MINUTES OF THE MONETARY COUNCIL MEETING
22 JUNE 2021

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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 primary objective of the Magyar Nemzeti Bank (MNB) was to achieve and maintain price stability. Without prejudice to its primary objective, the Magyar Nemzeti Bank preserved financial stability and supported the Government's economic policy, as well as its policy on environmental sustainability under the Bank's extended mandate effective from 2 August 2021.

In the last months, a growing number of countries had begun to reopen their economies, the pace of which had been strongly influenced by developments in the pandemic and the population's vaccination level. World trade and global industrial production had already exceeded pre-crisis levels and there had been an improvement in the outlook for services activity. Incoming GDP data for the first quarter of 2021 had significantly exceeded earlier expectations across a number of countries and regions.

Risk appetite had still been driven primarily by the events related to the coronavirus pandemic, global supply problems and reflation concerns. Commodity prices had risen sharply since the beginning of the year. Global oil prices had surged above USD 70.

The Federal Reserve's decision-makers had left loose monetary conditions unchanged at their policy meeting in June and reiterated that the asset purchase programmes would be continued at an unchanged pace. In the decision-makers' view, the rise in inflation had been mainly due to temporary factors, but inflation expectations had also risen in the recent period. The European Central Bank had maintained the amount, raised in the second quarter of purchases made under the Pandemic Emergency Purchase Programme (PEPP) in the third quarter.

However, in the region a number of central banks had indicated recently that they would stand ready to tighten monetary conditions, when necessary due to the increase in the outlook for inflation. The Polish central bank had left its policy rate unchanged since the MNB's previous interest rate decision.

Hungarian economic growth had continued in the third wave of the coronavirus pandemic. Hungary's GDP had grown by 2.0 percent in the first quarter of 2021 relative to the previous quarter, but it had been 2.1 percent below the level a year earlier. Incoming data had substantially exceeded expectations. Wage growth had remained dynamic despite the pandemic; and the unemployment rate had remained low by international standards.

The vaccination coverage rate of Hungary's population was at the top in the European Union, which had provided a good foundation for restarting economic life. As a result of the earlier opening than the European average, the economic recovery was expected to pick up significantly in the second quarter. Real-time data pointed to double-digit economic growth in the second quarter. Hungarian economic output was expected to recover to pre-Covid levels in the third quarter. The rapid recovery of industry was followed by retail trade, while the recovery of the service sector, which was most exposed to the pandemic, would take longer.

The historically high investment rate was expected to continue rising on the forecast horizon. Hungarian export performance was expected to improve markedly already in 2021 as external markets recovered. Driven by the gradual increase in the output of new export capacities built up in previous years, domestic exports were expected to remain an important source of GDP growth over the entire forecast horizon. Household demand was likely to pick up as restrictions were lifted gradually. The MNB had revised up its growth projection, according to which the Hungarian economy grew by 6.2 percent this year, by 5.5 percent in 2022 and by 3.5 percent in 2023.

In May 2021, annual inflation had been 5.1 percent, while core inflation had stood at 3.4 percent. The consumer price index had been unchanged and core inflation had risen by 0.3 percentage points relative to the previous month. Inflation had been consistent with the MNB’s expectation; however, its structure had confirmed that upside risks related to the reopening had appeared. The rapid recovery in demand would provide an opportunity to pass on higher raw material costs to consumer prices since the beginning of the year. Since April, the pace of increase in the prices of services and industrial goods had accelerated. At the same time, underlying measures of inflation had also increased.

Inflation was likely to stay mostly above the central bank's tolerance band until end of the year. After the spike in the second quarter, the consumer price index was expected to fall close to 4 percent at a slower-than-expected pace during the summer months before rising slightly again at the end of the year. Annual average inflation was expected to be 4.1 percent in 2021, higher than in the March projection. Due to base effects, inflation was expected to fall back into the central bank's tolerance band again at the beginning of 2022 and to stabilise around the central bank target from mid-2022 as a result of monetary policy measures.

