



MACROECONOMIC AND FINANCIAL MARKET DEVELOPMENTS

BACKGROUND MATERIAL
TO THE ABRIDGED MINUTES
OF THE MONETARY COUNCIL MEETING
OF 27 JULY 2021

JULY
2021

Time of publication: 2 p.m. on 11 August 2021

The background material ‘Macroeconomic and financial market developments’ is based on information available until 22 July 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

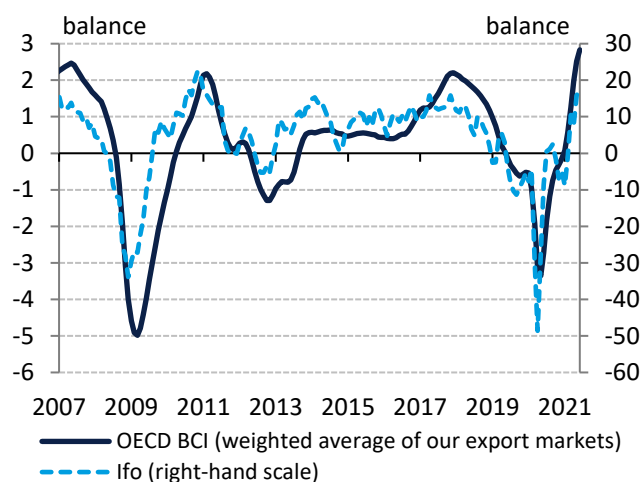
In the second quarter of 2021, the economic performance of China increased by 7.9 percent year-on-year. Due to last year's low base, the monthly production indicators registered double-digit growth also in May, in the euro area, the United States and in the United Kingdom as well. In June, manufacturing and service sector confidence indicators implied positive growth prospects at international level. In the second quarter of 2021, the external inflationary environment remained high. In the United States the consumer price index rose to 5.4 percent in June, which was the highest since August 2008. In Poland the June consumer price index remained above the central bank's target, at 4.4 percent. In the Czech Republic inflation in June was 2.8 percent, exceeding the 2 percent inflation target of the Czech central bank. Euro area inflation declined – in line with market expectations – to 1.9 percent. The increase observed in the number of cases in recent weeks signals the onset of the fourth wave of the coronavirus pandemic, which may interrupt the recovery of the economy. In countries with higher vaccination coverage the negative impact of the potential tightening is likely to be more moderate.

Global industrial production exceeded its pre-pandemic level already in September 2020, and has continued to outstrip it ever since then, while in parallel with the restart of the economies the service sector's prospects also improved significantly. Contrary to previous expectations, the global semiconductor shortage caused no decline in industrial production until April this year; nevertheless, it still represents a downside risk. Prospects of the service sector improved in parallel with the rise in vaccination coverage; nevertheless, recovery is still expected to be slow. The number of daily commercial flights moderately declined by February from the average 65-70 thousand flights registered in the second half of last year, followed by a rise from March and now, in parallel with the commencement of the travel season, it is around 93 thousand, which – however – is still well below the 2019 figures.

GDP data in the first quarter of 2021 were more favourable than expected in most economies; however, the recovery of the countries follows different patterns. In the second quarter of 2021, the economic performance of China increased by 7.9 percent year-on-year (while quarter-on-quarter it rose by 1.3 percent according to the seasonally and working-day adjusted data). Economic recovery in the world's two largest economies (China, United States) is stronger. Performance of the United Kingdom and the European Union in the first quarter 2021 was below that of the fourth quarter of 2019. The countries where tourism has a larger weight within the gross national product typically show slower recovery. Within the European Union the greatest lag can be identified in Spain and in Portugal. GDP exceeded its pre-pandemic level only in Ireland, Estonia, Luxembourg, Lithuania and Romania.

Due to last year's low base, monthly production indicators registered double-digit or close to double-digit growth in

Chart 1 Business climate indices in Hungary's export markets



Source: OECD, Ifo

May as well. Industrial production in the euro area, the United States, the United Kingdom and in China rose by 20.5 percent, 16.1 percent, 20.6 percent and 8.8 percent, respectively, compared to last May. In May, the volume of retail sales grew by 12.4 percent in China, 28.1 percent in the USA, 24.6 percent in the United Kingdom and by 9 percent in the euro area, on an annual basis. The indices compared to previous month rose in China, while they varied in the euro area countries.

Forward-looking confidence indices related to the manufacturing and service sector implied positive outlooks in June.

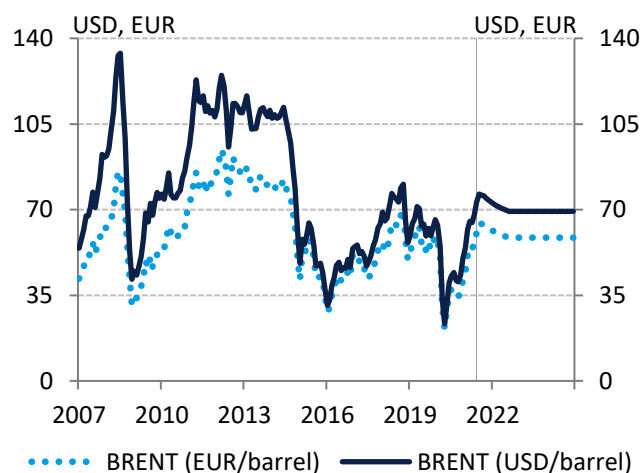
Business sentiment in China moderately declined in April, but the Purchasing Manager Indices were still in the (growth) range of over 50 points. The Purchasing Manager Index of the United States and the euro area rose further in June. German business sentiment (Ifo Business Climate Index) improved in June, reaching a multi-year high (Chart 1).

International labour market trends improved in May. In the United States, the number of new unemployment benefit claims was 360,000 in the week ending on 10 July, which is a decrease compared to previous week and the lowest since the pandemic began. The unemployment rate declined, and in May it stood at 5.8 percent. In May, euro area unemployment rate declined by 0.2 percentage point, compared to the previous month, to 7.9 percent.

Euro area inflation, in line with analysts' expectations, declined to 1.9 percent in June, after 2.0 percent registered in May. Core inflation also corresponded to analysts' expectations and fell to 0.9 percent. In Poland the June consumer price index remained above the central bank's target. In the Czech Republic inflation in June was 2.8 percent, which also exceeded the 2 percent inflation target of the Czech central bank. The soar observed in the number of cases in recent weeks may entail the onset of the fourth wave of the coronavirus pandemic, which may interrupt the recovery of the economy. In countries with higher vaccination coverage the negative impact of the potential tightening is likely to be more moderate.

