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Deputy Governor | Magyar Nemzeti Bank

# BACKGROUND DISCUSSION FOLLOWING THE MONETARY COUNCIL'S 27 AUGUST 2024 DECISION

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Analyst background discussion

27 August 2024



## KEY MESSAGES:

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- **In July, inflation was at the higher end of our forecast range, while core inflation was in line with our expectations.**
  - The surprise was mainly driven by food prices; however, our longer-term outlook for inflation has remained unchanged. Inflation will return to the tolerance band in the coming months, the disinflationary trend in underlying processes is expected to continue in 2025 Q1.
  - Inflation casts a long shadow: Expectations must be anchored at the inflation target again.
- **In 2024 Q2, economic recovery stalled.**
  - External demand – especially by Hungary’s European export partners – has remained persistently weak.
  - Consumer and business investment confidence are improving slowly.
- **Our current account position improved significantly in the first half of 2024.**
- **The government balance was in a surplus in July, the attainability of the 4.5 percent deficit target has improved.**
- The appropriate management of the economic-psychological factors is key to the outlook for both inflation and the real economy.

**STABILITY, SECURITY AND TRUST ARE NEEDED!**



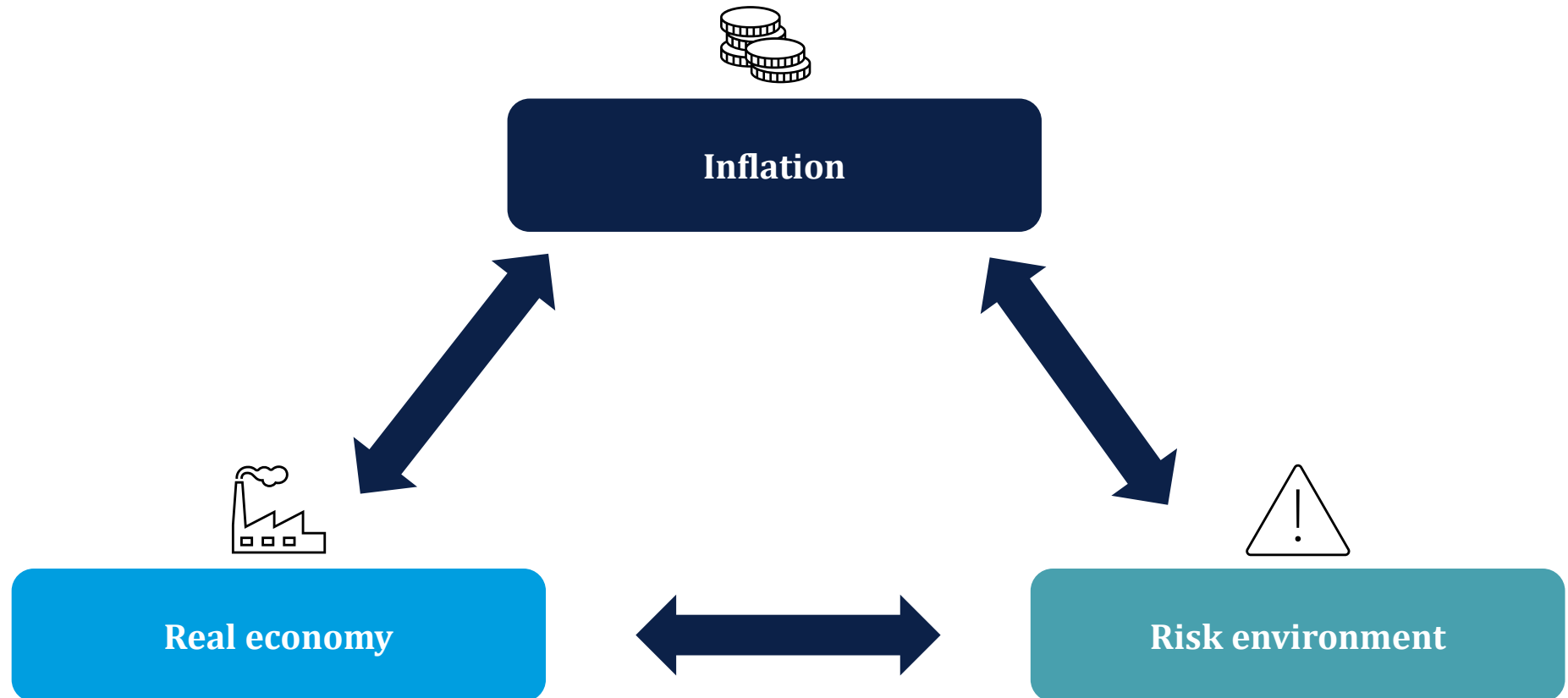
## KEY MESSAGES: MONETARY POLICY DECISION IN AUGUST

- Volatile financial market developments, the renewed increase in geopolitical tensions and the risks to the outlook for inflation continue to warrant a careful and patient approach.
- Reducing inflation expectations further and preserving financial market stability remain key to achieving price stability again and restoring the sustainable growth path of the domestic economy.
- In line with its stability-oriented approach to monetary policy, at its meeting today the Monetary Council decided to temporarily pause interest rate reductions and left the base rate unchanged at 6.75 percent.
- There may be scope for cautiously lowering interest rate conditions further in the coming period. The decisive factors for September's policy decision will be:
  - August inflation data,
  - the decisions of major central banks in September,
  - Hungary's risk perception,
  - and trends in consumer as well as business confidence.
- **We cannot sit back: a careful and patient monetary policy** remains warranted.





