MINUTES
OF THE MONETARY COUNCIL MEETING
19 OCTOBER 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) is to achieve and maintain price stability. Without prejudice to its primary objective, the Magyar Nemzeti Bank preserves financial stability and supports the Government's economic policy, as well as its policy on environmental sustainability.

Global economic recovery had continued in recent months, and in parallel, inflation had risen. Where the reopening had taken place earlier an increase in consumer prices had occurred faster as well. The fourth wave of the coronavirus pandemic had led to a renewed increase in risks surrounding the economic recovery. International confidence indicators in manufacturing and services had weakened in September.

Global investor sentiment had deteriorated since the Council's previous policy decision. Among already existing risks, the spread of the Delta variant of coronavirus, the shortage of microchips, and monetary policy messages of the world's leading central banks had contributed to this. In addition, as new factors, the energy crisis and the emergence of risks related to the Chinese real estate market had also contributed to a worsening in investor sentiment. In commodity markets, another significant wave of price increases had occurred in September. In the case of energy sources, the rise in prices had been extraordinarily high. The price of natural gas had more than tripled since the beginning of the summer, while the price of electricity had more than doubled. World market price of crude oil had risen to over USD 80. Overall, the US dollar had appreciated against the euro and most emerging market currencies.

The world's leading central banks had maintained loose monetary conditions in the past month, but there had been a shift in their communications towards a tighter tone. At its September policy meeting, the decision-makers of the Federal Reserve had signalled that a moderation in the pace of asset purchases might soon be warranted if the economy developed in line with expectations. The European Central Bank had slowed the pace of purchases under the Pandemic Emergency Purchase Programme (PEPP) in September. In the CEE region, the Romanian and Polish central banks had started to raise policy rates due to an increase in the inflation outlook, and the Czech central bank had raised its policy rate more than expected by market participants.

The Hungarian economy had restarted successfully. GDP had reached its pre-pandemic level in the second quarter. Hungary was among the economies in Europe showing the fastest recovery. Based on monthly data, strong economic recovery had continued in the third quarter. A wide range of sectors had contributed to growth, but there had been differences in the pace of recovery. The year-on-year rate of industrial and construction output growth had slowed in August compared to the previous month. The recovery in the domestic automobile industry had been held back by a global shortage in microchips; however, robust growth in battery manufacturing was becoming increasingly dominant in industrial production. The volume of retail sales had continued to rise in August, approaching pre-pandemic levels. The unemployment rate continued to be low in international comparison.

Hungary's GDP was expected to grow by between 6.5 and 7 percent in 2021 and by between 5 and 6 percent in 2022. In the favourable labour market environment, growth in household consumption was expected to continue, while a general pick-up in investment was likely to make a positive contribution to GDP growth from 2021 again. The investment rate would rise to a historically high level in the second half of the forecast horizon. Hungarian export performance had rebounded strongly in 2021, and with the utilisation of new export capacities built in previous years, it was expected to grow markedly over the entire forecast horizon. The fourth wave of the coronavirus pandemic and the energy crisis were increasing the risks to the economic outlook.

In September 2021, annual inflation had been 5.5 percent, and core inflation had stood at 4.0 percent. Headline inflation had risen by 0.6 percentage points and core inflation by 0.4 percentage points compared to the previous month. The rise in inflation had been driven by price increases affecting a wide range products and services. The global pick-up in commodity prices was gradually appearing in consumer prices of a growing range of products.

Inflation was expected to rise further in the autumn months. The significant rise in commodity prices in recent weeks pointed to a higher inflation path in the short run than expected in September. The pass-through of increased commodity prices and freight costs into industrial goods prices was expected to be crucial in the case of underlying inflation. Core inflation was expected to be around 4 percent throughout the remainder of the year. The effects of the Bank's tightening cycle would be clearly felt in 2022. According to the September Inflation Report's projection, inflation was expected to start to fall from the beginning of 2022 and to return to the central bank tolerance band in the second quarter, before stabilising around the 3 percent central bank target in the second half of 2022.

The risks to the outlook for inflation remained on the upside. Rises in commodity and energy prices as well as international freight costs continued to point to a higher external inflationary environment which was more persistent than previously expected. Demand-supply frictions emerging temporarily, and the renewed tightening of labour market capacities in certain sectors, combined with dynamic wage growth, also carried upside risks to inflation.

The government deficit was expected to fall from this year and the debt-to-GDP ratio to shift to a declining path even taking into account the September issuance of foreign currency denominated bonds. The current account balance was expected to improve over the forecast horizon, with a growing contribution from net exports due to new export capacities built up. The economy's net lending was likely to increase further and to stabilise around 3 percent of the GDP, and therefore Hungary's net external debt would continue to fall.