In June 2021, the average world market price of Brent crude oil was USD 73.1 per barrel, while the spot price stands close to USD 76 per barrel since early July (Chart 2). In the recent period, the price of Brent crude oil rose as a result of the economic recovery and the lifting of the restrictions. The OPEC+ meeting in early July provided additional support for the rise in oil prices. Although the member countries managed to reach an agreement with regard to this year to increase production between August and December by 400 thousand barrels per day every

Chart 2 World market prices of Brent crude oil



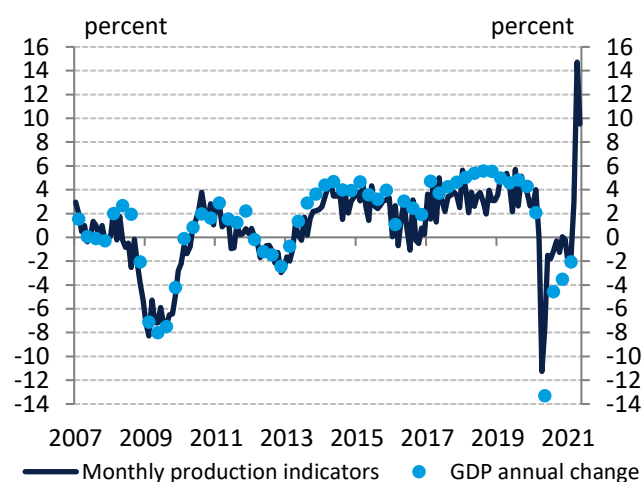
Source: Bloomberg

month, there was no agreement between the United Arab Emirates and the other member countries concerning the prolongation of the oil production agreement, expiring in April, until the end of 2022 under the present conditions. Oil prices moderately declined in the middle of the month, since investors worry about the potential consequences of the OPEC and OPEC+ countries' failure to reach an agreement on the production limits. **The price of industrial commodities slightly increased, while the world market price of unprocessed food declined in June.**

1.2. Domestic real economy developments

The Hungarian economy was able to grow even during the third wave of the coronavirus pandemic. In the first quarter of 2021, Hungary's GDP grew by 2.0 percent quarter-on-quarter, while, according to raw data, it fell short of the year-on-year level by 2.1 percent. Real time data project double-digit economic growth for the second quarter. In May, industry and construction performance rose both on a monthly and annual basis; industrial output exceeded its pre-crisis level. In May, the volume of retail sales rose compared to last year's low base. The labour market proved to be resilient to the coronavirus pandemic. In May 2021, the unemployment rate fell from 4.4 percent of April to 3.9 percent, while the number of people in employment rose by 55,000 persons year-on-year, which is also attributable to a base effect.

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

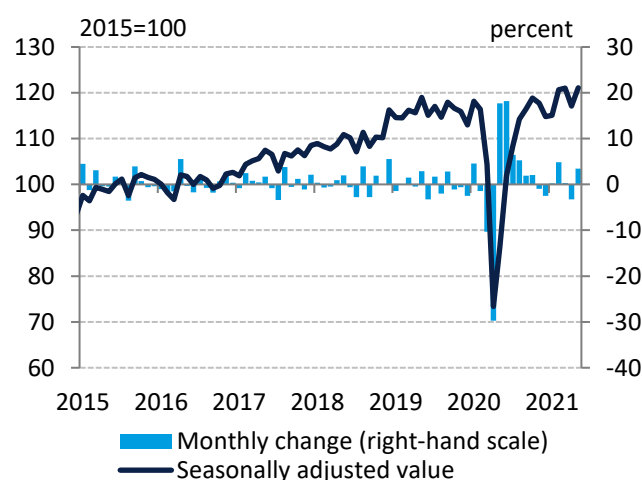
1.2.1. Economic growth

The Hungarian economy grew further during the third wave of the coronavirus pandemic; Hungary's GDP rose by 2.0 percent quarter-on-quarter (based on the seasonally and calendar adjusted data). **According to raw data, in the first quarter of 2021 Hungary's gross domestic product declined by 2.1 percent year-on-year** (Chart 3). Industrial and agricultural performance rose by 3.4 and 2.5 percent, respectively, year-on-year. By contrast, construction and services value added fell by 2.4 and 3.5 percent, respectively, on an annual basis. The largest decline was seen in the accommodation and food services activities, as well as in the transportation and storage sectors. Value added of the financial and insurance activities and of the information communication sectors increased. On the expenditure side, household consumption expenditure fell by 4.8 percent in the first quarter of 2021 year-on-year, with the largest decline registered in services consumption. As regards gross fixed capital formation, HCSO registered a decline of 0.1 percent compared to previous year. The volume of construction investments declined moderately, while the volume of machinery and equipment investments rose. The volume of both exports and imports increased. The structure of exports reflects duality: in line with the favourable industrial performance goods exports rose, while services exports declined year-on-year.

The decline in domestic economic output on an annual basis slightly exceeded the average of the euro area (-1.3 percent) and the European Union (-1.2 percent). In a quarterly comparison, Hungary is in the first third of the European ranking, while in an annual comparison it is in the mid-range, based on the GDP data registered in the first quarter of 2021.

In May 2021, industrial production rose by 39.1 percent year-on-year. The significant growth is attributable to the low base of last May. Based on the seasonally and calendar adjusted data, the volume of production increased by 3.4 percent on a monthly basis (Chart 4). In May, industrial output outstripped its pre-crisis level, but still lagged behind its pre-pandemic trend. All manufacturing subsectors

Chart 4 Development in industrial production



Source: MNB calculation based on HCSO data

contributed to the year-on-year growth. Based on raw data, output of the automotive industry – representing the largest weight in domestic output – registered an outstanding, i.e. 81.1 percent, growth, which is mostly connected to the low base value resulting from the factory stoppages last May and from the single-shift work schedule. On the other hand, this May the performance of the sector remained below its pre-crisis level, which may have been partly attributable to the stoppages resulting from the semiconductor shortage. The manufacture of electrical equipment rose by 73.3 percent in May on an annual basis, which is partly attributable to the pickup in domestic battery and electric engine production.

In May 2021, the volume of construction output was up by 18.7 percent year-on-year, as a result of which it came slightly below to the level registered prior to the outbreak of the coronavirus pandemic. Compared to April 2021, the volume of output rose by 2.3 percent based on seasonally and calendar adjusted data. Construction of buildings rose by 38.6 percent, while other construction fell by 0.8 percent, year-on-year. Based on seasonally adjusted data, the volume of new contracts concluded rose by 12.6 percent, while the construction companies' contract portfolio at the end of May grew by 11.5 percent in an annual comparison.

