MACROECONOMIC AND

FINANCIAL MARKET DEVELOPMENTS

BACKGROUND MATERIAL

TO THE ABRIDGED MINUTES

OF THE MONETARY COUNCIL MEETING

OF 21 SEPTEMBER 2021

SEPTEMBER

2021

Time of publication: 2 p.m. on 6 October 2021

The background material 'Macroeconomic and financial market developments' is based on information available until 15 September 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

Table of contents

Table of contents 3
1. Macroeconomic developments 4
1.1. Global macroeconomic environment 4
1.2. Domestic real economy developments 7
1.2.1. Economic growth 7
1.2.2. Employment 9
1.3. Inflation and wages 11
1.3.1. Wage setting 11
1.3.2. Inflation developments 11
1.3.3. Inflation risks 12
1.4. Fiscal developments 14
1.5. External balance developments 15
2. Financial markets 16
2.1. International financial markets 16
2.2. Developments in domestic money market indicators 19
3. Trends in lending 21

1. Macroeconomic developments

1.1. Global macroeconomic environment

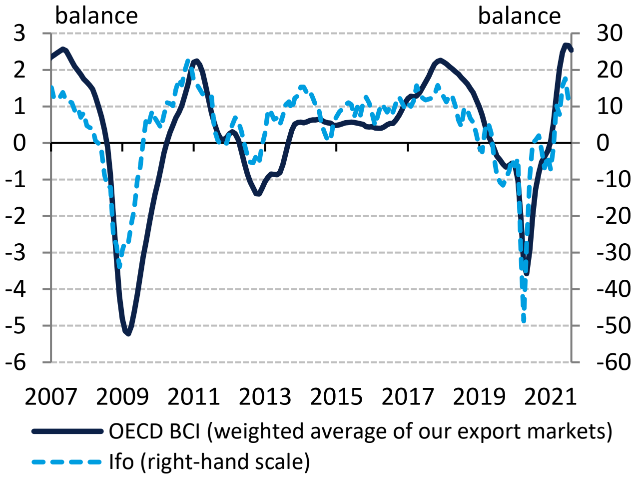
In the second quarter of 2021, the economic performance of China and the United States improved by 7.9 percent, 12.2 percent, respectively, while that of the euro area by 13.6 percent, year on year. Confidence indices related to the international manufacturing and service sectors slightly deteriorated in August. The pick-up in the number of coronavirus cases in recent weeks may suggest the onset of the fourth wave of the pandemic, which may interrupt economic recovery. In countries with higher vaccination coverage, the negative impact of the potential epidemic restrictions is likely to be more moderate. In the second quarter of 2021, external inflationary environment remained high. In August, euro area inflation rose to 3.0 percent.

Global industrial production exceeded its pre-pandemic level already in September 2020, and has continued to surpass it ever since then, while after the restart of the economies, outlook for the service sector also improved significantly. Industrial production increased despite the global semiconductor shortage. 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 90-95 thousand, which - however - is still well below the 2019 figures.

Economic recovery continued in the second quarter of 2021. 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). **In the second quarter, the economic performance in the United States exceeded the low base of 2020 by 12.2 percent, which did not match analysts' expectations.** Economic recovery in the world's two largest economies (China and the United States) is stronger than in the euro area. Performance of the United Kingdom and the European Union in the second 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. Economic performance of most countries is still below the pre-crisis level. The greatest lag within the European Union can be identified in Spain, Malta and the Czech Republic. GDP reached its pre-crisis level in Ireland, Estonia, Luxembourg, Lithuania and Romania already after the first quarter, and also in Poland, Denmark, Hungary, Finland and Latvia in the second quarter.

Due to last year's low base, monthly production indicators showed buoyant growth in June as well. Industrial production in the euro area, the United States, the United Kingdom and in China rose by 9.7 percent, 9.8 percent, 8.3 percent and 8.3 percent, respectively, compared to last June. In June, the volume of retail sales grew by 12.1 percent in China, 18.0 percent in the USA, 9.7 percent in the United Kingdom and by 5 percent in the euro area, on an annual basis. Compared to previous month the indices typically rose.

Chart 1 Business climate indices in Hungary's export markets



Source: OECD, Ifo

Monthly production indicators grew further in July. Industrial production in the euro area, the United States, the United Kingdom and in China rose by 7.7 percent, 6.6 percent, 3.8 percent and 6.4 percent, respectively, compared to last July. In July, the volume of retail sales grew by 8.5 percent in China, 15.8 percent in the USA, 2.4 percent in the United Kingdom and by 3.1 percent in the euro area, on an annual basis.

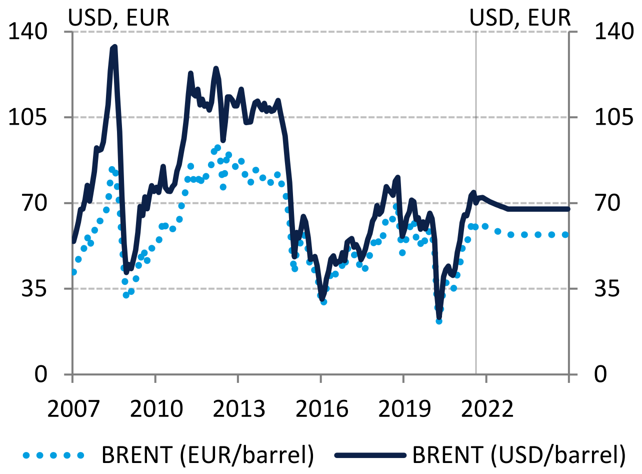
Forward-looking confidence indices related to the manufacturing and service sectors moderately deteriorated in August. Purchasing Manager Index of China declined close to the threshold value (50 points) in August. Business sentiment in the United States improved, while in the euro area it declined further during the month under review. German business sentiment (Ifo Business Climate Index) deteriorated in August, but despite of this it is at a multi-year high (Chart 1).

International labour market trends improved further. In the United States, the number of new unemployment benefit claims was 310,000 in the week ending on 4 September, which is a decrease compared to previous week, but it still substantially exceeded the 2019 average (200,000). The unemployment rate declined to 5.2 percent in August. In June, euro area unemployment rate declined by 0.3 percentage point, compared to the previous month and now is at 7.7 percent.

