MACROECONOMIC AND FINANCIAL MARKET DEVELOPMENTS

BACKGROUND MATERIAL

TO THE ABRIDGED MINUTES

OF THE MONETARY COUNCIL MEETING

OF 26 JANUARY 2021

JANUARY

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The background material 'Macroeconomic and financial market developments' is based on information available until 21 January 2021.

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. As a summary of the analyses prepared by staff for the Monetary Council, the background material presents economic and financial market developments, as well as new information which has become available since the previous meeting.

The abridged minutes and the background materials to the minutes are available on the MNB's website at:
http://www.mnb.hu/en/monetary-policy/the-monetary-council/minutes

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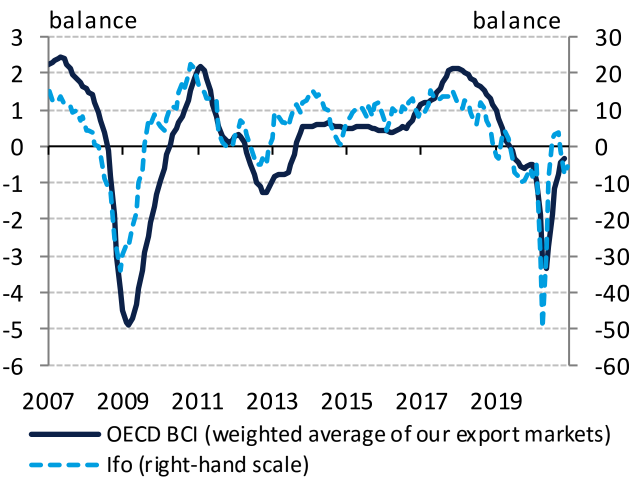
1. Macroeconomic developments

1.1. Global macroeconomic environment

Based on currently available data, the impacts the second wave of coronavirus had on the countries in the world varied. The measures taken to contain the second wave, typically curbed industrial production to a lesser degree than services' performance. Euro area industrial production data indicate moderate, gradual recovery. On the other hand, in the fourth quarter of 2020, the recovery of the world's economies seemed to come to a halt, and global air traffic continued to stagnate. Currently, the Covid-19 vaccine is not widely available; as a result, the easing of the restrictive measures linked to the pandemic has yet to come.

Chart 1 Business climate indices in Hungary's export markets



Source: OECD, Ifo

Recently, trends in economic performance have primarily been shaped by Covid-19 and the measures implemented to control it. The second wave appears to have restrained industrial production to a lesser degree, while the service sector remains significantly exposed to the impacts of the measures related to the pandemic. World trade and global industrial production already exceed the level registered in January 2020, and the Dow Jones Transportation Average index is also at a high of several years. However, the future performance of air traffic, which has been basically stagnant since mid-August, is surrounded by a strong uncertainty. Until the Covid-19 vaccine becomes widely available and the necessary vaccination rate is achieved, the sector's global outlook will remain markedly uncertain.

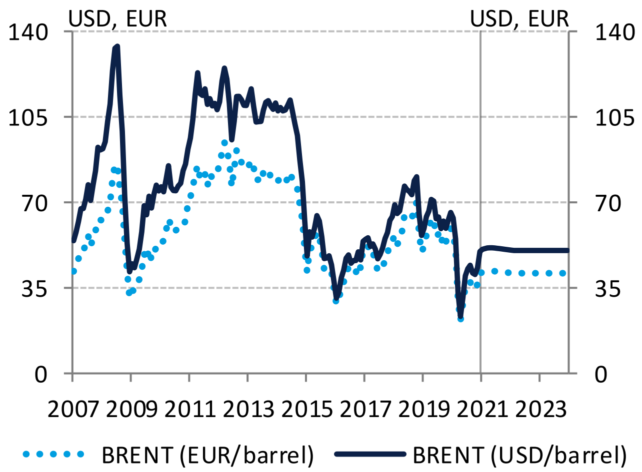
In 2020, Chinese economy grew by 2.3 percent in the first quarter despite a major decline resulting from coronavirus. In the fourth quarter, Chinese economy rose by 6.5 percent in annual terms, continuing the growth that had started in the second quarter. Business sentiment in China somewhat deteriorated in December (the composite index and the manufacturing PMI were both at their high in a decade in November), but it is still positive; the Purchasing Manager Indices were in the (growth) range of over 50 points. **In December, industrial production rose by 7.3 percent on an annual basis**, showing the highest growth rate since June 2017. Considering the entire year, industrial production rose by 2.8 percent. The number of motor vehicle registrations has been rising for nine months, exceeding the previous year's figures by 6.4 percent in December. The volume of retail sales rose by 4.6 percent in December year-on-year, while in terms of 2020 as a whole it was down by 3.9 percent.

In the third quarter, the US GDP fell by 2.9 percent year-on-year. Compared to the previous quarter, a major adjustment took place in all areas; however, GDP still falls short of its pre-pandemic value. The largest decline was seen in exports, but households' consumption and investments also decreased. **In November, US industrial output fell by 3.6 percent, year-on-year, showing a decline for the 15th consecutive month.** However, this is the smallest fall measured since the start of the coronavirus crisis. Manufacturing performance decreased by 2.8 percent. **In November 2020, retail sales were up by 2.9 percent year-on-year.** In the week ending on 9 January, **the number of new unemployment benefit claims rose sharply again to 965,000 as a result of the second wave** instead of around 800,000, as expected by analysts. **The unemployment rate** in the age group of above 16 years old remained unchanged compared to the previous month, and it **stood at 6.7 percent.**

In the third quarter, economic performance of the euro area fell by 4.3 percent year-on-year, while quarter-on-quarter it grew by 12.6 percent according to data adjusted for seasons and working-days. **In November, industrial production fell by 0.6 percent in annual terms,** while the monthly growth indicates moderate, gradual recovery, as industry grew by 2.5 percent compared to October 2020, according to seasonally and calendar effect adjusted data. As a result of the measures taken to contain the second wave, **the volume of retail sales** started to decline again and **fell short of its year-on-year level by 2.9 percent.** On a monthly basis, there was even a stronger decline of 6.1 percent. **The unemployment rate** declined further, and in November it **stood at 8.3 percent.**

Hungary's main trading partner, **Germany's economy shrank by 4.0 percent in the third quarter. In October, Germany's industrial production fell by 3.7 percent** in annual terms. However, based on the industrial orders and monthly growth, Germany's industry continued to recover at a slow pace. In contrast with the euro area, **German retail sales volume** continues to rise, **growing by 8.8 percent** in November year-on-year. **After**

Chart 2 World market prices of Brent crude oil



Source: Bloomberg

weakening for two months, German business sentiment (Ifo Business Climate Index) **improved once again in December** (Chart 1).