Available real time data project double-digit growth for the second quarter. Based on the online cash register data in May and June the volume of retail sales rose by 16 and 14 percent, respectively, in nominal terms, which was also attributable to last year's low base. Due to last year's low base **air passenger traffic** registered a triple-digit growth in May and June, albeit it still fell short of the level of two years ago by 90 percent in end-June. **Catering turnover** also registered a double-digit growth in June, and it even exceeded the level observed in the same period of 2019 due to the more moderate restrictive measures. Cinema attendance is recovering gradually after the opening, with the decline in May still exceeding 90 percent compared to its level two years ago, which fell to 18 percent by the end of June. Road passenger traffic has been improving strongly since mid-March, and by the end of June it even exceeded its level registered two years ago by more than 6 percent. In May, industrial production increased by 40.3 percent (based on seasonally and calendar adjusted data) year-on-year, while on a monthly basis the volume of output rose by 3.4 percent. In June, the **electricity load** and **road goods traffic** data exceeded the level of last year.

Household borrowing developed favourably. In June it exceeded its level one year and two years ago by 71 percent and 60 percent, respectively. Since last July the number of **housing market transactions** has been rising year-on-year,

albeit at a varying rate, and annual growth was particularly high due to last year's low base in April and May. **So far, labour market adjustment has been modest in Hungary.** In May 2021, the unemployment rate declined from 4.4 percent to 3.9 percent, while the number of people in employment rose by 55,000 persons year-on-year. **Google searches** related to unemployment also show a favourable picture. Online searches in Hungary for the terms "unemployment benefit" and "jobseeker's allowance" are at the average levels before the outbreak of the pandemic.

According to the HCSO's preliminary data release, **goods exports and imports rose by 37.9 percent and 38.2 percent, respectively, in euro terms, year-on-year in May 2021.** Merchandise trade surplus amounted to EUR 97 million, representing a year-on-year increase of EUR 9.8 million.

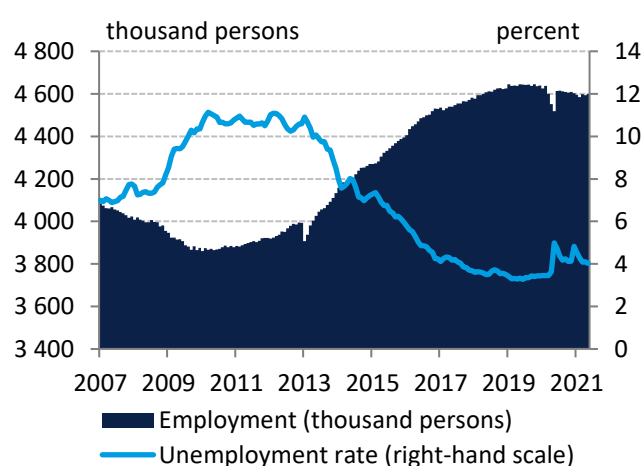
In May, the volume of retail sales was up by 5.8 percent year-on-year, based on the data adjusted for the calendar effect. Compared to previous month the volume of sales remained broadly unchanged (+ 0.1 percent). The volume of retail sales in food stores and groceries rose by 2.6 percent, while that in non-food stores was up by 8.7 percent on an annual basis. The volume of sales rose by 60 percent in the textile, clothing and footwear shops, by 48 percent in the shops selling second hand goods, by 13 percent in shops selling books, IT goods and other industrial goods, while automotive and vehicle part sales were up by 18 percent, according to the data adjusted for the calendar effect. The volume of fuel sales was up by 9.7 percent year-on-year.

In May 2021, the number of tourist overnight stays at domestic commercial accommodations was almost a quarter of the pre-pandemic level. Due to the historic low base of last year, the number of tourist overnight stays rose by 207.5 percent year-on-year. Domestic tourist overnight stays rose from 186,000 of last year to 522,000, while compared to May 2019 they fell by 55.8 percent. According to the HCSO's data release, the number of overnight stays by foreign tourists in Hungary was 125,000, while a year ago it was merely 25,000. However, this year's figure still fell short of the period two years ago by 91.2 percent.

1.2.2. Employment

Based on the data of the Labour Force Survey (LFS), **in May 2021 total employment counted 4,607,000 persons, which is an increase of 55,000 persons year-on-year** (Chart 5). Since May 2020, the number of employees in the primary labour market rose by 71,000, while the number of public employees and the number of those working abroad declined by 3,000 persons and 13,000 persons, respectively.

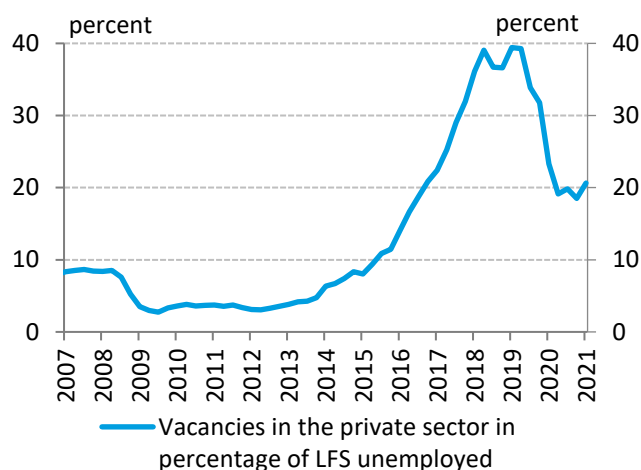
Chart 5 Number of persons employed and the unemployment rate



Source: HCSO

In May, the number of the unemployed was 189,000, falling short of the year-on-year figure by 26,000 persons, and thus on the whole the unemployment rate stood at 3.9 percent. The number of the unemployed decreased by 3,300 persons in May. Based on the data published by the National Employment Service (Nemzeti Foglalkoztatási Szolgálat - NFSZ) in May and June the number of registered jobseekers in Hungary was 274,000 (-89,000 on an annual basis) and 266,000 (-111,000 on an annual basis), respectively.

Chart 6 Development of labour market tightness indicator



Note: Quarterly data.

