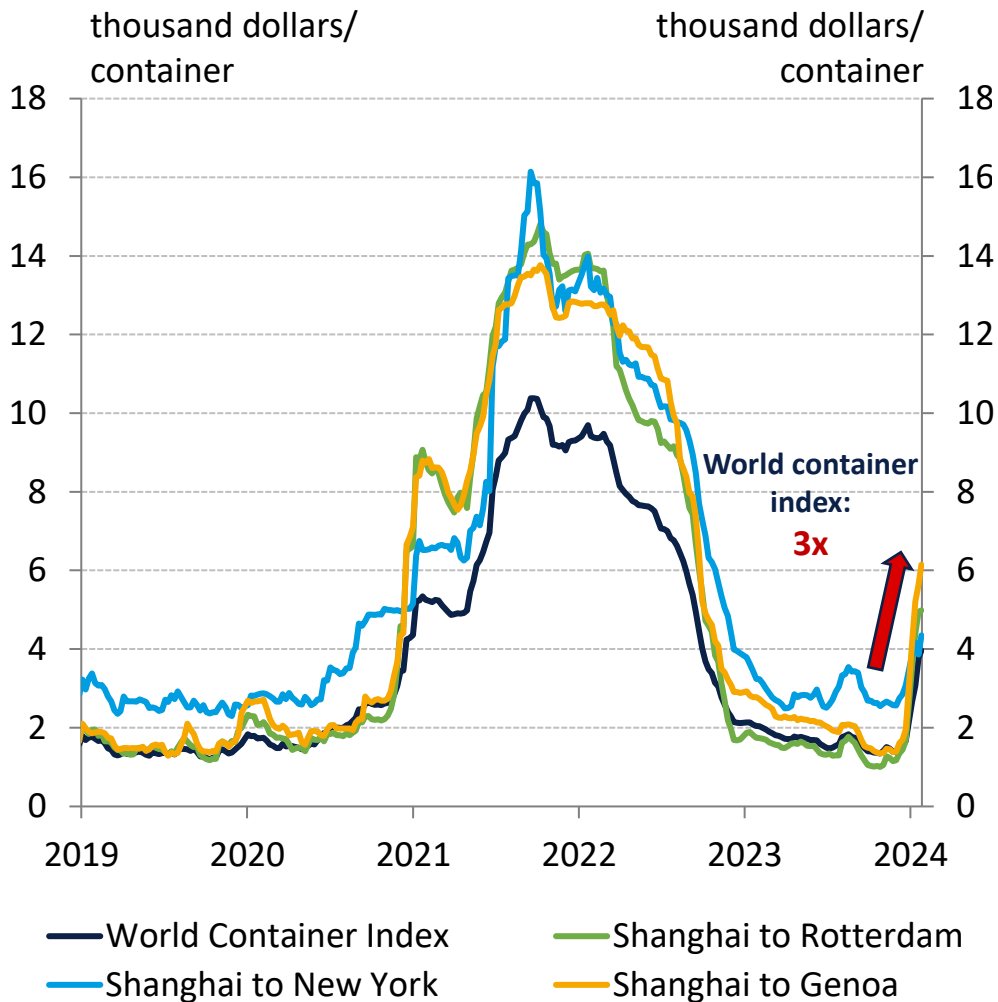
INFLATION IS FALLING GLOBALLY



INFLATION IN THE US, CHINA AND THE EURO AREA

Source | Eurostat, OECD

DISRUPTIONS IN GLOBAL VALUE CHAINS COULD CAUSE TRANSPORT COSTS TO RISE AGAIN



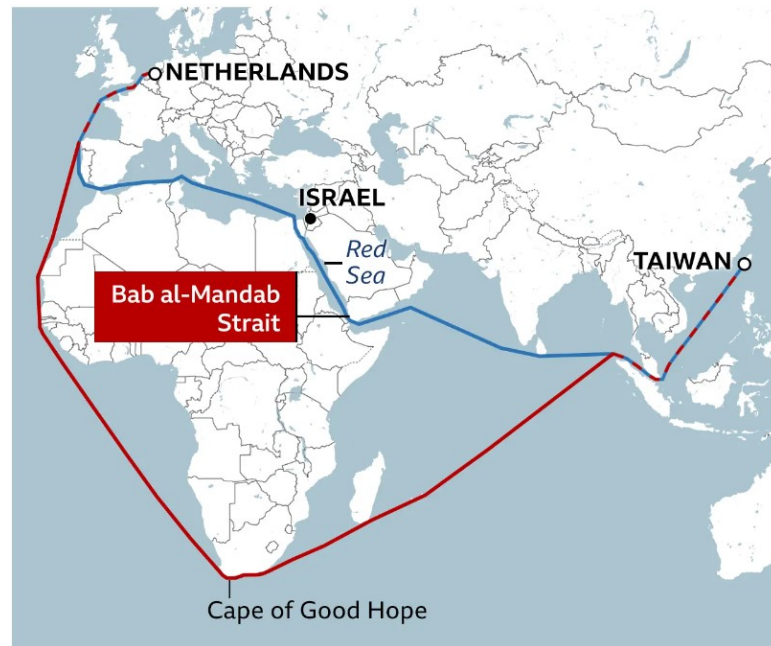