After having experienced one of the greatest declines in its history, the United Kingdom still significantly falls short of its economic performance last year: **in the third quarter, British GDP fell by 9.6 percent year-on-year.** Recovery has halted. Published also with monthly frequency uniquely in Europe (along with Norway) by the Office for National Statistics GDP fell short of the data a year earlier by 8.9 percent in November. **Industrial production fell short of the level in November 2019 by 4.7 percent,** while **the volume of retail sales was up by 2.4 percent on an annual basis.** Compared to the previous month, monthly growth fell in both cases: industrial production was basically stagnant (-0.1 percent), while retail sales volume reflected the impact of the tightening measures related to the pandemic (-3.8 percent).

Most economies in the European Union showed a major rebound in the third quarter of 2020. Based on the currently available data, the onset of the second wave of the pandemic had mixed impact on the countries. In November, industrial production and the volume of retail sales both increased on a monthly basis in several countries.

In December, in line with analysts' expectations, **euro area inflation remained unchanged compared to November, and stood at -0.3 percent. Core inflation stagnated at 0.2 percent,** corresponding to the value expected by analysts. In the fourth quarter of 2020, the average world market price of Brent crude oil was USD 44.5/barrel, exceeding the average price in the second and third quarters (Chart 2). **Last month the world market price of Brent rose to levels unprecedented since March, averaging around USD 52/barrel.** In addition to the positive effect of the developments surrounding the vaccine on oil market demand outlook, the agreement reached by the OPEC+ member states also contributed to the price increase. In contrast with the previously planned daily production increase of 500,000 barrels, under the agreement, member states will increase their output by only 75,000 and 120,000 barrels in February and in March, respectively. Developments in oil prices were further supported by Saudi Arabia's voluntary undertaking, after the meeting, to reduce its production in February and March by an additional 1 million barrels per day. **The world market price of industrial commodities and unprocessed food increased in December.**

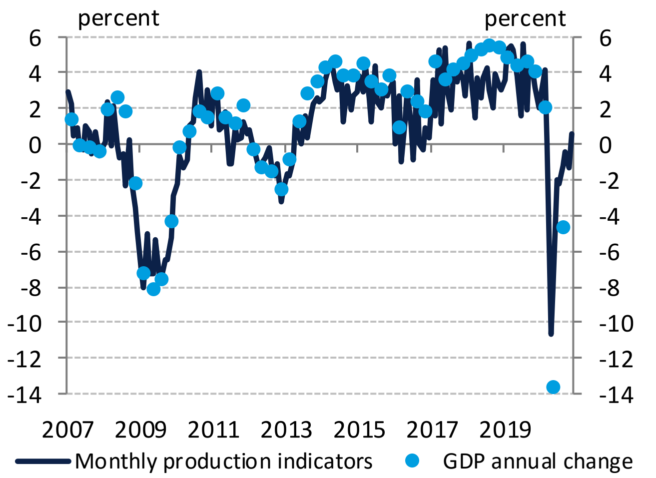
1.2. Domestic real economy developments

The adverse effects arising from the second wave of Covid-19 can already be traced in a number of real time data; the available weekly data from December confirm that recovery will be slow and long. Based on data from online cash registers, the improving trend in sales volumes was interrupted in September, and from mid-November turnover significantly declined. In December, passenger air traffic, cinema attendance and catering turnover fell short of the year-on-year value by 99 percent, 100 percent and 47 percent, respectively. Since mid-June, road passenger transport has steadily fallen short of the year-on-year value by 15-25 percent; on the other hand, industrial recovery has continued. So far, labour market adjustment has been modest in Hungary. In November, total employment fell by 0.6 percent year-on-year. The number of the unemployed was 190,000, which exceeded the year-on-year figure by 34,000 persons. Consequently, unemployment rate stood at 4.1 percent in November.

1.2.1. Economic growth

As reported in HCSO's data release, in the third quarter of 2020, Hungary's gross domestic product declined by 4.6 percent year-on-year (Chart 3). Data shows that **the economy grew by 11.4 percent quarter-on-quarter,** after adjusting for seasonal and calendar effects**.** In the first three quarters the national economy's performance fell by 5.5 percent. **In the third quarter, recovery from the crisis caused by the pandemic has commenced. Quarter-on-quarter performance of most national economy sectors improved. At the same time, the available high frequency data imply slow and protracted recovery.**

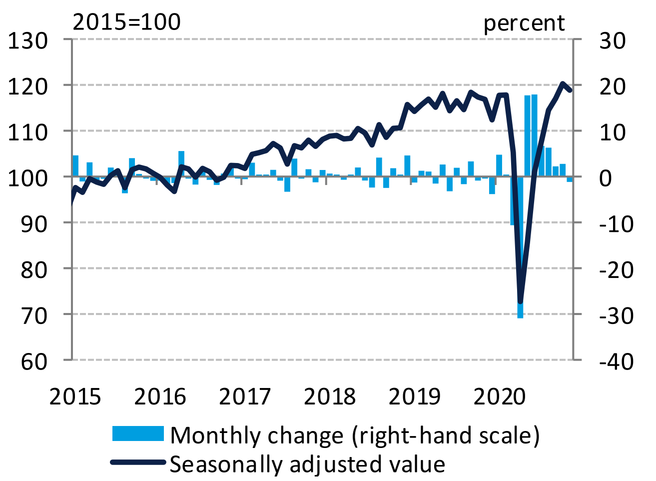
Chart 3 Monthly production indicators and GDP growth