## THE MONETARY COUNCIL'S ASSESSMENT THAT INFORMS ITS DECISION FOCUSES ON THREE MAIN AREAS



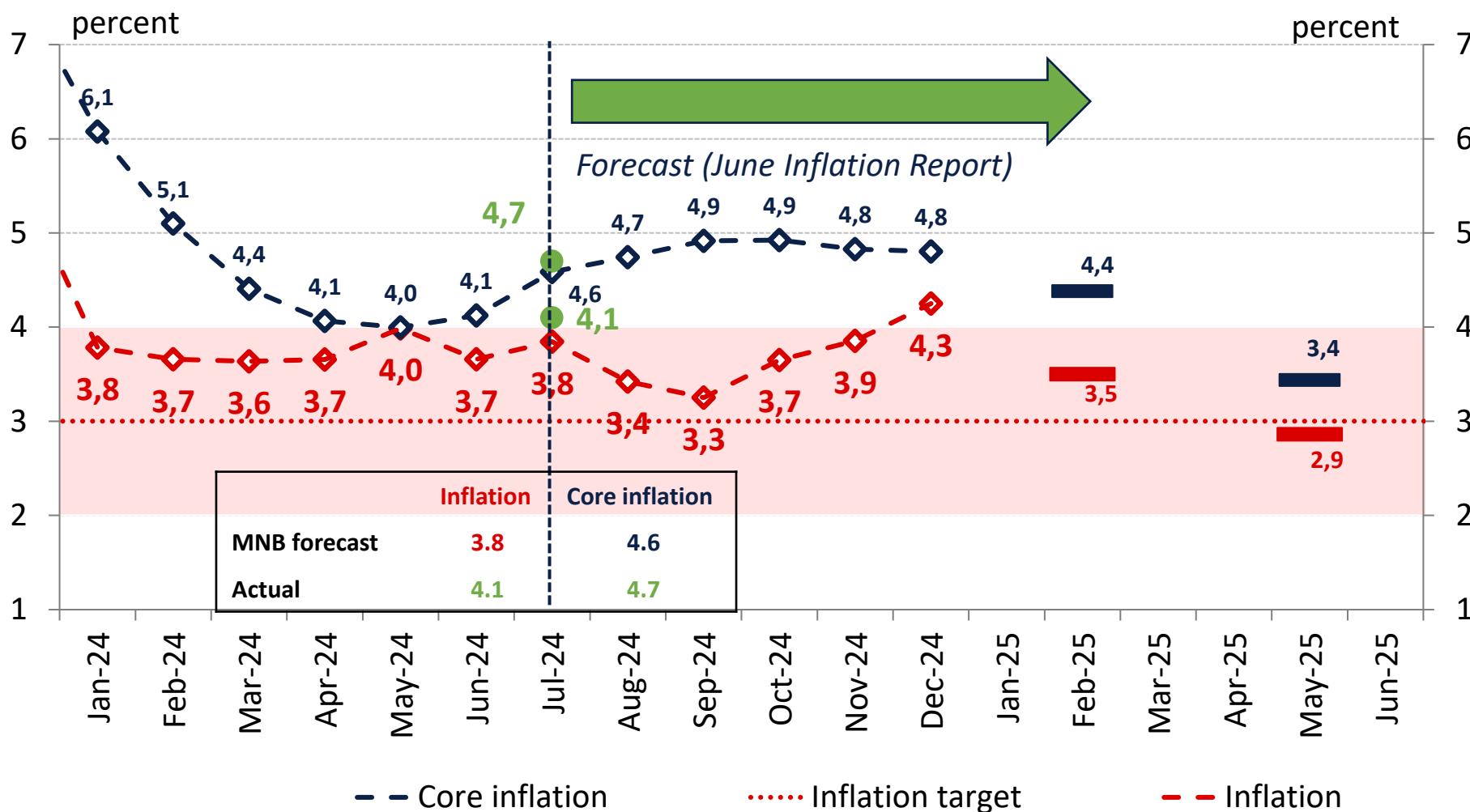


# INFLATION ASSESSMENT





## INFLATION EXCEEDED EXPECTATIONS IN JULY, WHILE LEAVING THE TOLERANCE