THE DREWRY WORLD CONTAINER INDEX (WCI) AND ITS SUB-INDICES

Source | Bloomberg

Using Red Sea:
10 000 nautical miles
(18 520 km)
25,5 days*

Around Cape of Good Hope:
13 500 nautical miles
(25 002 km)
34 days*

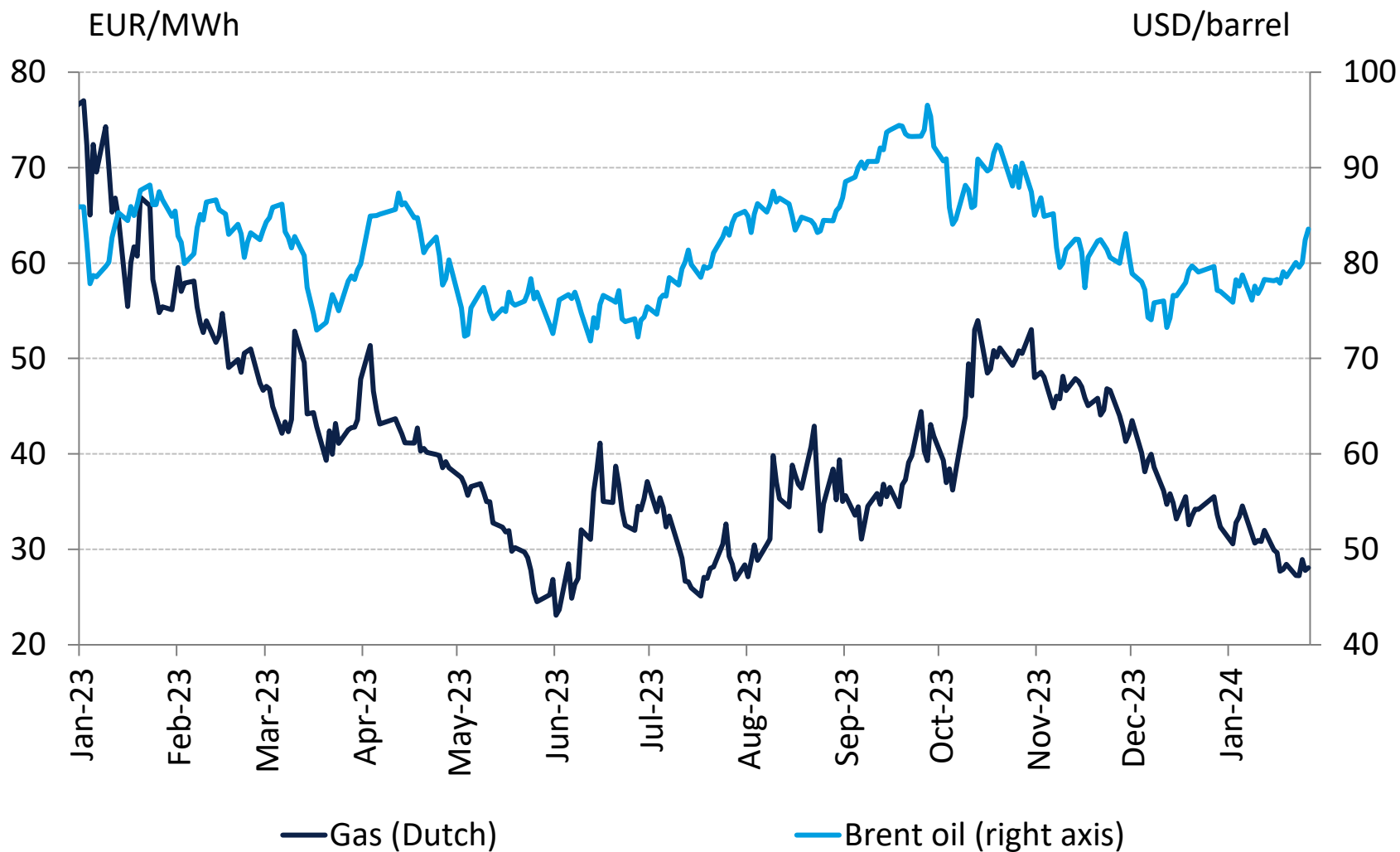
*Based on ultra large container vessel's average speed of 16.48 knots.



