MINUTES
OF THE MONETARY COUNCIL MEETING
25 APRIL 2023

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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.

The global economic outlook continued to be characterised by duality. In 2023, output growth was expected to slow in developed countries. In emerging countries, growth was likely to be similar to last year. In most countries, labour markets were tight. The Russia-Ukraine war and the persistently high inflation environment were posing downside risk to growth. The reversal of energy prices and the favourable level of gas storage facilities were mitigating the adverse effects of the energy crisis in Europe, which pointed to an improvement in the outlook for economic activity on the Continent.

The turnaround in inflation had been emerging in an increasing number of countries. However, changes in core inflation indicators suggested that the fall in price indices in most countries might take longer than previously expected. The slowdown in global economic activity, the correction in global energy and commodity prices and the fall in international freight costs pointed to continued global disinflation.

Investor sentiment had improved since the Monetary Council’s last policy decision. Concerns about the US and European banking sectors had eased, and expectations for interest rate policies of the world’s leading central banks had shifted back into focus.

Communications from the Federal Reserve’s (Fed) and the European Central Bank’s (ECB) decision makers indicated that interest rate hikes were likely to be continued. Based on market expectations, interest rate increases by the Fed and the ECB might soon come to an end. In line with expectations, central banks in the CEE region had not changed monetary conditions.

The Hungarian economy had grown by 4.6 percent in 2022. High-frequency data suggested that the pace of economic growth had generally slowed in the first months of the year. In February, the volume of retail sales and construction output had fallen significantly, while industrial production had decreased to a smaller extent relative to a year earlier. The household confidence indicator had risen significantly in the past month but remained at a low level. The labour market remained tight, and the unemployment rate was low.

The time profile and structure of domestic GDP was expected to be characterised by a duality this year. Output growth would be weighed down mainly by domestic demand factors. Economic growth was expected to pick up again from the second half of the year as inflation declined markedly and investment recovered. Both internal and external factors might make a positive contribution to growth in 2024. Hungary's GDP was expected to grow by 0.0–1.5 percent in 2023, by 3.5–4.5 percent in 2024 and by 3.0–4.0 percent in 2025.

Domestic inflation had peaked in January 2023. In March, annual inflation had been 25.2 percent and core inflation had stood at 25.7 percent. Inflation had declined by 0.2 percentage points compared to the previous month. The slowdown in food and fuel price inflation had continued. Compared to February, core inflation had risen slightly, which had been driven by one-off price increases linked to market services, particularly in the telecommunications sector. By contrast, within core inflation items the prices of durables had decreased on a monthly basis. Inflation expectations continued to be elevated; however, corporate price expectations for retail sales and services had been slowing for months.

The consumer price index was expected to decrease at an accelerating pace in the next months, which would also be supported by the growing impact of base effects from the middle of the year. Tight monetary conditions were expected to have broader disinflationary effects. The consumer price index would return to the central bank tolerance band in 2024. Inflation was projected to be 15.0–19.5 percent in 2023, 3.0–5.0 percent in 2024 and 2.5–3.5 percent in 2025.

The fiscal deficit would continue to decline this year. The deficit was projected to be 3.9 percent in 2023. Based on detailed data, the government debt ratio had decreased to 73.3 percent of GDP by the end of 2022, and it was expected to decline to 69 percent this year and close to 65 percent by the end of 2025.

The external balance had continued to improve. The current account deficit had fallen significantly in February 2023, bringing Hungary's financing balance back into surplus after more than a year. The trend-like improvement in the external balance had been driven by a decrease in the energy balance, more favourable terms of trade, the adjustment of domestic demand and the dynamic growth of exports. The current account deficit was expected to be halved this year. In parallel with a normalising global economic environment and the utilisation of new export capacities built recently, the trade balance and the net lending would continue to improve in 2024.

Following the review of macroeconomic and financial market developments, the Monetary Council discussed the details of its April monetary policy decision. In the Council's assessment, the outlook for global growth continued to be characterised by duality. In the Council members' view, the Russia-Ukraine war and the persistently high inflation environment continued to pose downside risks, while the reversal of energy prices and the easing in the adverse effects of the energy crisis in Europe pointed to an improvement in the continent's economic prospects. A turnaround in inflation could be observed in more and more countries; however, some members highlighted that core inflation indicators rose in several countries relative to the time of peaks in inflation. Based on this, the consumer price index in most countries might decrease more slowly than earlier expected.

Discussing domestic real economic developments, the Monetary Council concluded that high-frequency data suggested a general slowdown in economic activity. Council members agreed that the duality identified in the time profile and structure of domestic GDP growth persisted. In the Council's assessment, the improvement in external balance developments that had started at the end of 2022 continued. This was driven by an improvement in the energy balance, the more favourable terms of trade, declining domestic demand and dynamic export growth. Based on incoming data, the trend-like improvement in the external balance continued and looking ahead, it might be even more favourable than the forecast trajectory of the March Inflation Report.