In the Monetary Council’s assessment, it was of key importance to ensure that inflation expectations are properly anchored. Upside risks to the outlook for inflation had generally increased. Inflation in the euro area and the US had risen since the beginning of the year. Sustained rises in commodity prices and international freight costs pointed to a higher external inflation environment. Demand-supply frictions, re-emerging temporarily due to the rapid restart of the domestic economy, renewed tightening of labour market capacities expected in certain sectors combined with dynamic wage growth had increased inflation risks. Global reflation and persistent rises in commodity prices as well as potential second-round effects arising during the restart of the economy had posed the greatest risks to the outlook for inflation.

Following 8.1 percent in 2020, from 2021 the government deficit was expected to decline and, in parallel, the debt-to-GDP ratio to shift to a downward path. The current account surplus and the economy’s net lending were expected to continue rising on the forecast horizon. The decline in the country’s net external debt would continue.

Following the review of macroeconomic and financial market developments as well as the Inflation report’s projection, the Monetary Council discussed the details of its monetary policy decision. Council members unanimously noted that Hungary’s economy had a strong potential for recovery. As a result of the successful vaccination programme, economic life started to normalise earlier in international comparison. In the second quarter of 2021, the economy had been restarted. In this period, Hungary's GDP was expected to exhibit signs of a strong double-digit growth. The Monetary Council agreed that economic performance would reach the levels seen before the crisis in the third quarter of 2021. If the fourth wave of coronavirus could be avoided globally, Hungarian GDP was expected to grow strongly even in European comparison, by around 6 percent in 2021.

The Council pointed out that a rapid economic recovery in Hungary and a pick-up in demand caused inflation to rise. Few members noted that although inflation in May had been consistent with the MNB's expectation, its structure had confirmed that upside risks related to the reopening had appeared. After April, the inflation of market services and industrial goods also continued to grow in May. In addition, some decision-makers indicated that measures capturing more persistent inflationary trends also rose relative to April. In the Monetary Council's assessment, upside risks to the outlook for inflation had increased, which lead to the outlook for inflation shifting up along with favourable economic developments. Council members underlined that based on the latest projection, inflation was declining at a slower pace than earlier expected following the spikes in April and May and it might be stuck fluctuating above the central bank tolerance band until the end of the year. Average inflation in 2021 was expected to be nearly 4 percent. Decision-makers stressed that, consistent with the projection in the Inflation Report, a proactive monetary policy was necessary for inflation to stabilise around the central bank target from mid-2022.

The Monetary Council unanimously took a decision that launching a cycle of interest rate hikes was warranted to ensure price stability, avoid persistent inflationary risks, and anchor inflation expectations. Several members pointed out that it was of key importance to anchor inflation expectations to prevent persistent inflation issues from emerging in the Hungarian economy.

With a general tightening of monetary policy conditions, the cycle of base rate hikes was a definite indication to economic agents, that monetary policy was committed to low inflation. Furthermore, Council members agreed that maintaining the difference between the base rate and the interest rate on the one-week deposit instrument was currently no longer warranted; therefore, the interest rate on the one-week deposit instrument would be changed in accordance with the base rate during the cycle of interest rate hikes. However, several members thought it was important to note that the one-week deposit instrument continued to be included in the set of central bank instruments. Decision-makers agreed that the Council would conduct the cycle of interest rate hikes gradually, in a data-driven manner at its monthly policy meetings. The Monetary Council unanimously argued that the cycle of interest rate hikes would need to be continued until the outlook for inflation stabilised around the central bank target and inflation risks became evenly balanced on the horizon of monetary policy.