ALTERNATIVE SHIPPING ROUTE AVOIDING RED SEA

Source | BBC

DESPITE GEOPOLITICAL TENSIONS, EUROPEAN GAS PRICES MODERATED



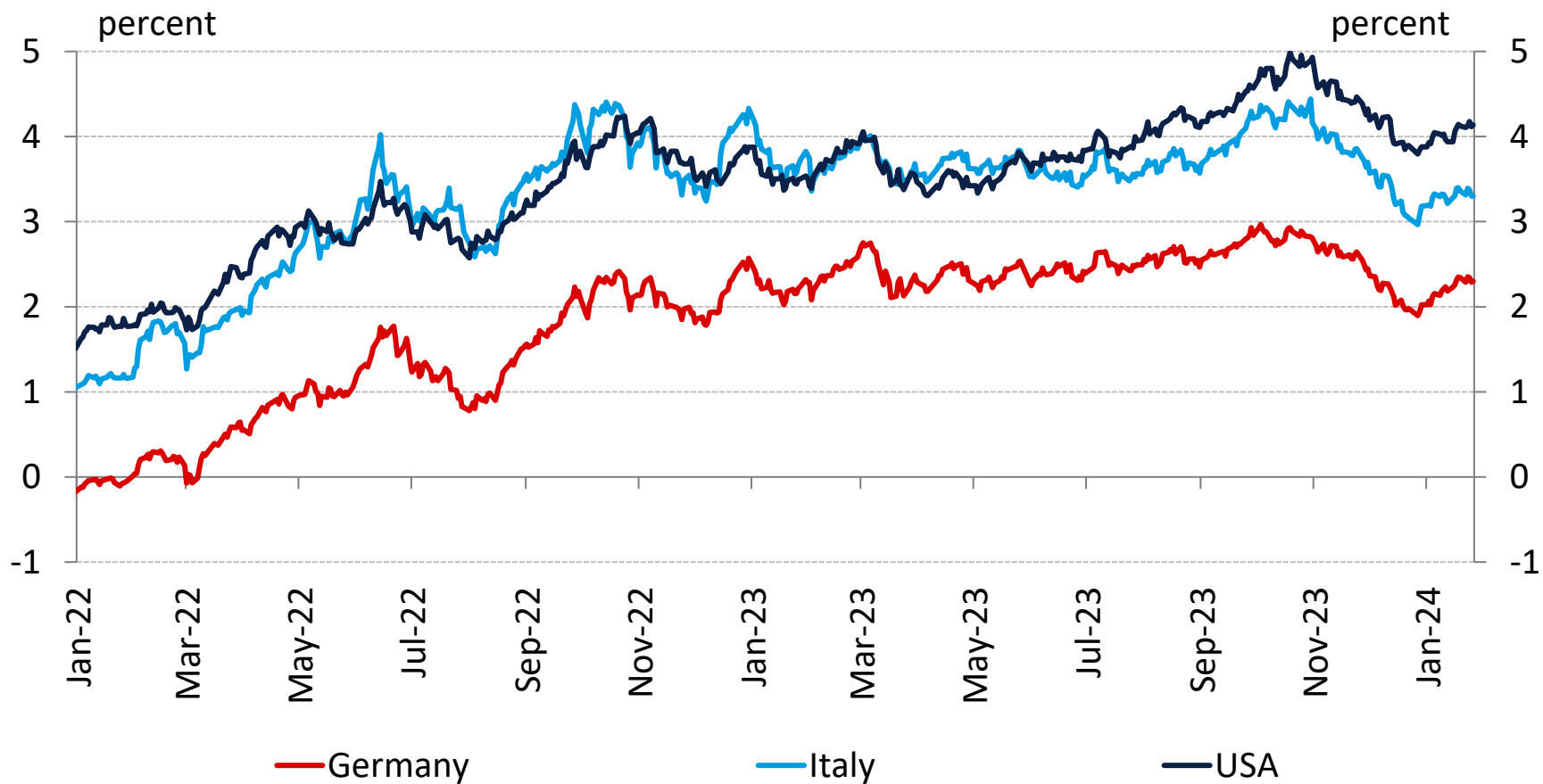
DEVELOPMENTS IN OIL AND GAS PRICES

Source | Bloomberg

DEVELOPED MARKET LONG YIELDS HAVE RISEN SLIGHTLY RECENTLY



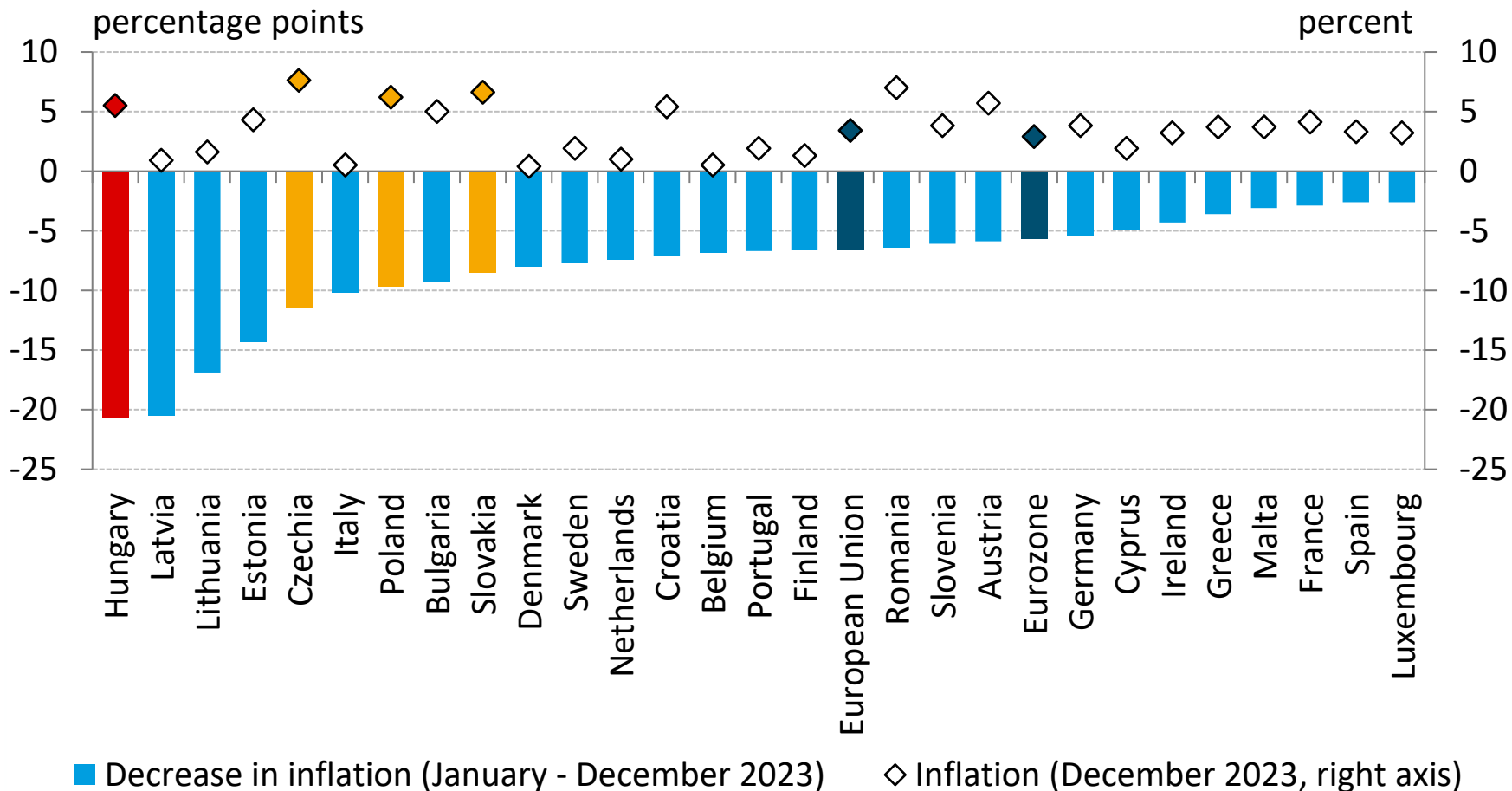
However, they are substantially lower than their peak levels in October last year.