Members emphasised that inflation had continued to moderate in March, mainly driven by a slowdown in food and fuel price inflation. Some decision makers underlined that food and fuel price indices had been declining for the third and second consecutive month, respectively. Members concluded that core inflation had risen slightly compared to February; however, this was mainly related to a small group of market services, the unique price increase in telecommunications services. Some members underlined that the decline in the prices of durable industrial goods within core inflation items pointed to a further improvement in underlying inflation. Council members were unanimous in arguing that the consumer price index might fall at an accelerating pace in the coming months. In this context, some members noted the growing impact of base effects from the middle of the year. The Council agreed that the tight monetary conditions achieved by the cycle of rate hikes, which had been started in Hungary in June 2021, the first in the European Union, and accelerated in 2022, would have an increasingly strong disinflationary effect.

The Monetary Council was in agreement that maintaining tight monetary conditions would be necessary to achieve price stability over the long term; therefore, they unanimously argued in favour of maintaining the base rate at its prevailing level over a prolonged period. In the Council's view, financial market stability would be key in the future too; therefore, members considered it justified to leave the interest rate level of overnight instruments unchanged.

In view of the market turbulence last October, the Monetary Council had raised the upper bound of the interest rate corridor to 25 percent in its decision of 14 October 2022. In the MNB's assessment, the risk environment, including Hungary's risk perception, had improved significantly since the middle of October 2022. Members pointed out that within external factors, energy prices had adjusted, the adverse effects of the energy crisis had subsided, capital inflows into emerging markets had increased and the end of the tightening cycle of the world's leading central banks was within sight. At the same time, Hungary's foreign exchange market had stabilised, the government securities market was stable, an agreement with the European Union had been reached and there had been a significant improvement in Hungary's external balance position. In the Council's view, the risks of extreme scenarios had significantly decreased. Therefore, members unanimously decided to narrow the upward room for manoeuvre offered by the interest rate corridor by reducing the O/N collateralised lending rate from 25 percent to 20.5 percent. The Council emphasised that this decision was part of the normalisation of monetary conditions.

Decision makers noted that the banking sector's transition to the revised reserve requirement system had been smooth. In the Monetary Council's assessment, in addition to ensuring market stability, the proper functioning of monetary transmission was essential to achieve price stability; therefore, the Bank would continue to use its longer-term instruments.

Council members underlined that a careful, cautious approach was warranted when setting the interest rates on overnight instruments. Therefore, at the following rate-setting meetings the MNB would consider the persistence of the improvement in risk perceptions, which would be a key factor in setting the interest rate conditions on overnight instruments.

In the Monetary Council's assessment, it was necessary to maintain tight monetary conditions in order to achieve price stability, and therefore the base rate was left unchanged at 13 percent at its meeting on 25 April 2023. In the Council's evaluation, it was warranted to announce one-day deposit quick tenders and FX swap transactions at unchanged interest rate levels. The prevailing level of the base rate was adequate to manage fundamental inflation risks.

On 14 October 2022, the Monetary Council had widened the interest rate corridor substantially in a turbulent financial market environment. In recent times, the risk environment, including Hungary's risk perception, had improved significantly, driven by external and internal factors. In response to the reduction in the risks of extreme scenarios, the Council decided to narrow the interest rate corridor. Accordingly, the O/N deposit rate was left unchanged at 12.5 percent and the O/N collateralised borrowing rate was reduced to 20.5 percent.

The transition to the revised reserve requirement system, which had taken effect from 1 April 2023, was smooth. The Bank would use the instruments to absorb interbank forint liquidity on a long-term basis in the coming period in order to strengthen monetary policy transmission.

In the Monetary Council's assessment, it was necessary to maintain the current level of the base rate over a prolonged period, which would ensure that inflation expectations were anchored and the inflation target was achieved in a sustainable manner. Looking ahead, maintaining market stability and strengthening monetary policy transmission were also key to achieving price stability. The MNB was constantly assessing incoming data and developments in the outlook for inflation, and was closely monitoring the effects of international financial market developments on the domestic risk environment. The central bank would take into account the persistence of improvements in risk perceptions at the following policy meetings before making a decision to setting the interest rate conditions of overnight instruments.

Votes cast by individual members of the Council:

In favour of maintaining the base rate at 13.00 percent, **reducing the overnight collateralised lending rate to 20.50 percent** **and** **maintaining the interest rate on the overnight central bank deposit at 12.50 percent:**	9	Éva Búza, Péter Gottfried, Csaba Kandrács, Kolos Kardkovács, Zoltán Kovács, György Matolcsy, Mihály Patai, Gyula Pleschinger, Barnabás Virág
Vote against:	0	

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

Éva Búza

Péter Gottfried

Csaba Kandrács

Kolos Kardkovács

Zoltán Kovács

György Matolcsy

Mihály Patai

Gyula Pleschinger

Barnabás Virág

The Council will hold its next policy meeting on 23 May 2023. The minutes of that meeting will be published at 2 p.m. on 7 June 2023.