MINUTES
OF THE MONETARY COUNCIL MEETING
27 FEBRUARY 2024

Time of publication: 2 p.m. on 13 March 2024

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) is to achieve and maintain price stability. Without prejudice to its primary objective, the Magyar Nemzeti Bank preserves financial stability and supports the Government's economic policy, as well as its policy on environmental sustainability.

The US and Chinese economies had grown strongly, while European economic growth had stagnated in 2023 Q4. The short-term economic outlook was still exposed to downside risks, which was further exacerbated by the generally tense geopolitical situation.

Inflation in the euro area had fallen in January following a temporary increase in December. Underlying developments still pointed to a decline. In the US, the pace of price increases had slowed in January, but both headline inflation and core inflation had been higher than expected. Weakening global economic demand and lower commodity prices compared to previous years suggested a continued decline in inflation rates. However, the increase in international freight costs due to the Red Sea conflict might cause disruptions in global value chains, leading to a renewed rise in freight costs. Despite geopolitical tensions, oil prices had remained around USD 80 while European gas prices had fallen.

International risk appetite had remained broadly unchanged since the January interest rate decision. Sentiment in global financial markets had been influenced by expectations for the interest rate policies of the world's leading central banks, incoming macroeconomic data, and particularly the higher-than-expected inflation figure in the US, as well as by developments related to the conflicts in the Middle East. Based on market pricings, the expected date of the first interest rate cuts by the Federal Reserve and the European Central Bank had been pushed back. In the CEE region, the Czech central bank had lowered its policy rate by 50 basis points, while the Polish and the Romanian central banks had left monetary conditions unchanged in February.

Hungarian economic performance had stagnated in 2023 Q4 following the rebound in the previous quarter. Primarily due to high inflation, domestic GDP had decreased by 0.8 percent throughout 2023. The performance of agriculture had moderated the decline in 2023. In December, industrial and construction output had fallen sharply, while the volume of retails sales had declined slightly relative to a year earlier. As regards the main determinants of household consumption, real wages had continued to rise in 2023 Q4, in line with disinflation. At the same time, the development in the consumer confidence index in recent months implied a gradual easing of the precautionary motive. Strong tightness of the labour market had eased in the last months. Accompanied by a high level of employment the unemployment rate was low even by EU standards.

As inflation moderated, real wages rose and confidence gradually recovered, leading to a recovery in domestic demand, a balanced economic growth was expected in 2024. Persistently weak European economic activity was holding back domestic exports, but with the pick-up in the production of new export capacities built recently, Hungary's export market share was expected to increase.

Disinflation had been strong and general in the Hungarian economy. In January, consumer prices had risen by 3.8 percent in annual terms, bringing inflation within the Bank's tolerance band. The consumer price index had fallen by 1.7 percentage points from the previous month, with market services and non-durable industrial goods making the largest contributions, in addition to fuel. The impact of the increase in excise duties, taking effect from 1 January 2024, had been mainly reflected in a compression of retail margins, and therefore had had a small impact on fuel prices so far. Core inflation had eased by 1.5 percentage points to 6.1 percent relative to a year earlier. Domestic inflation had been one of the lowest in the region in January. The annualised three-month change in core inflation had been below 3 percentage since October, and repricings at the start of the year had been subdued. Household inflation expectations had fallen in recent months.

In the coming months, inflation developments would be driven by two opposing factors. The impact of the increase in excise duties on fuel would raise headline inflation, while underlying inflation would continue to moderate. Inflation would remain close to the upper bound of the tolerance band in the coming months, before rising temporarily in the middle of the year, as in other countries, due to base effects. The consumer price index was expected to return to the Bank's inflation target on a sustained basis in 2025.

The current account had improved significantly in 2023, turning into a surplus of 0.2 percent of GDP from a deficit of more than 8 percent of GDP in 2022, according to preliminary monthly data. The current account had been in a EUR 1,049 million deficit in December 2023 following a surplus in the previous four months. The improvement in Hungary's external position over the past several months had slowed down, which had mainly been driven by a deterioration in the trade balance, while the services balance had remained in surplus. At the same time, the current account balance had recovered at an unprecedented rate by historical standards in 2023.

The current account balance was expected to improve further in 2024 and in the coming years. Looking ahead, the utilisation of new export capacities built recently, and the recovering global economic environment were expected to give new impetus to exports. The inflow of EU funds would contribute to a strengthening in Hungary's net lending and a further increase in central bank foreign exchange reserves which were already at historically high levels.

According to preliminary financial accounts data released by the MNB, general government net lending had amounted to -6.7 percent of GDP in 2023. The government deficit-to-GDP ratio had fallen to 73.5 percent in 2023 from 74 percent a year previously.

Following the review of macroeconomic and financial market developments, the Monetary Council discussed the details of its February monetary policy decision. In the Council's assessment, the outlook for global economic growth continued to be exposed to downside risks, while the escalation of the conflicts in the Middle East continued to be a source of tension. Council members judged that there was a slowdown in global disinflation; however, several factors pointed to a continued decrease in inflation rates. Several decision makers noted that the Red Sea conflict might cause disruptions in global value chains, which might lead to additional increases in freight costs.

Discussing the international monetary policy environment, members pointed out that expectations for interest rate cuts by the Federal Reserve and the European Central Bank had fallen back. Based on this, market participants projected that the reduction in policy rates might start later than previously expected, in June at the earliest.