DEVELOPMENTS IN YIELDS OF 10-YEAR BONDS

Source | Bloomberg

THE HIGHEST RATE OF DISINFLATION IN THE EU WAS IN HUNGARY IN 2023



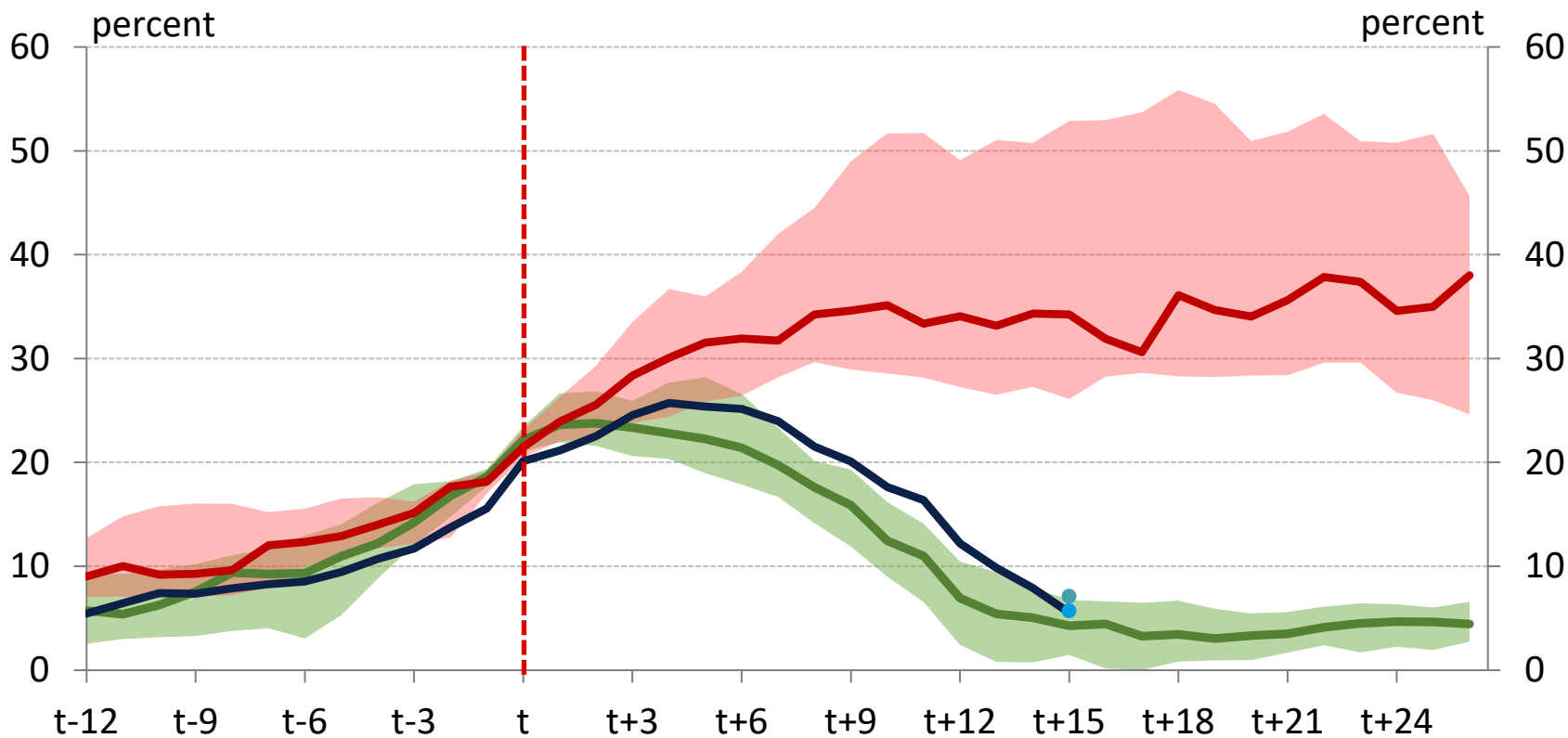
HICP INFLATION IN DECEMBER 2023 AND RATE OF DECLINE SINCE JANUARY 2023 IN THE EU

Note | HICP inflation rates.
Source | Eurostat

DOMESTIC PRICE DYNAMICS CONTINUE TO FOLLOW THE PATH OF COUNTRIES THAT HAVE SUCCESSFULLY DISINFLATED IN THE PAST



Inflation is falling even faster than previously expected.



HISTORICAL DISINFLATIONS, BOTH SUCCESSFUL AND UNSUCCESSFUL, FOLLOWING PERIODS OF INFLATION ABOVE 20 PERCENT AND THE DEVELOPMENTS IN CURRENT INFLATION IN HUNGARY