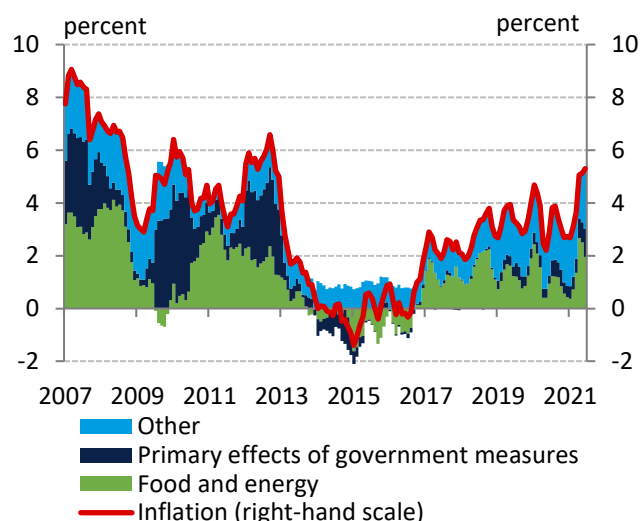
Source: National Employment Service, HCSO

In the first quarter of 2021, private sector vacancies amounted to 41,800, exceeding the year-on-year value by 14 percent. **Labour demand rose substantially in manufacturing, while it increased moderately in market services, on an annual basis.** Manufacturing job vacancies exceeded the figure a year ago by almost 5,000. In the market services sector, job vacancies slightly increased in the real estate, professional and administrative activities, and in the information and communication sectors, while they declined in the transportation and trade sectors. The number of vacancies increased in annual terms 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). Overall, the labour market tightness indicator calculated from the ratio of job vacancies and unemployed persons, **rose compared to the previous quarter**, but it still falls short of the values registered in the previous three years (Chart 6).

1.3. Inflation and wages

In June 2021, inflation calculated on a year-on-year basis was 5.3 percent, while both core inflation and core inflation excluding indirect taxes stood at 3.8 percent. Incoming inflation data exceeded both the central bank's projection and market expectations. The rise in inflation was mostly caused by the increase in the prices of regulated products and services and of market services. Underlying inflation indicators capturing persistent trends (price index of demand sensitive and inflation of sticky price products and services) increased compared to the previous month. In April 2021, gross average wages in the private sector rose by 9 percent year-on-year.

Chart 7 Decomposition of inflation



Source: MNB calculation based on HCSO data

1.3.1. Wage setting

In April 2021, gross average wages in the private sector rose by 9 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 increased compared to February and March, and its direction also changed. **According to our estimate, after adjustment for the statistical effects (part-timers, composition effect), the annual wage increase would be 12.1 percent in the primary labour market.** Regular average wage slightly increased compared to March, while bonus payments slightly fell short of the level observed in previous years.

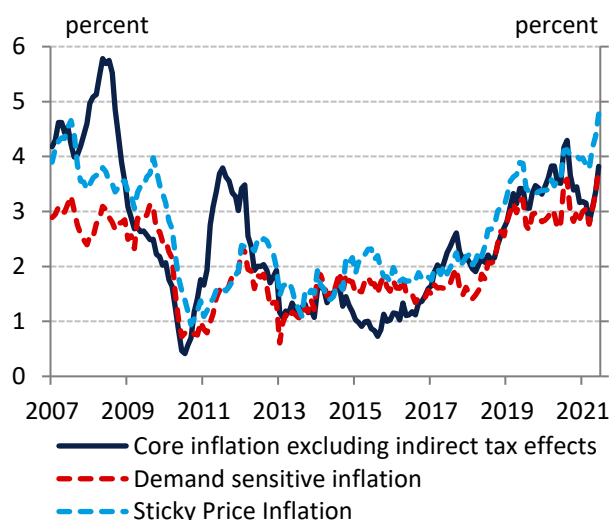
In the private sector wage dynamics of manufacturing significantly outstripped that of market services. In April, manufacturing wages were higher by 15.5 percent year-on-year. Wages in the automotive industry – representing the largest share – increased by 28.4 percent in annual terms. In market services, HCSO registered a growth of 4.9 percent. Wages in construction, trade and catering rose by 9.5 percent, 6.1 percent and 10.5 percent, respectively, year-on-year.

1.3.2. Inflation developments

In June 2021, inflation calculated on a year-on-year basis was 5.3 percent, while both core inflation and core inflation excluding indirect taxes stood at 3.8 percent (Chart 7). Compared to the previous month, inflation increased by 0.2 percentage point and core inflation by 0.4 percentage point. The rise in inflation was mostly caused by the increase in the prices of regulated price products and services and of market services. The higher price dynamics compared to the average of previous years was mostly attributable to the change in the price of domestic holidays, mobile phone and internet services. **Inflation exceeded the MNB's expectations and its structure confirms the inflation risks associated with the reopening of the economy. After the lifting of the restrictive measures, the increase in the price of market services accelerated, while underlying inflation trends also rose.**

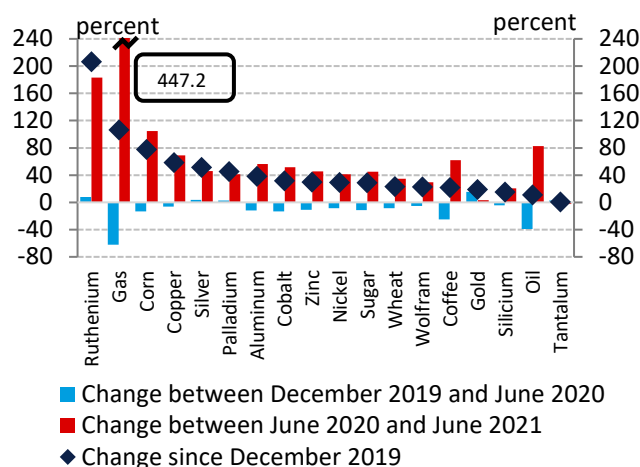
Underlying inflation indicators capturing persistent trends (inflation of demand sensitive and sticky price products and services) increased compared to the previous month (Chart

Chart 8 Measures of underlying inflation indicators



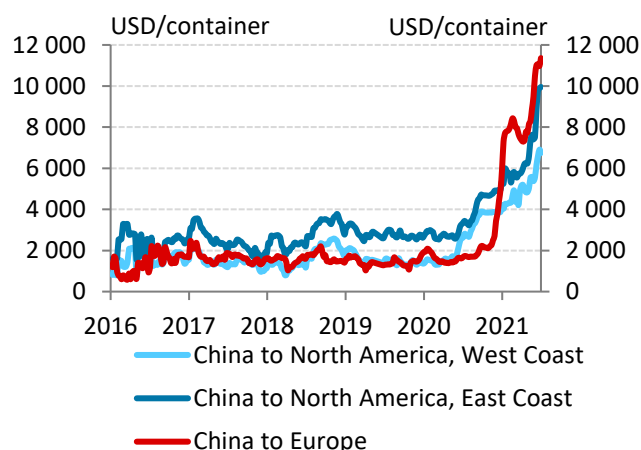
Source: MNB calculation based on HCSO data

Chart 9 Changes in major commodity prices since December 2019



Source: Bloomberg

Chart 10 Developments in the Freightos Baltic Index for shipments from China



Source: Bloomberg

8). In May 2021, agricultural producer prices increased by 17.4 percent in annual terms, while domestic sales prices in sectors of consumer goods increased by 3.9 percent.

