MINUTES
OF THE MONETARY COUNCIL MEETING
19 DECEMBER 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:

https://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.

In 2023 Q3, economic growth had slowed in the EU and China, while it had accelerated in the US. The short-term economic outlook was exposed to downside risks, which was further exacerbated by the generally tense geopolitical situation.

In the euro area, inflation had been below expectations at 2.4 percent in November, approaching the inflation target. In the US, the pace of price increases had also continued to moderate. Global trends pointed to continued disinflation. Weakening global economic demand, lower commodity prices compared to the previous year and the correction in international freight costs suggested a continued decline in inflation rates. However, core inflation indicators, falling at a slower pace, suggested that achieving persistent price stability again was expected to be a protracted process in general.

International risk appetite had increased since the November policy decision. Sentiment in global financial markets had been influenced by expectations for the monetary policies of the world's leading central banks, incoming macroeconomic data and developments related to the Gaza conflict. The Federal Reserve and the European Central Bank had left their policy rates unchanged at their rate-setting meetings in December. Based on market pricings, both central banks' interest rates had peaked, and looking ahead, expectations for the beginning of interest rate cuts in 2024 had strengthened. Central banks in the CEE region had left their policy rates unchanged in the month.

Hungary's economic fundamentals had continued to improve. The recession had ended in 2023 Q3. Hungary's GDP had risen by 0.9 percent compared to the previous quarter, and it had fallen by 0.4 percent in annual terms. The main contributor to the downturn in economic performance relative to the previous year had been the fall in industrial output and market services, while agricultural performance had moderated the decline. The improvement in the household confidence indicator had slowed in the autumn months. Accompanied by a high level of employment, the labour market remained tight, the unemployment rate was low even by EU standards.

The gradual economic recovery had continued in 2023 Q4. The downturn in domestic economic performance throughout 2023 had been primarily caused by high inflation. Household consumption had fallen due to high inflation and increased caution. Investment growth had been restrained by the cancellation of government development projects, in addition to the more uncertain outlook for demand. Net exports had made a positive contribution to economic growth in 2023. As inflation moderated, real wages rose substantially and confidence gradually recovered, leading to an increase in domestic demand, more balanced and stronger economic growth was expected even by EU standards in 2024. Subdued European economic activity was holding back domestic exports, but with the pick-up in the production of new export capacities built recently, Hungary's export market share was expected to increase further over the entire forecast horizon. In our projection, Hungary's economic performance may have been in the range of (-0.6)–(-0.4) percent in 2023. Economic performance was projected to increase by 2.5–3.5 percent in 2024, by 3.5–4.5 percent in 2025, and by 3.0–4.0 percent in 2026.

The widespread and general decline in domestic inflation had continued at a rapid pace in November. Consumer prices had risen by 7.9 percent in annual terms. Core inflation had stood at 9.1 percent. The consumer price index had fallen significantly by 2.0 percentage points, while core inflation had declined by 1.8 percentage points from the previous month. The continued slowdown in underlying inflation was indicated by the fact that the annualised three-month change in core inflation had been below 3 percent in November as well.

In the coming months, domestic CPI inflation and core inflation would continue to decrease. Disciplined monetary policy, the Government's measures to strengthen market competition and subdued domestic demand combined with a significantly lower external cost environment than last year supported a further moderation in price growth. Inflation had fallen from above 25 percent at the beginning of the year at one of the fastest paces in Europe, and domestic inflation was expected to fall to around 6.0 percent, a level corresponding to the region's average, by the end of 2023. Strong disinflation was expected to continue in 2024 Q1, before slowing down, and thus the consumer price index was likely to return to the central bank inflation target persistently in 2025. Annual inflation may have been between 17.6 and 17.7 percent in 2023, between 4.0 and 5.5 percent in 2024 and between 2.5 and 3.5 percent in 2025 and 2026.

The rapid and substantial improvement in the external balance had continued. The monthly current account balance had been in surplus in October 2023 as well. The sustained improvement in the external position reflected shrinking imports caused by significantly lower energy prices and the adjustment of energy consumption on the one hand, and by the decline in domestic demand on the other. Goods exports had been supported by a decrease in inventories, while the services balance had also developed favourably. The utilisation of new export capacities built recently and the improving global economic environment were expected to give new impetus to exports in the coming years. The current account balance-to-GDP ratio was likely to improve by over 8 percentage points in 2023, a stronger improvement than seen after the financial crisis. In 2023, the annual current account balance was expected to turn slightly positive. The current account balance was expected to continue rising over the forecast horizon.

As a result of the negotiations on the EU funds, the drawdown of Cohesion Funds for the period between 2021 and 2027 might start. The agreement would improve Hungary’s risk perception and net lending. In addition, incoming funds would have a favourable effect on the government debt path.

In our projection, the government deficit may have been between 5.2 percent and 6.0 percent of GDP in 2023, between 2.9 percent and 3.9 percent in 2024, between 1.9 percent and 2.9 percent in 2025 and between 1.4 percent and 2.4 percent in 2026. There were risks to meeting the deficit targets over the entire forecast horizon. The government debt ratio may have fallen to around 73 percent of GDP in 2023, followed by a further decline over the forecast horizon.

The Monetary Council had highlighted three alternative risk scenarios around the baseline projection in the December Inflation Report. Both economic growth and inflation might be lower compared to the baseline in the scenarios that assume deceleration in global economic activity and a slower recovery in consumption. However, possible capital outflows from emerging markets were consistent with a higher inflation path.