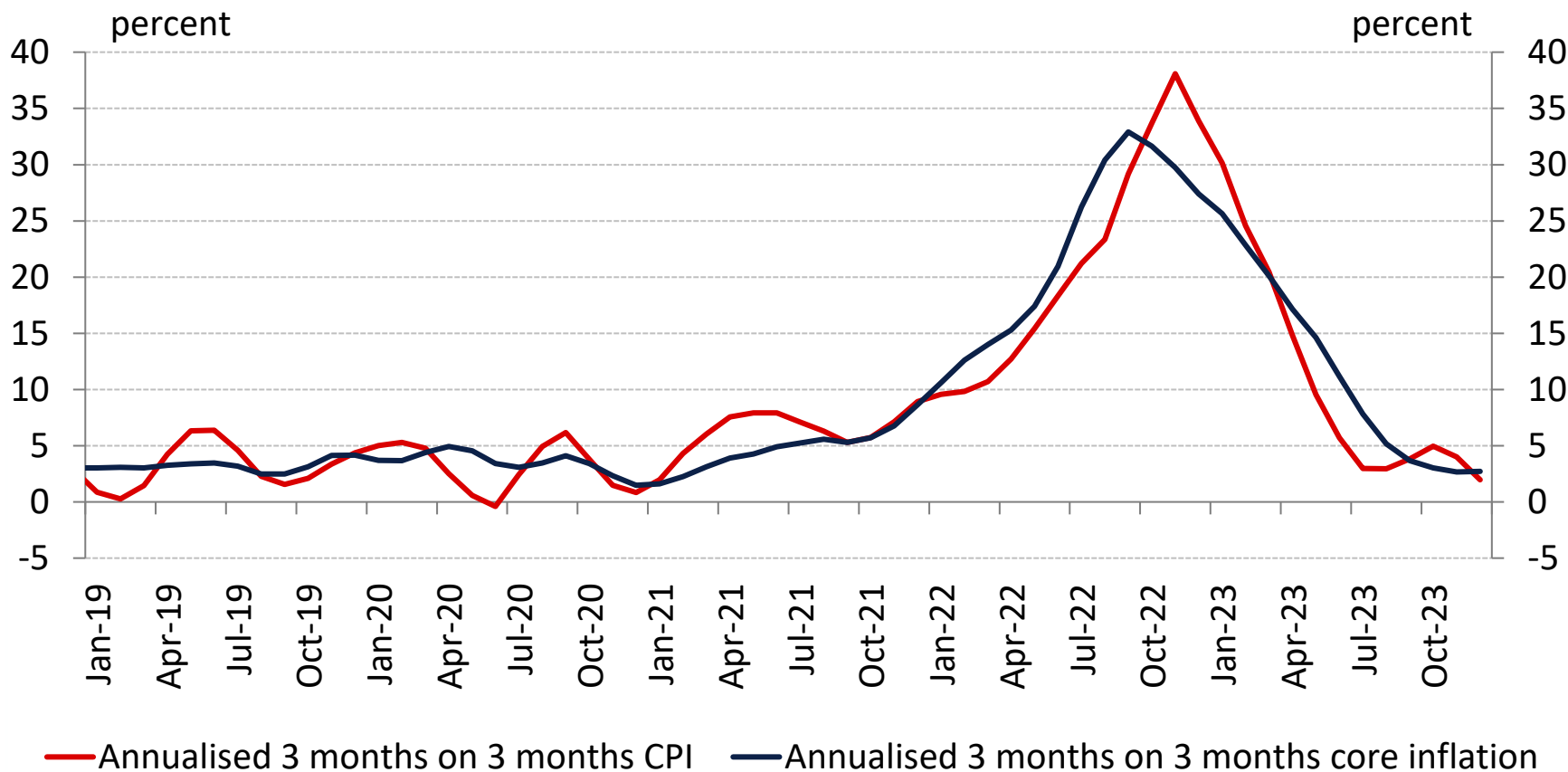
Note | The figure shows the median (solid line) and the 25th and 75th percentiles (range). Green: successful, red: unsuccessful cases. For Hungary, t is September 2022, while dots represent the middle of the September and December 2023 Inflation forecast bands for December 2023.

Source | World Bank, HCSO, MNB calculation

ANNUALISED THREE-MONTH CHANGE IN CORE INFLATION HAS BEEN AROUND 3 PERCENT SINCE SEPTEMBER



Short-base inflation indicators already show pre-2020 patterns.