1.3.3. Inflation risks

In line with the forecast in the June Inflation Report, inflation declines more slowly than previously expected, and the indicator peaked at 5.3 percent in June. Although incoming data exceeded the MNB's expectations, we still expect inflation to decline from July. On the other hand, the data confirm that inflation effects resulting from the reopening of the economy were strong in June as well.

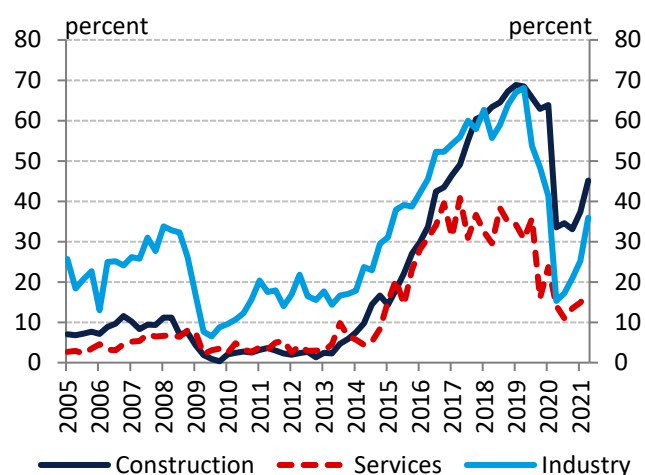
The growth in risks is equally attributable to international and domestic trends. Due to the different nature and management of the crisis, global economic activity and the labour market may recover faster than in the 2008/2009 crisis. In addition to the rapid economic recovery, a loose fiscal and monetary policy stance, high public debt ratios and expanding lending, together with deglobalisation and shortening value chains, all point to rising inflation globally. Globally, the prices of key commodities significantly rose in the first months of the year, and by now they exceed even the levels observed at the end of 2019 (Chart 9). The rise in global commodity prices may trigger another commodities super cycle.

Global value chains may recover more slowly than demand, leading to increased cost pressures in global transportation and industrial production. For example, the costs of shipments from China to Europe rose almost 7 times by early July 2021 from the level seen in July 2020 (Chart 10). In addition to a fast recovery in demand, the global chip shortage has caused disruptions in industrial production, particularly in the automotive sector, which may have a knock-on effects on prices.

In addition to international developments, several factors in the Hungarian economy also point to a higher inflation path than previously expected. In the second quarter of 2021, as a result of economy reopening and the low base of last year, a double-digit growth is likely to be achieved. Full employment may be achieved as early as next year, but based on pre-crisis patterns, bottlenecks may be in place, especially in the services and construction sectors, in parallel with the recovery (Chart 11).

Higher than expected wage dynamics may persist as the labour market tightens (Chart 12), with the rise in savings over the past year, postponed consumption and the availability of an increasing range of services projecting a growth in consumption expenditures. The opening of the economy could generate supply-demand conflicts, also

Chart 11 Labour shortage as a factor limiting production in Hungary

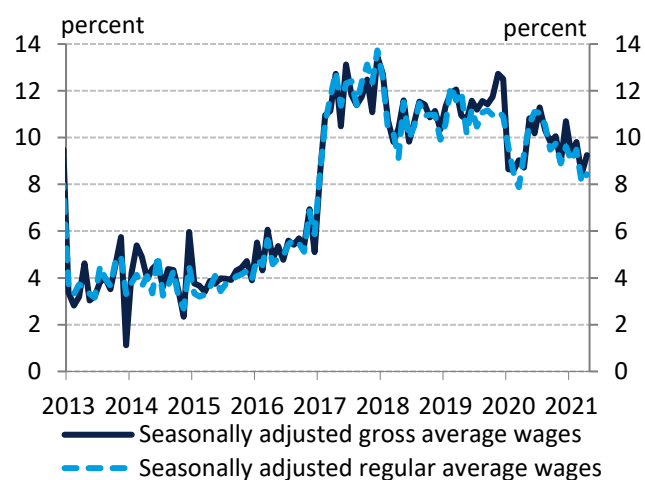


Note: Percentage of companies reporting that "Shortage of labour force" is a main factor currently limiting their production.

Source: European Commission

observed last year, which could lead to a rise in inflation in the short run. Moreover, a higher-than-expected budget deficit next year also points to a higher inflation path.

Chart 12 Dynamics of average earnings in the private sector

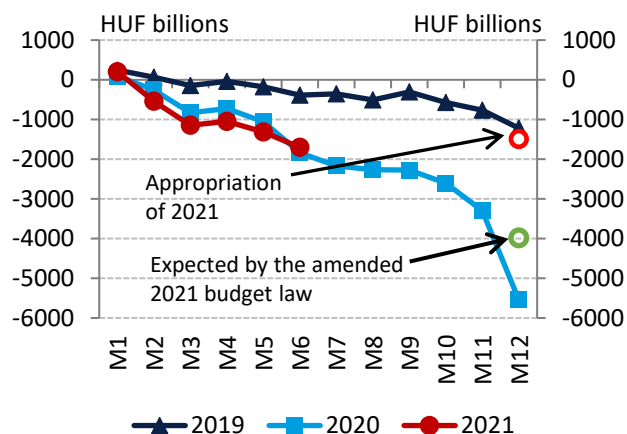


Source: MNB calculation based on HCSO data

1.4. Fiscal developments

In June 2021, the deficit of the central sub-sector of general government was HUF 392 billion. As a result, the current year's cumulated cash deficit rose to HUF 1,705 billion, which is lower than the year-on-year figure.

Chart 13 Intra-year cumulative cash balance of the central government budget



Source: Budget Act of 2021, Hungarian State Treasury

In June 2021, the deficit of the central sub-sector of the general government was HUF 392 billion. Thus, the current year's cumulated cash deficit rose to HUF 1,705 billion, which is lower than the year-on-year figure (Chart 13).

