MINUTES
OF THE MONETARY COUNCIL MEETING
27 APRIL 2021

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Article 3 (1) of the MNB Act (Act CXXXIX of 2013 on the Magyar Nemzeti Bank) defines achieving and maintaining price stability as the primary objective of the Magyar Nemzeti Bank. The MNB's supreme decision-making body is the Monetary Council. The Council convenes as required by circumstances, but at least twice a month, according to a pre-announced schedule. At the second scheduled meeting each month, members consider issues relevant to decisions on interest rates. Abridged minutes of the Council's rate-setting meetings are released regularly, before the next policy meeting takes place. The minutes present the decision-makers' assessment of current economic conditions and the factors they consider when deciding on the base rate. Until December 2013, the Monetary Council presented the information underlying its assessments as part of the abridged minutes. In order to provide more detailed information, background materials will henceforth appear as a separate publication with enhanced content under the title 'Macroeconomic and financial market developments', at the same time as the abridged minutes.

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

THE COUNCIL'S ASSESSMENT AND INTEREST RATE DECISION

The primary objective of the Magyar Nemzeti Bank (MNB) was to achieve and maintain price stability. Without prejudice to its primary objective, the Magyar Nemzeti Bank preserved financial stability and supports the Government's economic policy.

Global macroeconomic and financial market developments continued to be primarily driven by the events related to the coronavirus pandemic. The timing of the reopening largely depended on the course of the third wave of the pandemic and the population's vaccination coverage rate. However, vaccination had progressed more slowly than expected in most countries, and consequently there remained an exceptionally high degree of uncertainty surrounding the pace of global economic recovery.

World trade and global industrial production were already above the levels seen in January 2020. In the first quarter of 2021, the outlook for growth in the United States had improved and Chinese economic growth had continued. The euro area's economic performance had declined in the first quarter, and therefore the recovery would take longer than previously expected.

In the past month, risk appetite had been driven by developments related to the coronavirus pandemic and global reflation concerns. After a significant increase at the beginning of the year, there had been a slight reversal in developed market yields. Since the beginning of 2021, commodity prices had risen significantly, and global oil prices had remained around USD 65.

The European Central Bank had continued its asset purchase programmes, and decision-makers had indicated that more purchases would be made under the Pandemic Emergency Purchase Programme (PEPP) in the second quarter of 2021. In the CEE region, the Czech and the Polish central bank had left policy rates unchanged since the Council's previous interest rate decision. As a result of the protracted economic recovery, loose monetary conditions were expected to be maintained by the world's leading and regional central banks over the longer term; however, decision-makers disagreed as to the time frame over which emergency asset purchase programmes should operate.

The Hungarian economy had proved to be crisis-resilient to the second wave of the pandemic. The effects of strict lockdowns due to the third wave were expected to be less severe on the real economy than those of the first wave. With the restrictive measures remaining in effect and the interruptions in production chains, the third wave of the coronavirus pandemic was expected to cause a decline in GDP in the first quarter of 2021. In February, construction output had declined; however, industrial production had already exceeded the level before the crisis, and it had moved closer to the trend seen before the pandemic. Although the volume of retail sales had declined, households' confidence indicators and the real net wage bill, which was important in terms of consumption expenditure, had grown further at the beginning of the year. The vaccination coverage rate of Hungary's population was at the top in the European Union; therefore, restrictive measures had started to be lifted gradually. In parallel, the recovery in the services sector's performance might also begin.

In terms of demand and supply, the Hungarian economy exhibited the potential for a rapid recovery. Throughout 2020, the business investment rate had stood at a high level, at 27.3 percent, while the unemployment rate had remained low compared to international levels. Credit markets had continued to expand strongly even in international comparison. The recovery in demand had been driven by an increase in household income, a pick-up in government and private investment and the accelerating withdrawal of EU funds.

GDP was expected to grow by between 4.0 and 6.0 percent in 2021, by between 5.0 and 6.0 percent in 2022 and by 3.5 percent in 2023. Domestic demand might pick up as progress was made in vaccination and in the opening of the economy. Continued growth in investment was key to the economic recovery. The financing environment remained supportive, in which the Bank's FGS Go! and the Bond Funding for Growth Scheme played a key role. In addition to the current, ongoing capacity improvements, growth in corporate investment was supported by new development projects financed by foreign direct investments. Household investment, in turn, had been stimulated by the Government's housing allowance programmes. In the coming years, Hungary's economic performance was likely to improve to a greater extent than the European Union's average, and therefore real economic convergence was expected to continue.

