MINUTES OF THE MONETARY COUNCIL MEETING
20 JUNE 2023

Time of publication: 2 p.m. on 5 July 2023

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:
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.

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 reversal of energy prices due to supply and demand factors was mitigating the adverse effects of the energy crisis in Europe, which pointed to an improvement in the outlook for economic activity on the Continent. However, the ongoing Russia-Ukraine war and the persistently high inflation environment were posing downside risks to growth.

Global disinflation had continued. The slowdown in global economic activity, the correction in energy and commodity prices and the fall in international freight costs pointed to a continued decline in inflation rates. However, core inflation indicators, stuck at a high level, suggested that achieving price stability again might take longer than earlier expected.

Investor sentiment had worsened at the beginning of the period, before improving overall since the Monetary Council's last policy decision. Market turbulence, spilling over to Europe, had eased as the effects of US bank failures waned. In addition, volatility in global financial markets had decreased, mainly due to the conclusion of debates about the US debt ceiling. Oil prices had declined slightly amid high volatility, while European gas prices had risen over the past month. The uncertainty due to the Russia–Ukraine war continued to have a negative impact on investor sentiment.

The Federal Reserve (Fed) had kept the target range of the benchmark rate unchanged at its policy meeting in June, while the European Central Bank (ECB) had raised its key interest rate by 25 basis points. Based on market expectations, the Fed and the ECB were nearing the end of their tightening cycle; however, further interest rate hikes had been indicated by the two central banks until the end of the year.

In 2023 Q1, Hungary's GDP had declined by 0.9 percent. The performance of industry and construction had fallen significantly, which had been only partly offset by growth in agricultural output and public services. In April, industrial and construction output as well as the volume of retail sales had continued to decline. The household confidence indicator remained at a low level. The labour market remained tight, with the unemployment rate standing at 3.9 percent in April.

In 2023, decreasing real wages, rising corporate costs and cautious consumer and investment decisions all contributed to a decline in domestic demand, while net exports supported output growth. This year’s economic performance was also improved by the correction in agricultural growth after last year’s drought. 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.

In May, inflation had fallen at an increasing pace. Consumer prices had risen by 21.5 percent in annual terms, while they had fallen by 0.4 percent month-on-month, in contrast to the rise seen in recent years. Core inflation had stood at 22.8 percent. The consumer price index had decreased by 2.5 percentage points compared to April. Inflation had slowed across a wide range of products. Within core inflation, price dynamics had moderated in most product groups, with only the price index of market services continuing to rise, due to the increase in banking services prices. Inflation expectations of both households and companies had fallen.

In the coming months, domestic inflation and core inflation would continue to decrease at a rapid pace. During 2023, the disinflationary effect of tight monetary policy, falling global commodity prices, declining domestic consumption and the Government’s measures to strengthen market competition became increasingly apparent. Disinflation would continue to accelerate. As a result, inflation might reach single digits by the end of the year. Due to the significant increase in market services prices, core inflation might decrease at a slower pace. The inflation path expected for next year had shifted slightly upwards relative to March due to the Government’s tax measures, and thus the consumer price index might return to the central bank tolerance band in early 2025. Annual inflation might fluctuate between 16.5–18.5 percent in 2023, 3.5–5.5 percent in 2024 and 2.5–3.5 percent in 2025.

The fiscal deficit would continue to decline this year. The budget appropriation for the 2023 deficit was 3.9 percent. Based on the 2024 Budget Act, the accrual-based deficit target was 2.9 percent in 2024 and 1.9 percent in 2025. The government debt ratio was expected to fall from 73.3 percent at the end of 2022 to below 70 percent by the end of 2023, and then below 65 percent by the end of the forecast horizon, driven by economic growth and a declining deficit.

The external balance had continued to improve. In April 2023, the current account had been close to balance. The trend-like improvement in the external balance had been driven by a more favourable energy balance and terms of trade, the adjustment of domestic demand and dynamic export growth. This year, the current account deficit was expected to be more favourable than projected in March, being around 2-3 percent of GDP as the trade balance improved. In parallel with the utilisation of new export capacities built recently and a normalising global economic environment, in particular falling energy prices, trade balance and net lending would continue to improve in 2024.

The Monetary Council had highlighted three alternative scenarios around the baseline projection in the June Inflation Report. In the scenario presuming faster easing of supply constraints, the settlement of problems facing global supply chains and the decrease in energy and commodity prices would have a stronger impact on domestic production processes, resulting in a lower inflation and higher growth path. The scenario presenting persistently lower consumption was consistent with a lower growth and inflation path. The scenario assuming a persistent increase in inflation expectations presumed a higher inflation path and a somewhat lower growth path compared to the baseline scenario.