Note: Weighted average of monthly production indicators (industrial output, construction output and retail sales). The weights are derived from regression explaining GDP growth.
Source: MNB calculation based on HCSO data

On the output side construction, transportation, warehousing, hotels and restaurants were the sectors that showed particularly poor performance. The change in the year-on-year economic performance was curbed to the largest degree by the transportation and warehousing sectors. **In the third quarter, of the sectors suffering the largest decline in the second quarter, the decline in industry and collective services was substantially more moderate.** In the case of industry, this was attributable to the supply chains, faltering in the first, acute phase of the pandemic, returning to normal and to the recovery of the automotive industry, while community services were supported by the restart of the public healthcare services. By contrast, **the performance of construction deteriorated further in parallel with the decline in building-type investments,** and the transportation and warehousing sectors were also unable to improve materially compared to the second quarter's data. **Due to the wide-ranging teleworking arrangements, the**

Chart 4 Development in industrial production

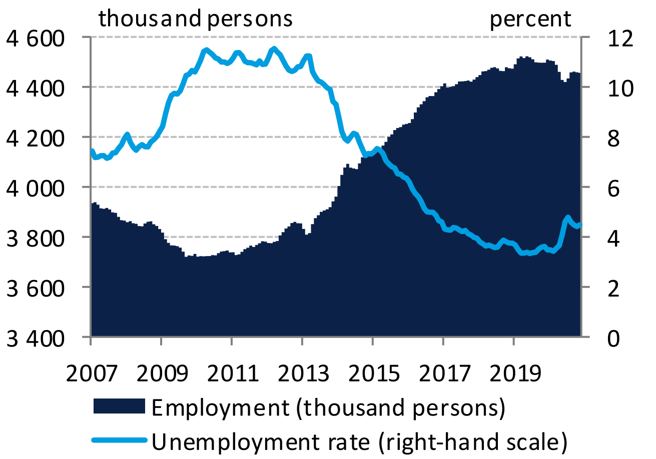


Source: MNB calculation based on HCSO data

infocommunication sector – contrary to the majority of sectors – registered a growth (+5.3 percent). Although accommodation and catering services, connected to tourism, as well as arts, entertainment and other services all registered substantial adjustment compared to the previous quarter, their performance still materially falls short of that of 2019.

On the expenditure side, the shortfall in the economy's performance compared to previous year was mostly attributable to the decline in investments. The fall in investments rested on a broad base, since all three sectors (corporations, households and government) contributed to the decline. By contrast, the positive change in inventories dampened the contraction of the economy. The decline in the external trade of services continued to play a major role in the decline in net exports, as the balance of goods exports made positive contribution to output. **Households' consumption expenditures declined only slightly in a European comparison.** The relatively favourable consumption performance was supported by the comparatively moderate response of the labour market to the first wave of the crisis, also contributed to by the government's job protection measures, the continued functioning of the credit market and the moratorium on loan instalments.

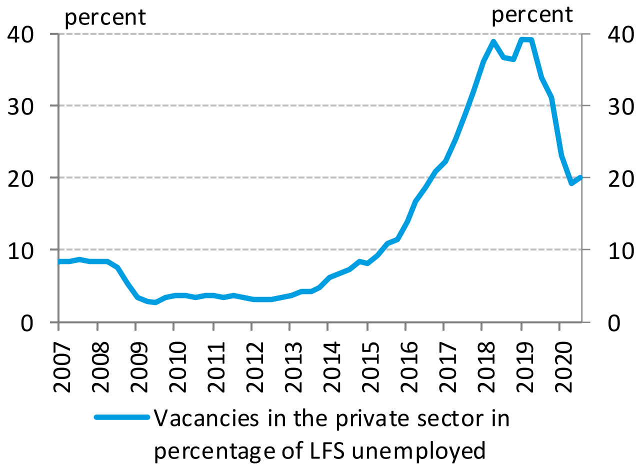
Chart 5 Number of persons employed and the unemployment rate



Source: HCSO

Growth in domestic industry continued in annual terms. According to the HCSO's data release, in November 2020 **industrial output was up by 1.6 percent year-on-year** based on calendar adjusted data. **At the same time, production (based on seasonally and calendar adjusted data) decreased by 1.2 percent on a monthly basis** (Chart 4). According to detailed data in November, production of the automotive industry, representing the largest share among the manufacturing subsectors, grew by 7.4 percent year-on- year. Growth was registered in the production of computers, electronic and optical products (+5.7 percent) as well as in the manufacture of machinery (+7.3 percent). The largest growth was registered in the production of electrical equipment (+27.4 percent), mostly due to the soar in battery manufacture, linked to the automotive industry. On the other hand, the food, rubber, plastic, metal and textile industries registered a decline on an annual basis. **Hungarian manufacturing PMI moderately declined in December and at present it stands at 51.1 points. Available high frequency data imply slow and protracted recovery.**

Chart 6 Development of labour market tightness indicator



Note: Quarterly data.
Source: National Employment Service, HCSO

According to the HCSO's preliminary data release, **goods exports and imports rose by 6.9 percent and 1.9 percent, respectively, in euro terms, year-on-year in November 2020**. Goods balance improved by EUR 482 million compared to November 2019.

In November 2020, the volume of construction output was up by 5.0 percent year-on-year. Output of both main construction groups increased: construction of buildings and other construction rose by 7.7 percent and 2.2 percent, respectively. **Construction output compared to the previous month was up by 12.1 percent** (based on seasonally and calendar adjusted data). The volume of new contracts concluded in November and the construction companies' contract portfolio exceeded the previous year's value by 55.5 percent and 2.7 percent, respectively.

In November, the volume of retail sales (including fuel sales) **was down by 0.8 percent year-on-year after accounting for calendar effects. The volume of retail sales recovers slowly; the pandemic situation and the restrictive measures continued to have negative impact on the turnover.** In November, the volume of retail sales in food stores and groceries rose (+1.8 percent), while in non-food stores it declined (-0.8 percent). The volume of retail sales declined primarily in consumer goods (-28 percent), textile, clothing and footwear shops (-27 percent) and in the furniture and appliances shops (-21 percent). The retail sales volume of mail order shops or web shops (+43 percent), and medicine and therapeutic product shops (+7.7 percent) rose according to the data adjusted for calendar effects. The volume of fuel retail sales declined by 9.4 percent on an annual basis. **Vehicle and components sales,** not belonging to retail sales, **fell by 12.7 percent in November.**

In November, the number of tourist overnight stays declined by 85 percent in year-on-year terms. As a result of the entry restrictions and the measures taken to contain the pandemic, applicable to commercial accommodations, the number of overnight stays by foreign and domestic tourists fell by 93 and 76 percent, respectively. In November, domestic tourists accounted for 76 percent of all tourist overnight stays.