In March 2021, annual inflation had been 3.7 percent, core inflation had been 3.9 percent and core inflation excluding indirect tax effects had stood at 3.1 percent. Inflation had risen by 0.6 percentage points and core inflation excluding indirect tax effects had fallen by 0.3 percentage points relative to the previous month. The rise in inflation had primarily reflected an increase in fuel prices, which had accounted for 0.8 percentage points of the pick-up in inflation in March.

Inflation was likely to be highly volatile in the coming months. In analysing longer-term trends, the MNB placed great emphasis on the assessment of underlying indicators, especially core inflation excluding indirect tax effects. In the coming months, spikes in inflation would occur due to base effects, rising fuel prices, a further increase in excise duties and demand-supply frictions as the economy restarted. The consumer price index would approach 5 percent in the second quarter. Rising fuel prices and tax changes accounted for about half of this level. Inflation was likely to return to the central bank tolerance band from the summer months as temporary effects faded. In 2021, annual average inflation was expected to be in the range of 3.8–3.9 percent and core inflation excluding indirect tax effects would be around the 3 percent level.

Spikes in inflation were mainly caused by supply-side and cost factors. With inflation expectations anchored, we did not expect second-round effects according to our baseline scenario. Fading temporary effects, unused capacity in the economy and the moderate external inflation environment were expected to contribute to a decline in domestic prices from the first quarter of 2022. As a result, inflation was expected to stabilise around the central bank target again. The MNB laid special emphasis on developments in inflation expectations following the restart of the economy, and on the neutralisation of potential second-round effects.

The three large credit-rating agencies had confirmed that Hungary had a relatively strong economic performance and recovery potential, as well as a solid debt repayment ability. According to the

April EDP notification, the accrual-based government deficit had been 8.1 percent of GDP in 2020 due to the coronavirus pandemic, but it might decline again from this year. After falling steadily since 2011, gross government debt had increased temporarily to over 80 percent of GDP in 2020; however, it was likely to shift to a downward path from this year as economic growth was restored and the deficit declined. Debt financing had been stable, strongly supported by domestic savings. The MNB had raised Hungary's gold reserves from 31.5 tons to 94.5 tons, thereby strengthening confidence further in the country.

Outstripping expectations, the current account had been in a surplus in 2020. The country's current account balance was expected to improve further in the coming years, driven by the recovery in external demand and the gradual increase in the output of new capacities. With the capital account strongly in surplus, Hungary's net lending was expected to improve significantly and Hungary's net external debt to continue to fall further.

In response to the adverse economic effects arising from the coronavirus pandemic, the MNB had expanded significantly the central bank balance sheet in 2020. The Monetary Council continued to be ready to manage risks arising from the coronavirus pandemic and to foster the quick and sustainable recovery of economic growth in a targeted way.

At its meeting today, the Monetary Council performed the revision of its government securities purchase programme. In the Monetary Council's assessment, even during the third wave of the pandemic and in a volatile international financial market environment, the programme had been successful. The purchases by the Bank had contributed to maintaining a stable liquidity position in the government securities market and improved the effectiveness of monetary policy transmission. The MNB would continue to use its government securities purchase programme by maintaining a lasting presence in the market, taking a flexible approach to changing the structure of weekly securities purchases, to the extent and for the time necessary. The Council would still not set a total amount for its government securities purchase programme. In addition to continuously monitoring the implementation of the asset purchase programme, the Monetary Council would perform the next revision when stocks reached HUF 3,000 billion.

The FGS Go! and the Bond Funding for Growth Scheme remained key in the process of economic recovery. The MNB would continue to sterilise the resulting surplus liquidity issued under the programmes in full, using the preferential deposit instrument.

Following the review of macroeconomic and financial market developments, the Monetary Council discussed the details of its monetary policy decision. In assessing domestic macroeconomic developments, decision-makers pointed out that Hungary's industrial production had picked up significantly in the past months and it was already above the levels seen before the crisis. Although there was a slight downturn in construction and retail trade at the beginning of 2021, in the Council members' opinion, the effects of the third wave of coronavirus on the real economy were overall substantially less severe than those of the first wave. The Monetary Council noted that with the rapidly increasing vaccination coverage in Hungary, the gradual reopening enhanced the economy's recovery potential. In the decision-makers' assessment, the early opening before the European average would support a dynamic recovery from the summer months.