Following the review of macroeconomic and financial market developments as well as the latest Inflation Report projection, the Monetary Council discussed the details of its December monetary policy decision. In the Council’s assessment, the short-term outlook for global economic growth was continuously exposed to downside risks, which was further exacerbated by the generally tense geopolitical situation. Council members judged that weakening global economic demand, lower commodity prices compared to the previous year and the correction in international freight costs suggested a continued decline in inflation rates. Risks surrounding global disinflation and volatility in international investor sentiment warranted a careful approach to monetary policy.

Decision makers agreed that international risk appetite had increased since the previous interest rate decision. Regarding the international monetary policy environment, some members pointed out that based on market pricings, the Federal Reserve's and the European Central Bank's interest rates had peaked and looking ahead, expectations for the beginning of interest rate cuts in 2024 had also strengthened.

Council members were of the view that Hungary's economic fundamentals had definitely continued to improve in several areas. In line with this, in assessing November inflation data, members concluded that disinflation was fast-paced, broad-based and general. In addition, several Council members noted that disciplined monetary policy, the Government's measures to strengthen market competition, subdued domestic demand combined with a lower external cost environment played a crucial part in a further moderation in price growth. Some members underlined that inflation had fallen from above 25 percent at the beginning of the year at one of the fastest paces in Europe, and domestic inflation was expected to fall to around 6.0 percent, a level corresponding to the region's average, by the end of 2023. In the Council's unanimous view, strong disinflation was expected to continue in 2024 Q1, before slowing down, and thus the consumer price index was likely to return to the central bank inflation target persistently in 2025.

The decision makers pointed out that the gradual economic recovery had continued in 2023 Q4. In the decision makers' view, the downturn in domestic economic performance throughout 2023 had been primarily caused by high inflation. Accordingly, several members pointed out that household consumption had fallen due to high inflation and increased caution, and investment growth had been restrained by the cancellation of public development projects, in addition to the more uncertain outlook for demand. The Council expected domestic demand to grow due to moderated inflation, substantial rise in real wages and the gradual recovery in confidence in 2024. Consequently, more balanced and stronger economic growth was expected even by EU standards in 2024. In line with this, members emphasised that it was critical to achieve price stability again. Some decision makers pointed out that the current account balance-to-GDP ratio was likely to improve by over 8 percentage points in 2023, an even stronger improvement than seen after the global financial crisis. It was noted that the current account balance was likely to improve further over the forecast horizon. Decision makers concurred that the agreement regarding EU funds would improve Hungary’s risk perception and net lending position.

In the Council’s risk assessment, the baseline scenario in the Inflation Report was characterised by symmetrical risks to inflation and downside risks to economic growth.

The consensus among decision makers was that Hungary’s economy was clearly on a disinflationary path, and risk perceptions improved further. Decision makers discussed alternatives of reducing the base rate by 75 or 100 basis points. In the Council’s assessment, faster-than-expected domestic disinflation, the significant improvement of Hungary’s economic fundamentals, the improvement of international risk appetite at the end of the year and the agreement related to EU funds allowed the consideration of the possibility of a larger interest rate cut than in previous months. However, Council members agreed that in the rapidly changing environment, a cautious approach was still warranted, and the assessment of the persistence of favourable developments was a key factor in setting the optimal pace of the easing cycle. In this context, the decision makers were unanimously in favour of reducing the base rate and the interest rate corridor by 75 basis points from the two alternatives.

Members noted that positive real interest rates supported the continuation of disinflation. However, several members pointed out that as inflation approached the central bank tolerance band, real interest rates were expected to fall. In addition, Council members considered it appropriate for the central bank to hold an additional tender with maturity extending through the end of the year in order to strengthen monetary policy transmission and with a view to ensuring that developments in foreign currency swap market yields were in line with interest rates deemed optimal by the Monetary Council.

In the decision makers’ assessment, the risks surrounding global disinflation and volatility in international investor sentiment warranted a careful approach to monetary policy. The Monetary Council continued to constantly assess incoming macroeconomic data, the outlook for inflation and developments in the risk environment. There was a consensus among the decision makers that in the coming months, decisions on any further reductions in the base rate and their optimal pace would be made on the basis of this information, in a data-driven manner.

Hungary’s economy was clearly on a path of disinflation, while risk perceptions had improved further. According to the Monetary Council, this allowed the base rate to continue to be lowered. In line with this, at its meeting on 19 December 2023, the Monetary Council cut the base rate by 75 basis points to 10.75 percent. Accordingly, the lower bound of the interest rate corridor, i.e. the

O/N deposit rate, was reduced to 9.75 percent, while the upper bound, i.e. the O/N lending rate, was lowered to 11.75 percent. The positive real interest rates supported the continuation of disinflation. As inflation approached the central bank tolerance band, real interest rates were expected to decline.

Risks surrounding global disinflation and volatility in international investor sentiment warranted a careful approach to monetary policy. The Council was constantly assessing incoming macroeconomic data, the outlook for inflation and developments in the risk environment. In the coming months, decisions on any further reductions in the base rate and their optimal pace would be made on the basis of this information, in a data-driven manner.

Votes cast by individual members of the Council:

In favour of reducing the base rate to 10.75 percent, **reducing the overnight collateralised lending rate to 11.75 percent** **and** **reducing the interest rate on the overnight central bank deposit to 9.75 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 30 January 2024. The minutes of that meeting will be published at 2 p.m. on 14 February 2024.