In annual terms, euro area inflation and core inflation rose to 3.0 percent and 1.6 percent, respectively in August. The data exceeded analysts' expectations. The market consensus for HICP and core inflation was 2.7 percent and 1.5 percent, respectively.

Exceeding analysts' expectations by 0.1 percent, CPI inflation in July stood at 5.4 percent in the United States. Then in August, the consumer price index declined slightly, to 5.3 percent. In Poland, the August consumer price index remained above the central bank's target, at 5.5 percent. In the Czech Republic inflation in August was 4.1 percent, significantly exceeding the 2 percent inflation target of the Czech central bank.

Chart 2 World market prices of Brent crude oil



Source: Bloomberg

The sharp rise in the number of cases in recent weeks may result in the onset of the fourth wave of coronavirus, which may interrupt the recovery of the economy. In countries with higher vaccination coverage the negative impact of the potential epidemic restrictions is likely to be more moderate.

In August 2021, the average world market price of Brent crude oil was USD 70 per barrel, while the spot price has stood close to USD 72 per barrel since early September (Chart 2). In the first three weeks of August, the price of Brent crude oil declined. This was mostly attributable to the resurgence of the pandemic, which significantly jeopardised US and Chinese oil demand. On the other hand, China made progress in containing the fast spreading delta variant, local cases were reduced to zero and financial markets sentiment was also more positive, leading to an increase in oil prices after 20 August. Since then prices rose further, and now stand at around USD 72/barrel. The price of industrial commodities significantly decreased with the world market price of unprocessed food remaining broadly unchanged in August.

1.2. Domestic real economy developments

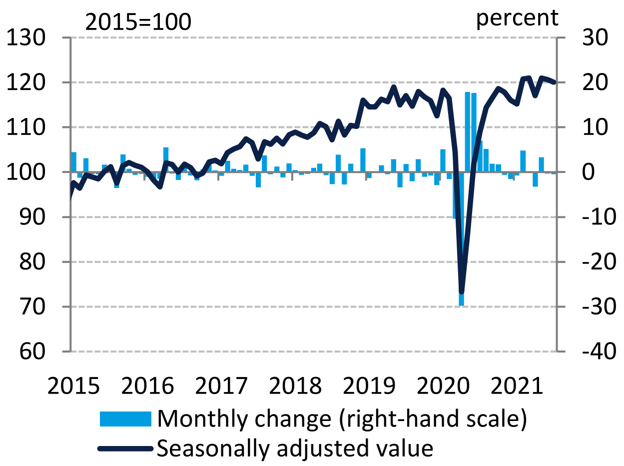
In the second quarter of 2021, Hungary's GDP rose by 17.9 percent year on year, while economic performance grew by 2.7 percent quarter on quarter. As a result, Hungary's GDP reached its pre-crisis level. Based on the GDP data on the second quarter of 2021, Hungary is at the forefront, among others, of the European ranking, both in year on year and in quarter-on-quarter terms. Real time data suggest a slowdown in GDP growth rate in the summer months, which is attributable to the higher bases of 2020 resulting from partial lifting of the restrictions. In July, industrial output was above its pre-crisis level. Construction output slightly exceeded its level seen before the coronavirus pandemic, but still fell short of the growth trend of recent years. The volume of retail sales remains below the level before the outbreak of coronavirus. The labour market proved to be resilient to the coronavirus pandemic. In July 2021, unemployment rate stood at 3.9 percent, while the number of people in employment rose by 94,000 year on year, reaching a historic high.

1.2.1. Economic growth

As a result of the fast reopening, the Hungarian economy grew further. In the second quarter of 2021, Hungary's GDP rose by 17.9 percent year on year, while economic performance grew by 2.7 percent quarter-on-quarter.

The increase in domestic economic output exceeded the average of the euro area (+13.6 percent) and the European Union (+13.2 percent) in annual terms. Based on the GDP data registered in the second quarter of 2021, Hungary is among the leaders in the European ranking, both in year-on- year and in quarter-on-quarter terms.

Chart 3 Development in industrial production



Source: MNB calculation based on HCSO data

In July 2021, industrial production rose by 8.0 percent (by 10.3 percent based on calendar-adjusted data) year on year. Based on the seasonally and calendar adjusted data, the volume of production decreased by 0.5 percent on a monthly basis (Chart 3). In July, industrial output was above its pre-crisis level, but below its pre-pandemic trend. Most of the manufacturing subsectors contributed to the annual growth in industrial production, while the performance of the automotive industry declined. Based on raw data, the output of automotive industry – representing the largest share in domestic output – declined by 6.7 percent, year on year. The manufacture of electrical equipment rose to the largest degree (by 57.9 percent), primarily due to the pickup in electric engine and battery production.

In July 2021, based on raw data, the volume of construction output rose by 22.5 percent year on year. The level of construction output slightly exceeded the level before the outbreak of the coronavirus pandemic, but it fell short of the growth trend seen in recent years. Compared to June 2021, the volume of output decreased by 0.4 percent based on seasonally and calendar adjusted data. Construction of buildings and other construction rose by 21.1 percent and by 25.4 percent, respectively, compared to the low base of July 2020. Based on seasonally adjusted data, the volume of new contracts concluded rose by 47.3 percent, while the construction companies' contract portfolio at the end of July exceeded the level registered in end-July 2020 by 19.1 percent.

According to real time data, GDP growth declined in the summer months as the base effects wore off. Based on the online cash register data, turnover in July and August grew in nominal terms by 6 and 11 percent, respectively, year-on year. Due to last year's low base air passenger traffic registered a double-digit growth in both July and August, albeit at the end of August it still fell short of the level of two years ago by 55 percent. Catering turnover in nominal terms already exceeded its level of 2019 in the same period since mid-June. Cinema attendance is recovering gradually after the reopening, with the decline in July still being around 20 percent compared to its level two years ago, which fell to 15 percent by August. Road passenger and goods traffic have been both improving strongly since mid-March, and in August they already exceeded the level registered two years ago. In August, the electricity load data were close to the level of last year.

Household borrowing developed favourably. In August, it was above its level one year and two years earlier by 47 percent and 5 percent, respectively. In July, the number of housing market transactions rose by 4 percent on average, year on year. **Labour market adjustment was modest in Hungary.** In July 2021, the unemployment rate stood at 3.9 percent, while the number of people in employment rose by 94,000 persons, year on year. Google searches related to unemployment also show a favourable picture. Online searches in Hungary for the term “unemployment benefit” and "jobseeker's allowance” are close to the levels before the outbreak of the pandemic.

