MINUTES
OF THE MONETARY COUNCIL MEETING
24 AUGUST 2021

Time of publication: 2 p.m. on 8 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. 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 supported the Government's economic policy, as well as its policy on environmental sustainability.

Global economic recovery had continued in the summer months. In parallel, global inflation had also increased. In countries where the economy had reopened sooner, inflation had picked up earlier. International confidence indicators in manufacturing and services had continued to suggest a positive outlook in July. However, the fourth wave of the coronavirus pandemic caused a renewed increase in the risks surrounding the recovery.

International risk appetite had been driven by the spread of the Delta variant of the coronavirus, monetary policy messages of the world's leading central banks and macroeconomic data. Following a previous sustained rise, the prices of several important commodities had declined over the past month. Global oil prices had fallen overall in the period.

The Federal Reserve and the European Central Bank had maintained loose monetary conditions and continued their asset purchase programmes. Nevertheless, based on the communication by the Federal Reserve's decision-makers, the possibility of phasing out the crisis management programmes arose more often. Meanwhile, central banks in some developed countries had already slowed the pace of their asset purchases. In the region, a number of central banks had recently indicated that they would stand ready to tighten monetary conditions, when necessary, due to the increase in the outlook for inflation. In August, the Czech central bank had raised the base rate by an additional 25 basis points, while the central bank of Romania had left the policy rate unchanged.

The Hungarian economy had successfully restarted. In the second quarter of 2021, domestic GDP had grown by 17.9 percent year-on-year, while it had risen by 2.7 percent relative to the previous quarter, exceeding the level seen before the crisis. The pace of the economic recovery in Hungary was substantially better than the EU average.

A wide range of sectors had contributed to growth, but there were differences in the pace of the recovery. In June, construction output had approached, while industrial production had already exceeded pre-crisis levels. Retail sales continued to fall short of their value preceding the pandemic. Real earnings, affecting mostly household consumption, had risen further in May. Unemployment rate had remained broadly unchanged in June and could still be considered low in international comparison.

The historically high investment rate would continue to rise on the forecast horizon. Hungarian export performance was expected to improve markedly already in 2021 as external markets recovered. The increase in the production of new export capacities built in previous years caused a dynamic expansion of exports over the entire forecast horizon. Household demand was likely to pick up gradually. Economic recovery in Hungary was one of the fastest compared with other European countries.

In July 2021, annual inflation had been 4.6 percent, while core inflation had stood at 3.5 percent. The consumer price index had declined by 0.7 percentage points relative to the previous month. The decline in inflation was mainly attributable to base effects. The price index of market services had stopped rising in July, suggesting that the vast majority of repricings related to the reopening had already materialised.

The consumer price index would temporarily rise again in autumn due to base effects. Therefore, the pace of the increase in prices was expected to remain above the central bank tolerance band until the end of the year. Thereafter, inflation was expected to fall back into the central bank tolerance band at the beginning of 2022 and to stabilise around the central bank target from mid-2022 as a result of the monetary policy tightening cycle.

Increased commodity prices and a sustained rise in international freight costs pointed to a higher external inflation environment. Demand-supply frictions, emerging temporarily due to the rapid restart of the domestic economy, and the renewed tightening of labour market capacities expected in certain sectors, combined with dynamic wage growth, carried upside risks to inflation.

Following 8.1 percent in 2020, from 2021 the government deficit was expected to decline and, in parallel, the debt-to-GDP ratio to shift to a downward path. The current account surplus and the economy's net lending were expected to continue rising over the forecast horizon. The decline in Hungary's net external debt would continue.

Following the review of macroeconomic and financial market developments, the Monetary Council discussed the details of its monetary policy decision. The Monetary Council noted that as a result of the effective and quick management of the coronavirus pandemic, the Hungarian economy had successfully restarted and the pace of the recovery exceeded the EU average significantly. Some members pointed out that a wide range of sectors had contributed to growth; however, there were differences in the speed of the recovery in individual sectors.

Council members agreed that the recovery had led to an increase in inflation globally. Its extent across countries was driven by the timing of the reopening and the speed of the recovery. In this context, several members underlined the significance of a sustained rise in global freight costs and of movements in commodity prices in the past 18 months. The Council concluded that inflation in Hungary had declined in July primarily due to base effects. Some members pointed out that the price index of market services had stopped rising in July, suggesting that the vast majority of repricings related to the reopening had already materialised. Meanwhile, the effect of increases in global commodity prices had been increasingly reflected in industrial goods inflation, which continued to pose upside risks to inflation. Some members highlighted that following a rapid increase in prices in global commodity markets in the first half of 2021, the prices of several key commodities had eased back in recent weeks. However, the fourth wave of Covid caused risks surrounding the recovery to grow again. The Monetary Council was unanimous in its assessment that inflation would rise again in the autumn due to base effects, and as a result, it was expected to remain above the central bank tolerance band until the end of the year. The Council expected inflation to fall back into the central bank tolerance band at the beginning of 2022 and to stabilise around the central bank target from mid-2022 as a result of the Bank's proactive monetary policy tightening measures.

Council members unanimously argued that the proactive interest rate hiking cycle started in June should be continued in August and the base rate and the interest rate corridor should be raised by an additional 30 basis points. Members concluded that in order to ensure price stability, prevent second-round inflationary effects and anchor inflation expectations, a further tightening of monetary conditions was warranted.