At its October meeting, the Monetary Council decided to continue to tighten monetary conditions. In the decision-makers' assessment, the outlook for inflation and the risks surrounding it, which remained on the upside, clearly warranted the continuation of the monthly interest rate tightening cycle started in June.

Following the review of macroeconomic and financial market developments, the Monetary Council discussed the details of its monetary policy decision. The decision-makers concluded that based on incoming data, strong economic growth had continued in the third quarter. Several council members pointed out that a wide range of sectors had contributed to growth, but there had been differences in the pace of recovery. Several members noted that the fourth wave of the coronavirus pandemic and the energy crisis increased the risks surrounding the economic outlook.

Turning to inflation developments, the Monetary Council concluded that risks to the inflation outlook remained clearly on the upside and might persist longer than earlier expected. Several members highlighted that the rise in inflation was driven by rising prices in a wide range of products and services. Council members emphasised that there had been significant increases in commodity prices in recent weeks, which have resulted in a tripling in the prices of certain energy sources since the beginning of the summer. Members unanimously argued that the effects of the global increase in energy prices were being felt in an increasingly wide range of consumer prices. They agreed that the path of inflation had shifted to the risk scenario assuming a persistently elevated external inflation environment, published in the September Inflation Report.

The Monetary Council agreed that the upside risks to inflation might persist longer than previously expected, which warranted a further tightening of monetary conditions. Council members emphasized that avoiding second-round inflationary effects and properly anchoring expectations are key to achieving the inflation target. The Council unanimously argued that it was necessary to continue the tightening cycle on a monthly basis and that the tightening of monetary conditions was warranted 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. Members were of the view that due to cost shocks experienced in recent weeks, inflation would remain elevated over a longer period, and therefore the sustainable achievement of the inflation target may be delayed compared to the September Inflation Report's projection. In view of this, a longer series of monetary policy steps might have to be taken than previously planned.

Several decision-makers noted that maintaining an active presence in the market, the MNB had managed to cushion the spillover of tensions in international swap markets to Hungary at the end of the quarter. Members were of the view that it remained 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. To this end, the MNB would continue to phase out its FX swap facility providing forint liquidity in a dynamic way, taking into account developments in the swap market. Members agreed that the Bank should prepare further steps in the coming months to preserve the stability of the swap market and the effectiveness of monetary policy transmission. The decision-makers unanimously argued that the government securities purchase programme should be phased out without threatening to jeopardise market stability; therefore, the Bank would continue to use the instrument flexibly, taking into account developments in market conditions.

According to the October decision, the central bank base rate rose by 15 basis points to 1.80 percent. The Monetary Council also considered a 15 basis point increase in the interest rate corridor to be justified: the overnight deposit rate increased to 0.85 percent, while the overnight and the one-week collateralised lending rates increased to 2.75 percent. The MNB would continue to set the one-week deposit rate at weekly tenders. According to the Monetary Council's assessment, an increase in the interest rate on the one-week deposit instrument by the same measure as in the base rate was warranted.

Maintaining an active presence in the market, the MNB had managed to cushion the spillover effects of tensions in international swap markets, thereby contributing to preserving the stability of monetary conditions. It remained 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. To this end, the MNB continued to phase out its FX swap facility providing forint liquidity in a dynamic way, taking into account developments in the swap market. In addition, the Bank would prepare further steps to preserve the stability of the swap market and the effectiveness of monetary policy transmission in the coming months.

In the Council's assessment, a stable liquidity position in the government securities market remained crucial from the perspective of monetary policy transmission. In its September decision, the Council had set the target amount of the MNB's weekly purchases at HUF 40 billion. The MNB continued to use the government securities purchase programme taking a flexible approach to changing the quantity and structure of weekly purchases, to the extent and for the time necessary. If warranted by the maintenance of market stability, the MNB would stand ready to temporarily raise the volume of weekly purchases at any given time. The Bank would not sell the stock of government securities on its balance sheet, purchased government securities would be held to maturity. The Monetary Council would set the next target amount of weekly purchases for the following quarter in December.

The Monetary Council was committed to achieving and maintaining price stability. In the decision-makers' assessment, the inflation outlook continued to be surrounded by upside risks which might prove to be more persistent than earlier expected. For this reason, the Council considered it necessary to continue the monthly interest rate tightening cycle. 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 1.80 percent, **raising the overnight collateralised lending rate, the one-week collateralised lending rate to 2.75 percent** **and** **increasing the interest rate on the overnight central bank deposit to 0.85 percent:**	8	Péter Gottfried, Csaba Kandrács, Kolos Kardkovács, György Kocziszky, György Matolcsy, Bianka Parragh, 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

Gyula Pleschinger

Barnabás Virág

The Council will hold its next policy meeting on 16 November 2021. The minutes of that meeting will be published at 2 p.m. on 1 December 2021.