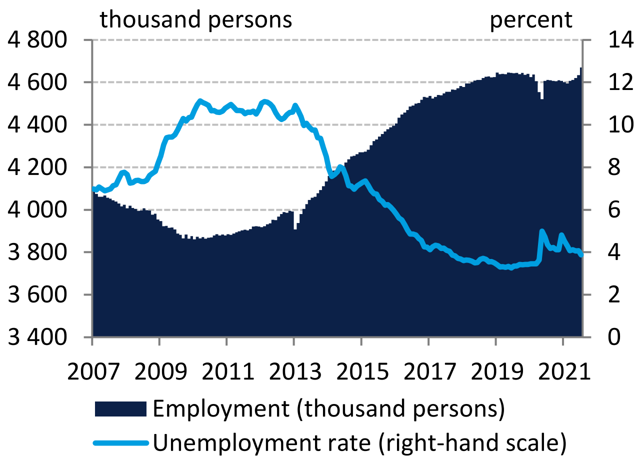
According to the HCSO's preliminary data release, in July **goods exports and imports rose by 10.0 percent and 14.7 percent, respectively, in euro terms,** year on year. In July 2021, the merchandise trade balance showed a deficit of EUR 193 million.

In July 2021, the volume of retail sales was up by 2.5 percent based on raw data and by 3.0 percent based on data adjusted for the calendar effect, year on year. The volume of retail sales still lagged behind the level seen before the outbreak of the coronavirus and was below the growth trend of recent years. Compared to previous month the volume of sales fell slightly (-0.3 percent). The volume of sales rose in most shop types in July. Based on the data adjusted for the calendar effect, the volume of retail sales in food stores and groceries rose by 3.7 percent, that in non-food stores by 2.6 percent, while the volume of fuel retail sales increased by 1.9 percent year on year.

In July 2021, the number of tourist overnight stays at commercial accommodations was less than half of the pre-pandemic level, while it rose by almost 10 percent compared to last July. Domestic tourist overnight stays rose from 2,118,000 of last July to 2,290,000, while compared to July 2019 they fell by 11 percent. 59 percent of the domestic tourist overnight stays were in hotels, representing a year on year growth of almost 8 percent. According to the HCSO's data release, the number of overnight stays by foreign tourists in Hungary was 571,000, while a year ago it was merely 492,000. The number of overnight stays by foreign tourists declined by 70 percent compared to July 2019. 64 percent of foreign tourists stayed in hotels, with the number of overnight stays in hotels increasing by 32 percent compared to July 2020.

1.2.2. Employment

Chart 4 Number of persons employed and the unemployment rate



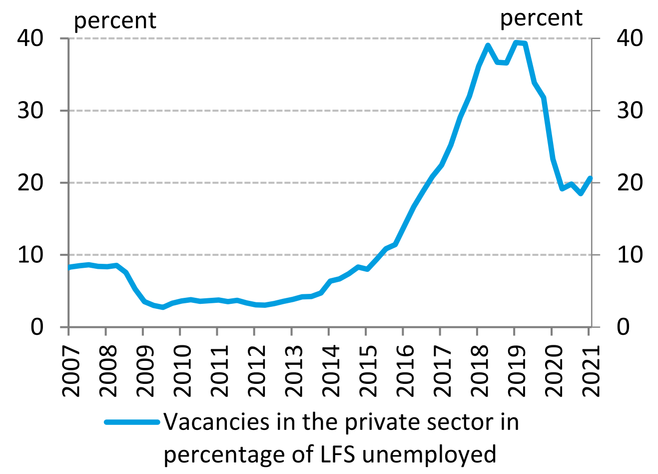
Source: HCSO

Based on the data of the Labour Force Survey (LFS), in June 2021 the total number of the employed amounted to 4,692,000 reflecting an increase of 98,000 persons year on year (Chart 4). Since June 2021, the number of employees in the primary labour market and the number of public employees rose by 103,000 and 4,000 persons, respectively, while the number of those working abroad declined by 10,000 persons.

In July, the number of the unemployed was 189,000, falling short of the year-on-year figure by 29,000 persons, and as a result, the seasonally adjusted unemployment rate overall stood at 3.9 percent. The number of the unemployed decreased by 6,000 persons in July. Based on the data published by the National Employment Service (Nemzeti Foglalkoztatási Szolgálat - NFSZ) in July and August the number of registered jobseekers in Hungary was 262,000 (-104,000 on an annual basis) and 256,000 (-89,000 on an annual basis), respectively.

Labour demand rose substantially in both manufacturing and market services, on an annual basis. In the second quarter of 2021, private sector vacancies amounted to 51,700, exceeding the year on year value by 38.5 percent and falling short of the pre-pandemic figure by merely 3 percent. Manufacturing job vacancies exceeded the figure a year ago by 4,200. In the market services sector, real estate, professional and administrative activities job vacancies increased by almost 6,000 and in the information and communication sectors by 1,500. In the rest of the sectors the rise was negligible in annual terms.

Chart 5 Development of labour market tightness indicator



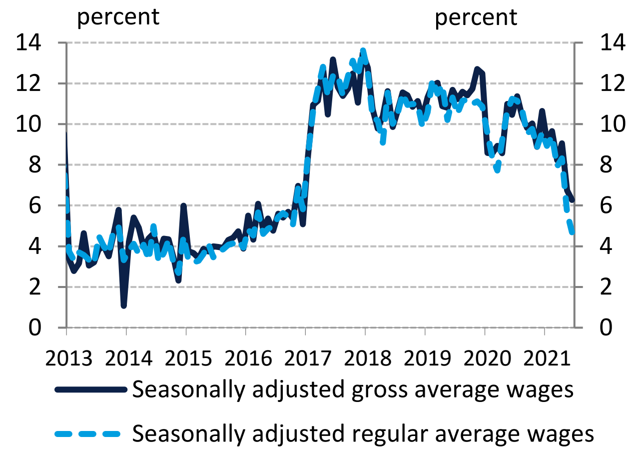
Note: Quarterly data.
Source: National Employment Service, HCSO

Within the public sector job vacancies decreased in healthcare and increased in education. Overall, the labour market tightness indicator calculated from the ratio of job vacancies and unemployed persons, **rose significantly compared to the previous quarter**, but it still falls short of the values registered in the previous two years (Chart 5).