1.2.2. Employment

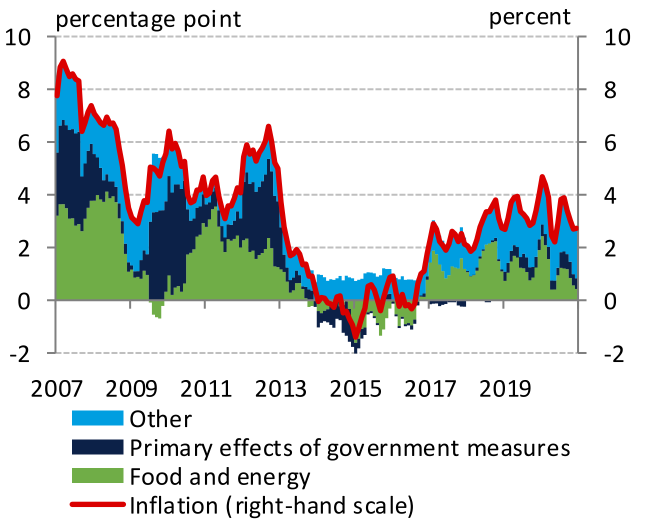
Based on the data of the Labour Force Survey (LFS), in November 2020 total employment fell by 25,800 persons (by 0.6 percent) to 4,496,000 persons year-on-year (Chart 5). Since November 2019, the number of employees in the private sector rose by 21,000 persons, the number of public employees and the number of those working abroad declined by 18,900 and 27,900 persons, respectively. **In November, the number of the unemployed was 190,200, exceeding the year-on-year figure by 33,800 persons,** thus on the whole **the unemployment rate stood at 4.1 percent**. Compared to the previous month, the number of the unemployed did not change significantly. Based on the data published by the National Employment Service (Nemzeti Foglalkoztatási Szolgálat - NFSZ) in November and December the number of registered jobseekers in Hungary was 296,500 (+57,300 on an annual basis) and 290,700 (+55,800 on an annual basis), respectively.

In the third quarter of 2020, private sector vacancies amounted to 42,800, falling short of the year-on-year value by 24.5 percent. **Compared to the previous quarter the annual decline in labour demand decreased; substantial improvement was registered primarily in manufacturing.** Among market services, the fall in the third quarter is primarily linked to trade and transport, while the HCSO registered material adjustment in sectors supporting administrative and services activity. The number of vacancies increased in annual terms only in the education sector, but this was unable to offset the declining number of jobs in the rest of the sectors connected to the government (healthcare, public administration). **The labour market tightness indicator** calculated from the ratio of job vacancies and unemployed persons, **has not changed significantly compared to the previous quarter,** and it still falls short of the values registered in the previous three years (Chart 6).

1.3. Inflation and wages

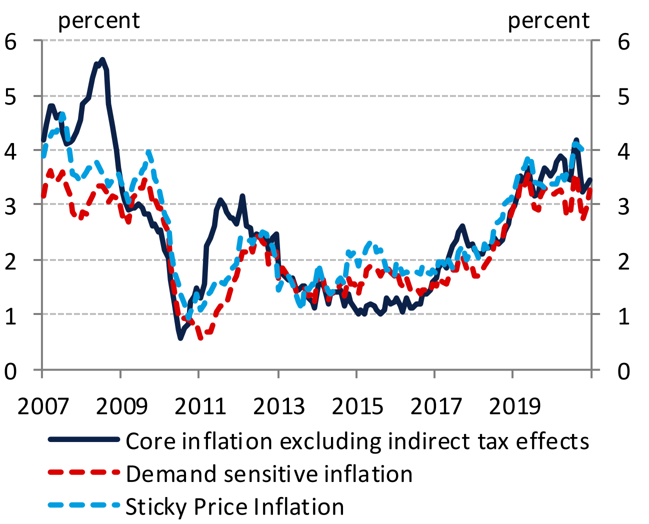
In December 2020, inflation, calculated on a year-on-year basis was 2.7 percent, while core inflation and core inflation excluding indirect tax effects stood at 4.0 and 3.4 percent, respectively. Overall, underlying inflation indicators capturing persistent trends (price index of demand sensitive and inflation of sticky price products and services) did not change significantly relative to the previous month. In October 2020, gross average wages in the private sector rose by 9.4 percent year-on-year, partly due to statistical effects.

Chart 7 Decomposition of inflation



Source: MNB calculation based on HCSO data

Chart 8 Measures of underlying inflation indicators



Source: MNB calculation based on HCSO data

1.3.1. Wage setting

In October 2020, gross average wages in the private sector rose by 9.4 percent year-on-year. Based on the detailed analysis of the sectors, the degree of the distortion in the gross average wage of full-time employees decreased compared to previous months, which may be attributable to the fall in the number of part-time workers. Regular average wages rose on a monthly basis, while bonus payments did not change materially compared to previous years.

Within the private sector, the wage dynamics of market services exceeds that in manufacturing similarly to the previous months. According to seasonally adjusted data, **manufacturing** wage dynamics accelerated compared to September; **wages were higher by 8.8 percent year-on-year.** Wages in the automotive industry – representing the largest share – increased by 8.6 percent in annual terms. **In market services, HCSO registered a growth of 10.1 percent.** Wages in construction, trade and catering rose by 9.9 percent, 9.8 percent and 4.9 percent, respectively, year-on-year.

1.3.2. Inflation developments

In December 2020, inflation calculated on a year-on-year basis was 2.7 percent, core inflation and core inflation excluding indirect tax effects stood at 4.0 and 3.4 percent, respectively (Chart 7). Compared to the previous month inflation did not change, while core inflation increased by 0.1 percentage point. This is attributable to the higher price dynamics of alcohol and tobacco products.

