MINUTES
OF THE MONETARY COUNCIL MEETING
23 MARCH 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. In the fourth quarter of 2020, the performance of the global economy had been more favourable than expected. However, the third wave of the coronavirus pandemic had led to the maintenance of restrictions and the imposition of further restrictive measures. The timing of the reopening of economies largely depended on the population's vaccination coverage rate; however, vaccination was progressing at a slower pace than expected in most countries around the world. There continued to be an exceptionally high degree of uncertainty surrounding the pace of global economic recovery.

In the past month, risk appetite had been driven by developments related to the coronavirus pandemic, news on the approval of the US budget stimulus package and global reflation concerns. In developed markets, there had been a general increase in yields. Since the beginning of 2021, commodity prices had increased significantly, and global oil prices had continued to rise.

At its policy meeting in March, the Federal Reserve had maintained loose monetary conditions. The European Central Bank had also held its interest rate conditions unchanged and had continued its asset purchase programmes. Decision-makers had pointed out that more purchases might be made under the pandemic emergency purchase programme (PEPP) in the second quarter. In the CEE region, the central banks of Poland and Romania had left policy rates unchanged in March. Due to the protracted economic recovery, the world's leading central banks and those in the region were likely to maintain loose monetary conditions over a prolonged period.

The Hungarian economy had proved to be crisis-resilient to the second wave of the pandemic. In the fourth quarter of 2020, gross domestic product had risen by 1.4 percent from the third quarter but had fallen by 5.0 percent throughout the year. In 2020, Hungary's economic performance had fallen to a lesser extent than the average of the European Union. As a result, economic convergence had continued.

In terms of demand and supply, the Hungarian economy exhibited a potential for rapid recovery. Throughout 2020, the business investment rate had stood at a high level, at 27.5 percent, while the unemployment rate had remained low compared to international levels. Credit markets had continued to expand strongly even in international comparison. In terms of demand, the recovery had been driven by an increase in household income, a pick-up in government and private investment and the accelerating withdrawal of EU funds. The vaccination process in Hungary was progressing more favourably compared to other European countries. The progress would be an important factor in determining the pace of economic recovery.

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. Domestic demand might pick up after progress was made in vaccination. Continued growth in investment was key to economic recovery. The financing environment remained supportive, in which the Bank's FGS Go! and the Bond Funding for Growth Schemes 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. 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.

In February 2021, annual inflation had been 3.1 percent, core inflation had been 4.1 percent and core inflation excluding indirect tax effects had stood at 3.4 percent. Inflation had risen by 0.4 percentage points and core inflation excluding indirect tax effects had fallen by 0.1 percentage point relative to the previous month. The rise in inflation had reflected an increase in fuel prices.

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 on core inflation excluding indirect tax effects. In the coming months, spikes in inflation would occur due to base effects, rising fuel prices, 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. As temporary effects faded, inflation would return to the central bank tolerance band from the summer months. 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 all 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.

As it had been confirmed by the latest credit ratings by S&P and Fitch, Hungary had a relatively strong economic performance and recovery potential, as well as a solid debt repayment ability. According to preliminary financial accounts data, the accrual-based government deficit might have been around 8.0 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.

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

The government securities purchase programme had contributed successfully to maintaining a stable liquidity position in the government securities market and had improved the effectiveness of monetary policy transmission. Since the start of the programme, the stock of government securities in the Bank's balance sheet had increased by over HUF 1,600 billion. 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 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 as well as the Inflation Report projection, the Monetary Council discussed the details of its monetary policy decision. Members were of the view that financial market developments had remained to be driven mainly by news related to the coronavirus pandemic. There had been a general rise in yields in developed markets, while global commodity prices had been rising since the beginning of the year. Members agreed that reflation concerns related to the restart of economies had remained elevated. Several decision-makers pointed out that the third wave of the pandemic had caused growth and financial market risks to rise again.

Reflecting on developments in domestic inflation, members concluded that inflation data for the beginning of this year had been in line with the MNB's December projection. Decision-makers unanimously argued that extreme volatility in inflation would persist over the coming period; therefore, special attention should be paid to developments in measures of underlying inflation capturing persistent trends, particularly core inflation excluding indirect tax effects. Some members highlighted that, due to spikes in inflation expected in the coming months, the consumer price index would approach 5 percent in the second quarter, about half of which would be accounted for by rising fuel prices and tax changes. In the Council's assessment, it would be crucial to ensure that factors causing these spikes in inflation would not lead to second-round effects. In this case, inflation would return to the central bank tolerance band from the second half of the year, before stabilising around the central bank target from the first quarter of 2022.

Regarding the outlook for growth, decision-makers agreed that the Hungarian economy had the ability to recover rapidly from both the demand and supply side. Members assessed that the economic recovery was expected to start in the second quarter of 2021, which would strengthen further in the second half of the year. Some members pointed out that continued growth in investment would be crucial for the recovery, which would ensure that the Hungarian economy returned to a sustainable growth path. In assessing the country's balance indicators, the Monetary Council highlighted that the current account balance had been more favourable than expected and had shown a surplus in 2020. Both the current account balance and Hungary's net lending position were expected to improve further in the coming years.

Council members agreed that developments in investors' risk appetite towards emerging markets continued to be a key risk factor in terms of the inflation outlook. In addition, however, potential second-round inflationary effects that might arise during the restart of the economy represented a new risk, the neutralisation of which would require special attention. Council members expressed their clear intention to prevent the current uncertain environment from causing a sustained rise in inflation. Finally, decision-makers unanimously argued that in the event of an increase in any upside risk to inflation, the MNB would be ready to use the appropriate instruments.

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 would hold foreign exchange swap tenders providing euro liquidity at the end of March, thereby 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. 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 27 April 2021. The minutes of that meeting will be published at 2 p.m. on 12 May 2021.