1.3. Inflation and wages

In August 2021, inflation calculated on a year on year basis was 4.9 percent, while both core inflation and core inflation excluding indirect tax effects stood at 3.6 percent. Underlying inflation indicators capturing persistent trends (price index of demand sensitive and inflation of sticky price products and services) increased slightly compared to the previous month. In June 2021, gross average wages rose by 3.5 percent year on year. The more moderate annual growth rate in the whole-economy average wages is attributable to the base effect.

Chart 6 Dynamics of average earnings in the private sector



Source: MNB calculation based on HCSO data

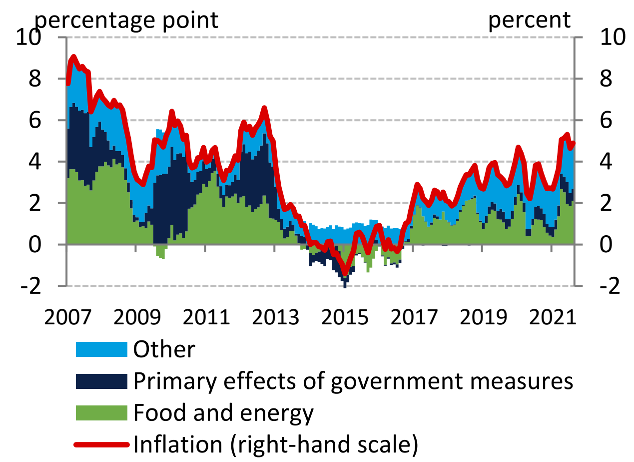
1.3.1. Wage setting

In June 2021, gross average earnings in the private sector rose by 6.4 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 increased and its direction flipped compared to the first quarter. Regular average wages slightly increased compared to May, while the degree of bonus payments exceeded the level of previous years.

According to seasonally adjusted data, the growth in gross average wage and regular average wage slowed down in the private sector compared to the previous month (Chart 6)**.** In the private sector wage dynamics of manufacturing outstripped that of market services. In June, manufacturing wages were higher by 8.7 percent year on year. Wages in the automotive industry - representing the largest share - increased by 11.9 percent in annual terms. In market services, HCSO registered a growth of 3.7 percent. Wages in construction and trade rose by 11.8 percent, 6.6 percent, respectively, while in catering fell by 1.9 percent, year on year.

1.3.2. Inflation developments

Chart 7 Decomposition of inflation

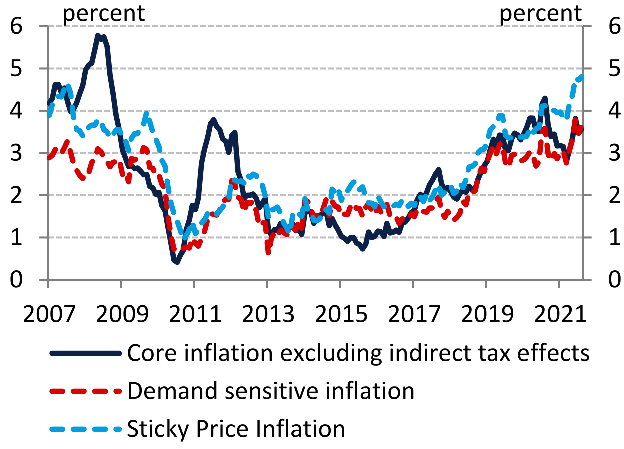


Source: MNB calculation based on HCSO data

In August 2021, inflation calculated in annual terms was 4.9 percent, while core inflation and core inflation excluding indirect tax effects stood at 3.6 percent (Chart 7)**.** Compared to the previous month, inflation increased by 0.3 percentage point and core inflation by 0.1 percentage point. Higher inflation was caused by the rise in the inflation of fuels, industrial goods and unprocessed food.

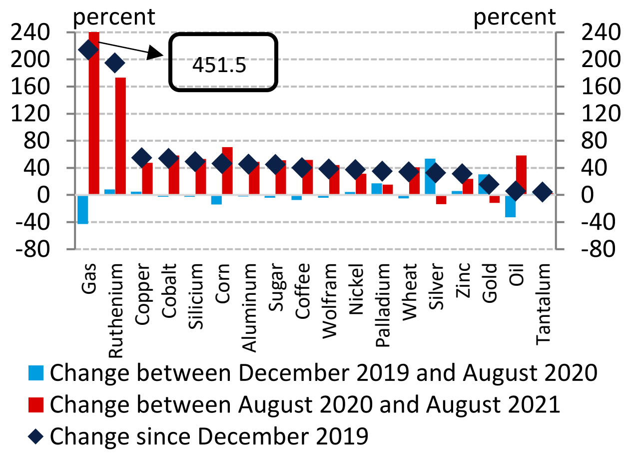
Overall, underlying inflation indicators capturing persistent trends (inflation of demand sensitive and sticky price products and services) **increased slightly compared to the previous month** (Chart 8). In July 2021, agricultural producer prices increased by 21.3 percent in annual terms, while domestic sales prices in sectors of consumer goods increased by 5.1 percent.

Chart 8 Measures of underlying inflation indicators



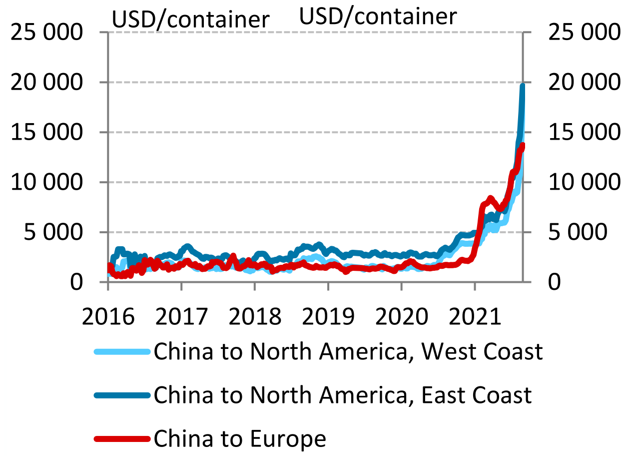
Source: MNB calculation based on HCSO data

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

1.3.3. Inflation risks

Inflation declines more slowly than previously expected. The indicator peaked at 5.3 percent in June and stood at 4.9 percent in August.