Following the review of macroeconomic and financial market developments as well as the latest Inflation Report projections, the Monetary Council discussed the details of its monetary policy decision in June. In the Council's assessment, the outlook for global growth continued to be characterised by duality. A turnaround in inflation in European countries had become common; however, some Council members highlighted that a slow decline in core inflation indicators pointed to prolonged disinflation.

In assessing May inflation data, Monetary Council members concluded that inflation was declining at an increasing pace. Some members pointed out that monthly repricings were well below the historical average. Some decision makers added that inflation had slowed across a wide range of products and prices had fallen in nearly 40 percent of the total consumer basket month-on-month. Members stressed that according to the latest forecast of the Inflation Report, inflation was expected to fall noticeably below 10 percent by the end of 2023. Accelerating disinflation might trigger GDP growth from the second half of the year. However, the Council agreed that the inflation path expected for next year had shifted upwards relative to March due to the 2024 tax measures. As a result, the consumer price index was expected to return to the central bank tolerance band in early 2025. However, this baseline scenario was accompanied by a slight increase in downside risks to inflation based on the alternative risk scenarios identified by the Council.

Discussing domestic real economic developments, the Monetary Council concluded that in 2023, cautious consumer and investment decisions contributed to a decline in domestic demand in addition to decreasing real wages and rising corporate costs, while net exports supported economic growth. Several decision makers noted that from 2024 onwards, components of domestic demand were also likely to support output growth. Decision makers agreed that the current account deficit was expected to fall significantly this year, and would be around 2-3 percent of GDP as the trade balance improved.

In the members' assessment, by its instruments introduced in mid-October 2022, the MNB had succeeded in ensuring financial market stability, and the risk environment had improved persistently and significantly since then. Nevertheless, decision makers underlined that persisting risks, i.e., the evolution of energy and gas prices, the expectations for the interest rate paths of the Fed and the ECB, and the uncertainties caused by the Russia-Ukraine war, warranted a cautious and gradual approach in monetary policy. The persistence of improvements in risk perceptions had to be assessed carefully.

The Monetary Council was in full agreement that it was necessary to maintain tight monetary conditions in order to achieve price stability; therefore, there was a strong consensus in favour of leaving the base rate at its level at that time. It was noted that there was no reason to apply changes in the coming months. Council members agreed that, at 13 percent, the level of the base rate would ensure that inflation expectations were anchored and the inflation target was achieved in a sustainable manner.

In the decision makers' assessment, the risk environment remained favourable, which enabled the Bank to continue the normalisation of the interest rates. Accordingly, the Council unanimously decided to reduce the upper bound of the interest rate corridor and the interest rate remunerated on optional reserves by 100 basis points to 18.5 percent and 16 percent, respectively. Council members were in consensus that it was also warranted to reduce the interest rate on one-day quick deposit tenders and foreign exchange swap tenders by 100 basis points. The normalisation of interest rate conditions needed to be implemented depending on the improvement of the risk environment, which the Monetary Council would continuously consider at the next policy meetings. The Monetary Council agreed unanimously that maintaining financial market stability was key to achieving price stability.

In the Monetary Council's assessment, it was necessary to maintain tight monetary conditions in order to achieve price stability. At its meeting on 20 June 2023, the Council left the base rate unchanged at 13 percent. The base rate's level at that time was adequate to manage fundamental inflation risks.

In the Monetary Council's assessment, the still favourable risk environment had enabled the Bank to continue the normalisation of the interest rate environment. In accordance, the Council had decided to reduce the interest paid on optional reserves by 100 basis points, from 17 to 16 percent at its June meeting, with effect from 21 June. In addition, the O/N collateralised lending rate serving as the top of the interest rate corridor had been lowered by 100 basis points to 18.5 percent. According to the Council's assessment, it was also warranted to reduce the interest rate on the one-day quick deposit tenders and foreign exchange swap tenders by 100 basis points.

In the Monetary Council's assessment, looking ahead, strengthening monetary policy transmission was also an important factor of achieving price stability. For this reason, the Bank would use the instruments to absorb interbank forint liquidity on a long-term basis in the coming period.

In the Monetary Council's assessment, maintaining the current level of the base rate would ensure that inflation expectations were anchored and the inflation target was achieved in a sustainable manner. Looking ahead, financial market stability was also key to achieving price stability. In the current environment, a cautious and gradual approach was warranted. The MNB was constantly assessing the effects of international financial market developments on the domestic risk environment, incoming macroeconomic data and developments in the outlook for inflation. If the improvement in risk perceptions persists, the Bank would continue the gradual convergence of the interest rate conditions of one-day tenders to the base rate.

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 18.50 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 25 July 2023. The minutes of that meeting will be published at 2 p.m. on 9 August 2023.