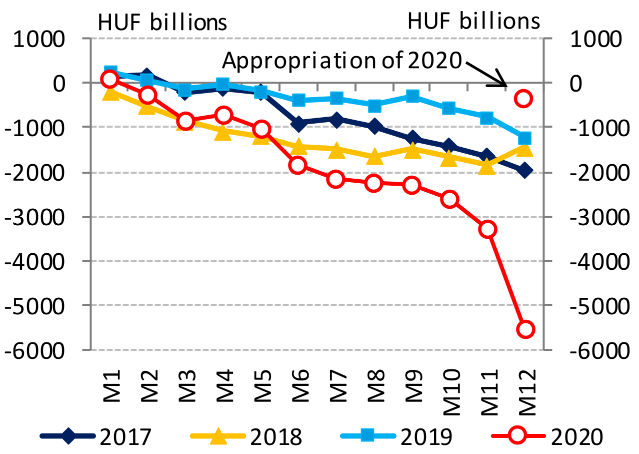
In 2020 as a whole – after receiving the data for December – average inflation stood at 3.3 percent, core inflation at 4.1 percent and core inflation excluding indirect tax effects at 3.7 percent.

Overall, underlying inflation indicators capturing persistent trends (inflation of demand sensitive and sticky price products and services) **did not change substantially compared to the previous month** (Chart 8). In November 2020, agricultural producer prices increased by 7.2 percent in annual terms, while the domestic sales prices in sectors of consumer goods increased by 3.2 percent.

1.4. Fiscal developments

The central sub-sector of the general government had a deficit of HUF 2,250 billion in December 2020, and as a result, the 2020 cash deficit reached a historic high, at HUF 5,549 billion.

Chart 9 Intra-year cumulative cash balance of the central government budget



Source: Budget Act of 2020, Hungarian State Treasury

The central sub-sector of the general government had a deficit of HUF 2,250 billion in December 2020, and thus the 2020 cash deficit reached a historic high at HUF 5,549 billion (Chart 9).

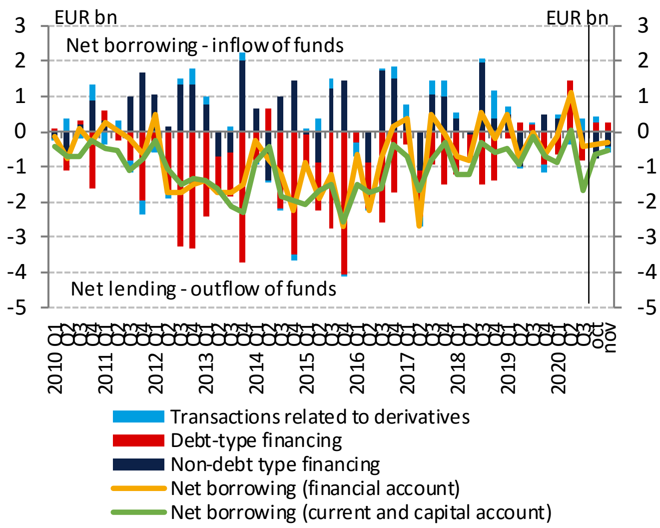
In December, revenues of the central sub-sector exceeded the year-on-year value by more than HUF 500 billion. The rise is primarily attributable to the revenues linked to EU transfers, however, tax revenues also exceeded those received in December 2019.

Expenditures of the central sub-sector reached a historic monthly high in December 2020 and also in the entire year, which is partly attributable to the preventive measures related to the coronavirus, and partly to the rise in the expenditures of the Economy Protection Fund. The discretional government decisions adopted in the last month of the year significantly raised the level of expenditures.

1.5. External balance developments

The current account surplus was also maintained in November, but it declined to EUR 272 million relative to the previous month. By contrast, net lending of the economy amounted to EUR 561 million. The decline in external balance indicators was attributable to the deteriorating services balance. On the financing side, the outflow of funds affected net foreign direct investments, and intercompany loans in particular, and the economy's net external debt rose slightly based on monthly transactions.

Chart 10 Structure of net lending (unadjusted transactions)



Note: Positive values indicate net borrowing (inflow of funds), while negative values indicate net lending (outflow of funds).
Source: MNB

Following the high balance registered in October, the current account surplus was maintained in November as well; however, its value at EUR 272 million represents a fall. The fall in the current account was primarily **attributable to the decline in the trade surplus**, while **the decreasing income deficit improved the position** (Chart 10). The decrease in the external balance indicators was attributable to the continued decline in the services balance, and particularly in tourism. The high trade surplus was primarily attributable to goods exports: measured in euro, exports – under stagnating goods imports – rose by almost 9 percent in annual terms, which may have been mostly attributable to industrial production, which also registered an increase in annual terms. The absorption of EU transfers somewhat decreased compared to the previous month, which was also reflected by the declining transfers balance. As a combined result of the foregoing **the economy's external position moderately deteriorated, but it still shows significant net lending, amounting to EUR 561 million in November**.

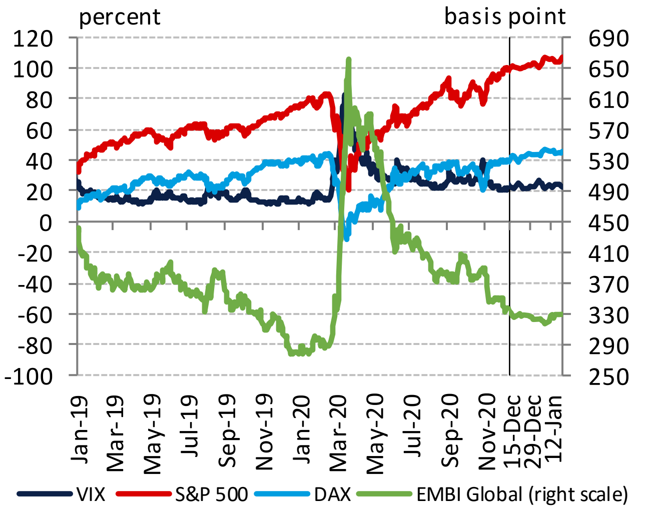
Based on the financial account data, November, in line with the net lending, was characterised by the outflow of external liabilities, which in November involved a decrease in net foreign direct investments, while the economy's net external debt moderately rose. In parallel with the FDI growth resulting from reinvestments, in November intercompany loans significantly decreased, which reduced the net FDI balance on the whole. The rise in the economy's net external debt was primarily attributable to the corporate sector, while the net external debt of the consolidated general government and banks practically remained unchanged.