Moving on to discuss inflation developments, Council members agreed that inflation was primarily shaped by temporary effects. Several members pointed out that changes in fuel prices had raised the consumer price index by 0.8 percentage points in March. According to the decision-makers' expectations, this effect might be more pronounced in April and May, which would reflect last year's base effects in addition to the rise in oil prices at the beginning of 2021. Council members reiterated that, following the temporary spikes in inflation in line with the baseline scenario in the March Inflation Report, the consumer price index was expected to return to the central bank tolerance band in the summer months before stabilising close to the inflation target from the first quarter of 2022.

Decision-makers agreed that upside risks to price stability persisted. In members' assessment, the increase in risk aversion vis-à-vis emerging markets and potential second-round effects following the restart of the economy posed the greatest risk in terms of inflation developments. Some members also noted that a general pick-up in the global economy and the significant rise in commodity prices in 2021 might result in further spikes in inflation. Taking account of these effects, decision-makers reiterated that great emphasis would be laid on developments in inflation expectations and on the neutralisation of potential second-round effects.

At its policy meeting in April, the Monetary Council revised the MNB's government securities purchase programme. Several Council members noted that in the third and fourth quarter of 2020, the international financial market environment had been relatively stable, but in 2021, volatility in bond markets had been higher due to stronger reflation concerns. In line with international developments, government securities market yields in Hungary had been rising until the beginning of March before declining again. In the decision-makers' assessment, asset purchases by the Bank even in this volatile environment greatly contributed to maintaining a stable liquidity position in the government securities market and to enhancing the effectiveness of monetary policy transmission. In summary, the Monetary Council members underlined the importance of maintaining a lasting presence in the government securities market and continuing the programme with unchanged conditions. The next revision would be performed by the Council when stocks purchased under the programme reached HUF 3,000 billion.

Monetary Council members agreed that the successful economic reopening was largely affected by inflation developments. Therefore, the appropriate response had to be given to increasing upside risks to price stability. The June Inflation Report would be key in assessing inflationary risks linked to the reopening. In view of that, the Monetary Council reiterated that the MNB would be ready to use the appropriate instruments if warranted by an increase in upside risks to inflation.

At its meeting today, the Monetary Council left the base rate and the overnight deposit rate unchanged at 0.60 percent and -0.05 percent, respectively, and the overnight and the one-week collateralised lending rates at 1.85 percent. The MNB would continue to set the one-week deposit rate at weekly tenders, in response to the increase in risk aversion vis-a-vis emerging markets. The

Bank would maintain the difference between the base rate and the one-week deposit rate as long as warranted by inflationary risks.

It was a key priority for the MNB that short-term rates in every sub-market and at all times should develop consistently with the level of short-term rates deemed optimal by the Monetary Council. Therefore, similarly to previous quarters, the MNB had held foreign exchange swap tenders providing euro liquidity at the end of March, thereby successfully contributing to maintaining the stability of monetary conditions.

In the Monetary Council's assessment, the increase in risk aversion vis-à-vis emerging markets and potential second-round effects following the restart of the economy posed the greatest risk in terms of the outlook for inflation. By contrast, the protraction of the pandemic threatened a quick economic recovery and pointed to a lower inflation path than projected in the baseline scenario.

The MNB continued to be committed to maintaining price stability even during the third wave of the coronavirus pandemic. It was the MNB's clear intention to prevent the current uncertain environment from causing a sustained rise in inflation. The Council closely monitored developments in investors' risk appetite in emerging markets and potential second-round inflationary effects resulting from the restart of the economy. The Monetary Council reiterated that if warranted by an increase in upside risks to inflation, the MNB would be ready to use the appropriate instruments.

Votes cast by individual members of the Council:

In favour of maintaining the base rate at 0.60 percent, **In favour of maintaining the overnight collateralised lending rate, the one-week collateralised lending rate at 1.85 percent** **and** **maintaining the interest rate on the overnight central bank deposit at -0.05 percent:**	9	Péter Gottfried, Csaba Kandrács, Kolos Kardkovács, György Kocziszky, György Matolcsy, Bianka Parragh, Mihály Patai, Gyula Pleschinger, Barnabás Virág
Vote against:	0	

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

Péter Gottfried

Csaba Kandrács

Kolos Kardkovács

György Kocziszky

György Matolcsy

Bianka Parragh

Mihály Patai

Gyula Pleschinger

Barnabás Virág

The Council will hold its next policy meeting on 25 May 2021. The minutes of that meeting will be published at 2 p.m. on 9 June 2021.