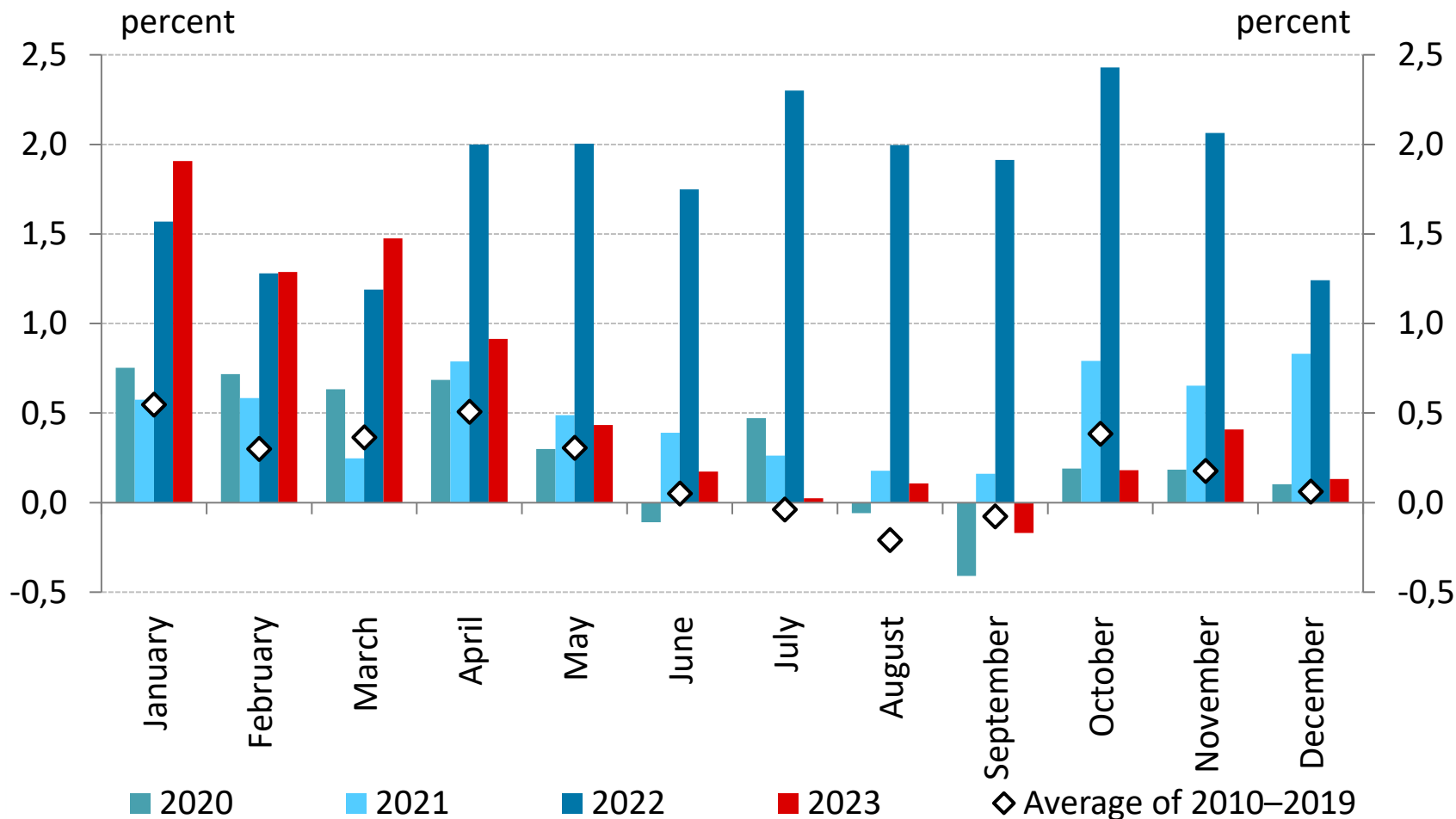


ANNUALISED 3MONTHS/3MONTHS CHANGE IN INFLATION AND CORE INFLATION

Note | Based on seasonally adjusted data.

Source | HCSO, MNB calculation

STRONG DISINFLATION IS EXPECTED TO PERSIST AT THE BEGINNING OF THE YEAR

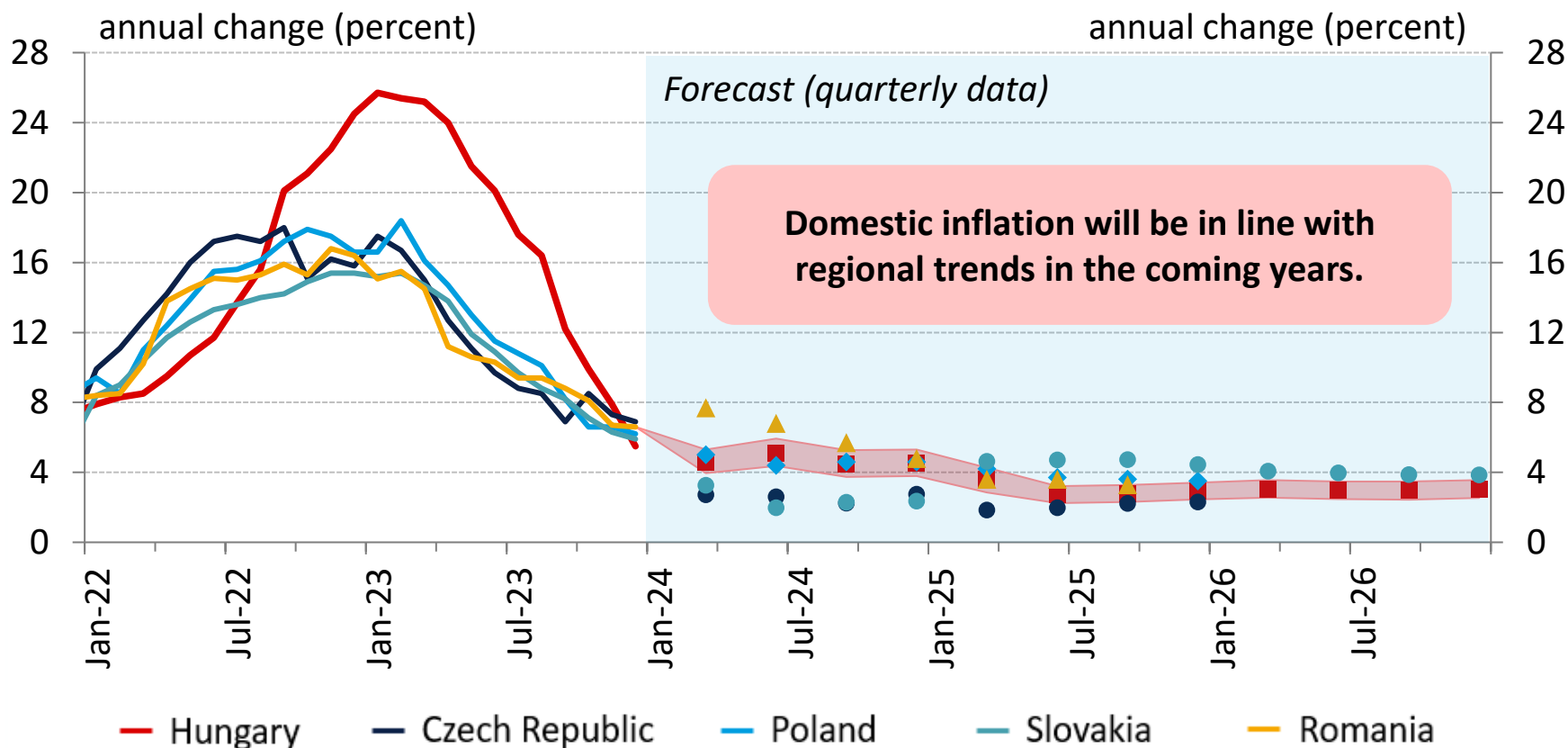


MONTHLY CHANGE IN CONSUMER PRICES EXCLUDING FUEL AND REGULATED PRICES

Note | Tax-adjusted, seasonally not adjusted monthly change.

