MINUTES
OF THE MONETARY COUNCIL MEETING
24 JANUARY 2023

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Article 3 (1) of the Central Bank Act (Act CXXXIX of 2013 on the Magyar Nemzeti Bank) defines the achievement and maintenance of price stability as the Magyar Nemzeti Bank's primary objective. 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.

Over the recent period, global economic growth had slowed and GDP had already declined in several countries. Looking ahead, the prolonged Russia-Ukraine war, the energy crisis in Europe and the generally rising interest rate environment continued to present significant uncertainty. Commodity and energy prices had fallen significantly in the past months but remained high relative to previous years.

Inflation had started to moderate slowly in an increasing number of countries. Weakening demand, falling energy and commodity prices, as well as lower international freight costs and the easing of difficulties in production chains, pointed to a continued fall in global inflation from 2023.

Investor sentiment had improved slightly since the last interest rate decision. Risk appetite had been mainly influenced by macroeconomic data releases, the economic outlook and expectations related to the monetary policy of the world's leading central banks. Developments in the Russia-Ukraine war continued to create significant uncertainties.

According to both market pricing and decision makers' communications, the Federal Reserve and the European Central Bank were expected to raise interest rates further. In addition, based on its earlier announcement, the ECB would start reducing the portfolio built under its asset purchase programme from March 2023. In the CEE region, the Romanian central bank had raised its policy rate by 25 basis points. By contrast, the Czech and the Polish central banks had left interest rates unchanged.

High frequency data suggested a further slowdown in GDP growth by the end of 2022. In November, the volume of retail sales excluding fuel sales had declined. Industrial production growth had slowed. The outlook for production activity had improved in the past month; however, confidence indicators had remained at low levels. The labour market continued to be tight, and the unemployment rate was low.

The pace of growth this year was likely to be slowed by both domestic and external demand factors. The decline in real incomes, rising corporate costs, delayed public investment and the stricter interest rate environment all had a restraining impact on domestic demand. Despite subdued global economic activity, Hungary's foreign market share was expected to increase due to growing domestic export capacities, which was also supported by the dynamic expansion of battery production. According to the December Inflation Report projection, Hungary's GDP had increased by 4.5–5.0 percent in 2022 before rising 0.5–1.5 percent this year, by 3.5–4.5 percent in 2024 and by 3.0–4.0 percent in 2025.

In December 2022, annual inflation had been 24.5 percent and core inflation had stood at 24.8 percent. The increase in inflation had been entirely accounted for by a pick-up in fuel prices. The incoming data had fallen short of expectations, which had been attributable in part to subdued energy consumption due to the weather, in addition to the slight decline in unprocessed food price inflation. Inflation expectations continued to be elevated; however, companies' expectations for retail and services prices had remained below their peak levels seen in the summer.

The effects causing a turnaround in inflation were expected to strengthen in the coming months. Global energy, commodity and food prices had fallen to the levels seen before the Russia-Ukraine war. In addition, the moderating effect on pricing arising from the fall in domestic demand and, from the spring months, the fading of base effects would support the decline in inflation. Tight monetary conditions contributed to avoiding second-round inflationary effects and anchoring inflation expectations. Domestic inflation was expected to decrease slowly in the first half of 2023, and then more significantly from the middle of the year. The consumer price index would return to the central bank tolerance band in 2024.

According to the press release by the Ministry of Finance the deficit target of 6.1 percent had been achieved in 2022, with the government debt-to-GDP decreasing to 73.5 percent. A trend reversal in the current account balance had started in recent months, as exports had expanded significantly, gas prices had moderated, and household consumption had adjusted. The higher-than-expected trade deficit in November had been mainly due to one-off factors. From 2023, increasing surplus in items of the current account excluding the energy balance, growing adjustment in the energy market and a decline in gas prices might lead to a rapid improvement. With the normalising global economic environment and terms of trade, as well as with the utilisation of new export capacities built recently, the trade balance would improve significantly, and as a result, the current account deficit was expected to be reduced further.