2. Financial markets

2.1. International financial markets

Since the last interest rate decision, global investor sentiment has improved slightly, mostly reflecting the start of vaccination and the dissipation of uncertainties surrounding the US Senate majority. The VIX index, the key measure of equity market volatility, and the emerging bond market EMBI Global spread both slightly declined, and thus both indices were close to their value at the end of February 2020 (i.e. the period before the financial market turbulence caused by coronavirus). The MOVE index, measuring the developed bond market volatility, decreased by 3 basis points to 45 basis points. In the period under review, both the developed and emerging market stock exchange indices and the developed long-term yields rose. The dollar exchange rate varied against the developed and emerging currencies, while it slightly appreciated against the euro, currently standing close to 1.2. Oil prices rose further in the last month.

Chart 11 Developed market equity indices, the VIX index (left-hand scale) and the EMBI Global Index (right-hand scale)



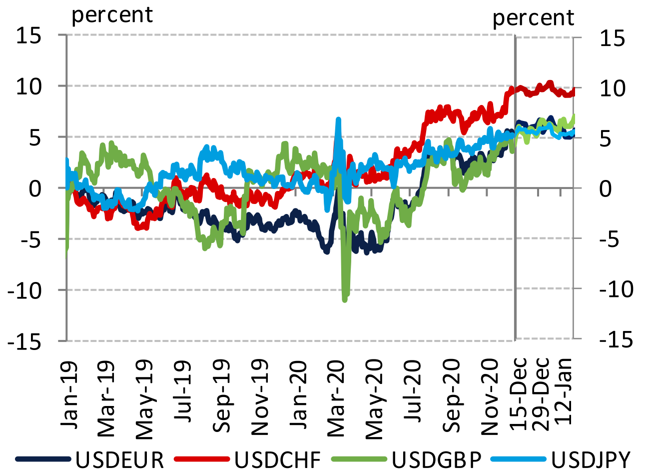
Source: Bloomberg

In the period since the last interest rate decision financial market sentiment slightly improved. The focus of market participants was on the news related to the vaccination programmes, the new and prolonged tightening measures adopted to contain the spread of the virus as well as the composition of the US Senate. In the first half of January, Democrats gained majority in the US Senate, as a result of which expectations related to the approval of the fiscal stimulus and more stringent regulation strengthened.

Of the risk indicators, after a temporary rise, the VIX index, the key measure of equity market volatility, decreased compared to the level registered at the previous interest rate decision by 0.4 percentage point to 22.5 percent, while the emerging bond market EMBI Global spread fell by 4 basis points to 329 basis points. At the end of the period, both indices still approximated their level registered at the end of February 2020 (i.e. before the financial market turbulence caused by the coronavirus) (Chart 11). The developed bond market MOVE index (measure of the developed bond market volatility) decreased by 3 basis points to 45 basis points.

Last month developed and emerging stock market indices both rose: the developed and emerging market MSCI composite index rose by 3.4 percent and 10.5 percent, respectively. **The key US and European stock exchange indices rose by 3-4 percent, while the Japanese one was up by 7 percent.** In the developed markets, the US Nasdaq outperformed and rose by 6.6

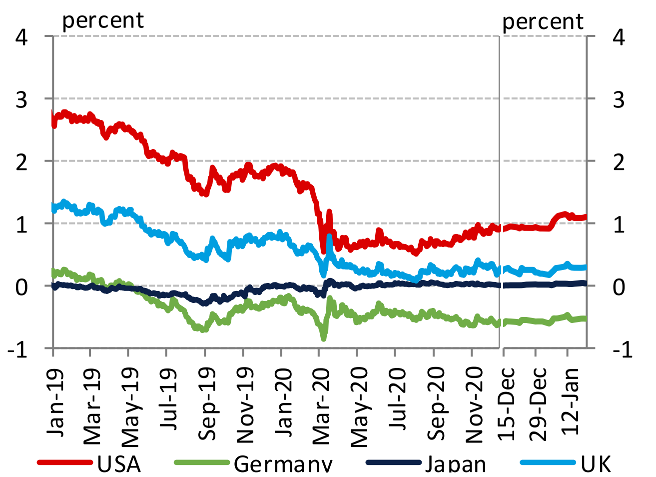
Chart 12 Developed market FX exchange rates



Note: Positive values indicate the strengthening of the variable (second) currency.

Source: Reuters

Chart 13 Yields on developed market long-term bonds



Source: Bloomberg

percent in a monthly comparison. **Within the emerging markets, the Chinese stock exchange outperformed, registering a rise of 14.3 percent**, which was also supported by the better than expected Chinese growth data. **Stock market indices rose in the countries of the region as well**: the Czech one rose by 8.9, the Romanian one by 6.8, the Hungarian one by 5.4 and the Polish one by 4.6 percent.

The dollar has varied against the developed currencies. The dollar appreciated against the euro and the Swiss franc by 0.4 and 0.5 percent, respectively, it depreciated against the British pound by 1.4 percent, while its exchange rate against the Japanese yen essentially has not changed (Chart 12). At the end of the period, the euro-dollar exchange rate stood at 1.21. **The exchange rate of the emerging market currencies against the dollar has also varied. Of the currencies of the region, the forint and the Czech koruna appreciated, while the Polish zloty and the Romanian leu depreciated.** Since the last interest rate decision the price of gold rose by 0.3 percent, to USD 1,859/oz.