Source | HCSO, MNB calculation

LOOKING AHEAD, DOMESTIC INFLATION IS IN THE REGIONAL RANGE

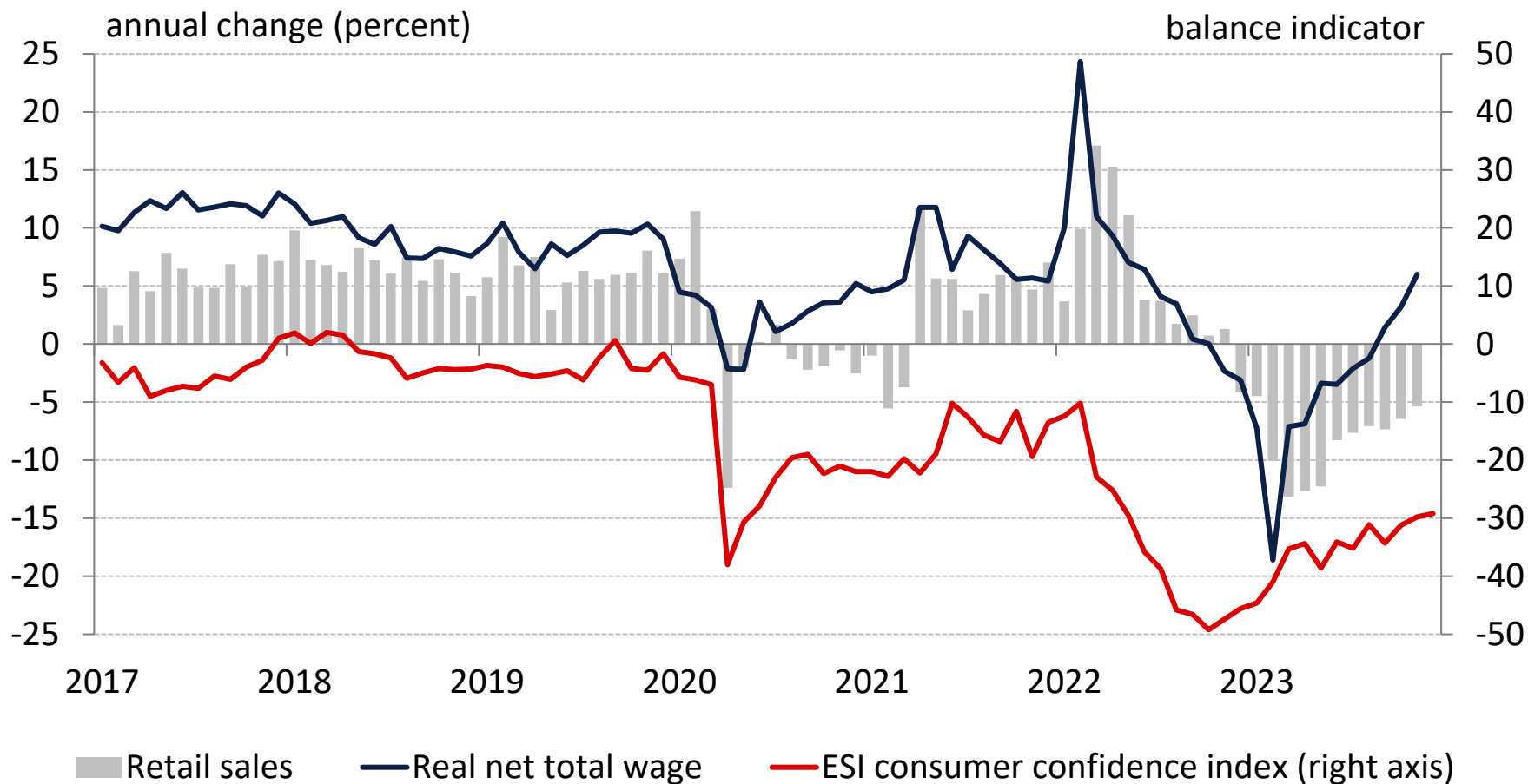


MONTH-ON-MONTH AND EXPECTED QUARTER-ON-QUARTER DEVELOPMENTS IN DOMESTIC AND REGIONAL INFLATION BASED ON CENTRAL BANK FORECASTS

Note | Regional forecasts are based on central banks' inflation forecasts. Publication date of the inflation reports: Czech Republic: 02.11.2023. Poland: 10.11.2023. Slovakia: 11.01.2024. Romania: 08.11.2023. For Hungary, the December Inflation forecast band.

Source | CNB, MNB, NBP, NBR, NBS

THE KEY TO THIS YEAR'S GROWTH ALONGSIDE DISINFLATION, IS RISING REAL WAGES AND A RECOVERY IN CONFIDENCE



DEVELOPMENTS IN RETAIL SALES, NET EARNINGS AND THE ESI CONSUMER CONFIDENCE INDEX

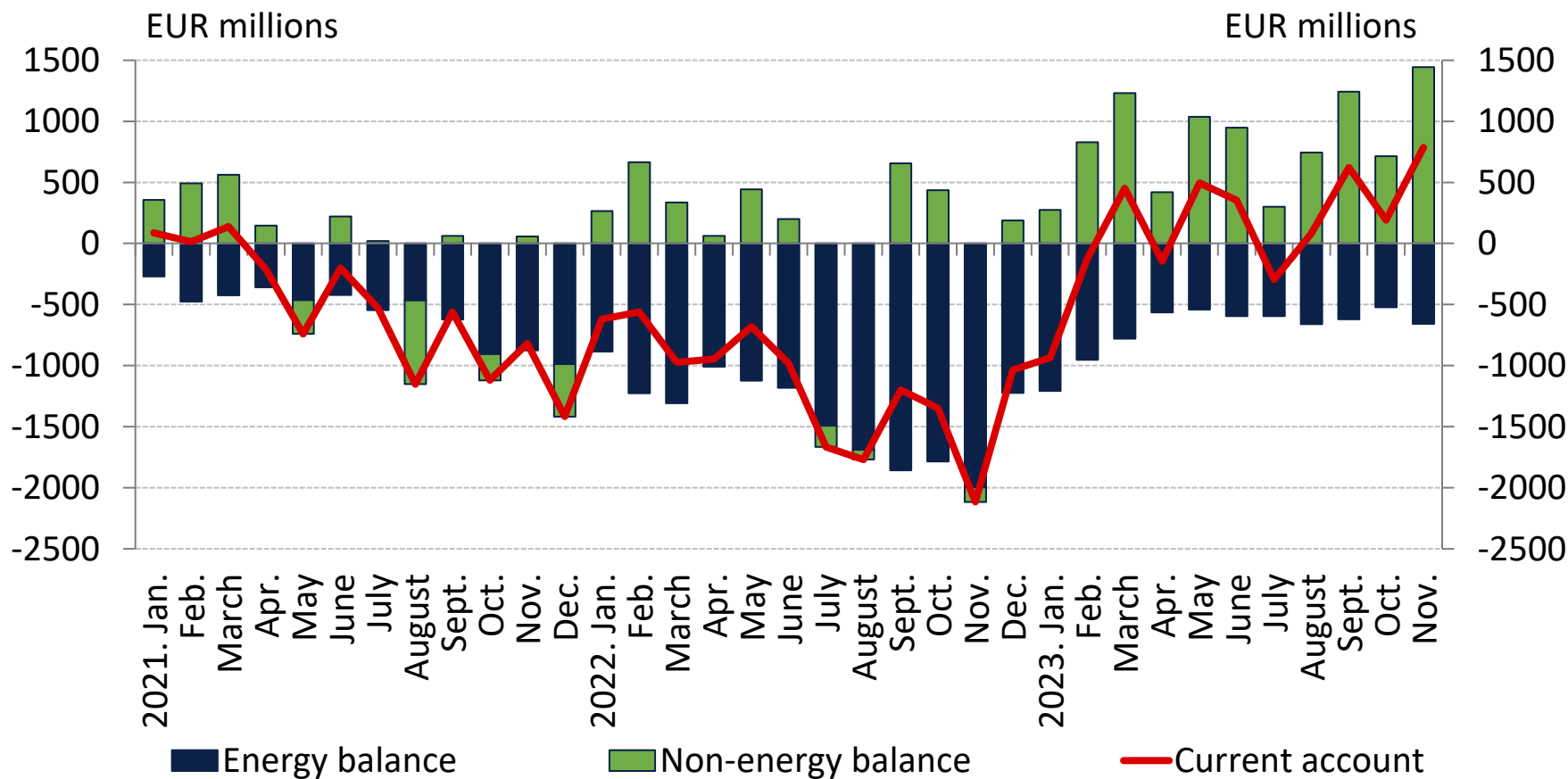
Note | Retail sales based on calendar adjusted, real net earnings and consumer confidence index based on seasonally and calendar adjusted data.