Council members were unanimous in their view that in order to tighten monetary conditions effectively, the central bank should support increases in interest rates by continuing the gradual phasing out of the crisis management instruments having an effect at longer maturities. Several members pointed out that in view of the MNB's monetary policy stance, earlier communication and the scheduled revision of the government securities purchase programme, the Monetary Council's August meeting was an optimal date to start gradually phasing out the government securities purchase programme. Nevertheless, it was also highlighted that the aspects of maintaining stability in the government securities market had to be monitored closely while the programme was being phased out. The Council agreed that the amount of weekly purchases should be reduced from HUF 60 billion to HUF 50 billion from the week starting on 23 August 2021. The MNB might depart from this arrangement in a flexible manner, depending on market conditions. Looking ahead, members argued that no additional revision limit should be set to the programme. Instead, the target amount of weekly purchases should be set on a quarterly basis. Accordingly, a decision would be taken on the target amount for the fourth quarter at the September policy meeting.

Council members noted that a comprehensive assessment of the results achieved by the cycle of interest rate hikes should be performed and risks to the inflation outlook should be identified in light of the September Inflation Report. The Monetary Council agreed that the cycle of interest rate hikes should be continued until the outlook for inflation stabilised around the central bank target in a sustainable manner and inflation risks became evenly balanced on the horizon of monetary policy.

In order to ensure price stability, prevent second-round inflationary effects and anchor inflation expectations, the Monetary Council tightened monetary conditions further at its August meeting, continuing the interest rate hiking cycle started in June. According to the August decision, the central bank base rate was raised by 30 basis points to 1.50 percent. The Monetary Council also considered a 30 basis point increase in the interest rate corridor to be justified: the overnight deposit rate increased to 0.55 percent, while the overnight and the one-week collateralised lending rates increased to 2.45 percent. The MNB would continue to set the one-week deposit rate at weekly tenders. According to the Monetary Council's assessment, it was warranted to increase the interest rate on the one-week deposit instrument by the same measure as in the base rate.

In parallel with the tightening of interest rate conditions, the Monetary Council continued to gradually phase out its crisis management instruments affecting longer maturities. Accordingly, with the exhaustion of the available amount, the MNB had announced the termination of the FGS Go! in June 2021 and discontinued the use of the long-term collateralised lending facility from its July decision. In August, the Monetary Council performed another revision of its government securities purchase programme. During the pandemic, the government securities purchase programme had successfully contributed to maintaining a stable liquidity position in the government securities market and strengthened the effectiveness of monetary policy transmission in a volatile international financial environment.

The Monetary Council decided to begin gradually withdrawing the government securities purchase programme from 24 August while considering aspects of maintaining market stability. In the future, the Monetary Council would not set a revision limit applicable to the entire stock purchased under the programme. Instead, the Council would set a target amount for weekly purchases.

As a first step, the MNB's purchases would decrease from a weekly amount of HUF 60 billion to HUF 50 billion from the week starting on 23 August 2021. The Bank might depart from this arrangement in a flexible manner, depending on the supply and other market conditions. Subsequently, the Monetary Council would perform a comprehensive assessment of the government securities purchase programme at the end of each quarter, starting in September 2021. As part of this, the Council would take a decision on the next step of the withdrawal, and it would set a target amount for weekly purchases over the next quarter.

The MNB would start reducing purchases of shorter-term government securities. As a result, the share of longer-term government securities within weekly purchases would increase. The central bank would not sell the stock of government securities on its balance sheet, purchased government securities would be held to maturity. As it would be phased out gradually, the MNB would continue to use the programme taking a flexible approach to changing the quantity and structure of weekly purchases, to the extent and for the time necessary. In the Monetary Council's assessment, a stable liquidity position in the government securities market remained crucial from a monetary transmission perspective; therefore, the MNB would stand ready to temporarily raise the volume of weekly purchases at any given time to maintain market stability.

At its June interest rate decision, the Monetary Council had indicated that instruments supporting long-term sustainability would persistently remain part of the MNB's set of instruments, while crisis management tools were being withdrawn. In order to support sustainability, the MNB had successfully launched its Green Mortgage Bond Purchase Programme. The Monetary Council increased the amount available under the Bond Funding for Growth Scheme by HUF 400 billion to HUF 1,550 billion in August.

The Monetary Council was committed to maintaining price stability. In the decision-makers' assessment, the Hungarian economy had successfully restarted. In light of the September Inflation Report, the Monetary Council would perform a comprehensive assessment of the results achieved by the cycle of interest rate hikes and would identify risks to the inflation outlook. The Monetary

Council would continue the cycle of interest rate hikes until the outlook for inflation stabilised around the central bank target in a sustainable manner and inflation risks became evenly balanced on the horizon of monetary policy.

Votes cast by individual members of the Council:

In favour of increasing the base rate to 1.50 percent, **raising the overnight collateralised lending rate, the one-week collateralised lending rate to 2.45 percent** **and** **increasing the interest rate on the overnight central bank deposit to 0.55 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 21 September 2021. The minutes of that meeting will be published at 2 p.m. on 6 October 2021.