In addition, members highlighted that the Bank would start to transform the use of instruments having an effect at longer maturities. Council members unanimously indicated that maintaining stable financial market developments and an economic recovery remained key in transforming the MNB's instruments having an effect at longer maturities during the recovery. A pick-up in economic recovery made it possible for the Bank to close the FGS Go! as the amount of HUF 3,000 billion available was exhausted. However, members also stressed that the government securities purchase programme remained crucial in its set of monetary policy instruments, and they wished to use it by maintaining a lasting presence in the market. Council members noted that based on modifications to the MNB Act, adopted by the Parliament, in addition to its current mandates, the Magyar Nemzeti Bank would support the Government's policy on environmental sustainability under its extended mandate effective from 2 August 2021. Therefore, decision-makers would continuously assess potential measures through the set of central bank instruments supporting environmental sustainability.

In the Monetary Council' assessment, in order to ensure price stability, to prevent the lasting effects of inflation risks and to anchor inflation expectations, it was warranted to launch a cycle of interest rate hikes. Accordingly, the Monetary Council increased the central bank base rate by 30 basis points to 0.9 percent. It kept the overnight deposit rate at -0.05 percent and the overnight and one-week collateralised lending rates at 1.85 percent unchanged. The MNB would continue to set the one-week deposit rate at weekly tenders. According to the Monetary Council's assessment, it was warranted to increase the interest rate on the one-week deposit instrument to the 0.9 percent level of the base rate.

As in previous quarters, the MNB would hold foreign exchange swap tenders providing euro liquidity at the end of June. Through an active market presence, the MNB cushioned the spillover of end-of-quarter tensions in international swap markets to the domestic market, thereby contributing to preserving the stability of monetary conditions and through this to maintaining price stability.

In parallel with the tightening of interest rate conditions, the Monetary Council had started to transform the use of instruments having an effect at longer maturities. The pick-up in economic recovery had made it possible for the Bank to phase out certain crisis management tools. Accordingly, with the exhaustion of the HUF 3,000 billion available, the Bank had closed the FGS Go!. However, the MNB intended to introduce instruments supporting environmental sustainability. The Monetary Council would provide information on those instruments in the coming months.

The Monetary Council continued to consider the government securities purchase programme to be crucial in its set of monetary policy instruments, which it judged to be successful during the third wave of the pandemic and in a volatile international financial market environment. Purchases by the Bank had contributed to maintaining a stable liquidity position in the government securities market and improved the effectiveness of monetary policy transmission. The MNB would continue to use the programme by maintaining a lasting presence in the market, taking a flexible approach to changing the quantity and structure of weekly securities purchases, to the extent and for the time necessary.

The Monetary Council was committed to maintaining price stability. The Council had launched a cycle of interest rate hikes to ensure price stability, to prevent inflation risks from having long-lasting effects and to anchor inflation expectations. In the Monetary Council's assessment, risks to the inflation outlook remained on the upside. In the context of the outlook for inflation and developments in risks, the Monetary Council assessed the need to further tighten monetary conditions in a data-driven manner at its monthly policy meetings. The Monetary Council would continue the cycle of interest rate hikes until the outlook for inflation stabilised around the central bank target and inflation risks became evenly balanced on the horizon of monetary policy.

Votes cast by individual members of the Council:

In favour of increasing the base rate to 0.90 percent, **maintaining the overnight collateralised lending rate, the one-week collateralised lending rate at 1.85 percent** **and** **maintaining the interest rate on the overnight central bank deposit at -0.05 percent:**	9	Péter Gottfried, Csaba Kandrács, Kolos Kardkovács, György Kocziszky, György Matolcsy, Bianka Parragh, Mihály Patai, Gyula Pleschinger, Barnabás Virág
Vote against:	0	

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

Péter Gottfried

Csaba Kandrács

Kolos Kardkovács

György Kocziszky

György Matolcsy

Bianka Parragh

Mihály Patai

Gyula Pleschinger

Barnabás Virág

The Council will hold its next policy meeting on 27 July 2021. The minutes of that meeting will be published at 2 p.m. on 11 August 2021.