Source | HCSO, MNB

THE RAPID AND SIGNIFICANT IMPROVEMENT IN OUR EXTERNAL POSITION CONTINUED



In November 2023, the current account was in a surplus not seen for more than seven years.



DEVELOPMENTS IN CURRENT ACCOUNT AND ENERGY BALANCE

Note | The November value of the energy balance is an estimate.

Source | HCSO, MNB

HUNGARY SUCCESSFULLY ISSUED FOREIGN CURRENCY BONDS TWICE AT THE BEGINNING OF THE YEAR



The Government Debt Management Agency (ÁKK) issued USD 2.5 billion in foreign currency bonds on 3 January and EUR 1.5 billion on 13 January.



Demand was strong at both auctions. Investor interest in the dollar bond was **more than double**, and in the green euro bond **close to quadruple** compared to the ÁKK's offer.



The pricing of both bonds was **more favourable than previously indicated** and even compared to earlier offerings.



The proceeds from the dollar bond will be used for **general financing purposes**. Proceeds from the green bond will be used to **finance and refinance green expenditures in the budget**, in line with the Green Bond Framework renewed in 2023.



With these transactions, a significant part of the planned foreign currency issuance for 2024 has already been achieved.



MONETARY POLICY

CHANGES IN THE DOMESTIC RISK ENVIRONMENT WARRANT A CAREFUL APPROACH



Only focusing on macroeconomic fundamentals would have enabled a larger decrease.

INTERNATIONAL FACTORS

DOMESTIC DEVELOPMENTS



The external inflation environment is better than expected.



In developed markets, long-term yields have risen; however, they are still significantly below their peaks.



The Fed and the ECB are expected to lower rates; however, their timing has been pushed back.



Geopolitical tensions are still with us.



The risk of shocks in energy and commodity markets remains high.



Disinflation has been widespread and persistent in the Hungarian economy



The current account balance is improving faster than expected.



The MNB successfully managed the year-end swap market tensions. The repo agreement with the ECB has been extended.



Relations with the EU have become more uncertain.



As uncertainty increased, tensions in domestic financial markets rose.

THE MONETARY COUNCIL'S JANUARY INTEREST RATE DECISION



Central bank instrument	Interest rate	Previous interest rate (percent)	New interest rate (percent)
Central bank base rate		10.75	10.00
O/N deposit rate	Central bank base rate minus 1.00 percentage point	9.75	9.00
O/N collateralised lending rate	Central bank base rate plus 1.00 percentage point	11.75	11.00

DISCIPLINED MONETARY POLICY IS STILL CONSIDERED TO BE JUSTIFIED BY THE MONETARY COUNCIL



The central bank aims to achieve the lowest possible interest rate path that ensures price stability and financial market stability, in addition to enabling the restart of market-based lending.

With this, the MNB contributes to sustainable economic growth.



The goal remains unchanged: reducing inflation further in a sustainable manner and reaching price stability.



Positive real interest rates



Maintaining financial market stability

The economic environment is rapidly changing



Monitoring Hungary's relative position against interest rate developments in the region



Monitoring the expectations of domestic economic actors



Inflation target

Inflation is likely to move close to the upper bound of the tolerance band in the spring months. The consumer price index is expected to return to the central bank inflation target persistently in 2025.

Data-driven mode

In the coming months, the Council will take decisions on any further reductions in the base rate and their optimal pace based on incoming data, the outlook for inflation and developments in the risk environment, in a data-driven manner.



Financial market stability

Ensuring financial market stability is a condition for achieving price stability.

Communication in advance

Currently, expectations are in line with the interest rate path that the MNB considers feasible.





*„Risks surrounding global disinflation and volatility in international investor sentiment warrant a **careful approach to monetary policy**. The Council is constantly assessing incoming macroeconomic data, the outlook for inflation and developments in the risk environment. **In the coming months, decisions on any further reductions in the base rate and their optimal pace will be made on the basis of this information, in a data-driven manner.**”*



**THANK YOU FOR YOUR
KIND ATTENTION!**