Following the review of macroeconomic and financial market developments, the Monetary Council discussed the details of its January monetary policy decision. Council members agreed that based on incoming data, economic growth had continued to slow in recent period. The volume of retail sales excluding fuel sales had declined in November, coupled with a slowdown in industrial production growth, while confidence indicators remained at low levels. In the context of real economic developments at the beginning of the year, several decision makers noted that real-time data also confirmed a further slowdown in economic growth. Some Council members pointed out that the high trade deficit in November was largely due to specific factors which were expected to be temporary and that looking ahead, the current account deficit may decline as a result of improving terms of trade, stronger energy market adjustment and newly built export capacities.

Regarding the outlook for inflation, Monetary Council members agreed that disinflationary effects were expected to become stronger in the coming months. Several Council members pointed out that lower global commodity prices and weaker electricity and gas consumption also pointed to a slowdown in price growth. In this context, some decision makers highlighted the moderating effects on pricing arising from the fall in domestic demand, as well as a decline in expectations for prices in the retail and services sectors. Assumed from the price declines observed in some sub-markets, many Council members indicated that a turnaround in the food market seemed to be underway, and was expected to fully materialize in the spring months. Based on these factors, the Council unanimously expected the decline in inflation to pick up in the second quarter of 2023 and to return to the single-digit range by the end of this year before easing back to the tolerance band in 2024.

Monetary Council members unanimously argued in favour of maintaining tight monetary conditions, stressing that the current level of the base rate was adequate to respond to fundamental inflation risks. Decision makers agreed that the Bank’s instruments introduced in the autumn to absorb interbank liquidity had successfully supported monetary policy transmission at the end of the year. Therefore, in order to further enhance the effectiveness of monetary policy transmission, members decided to raise the required reserve ratio to 10 percent and to continue to use the one-week discount bill and the long-term deposit tender regularly.

In addition to the significance of an effective monetary transmission mechanism, several decision makers drew attention to the key role of financial market stability and the risk perception regarding the Hungarian economy. Council members agreed that the Bank should continue to apply one-day deposit quick tenders and FX swap transactions announced in mid-October. Decision makers reiterated their earlier decision that the Bank would meet foreign currency liquidity needs to reach market balance related to the energy account. In reviewing the factors affecting Hungary’s risk perceptions, several decision makers indicated that, despite recent improving trends, the impact of the further tightening by the world’s leading central banks on emerging economies, the consequences of the Russia-Ukraine war, the uncertainty surrounding the details of the agreement between the EU and Hungary, the current account deficit and the volatile financial market environment continued to pose risks. Council members agreed that the Bank should maintain the current terms of its instruments, introduced in mid-October, until a trend improvement occurred in risk perceptions.

The Monetary Council kept the base rate at 13 percent at its meeting on 24 January. The current level of the base rate was adequate to manage fundamental inflation risks. The O/N deposit rate and the O/N collateralised borrowing rate were left unchanged at 12.5 percent and 25 percent, respectively.

Using its instruments introduced in the autumn to absorb interbank liquidity on a long-term basis, i.e. the revised reserve requirement system, the one-week discount bill and the long-term deposit tender, the MNB had strongly supported the maintenance of the effectiveness of monetary policy transmission over the year-end period. Based on this positive experience, the MNB would use these instruments regularly in the coming period. Accordingly, the Bank would hold its long-term deposit tender on 25 January, and from 1 February discount bill auctions would be held on a weekly basis. In addition to strengthening monetary policy transmission, the Bank would continue to use one-day deposit quick tenders and FX swap transactions to ensure financial market stability, and it would continue to meet foreign currency liquidity needs in the coming months to reach market balance related to the energy account.

The Monetary Council was constantly assessing incoming data and developments in the outlook for inflation and was ready to take appropriate actions if risks increase. Looking ahead, maintaining market stability and strengthening monetary policy transmission were also key to achieving price stability. The MNB still focused on sustained shifts in financial market conditions, and it would maintain the current terms of its instruments introduced in mid-October until a trend improvement in risk perceptions occurred. It was necessary to maintain tight monetary conditions over a prolonged period, which would ensure that inflation expectations were anchored and the inflation target was achieved in a sustainable manner.

Votes cast by individual members of the Council:

In favour of maintaining the base rate at 13.00 percent, **the overnight collateralised lending rate at 25.00 percent** **and** **maintaining the interest rate on the overnight central bank deposit at 12.50 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 28 February 2023. The minutes of that meeting will be published at 2 p.m. on 14 March 2023.