The growth in inflation 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, along with deglobalisation and shortening value chains, all point to rising inflation 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).

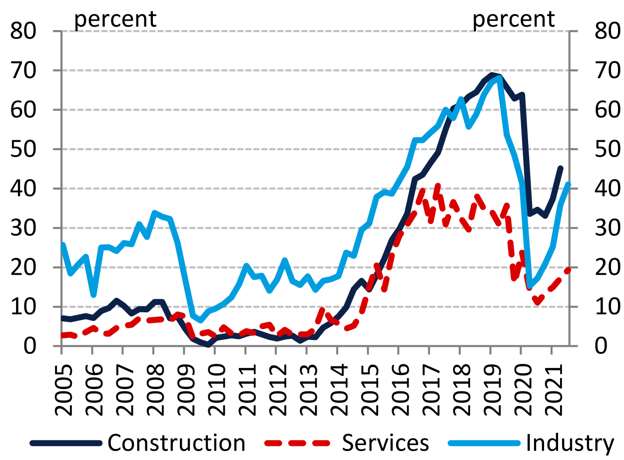
Global value chains may recover more slowly than demand, leading to increased cost pressures in global transportation and industrial production. In early September 2021, the costs of shipments from China to Europe rose more than 8.5 times the level seen in June 2020 (Chart 10)**.** Merchants are likely to charge part of the resulting extra costs to the consumers, thus the price increasing effect of the significantly higher shipping costs may appear also in the domestic consumer prices over time. 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, due to the reopening of the economy and the low base of last year, Hungarian GDP grew by 17.9 percent. As regards employment, bottlenecks may be in place, especially in the services and construction sectors, in parallel with the recovery (Chart 11).

Wage growth was stronger than expected, which may persist as the labour market tightens in certain sectors, with a 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 anticipated economic impacts of the fourth wave represent material downside risk. The economic impact of a new wave of the pandemic can be

Chart 11 Labour shortage as a factor limiting production in Hungary



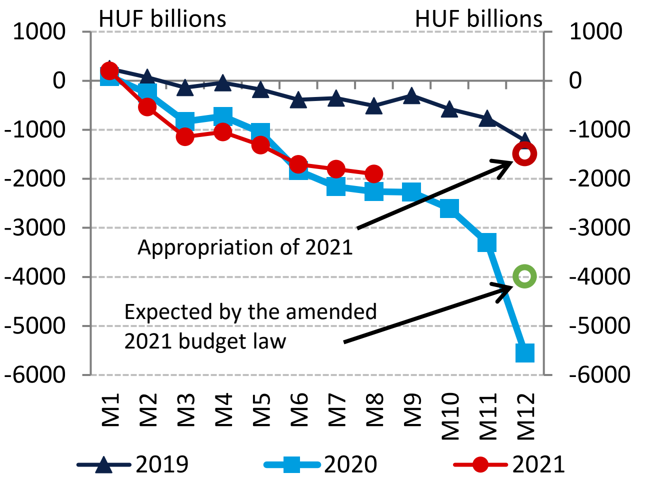
Note: Percentage of companies reporting that "Shortage of labour force" is a main factor currently limiting their production.
Source: European Commission

quantified with a high degree of uncertainty, as an unforeseen turn in the virulence of existing and new variants may occur at any time. In addition to the severity of the restrictions, the economic impact will also be influenced by the caution of the population.

1.4. Fiscal developments

In August 2021, the deficit of the general government's central sub-sector amounted to HUF 97 billion, and as a result, the accumulated cash deficit in 2021 rose to HUF 1,901 billion, which falls short of the cumulated deficit of August 2020 by roughly HUF 360 billion.

Chart 12 Intra-year cumulative cash balance of the central government budget



Source: Budget Act of 2021, Hungarian State Treasury

In August 2021, the deficit of the central sub-sector of the general government amounted to HUF 97 billion, and thus the current year accumulated cash deficit rose to HUF 1,901 billion, which falls short of the cumulated deficit of August 2020 by roughly HUF 360 billion (Chart 12).

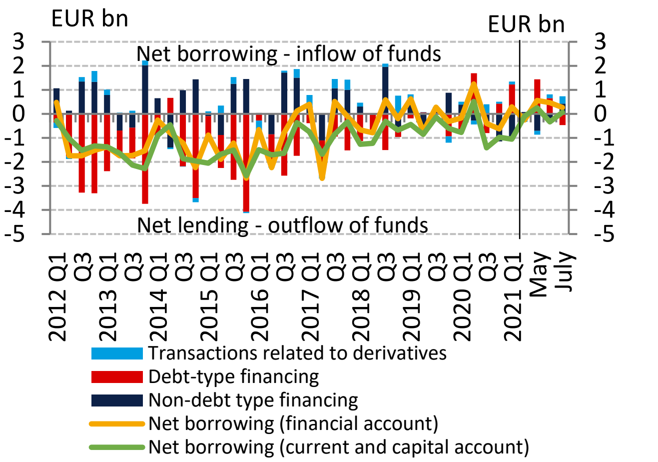
In August, **revenues of the central sub-sector** exceeded the year on year revenues by 7 percent, i.e. by roughly HUF 111 billion, which was primarily attributable to the rise in tax and contribution revenues. Within tax revenues, corporate income tax and labour tax revenues increased by HUF 11 billion and HUF 75 billion, respectively, year on year.

The volume of the **central sub-sector's expenditures in July 2021** exceeded that of August last year also by 7 percent. The growth in expenditures related to state property and interest expenses contributed to the increase. Support for local governments, the level of medical and preventive care as well as of pensions and pension-type benefits also substantially increased year on year.

1.5. External balance developments

In July, the current account showed a deficit of EUR 267 million and net borrowing was EUR 66 million. The deficit is attributable to the declining balance of trade. In terms of trends on the financing side, under a substantial rise in foreign direct investments the economy's debt liabilities declined.

Chart 13 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 July, the current account balance showed a deficit of EUR 267 million. The decline in the indicator was linked to the decreasing goods balance, connected to the growth in imports outstripping exports. Decelerating exports were mainly connected to the moderate performance of the automotive industry. The continued rise in the services balance surplus is mostly attributable to the recovery of tourism. The transfer balance surplus increased compared to previous month, while the income balance deficit remained broadly unchanged.