In the Council members' assessment, disinflation was strong and general in the Hungarian economy. Several decision makers noted that the better-than-expected January inflation data, one of the lowest figures in the CEE region, had been driven by changes in fuel prices, as the impact of the increase in excise duties, taking effect from the beginning of this year, had been reflected only in a compression of retail margins so far. Whether fuel prices would rise following the increase in excise duties in January or retail margins would remain compressed would be one of the main determining factors in the short-term outlook for inflation. Council members were of the view that core inflation was expected to decline further in the coming months.

Decision makers highlighted that following the rebound in 2023 Q3, Hungarian economic performance had stagnated in the fourth quarter, and domestic GDP had fallen by 0.8 percent throughout 2023. Members were of the view that the economy had declined in 2023 primarily due to high inflation, and therefore it was critical to achieve price stability again to restore economic growth. Several decision makers pointed out that from a deficit of more than 8 percent of GDP in 2022, the current account had moved into a surplus of 0.2 percent of GDP in 2023, according to preliminary monthly data. Although the current account balance had been in deficit in December following a surplus in the previous four months, Hungary's external balance had improved throughout 2023 at a historically strong pace. Council members unanimously agreed that the inflow of EU funds would contribute to a strengthening in Hungary's net lending and a further increase in central bank foreign exchange reserves which were already at historically high levels.

Several members noted that the causes of the noise that preceded the January policy decision and threatened financial market stability, had dissipated. The inflow of funds had started as a result of negotiations with the EU, leading to a further improvement in the country's risk perception. Council members agreed that it was crucial to ensure financial market stability in order to achieve price stability.

At the February policy meeting, the decision makers discussed the alternatives of reducing the base rate by 75 and 100 basis points again. Members stressed that they did not set interest rates by focusing on single decisions. Rather, they intended to reach an interest rate path that ensured that price stability was achieved, financial market stability was maintained and market-based lending recovered at the end of the process. In the Council's judgement, achieving an interest rate of 6-7 percent gradually by the end of 2024 H1 was still a realistic scenario. Council members were unanimously of the view that disinflation in the Hungarian economy was stronger than expected for months, while external and domestic demand pressures remained low and Hungary's risk perception had improved further. The majority of members judged that the room for monetary policy manoeuvre had increased by February. First, several macroeconomic fundamentals had strengthened, in particular, disinflation had been faster than expected and the current account balance had improved in 2023. Second, the causes of the financial market noise preceding the January interest rate decision had unwound. In accordance, the stabilisation of the domestic risk environment and the inflow of EU funds had led to an improvement in financial market stability. All these factors allowed a temporarily larger reduction in the base rate, of 100 basis points.

Council members made a generally positive assessment of the reduction in Hungary's vulnerability in several areas (external balance, terms of trade, inflation). However, some members stressed that increased geopolitical tensions in recent months and their implications for global markets pointed to volatility in international financial market sentiment. Furthermore, they also noted that market expectations for the starting date of interest rate cuts by the world's leading central banks had been pushed back. In their assessment, macroeconomic fundamentals had improved in several areas; however, inflation was expected to be close to the upper bound of the tolerance band in the coming months before rising temporarily during the middle of the year. In addition, the level of core inflation, the slowdown in the improvement in the monthly current account balance in December and the high fiscal deficit expected for 2024 called for caution. Two members were of the view that it was a key priority to assess the persistence of these developments and the risks to the external environment. Based on this, they considered it appropriate to take a more cautious approach to continuing the pace of interest rate reductions by applying a smaller increment of 75 basis points.

There was a consensus in the Council that the key aspects of monetary policy had remained unchanged. An appropriate positive real interest level was required which would help disinflation to continue. Disciplined, stability-oriented monetary policy was necessary in order to achieve price stability in a sustainable manner. In the coming months, the Monetary Council would continue to make 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. The March Inflation Report was expected to be key in judging the pace at which the interest rate cuts continue in 2024 Q2.

Over the past few months, disinflation in the Hungarian economy had been stronger than expected, while external and domestic demand pressures remained persistently low. As a result of the improvement in Hungary's current account balance, the country's risk perception had improved further despite a volatile global sentiment. In the Monetary Council's view, this allowed the base rate to be lowered at a temporarily faster pace. In line with this, at its February meeting the Monetary Council reduced the base rate by 100 basis points to 9 percent. Accordingly, the lower bound of the interest rate corridor, i.e. the O/N deposit rate, was reduced to 8 percent, while the upper bound, i.e. the O/N lending rate, was lowered to 10 percent. Positive real interest rates would help to continue disinflation and achieve the inflation target.

Risks surrounding global disinflation and volatility in international investor sentiment warranted a careful approach to monetary policy. The Council was 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 would be made on the basis of this information, in a data-driven manner.

Votes cast by individual members of the Council:

In favour of reducing the base rate to 9.00 percent, reducing the overnight collateralised lending rate to 10.00 percent and increasing the interest rate on the overnight central bank deposit to 8.00 percent:	7	Éva Búza, Péter Gottfried, Csaba Kandrács, Zoltán Kovács, György Matolcsy, Mihály Patai, Barnabás Virág
In favour of reducing the base rate to 9.25 percent, reducing the overnight collateralised lending rate to 10.25 percent and increasing the interest rate on the overnight central bank deposit to 8.25 percent:	2	Kolos Kardkovács, Gyula Pleschinger

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

Éva Búza

Péter Gottfried

Csaba Kandrács

Kolos Kardkovács

Zoltán Kovács

György Matolcsy

Mihály Patai

Gyula Pleschinger

Barnabás Virág

The Council will hold its next policy meeting on 26 March 2024. The minutes of that meeting will be published at 2 pm on 10 April 2024.