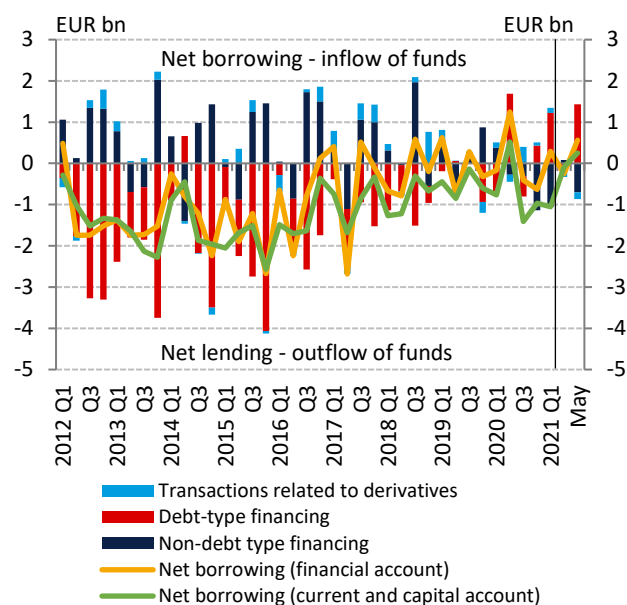
In June, revenues of the central sub-sector exceeded the year-on-year revenues by 16 percent, i.e. by roughly HUF 211 billion. The rise is attributable to the dynamic growth in tax and contribution revenues, partly resulting from the low base of 2020. Revenues from EU transfers also exceeded those of the base period. The generally strong dynamics of tax and contribution revenues was partly attributable to the rise in net VAT revenues, labour taxes and contribution payments.

In June 2021, expenditures of the central subsector fell short of the value registered last June by 9 percent, which was attributable – in addition to the lower expenditure of central budgetary organisations – to the fact that last year the one-off benefit paid to healthcare workers in the amount of HUF 500,000 increased the expenditures. The supplementary pension increase of 0.6 percent was paid in June, which increased expenditures by HUF 18 billion.

1.5. External balance developments

In May, the current account deficit amounted to EUR 424 million, while net borrowing was EUR 250 million. The rising deficit is attributable to the increase in the goods deficit. As regards trends on the financing side, foreign direct investments were broadly unchanged, while the economy's debt liabilities rose.

Chart 14 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

In May, the current account deficit rose to EUR 424 million.

The increase is linked to the goods balance and to import dynamics outstripping exports. Services balance surplus improved further during the month, albeit it substantially falls short of the level of previous years. The transfer balance surplus somewhat declined compared to previous month, while the income balance deficit remained unchanged.

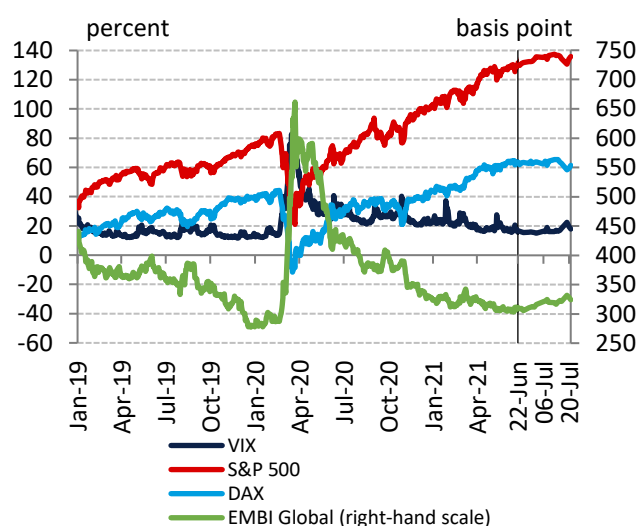
Based on the financial data, net foreign direct investment inflow significantly declined compared to previous month in connection with the usual dividend payments characterising this period. Growth in net external debt (Chart 14) was linked to the private sector. Accordingly, the government's indicator slightly declined, which related to the fall in non-residents' forint government securities holding.

2. Financial markets

2.1. International financial markets

In the period since the last interest rate decision financial market sentiment deteriorated slightly. The VIX index, measuring equity market volatility, rose to 17.9 percent, and the EMBI global spread in the emerging bond market and the MOVE index, measuring developed bond market volatility, also increased. Last month US stock exchange indices rose, while European and Japanese indices declined. The dollar appreciated against both the advanced and emerging currencies. It appreciated against the euro by 1.2 percent. Last month oil prices corrected their previous rise, which was mostly attributable to the raising of the OPEC+ oil supply and the expectations related to weakening demand due to the delta variant of the coronavirus.

Chart 15 Developed market equity indices, the VIX index (left-hand scale) and the EMBI Global Index (right-hand scale)



Source: Bloomberg

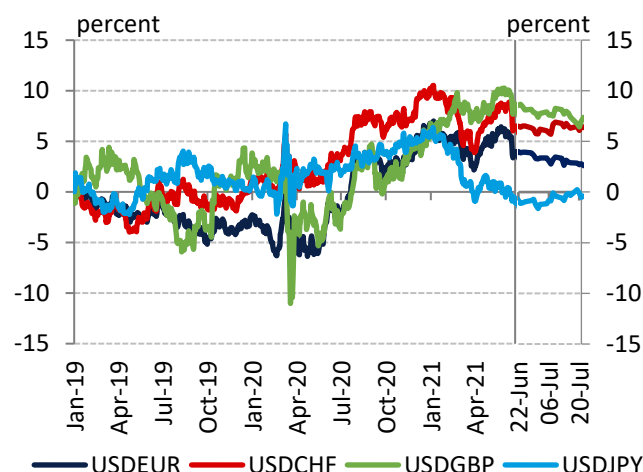
In the period since the last interest rate decision global financial market sentiment slightly deteriorated. The focus of market participant was on the spread of the delta variant of the coronavirus and the tightening measures introduced in connection with that. Trends in expectations related to global inflation developments was also a key factor in the period under review, as a result of which market participants also paid special attention to the central banks' latest communication.

Of the risk indicators, the VIX index, measuring equity market volatility, rose by 1 percentage point compared to its level at the previous interest rate decision to 17.9 percent, the EMBI global spread in the emerging bond market increased by 13 basis points to 324 basis points, while the MOVE index, measuring developed bond market volatility, stands at 65 basis points after a rise of 7 basis points (Chart 15).

Last month, S&P 500, the leading US stock index rose by 2.6 percent, the Nasdaq by 2.7 percent and the Dow Jones was up by 2.5 percent despite the moderately deteriorating global sentiment. On the other hand, the leading European stock indices declined: the German stock exchange fell by 0.6 percent, the British by 1.1 percent, the French by 1.8 percent and the Italian by 1.9 by percent. The Japanese stock exchange index fell by 4.6 percent, while the Chinese index rose by 0.5 percent. Stock market indices in the countries of the region showed a mixed picture: the Hungarian one fell by 0.7 percent, while the Polish and Czech one rose by 1.3 and 2.5 percent, respectively.