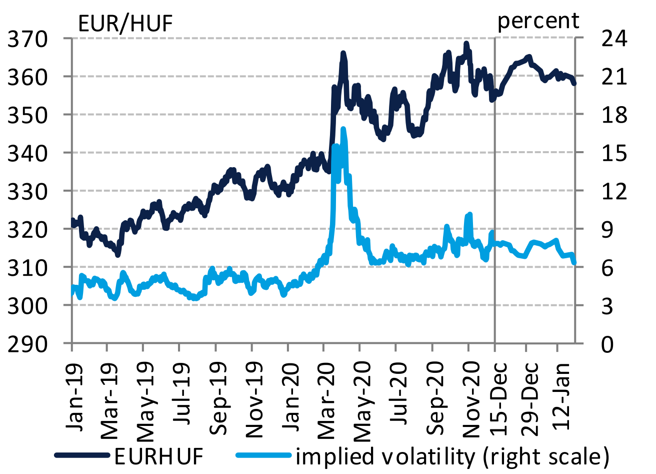
Developed bond yields have increased since the last interest rate decision. The Japanese and the British 10-year yield rose by 4, the German one by 8 and the US yields by 19 basis points, and thus at present the US and German yields stand at 1.10 and -0.53 percent, respectively (Chart 13). Developed long-term yields may have increased as a result of the vaccination programmes, despite the fact that new and prolonged restrictive measures have been adopted. The rise in US yields may have been mostly attributable to the reflation expectations connected to the Democrats' majority in the Senate. **Emerging countries' bond yields showed a mixed picture. Most countries of the region were characterised by falling yields**: the Romanian, Polish and Czech yield fell by 39, 8 and 3 basis points, respectively, while the Hungarian 10-year yield – partly due to the changeover to longer bonds as part of the benchmark change – rose by 23 basis points.

Since the last interest rate decision oil prices were supported both from the demand and supply side, and thus they registered significant further increase. On the demand side, the rise in oil prices was attributable to the emergence of the Covid-19 vaccines and the application of monetary and fiscal stimuli. On the supply side, the voluntary decision of Saudi Arabia to cut its output in February and March by 1 million barrel supported the rise in prices. Last month the price of Brent crude oil rose by 10.5 percent to USD 56.1/barrel, while the price of WTI by 11.8 percent to USD 53.2/barrel.

2.2. Developments in domestic money market indicators

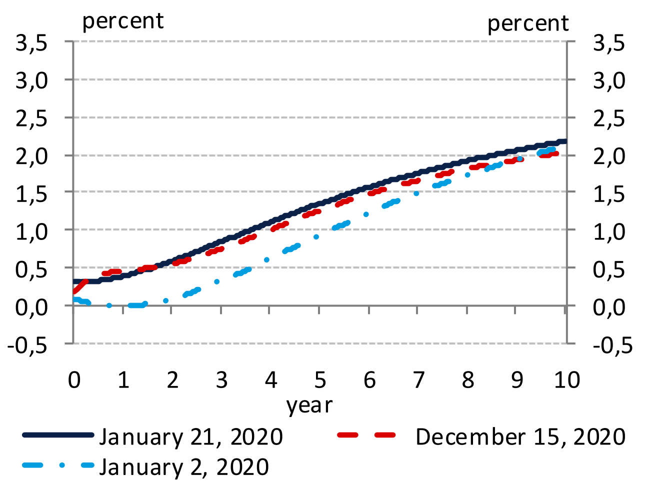
Overall, in the period under review, the forint weakened slightly against the euro. The currencies in the region showed a mixed picture. The government securities market's yield curve became slightly steeper. In the past month, there has been strong demand at both discount Treasury bill and government bond auctions, on the whole. The average auction yield of longer-term bonds showed a mixed picture compared to mid-December.

Chart 14 EUR/HUF exchange rate and the implied volatility of exchange rate expectations



Source: Bloomberg

Chart 15 Shifts in the spot government yield curve



Source: MNB, Reuters

Since the interest rate decision in December, the forint exchange rate against the euro slightly weakened, and at present it stands close to 357 (Chart 14). During the period under review, the volatility of the forint exchange rate was primarily caused by the news on the Polish foreign exchange market intervention, which was meant to depreciate the zloty. The currencies of the region showed a mixed picture last month; while the Polish zloty depreciated by more than 2 percent against the euro, the Romanian leu fluctuated in a relatively narrow band during the period, and the Czech koruna appreciated by 0.5 percent.

The government yield curve became slightly steeper (Chart 15). The shortest section of the yield curve declined by 1-9 basis points, while the 1-year section of the curve decreased by 1-7 basis points. An increase of 9 basis point was observed around the 5-year section of the yield curve, 15 basis points at the 10-year maturity and 20-28 basis points at the longest section.

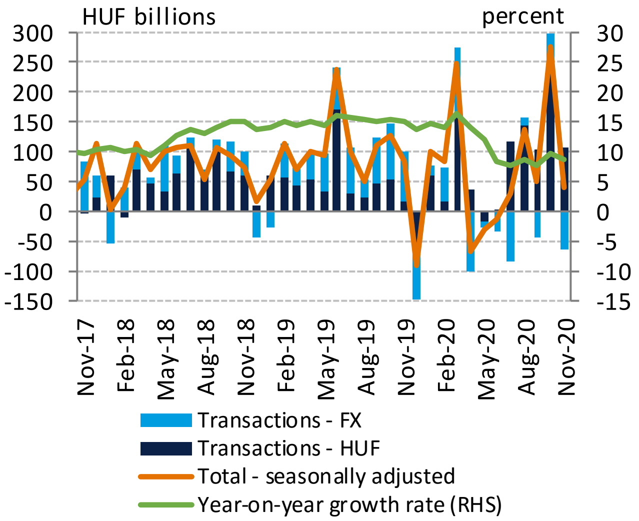
In the past month the discount Treasury bill and government bond auctions were mostly characterised by strong demand. With the exception of the last two auctions (12 and 19 January), the Government Debt Management Agency sold the announced volume at the auctions of the 3-month Treasury bills and at the 12-month auctions on each occasion. Since the last interest rate decision, the average yield at the 3-month auctions rose from 0.32 percent to 0.33 percent, while the average auction yield at the 12-month Treasury bill auctions dropped from 0.49 percent to 0.48 percent. The government bond auctions were characterised, by strong demand; accordingly, at the 3-, 5-, 7- and 10-year auctions the Government Debt Management Agency accepted bids in excess of the announced volume usually by HUF 10-15 billion, while at the 20-year auctions it sold by HUF 3 billion less than the announced volume. At the latest auction, the average yield of the 10-year securities was 2.28 percent, representing an increase of 9 basis points compared to the mid-December average auction yield. The average auction yield on the 5-year government securities declined by 7 basis points to 1.42 percent, while on the 3-year securities it fell by 23 basis points to 0.73 percent. The average auction yield on the 20-year securities rose by 5 basis points to 2.55 percent compared to the last auction held at the end of November. The Hungarian 5-year CDS spread remained unchanged during the period under review, and currently stands at 60 basis points.