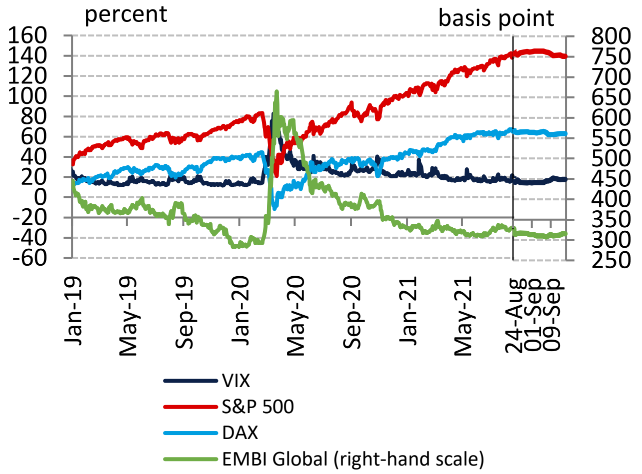
Based on the financial accounts the rise in net foreign direct investments related to the growth in outward investments, while debt liabilities of the economy decreased (Chart 13). Changes in net external debt at the end of the quarter were substantially influenced by the realignment following the foreign currency liquidity provided by the central bank to banks, which reduced the net external debt of the consolidated government and increased that of banks.

2. Financial markets

2.1. International financial markets

Since the last interest rate decision, financial market sentiment has remained broadly unchanged. The VIX index, measuring equity market volatility, rose to 19.5 percent, while the EMBI global spread in the emerging bond market and the MOVE index, measuring developed bond market volatility, decreased. Last month, stock exchange indices declined in the developed markets and rose in the emerging markets. The dollar exchange rate has varied against the developed currencies and it depreciated by roughly 0.3 percent against the euro. The growth in oil prices was attributable to the concerns related to the global oil demand and to the moderate decline in risks surrounding the spread of the delta variant. On the supply side, the interruption caused by the hurricane hitting the US extraction areas explained the rise in prices.

Chart 14 Developed market equity indices, the VIX index (left-hand scale) and the EMBI Global Index (right-hand scale)



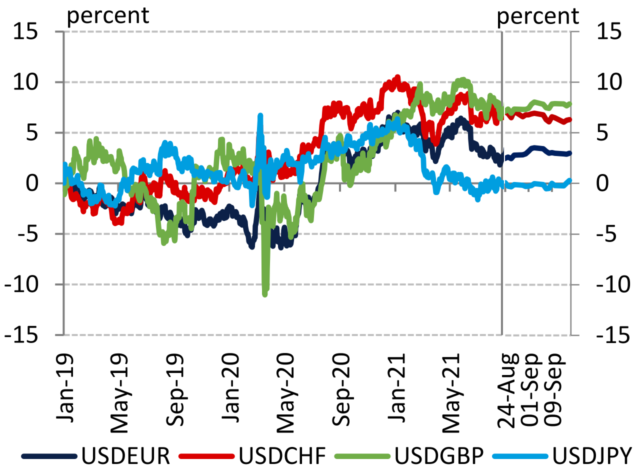
Source: Bloomberg

In the period since the last interest rate decision financial market sentiment remained broadly unchanged. Market participants continue to pay special attention to the spread of the coronavirus' delta variant and the related tightening measures, as well as to the incoming inflation data and the messages of major central banks. Incoming macroeconomic data reflected moderate deterioration in the period under review, but the post-crisis recovery still appears to be positive.

Of the risk indicators, the VIX index, the key measure of equity market volatility, increased compared to the level registered at the previous interest rate decision by 2.2 percentage point to 19.5 percent. Furthermore, analysts warn that the indicator measuring the expected volatility of the VIX index is also at a high level, which may imply rising risks in the coming period. At the same time, the EMBI Global spread in the emerging bond market fell by 3 basis points to 315 basis points, while the MOVE index, measuring developed bond market volatility, stands at 51 basis points after a fall of 12 basis points (Chart 14).

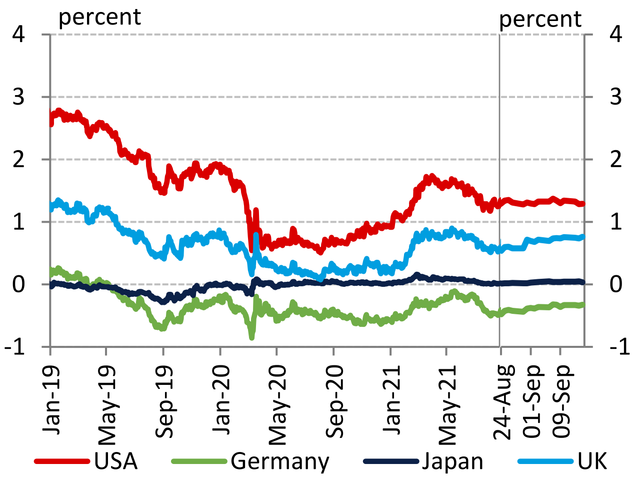
The spread of the delta variant has started to decline globally, while it just started to pick up in the United States and several European countries. Recently, increasing numbers of cases have been observed in the Asian region, but restrictive measures have successfully contained the spread of the pandemic. In Japan, the state of emergency has been extended until the end of September, but the number of new cases has already started to decline slowly there as well. In Europe and the USA, however, the virus is now on the rise and the number of cases is increasing substantially. Governments are therefore taking measures to make vaccination programmes more effective and other restrictions are being introduced. Meanwhile, in Colombia and Ecuador, the incidence of the artificial

Chart 15 Developed market FX exchange rates



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

Chart 16 Yields on developed market long-term bonds



Source: Bloomberg

variant of the coronavirus is increasing. The good news is that while South America has a significant prevalence of the variant, international studies show that the global occurrence of the artificial virus strain has declined, with those infected by this variant accounting for less than 0.1 percent of all cases recorded globally. In parallel with this, a new variant of the virus, currently known as C.1.2, has been detected by researchers in South Africa, which is mutating much faster than previously known variants.