The dollar appreciated against the developed market currencies: it appreciated against the euro, the British pound and the Australian dollar by 1.2 percent, 1.4 percent and 2.4 percent, respectively. Due to its safe haven nature, the Japanese yen appreciated by 0.4 percent against the dollar (Chart 16). At the end of the period, the euro-dollar exchange rate came close to 1.18. **All currencies of the**

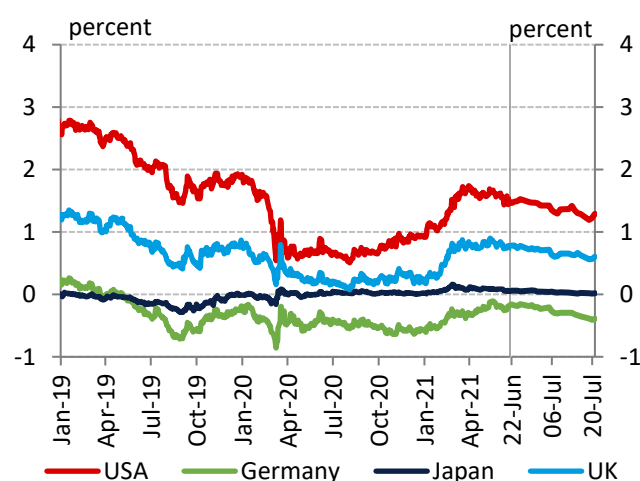
Chart 16 Developed market FX exchange rates



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

Source: Reuters

Chart 17 Yields on developed market long-term bonds



Source: Bloomberg

region depreciated against the dollar. Since the last interest rate decision, the price of gold rose by 1.2 percent, to USD 1,803/oz.

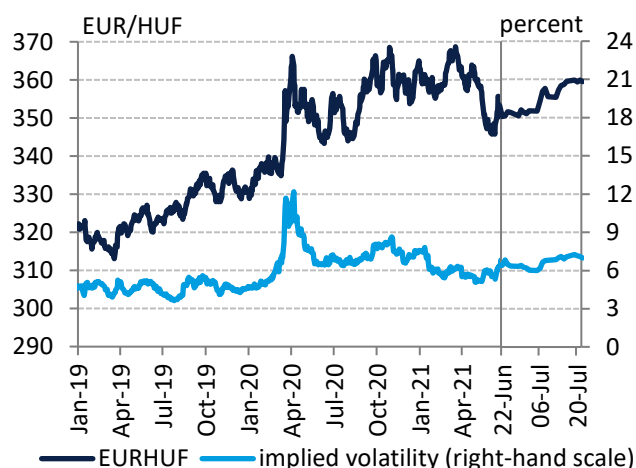
Developed bond yields have declined since the last interest rate decision (Chart 17). The US, German, British and Japanese 10-year yield was down by 19, 24, 18 and 4 basis points, respectively, and thus the US, German, British and Japanese yields closed the period at around 1.27, -0.4, 0.6 and 0.01 percent, respectively. **Yields in the Mediterranean countries also declined** by 13-23 basis points. In the countries of the region changes in yields followed opposite directions: the Hungarian and the Polish yields fell by 10 basis points and by 25 basis points, respectively. By contrast, the Czech and Romanian yields rose by 6 and 39 basis points, respectively.

In the past period, oil prices corrected part of the previous rise. The fall in oil prices was essentially caused by the OPEC+ agreement, according to which they raise supply by 400,000 barrels per day. On the other hand, due to the fast spread of the coronavirus' delta variant oil demand is expected to fall, which also contributed to the decline in oil prices. **Since the interest rate decision in June, the price of Brent crude oil decreased by 3.7 percent to USD 72, while the US benchmark WTI oil price fell by 4 percent to USD 70.1.**

2.2. Developments in domestic money market indicators

During the period, the forint depreciated against the euro to a larger degree than the currencies of the region. The government securities market's yield curve shifted downwards, while the interbank yield curve became flatter. In the past month, there was strong demand at government bond auctions and average auction yields at longer maturities declined.

Chart 18 EUR/HUF exchange rate and the implied volatility of exchange rate expectations



Source: Bloomberg

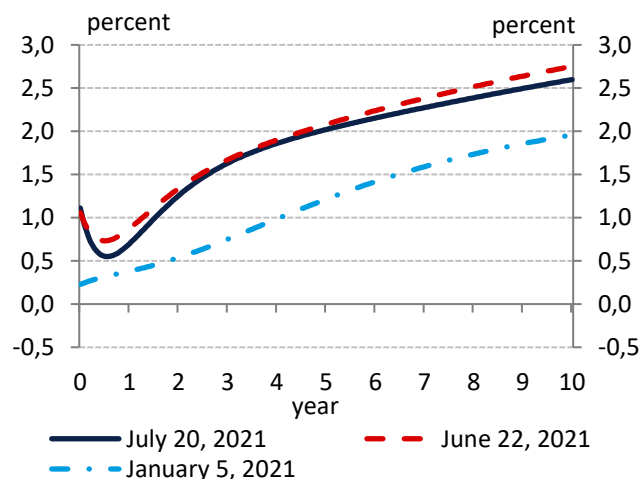
Since the interest rate decision in June, the forint depreciated against the euro. At the beginning of the period the forint was traded in a narrow band, but from the second week of July the Hungarian currency started to weaken and it depreciated by 2.7 percent in total against the euro. In parallel with the depreciation, exchange rate volatility moderately increased. Of the currencies of the CEE region, the Polish zloty and Czech koruna depreciated against the euro by 1.6 percent and 0.8 percent, respectively, while the Romanian leu essentially remained unchanged (Chart 18).

The 3-month BUBOR, relevant for monetary policy transmission, rose by 12 basis points to 1.07 percent since the last interest rate decision.

The government securities market's yield curve shifted downwards (Chart 19). Around the 1-year and middle section of the yield curve a fall of roughly 20 basis points and 5-10 basis points, respectively, was observed, while around the 10-year section a fall of 15 basis points was registered.