Non-residents' holdings in HUF government securities somewhat increased. Non-residents' holdings rose by HUF 197 billion to HUF 4,733 billion; and the market share of forint government securities held by non-residents increased from 22.1 percent to 22.5 percent.

3. Trends in lending

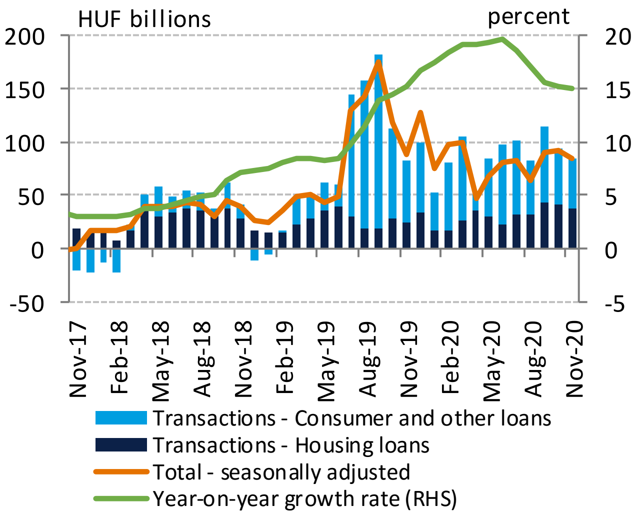
In November 2020, outstanding loans to non-financial corporations increased by HUF 45.4 billion, reflecting an increase in outstanding forint loans by HUF 107.7 billion and a decline in foreign currency loans by HUF 62.3 billion. In November, outstanding lending to households increased by HUF 84.9 billion due to transactions, and as a result, the annual growth rate was 15.0 percent, still mostly supported by the technical effect of the moratorium, reducing repayments.

Chart 16 Net borrowing by non-financial corporations



Source: MNB

Chart 17 Net borrowing by households

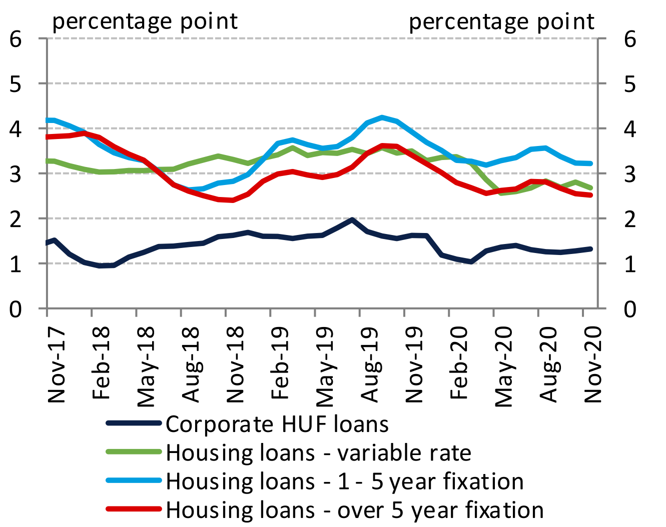


Source: MNB

In July 2020, outstanding borrowing of non-financial corporations grew by HUF 45.4 billion, as a combined result of the increase in outstanding forint borrowing by HUF 107.7 billion growth and a decline in foreign currency loans by HUF 62.3 billion (Chart 16). Due to the more moderate monthly growth, **the annual growth rate decelerated to 8.8 percent from 9.6 percent registered in previous month.** In November, credit institutions disbursed new loans in the amount of HUF 295 billion, which exceeds the value registered last November by 80 percent. In November, credit institutions concluded forint contracts with enterprises under FGS in the amount of HUF 174 billion, which accounts for almost 60 percent of the total placements to the corporate sector.

In November, outstanding borrowing of households increased by HUF 84.9 billion due to transactions, and thus the annual growth rate was 15.0 percent, still mostly supported by the technical effect of the moratorium, reducing instalments (Chart 17). The volume of new loans fell short of the year-on-year value by 12 percent, which is still mostly attributable to material decline in personal loans. On the other hand, the volume of housing loan contracts already exceeds the November 2019 value. The subsidised loans linked to the family protection and first-time homebuyers' programmes continue to provide support for lending to households, accounting for more than one third of the disbursements in November. During the month under review, outstanding prenatal baby support loans exceeded HUF 1,000 billion. Thereby the product accounts for 13 percent of the outstanding borrowing of households. Without the additional effect of this product, growth in outstanding lending would have been only 6 percent.

Chart 18 Development of corporate and household credit spreads



Note: In the case of corporate forint loans, the spread over the 3-month BUBOR. In the case of housing loans with variable interest or interest fixed for 1 year at the most, the 3-month BUBOR, while in the case of housing loans fixed for over one year, the APR-based margin above the relevant IRS.
Source: MNB

The smoothed interest rate spread of corporate loans in HUF was 1.32 percentage point in November 2020, representing an increase of 0.04 percentage point compared to the previous month (Chart 18). The average smoothed interest rate spread on variable rate housing loans calculated on the basis of the annual percentage rate (APR) also declined during the month and amounted to 2.68 percentage points. The spread on products with interest rate fixation periods longer than one year, up to 5 years and more than 5 years also decreased compared to October. The average spread on housing loans with an interest rate fixation longer than one year and up to 5 years reached 3.22 percentage points in November, while the spread on products with interest rate fixation for more than 5 years was 2.52 percentage points.