Last month, of the leading US stock indices, S&P 500 and Dow Jones fell by 0.8 and 2.9 percent, respectively. The leading European stock indices declined to a similar degree: the German stock exchange was down by 1.3 percent, the British by 1.7 percent and the French one 2.7 by percent. On the other hand, the Japanese and Chinese stock exchange indices rose by 10.9 and 4 percent, respectively. On the whole, the developed and emerging MSCI composite indices declined by 0.2 and rose by 1.9 percent, respectively. Stock market indices in the countries of the region also increased. Compared to the last interest rate decision, the Hungarian, Polish and Romanian index rose by 4.6 percent, 4.7 percent and 1.9 percent, respectively.

The dollar has varied against the developed currencies. While the US currency depreciated against the euro by 0.3 percent, it appreciated against the Swiss franc and the British pound by 0.8 and 0.2 percent, respectively (Chart 15)**.** At the end of the period, the euro-dollar exchange rate came close to 1.18. The exchange rate of the currencies of the region against the dollar strengthened; the forint, koruna and zloty appreciated by 0.8, 0.5 and 0.4 percent, respectively. Since the last interest rate decision the price of gold rose by 0.7 percent, to around USD 1,800/oz.

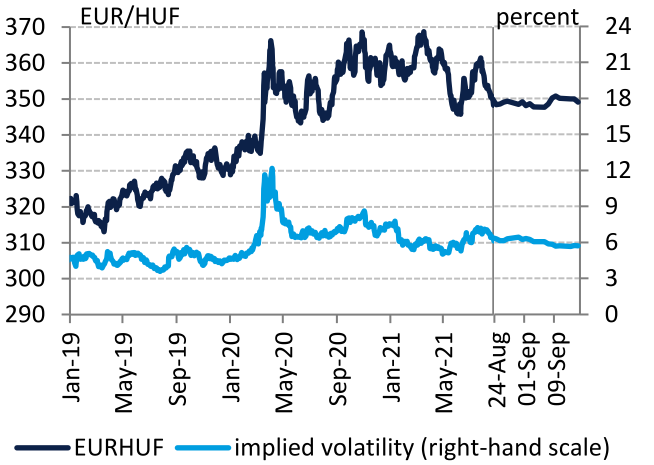
On the whole, the developed bond yields increased since the last interest rate decision (Chart 16)**.** The 10-year German yield rose by 14 basis points, while each of the Japanese and the US one were up by 2 basis points and thus the German, US and Japanese yield closed the period at -0.33, 1.29 and 0.03 percent, respectively. Yields in the Mediterranean countries also rose by 10-20 basis points. The yields in the countries of the region followed a similar trend: the Hungarian and Polish long-term yields rose by 25 basis points each, while the Czech and Romanian one by 9 and 30 basis points, respectively.

Oil prices rose in the previous period. The growth in oil prices was attributable to the concerns related to the global oil demand and to the moderate decline in risks connected to the spread of the delta variant. On the supply side, the interruption caused by the hurricane hitting the US extraction areas explained the rise in prices. Since the interest rate decision in August, the price of Brent crude oil increased by 6.9 percent to USD 74.3, and the US benchmark WTI oil price by 5.7 percent to USD 71.1.

2.2. Developments in domestic money market indicators

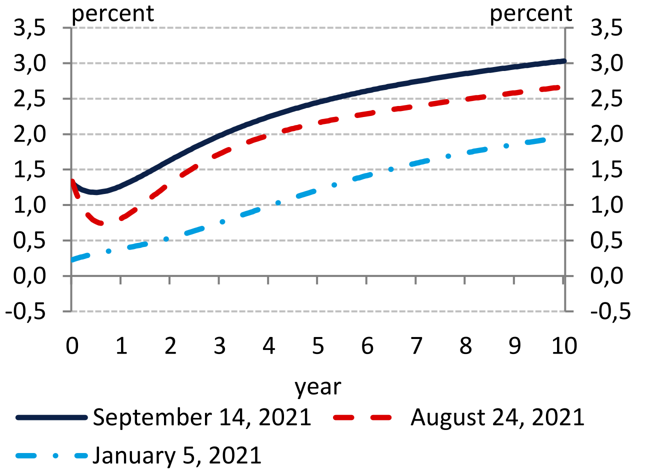
The forint exchange rate against the euro has remained broadly unchanged since the August interest rate decision. The government securities market and the interbank yield curve shifted significantly upward. The 3-month BUBOR rose by 16 basis points to 1.6 percent. Last month the government bond auctions were first characterised by moderate and then by strong demand, while average auction yields rose on the whole.

Chart 17 EUR/HUF exchange rate and the implied volatility of exchange rate expectations



Source: Bloomberg

Chart 18 Shifts in the spot government yield curve



Source: MNB, Reuters

The forint exchange rate against the euro has remained broadly unchanged since the August interest rate decision. In the first half of the period the steadiness of forint was in line with the regional trends, while in the middle of the period there was a country-specific depreciation. Including the adjustment last week, the forint depreciated against the euro by 0.3 percent in total, which falls short of the depreciation of the Romanian leu, while the Czech koruna and the Polish zloty appreciated during the period. The implied volatility of forint essentially remained unchanged last month (Chart 17).

The 3-month BUBOR, relevant for monetary policy transmission, rose by 16 basis points to 1.6 percent since the last interest rate decision.

The government securities yield curve shifted upward (Chart 18)**.** Around the 1-year section of the yield curve a rise of roughly 30 basis points, while at the middle section and around the 10-year section a rise of 25 and 36 basis points, respectively, was registered.