In the past month, the demand was mostly strong at government bond auctions. At the 3-month Treasury bill auctions the Government Debt Management Agency accepted bids for the announced volume whereas in the case of the 12-month Treasury bill auctions the acceptance was below the announced volume. Since the last interest rate decision, the average yield at the 3-month auctions declined from 0.57 percent to 0.51 percent, while the average auction yield at the 12-month Treasury bill auctions rose from 0.87 percent to 0.96 percent. Bond auctions were characterised by strong demand. Accordingly, the Government Debt Management Agency accepted bids in excess of the announced volume in almost all cases. At the latest auction, the average yield of the 10-year securities was 2.82 percent, representing a fall of 3 basis points compared to average auction yield before the May interest rate decision. The average auction yield on 5-year government securities rose by 3 basis points to 2.05 percent, while at the 20-year government securities it decreased by 11 basis points to 3.29 percent. The average yield of the 30-year green bonds, put up for auction for the second time, was around 3.44 percent, down by 25 basis points compared to the average yield at the first auction. The Hungarian 5-

Chart 19 Shifts in the spot government yield curve



Source: MNB, Reuters

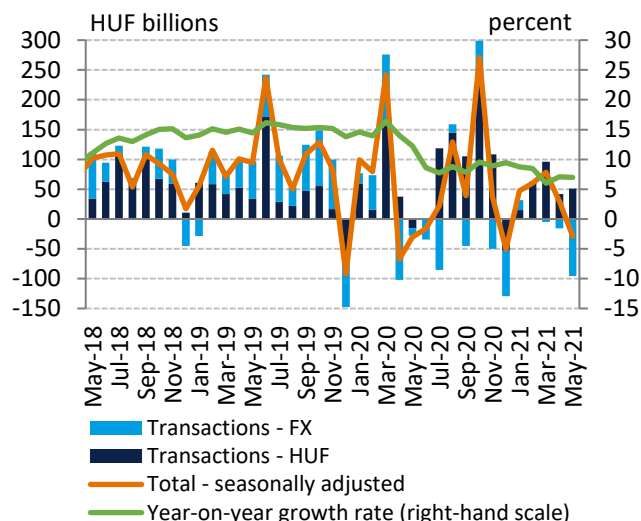
year CDS spread declined by 5 basis point to 55 basis points during the period under review.

Non-residents' holdings of forint government securities increased slightly. Non-residents' forint government securities holdings increased by HUF 123 billion to HUF 4,502 billion. Thus, the market share of forint government securities held by non-residents rose from 19.3 percent to 20 percent.

3. Trends in lending

In May 2021, outstanding lending to non-financial corporations fell by HUF 44 billion, reflecting a rise of HUF 51 billion in forint loans and a concentrated decrease of HUF 95 billion, attributable to large corporations, in foreign currency loans, thereby reducing the annual growth rate to 7 percent. In May, households' outstanding borrowing grew by HUF 144 billion, and as a result the annual growth rate rose to 15.2 percent

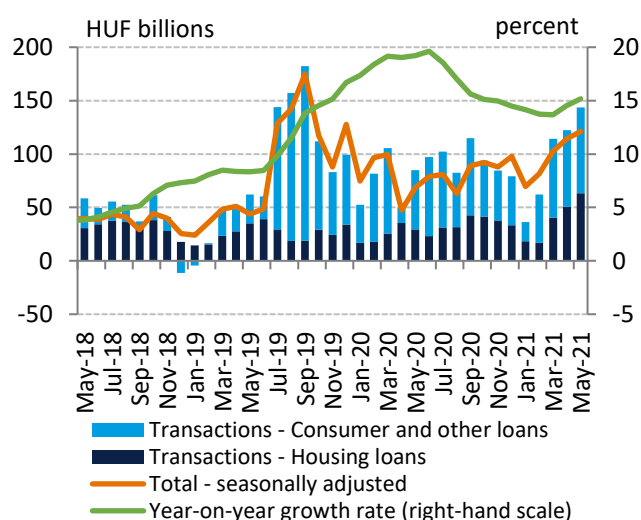
Chart 20 Net borrowing by non-financial corporations



Source: MNB

In May 2021, outstanding lending to non-financial corporations fell by HUF 44 billion, reflecting a rise of HUF 51 billion in forint loans and a concentrated decrease of HUF 95 billion, attributable to large corporations, in foreign currency loans, thereby reducing the annual growth rate to 7 percent (Chart 20). Due to the decline the annual growth rate fell to 7 percent. In May, credit institutions disbursed new loans in the amount of HUF 209 billion, which falls short of the year-on-year figure – already affected by the coronavirus and by the simultaneously launched credit schemes – by 15 percent; however, it exceeded its value registered two years ago by 40 percent. During the month under review, banks concluded non-overdraft forint contracts with enterprises under FGS Go! in the amount of HUF 120 billion, which accounted for 57 percent of the total forint corporate loan disbursements in May.

Chart 21 Net borrowing by households

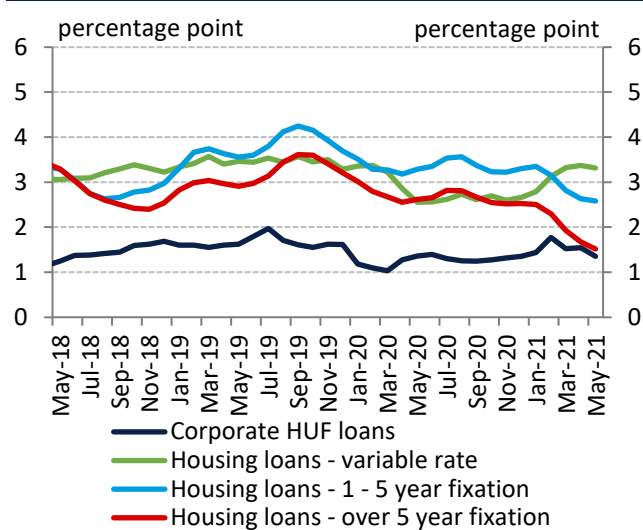


Source: MNB

In May, households' outstanding borrowing grew by HUF 144 billion, and as a result the annual growth rate rose to 15.2 percent (Chart 21). The volume of contracts concluded during the month in the amount of HUF 241 billion exceeded the year-on-year figure – already affected by the pandemic – by 60 percent, but it also outstripped the period two years ago, not affected by the pandemic, by 35 percent. The disbursement of housing loans in May reached a new historic high, with major contribution by the new measures aimed at first-time homebuyers. 29 percent, roughly HUF 35 billion, of the housing loans disbursed during the month were connected to the Home Purchase Subsidy for families, being the highest volume since the launch of the scheme. State-subsidised loans accounted for 30 percent of the total new retail lending in May. The largest volume is still represented by pre-natal baby support loans, with their stock of almost HUF 1,300 billion accounting for 15 percent of the total retail loan portfolio.

In May 2021 both corporate and household credit spreads decreased compared to previous month (Chart 22). The smoothed interest rate spread of forint corporate loans was 1.35 percent in May, representing a decrease of 0.2 percentage point compared to April. The average smoothed interest rate spread on variable rate housing loans calculated on the basis of the annual percentage rate (APR)

Chart 22 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

also decreased slightly during the month and amounted to 3.31 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 April. The average spread on housing loans with interest rate fixation periods longer than one year and up to 5 years reached 2.58 percentage points in May, while the spread on products with interest rate fixation periods of more than 5 years was 1.52 percentage points.