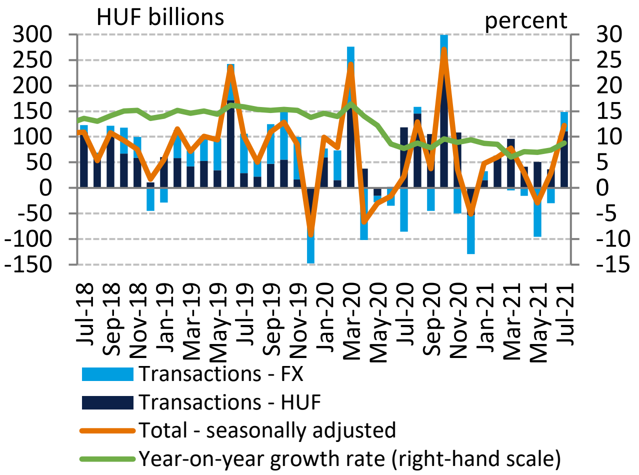
In the past month, demand at government bond auctions was first moderate and then strong. At the 3-month discount Treasury bill auctions the Government Debt Management Agency accepted bids over the announced volume on one occasion and the announced volume on two occasions, while in the case of the 12-month Treasury bill auctions it accepted bids below the announced volume. Since the last interest rate decision, the average yield at the 3-month auctions rose from 0.65 percent to 1.1 percent, while the average auction yield at the 12-month Treasury bill auctions increased to 1.57 percent. Bond auctions were first characterised by moderate and then by strong demand. Thus at the end of August, the Government Debt Management Agency accepted bids below and in athe first half of September over the announced volume. At the latest auction, the average yield of the 10-year securities was 3.07 percent, representing an increase of 23 basis points compared to average auction yield before the interest rate decision in August. The average auction yield on 5-year government securities rose by 44 basis points to 2.53 percent, while at the 20-year government securities it increased by 26 basis points to 3.56 percent. After a minor rise followed by a correction, the Hungarian 5-year CDS still stands at 50 basis points.

Non-residents' holdings of forint government securities decreased marginally. Non-residents' holdings in forint government securities decreased by HUF 3 billion to HUF 4,713 billion. However, the market share of forint government securities held by non-residents rose from 20.6 percent to 20.7 percent.

3. Trends in lending

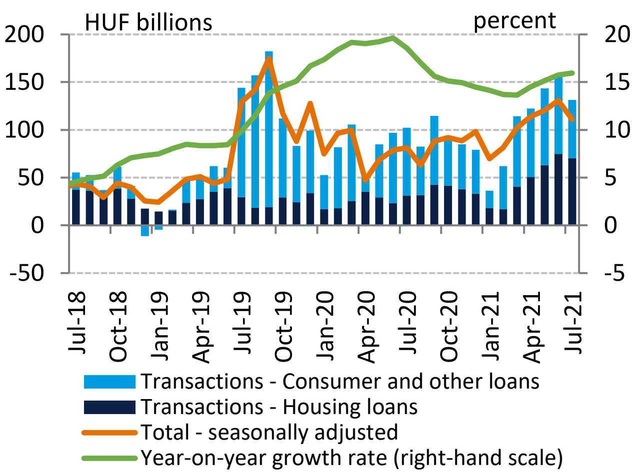
In July 2021, outstanding borrowing of non-financial corporations grew by HUF 148 billion, as a combined result of the increase in outstanding forint borrowing by HUF 111 billion and in foreign currency loans by HUF 37 billion. In July, outstanding borrowing of households grew by HUF 132 billion due to transactions, with the annual growth rate rising to 15.9 percent.

Chart 19 Net borrowing by non-financial corporations



Source: MNB

Chart 20 Net borrowing by households



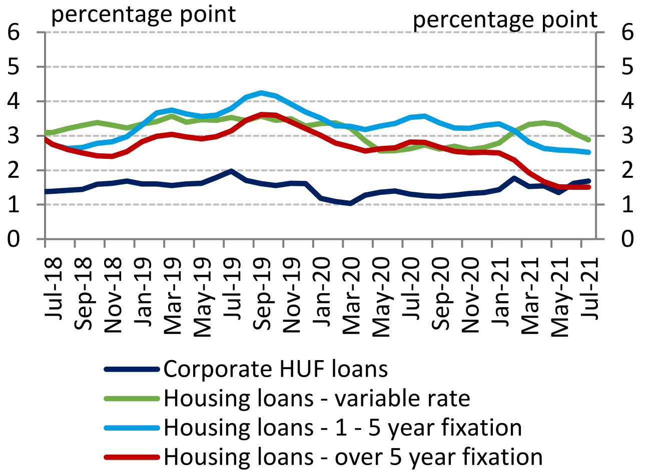
Source: MNB

In July 2021, outstanding borrowing of non-financial corporations grew by HUF 148 billion, as a combined result of the increase in outstanding forint borrowing by HUF 111 billion and in foreign currency loans by HUF 37 billion (Chart 19)**.** Due to the significant monthly growth, the annual growth rate rose to 8.8 percent from 7.4 percent registered in previous month. In July, credit institutions disbursed new loans in the amount of HUF 224 billion, which falls short of the year on year figure – the period already affected by the coronavirus and the subsidised loan schemes – by 27 percent, while it exceeds the value registered two years ago by 2 percent. Within the monthly disbursements – returning to the trends of the pre-pandemic period – the disbursements of market-based loans account for a major part, almost 80 percent, of new loans. During the month under review, banks concluded non-overdraft forint contracts with enterprises under FGS Go! in the amount of almost HUF 13 billion.

In July, outstanding borrowing of households grew by HUF 132 billion due to transactions, with the annual growth rate rising to 15.9 percent (Chart 20). According to our estimate, the annual dynamics would be 8 percent, when also considering the missed instalments due to the moratorium. Disbursement of new household loans during the month amounted to HUF 257 billion, exceeding the year on year figure by 34 percent. On the other hand, it falls short of the disbursements two years ago – a period not yet affected by the pandemic – by 2 percent, attributable to the high base resulting from the soar in prenatal baby support loans after launching the scheme in July 2019. The new measures aimed at first-time homebuyers, available from 2021, were key to the disbursement of housing loans in the amount of HUF 132 billion. Of the home improvement loans introduced at the beginning of the year for the pre-financing of the home improvement subsidy, banks disbursed interest-subsidised housing loans in July in the amount of HUF 6 billion, thereby reaching a cumulated contracted volume of HUF 30 billion. 28 percent of the housing loans disbursed during the month were connected to the Home Purchase Subsidy for Families.

The smoothed interest rate spread of forint-denominated corporate loans was 1.69 percentage point in July 2021, representing an increase of 0.06 percentage point

Chart 21 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

compared to the previous month (Chart 21)**.** The average smoothed interest rate spread on variable rate housing loans calculated on the basis of the annual percentage rate (APR) decreased during the month and amounted to 2.88 percentage points. The spread on products with interest rate fixation periods longer than 1 year, up to 5 years and more than 5 years changed only marginally during the month. After a decline of 0.04 percentage point, the average spread on housing loans with interest rate fixation periods longer than one year and up to 5 years reached 2.52 percentage points in July, while the spread on products with interest rate fixation periods of more than 5 years, similar to last month, was 1.51 percentage points.