BAND AGAIN



### DEVELOPMENTS IN INFLATION AND CORE INFLATION IN THE RECENT PERIOD

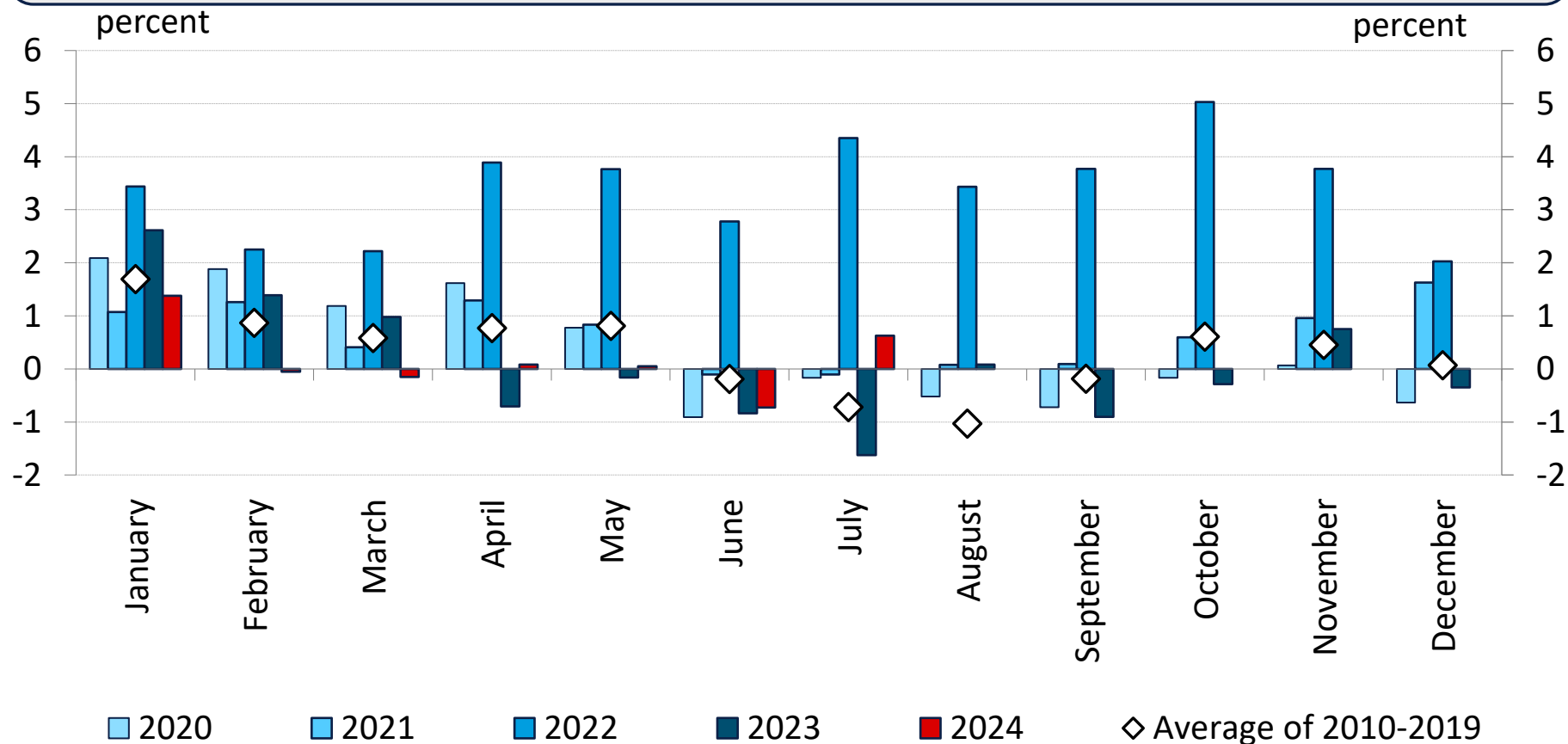
Note | The inflation projections for 2025 are shown as quarterly averages.

Source | HCSO, MNB



## FOOD PRICES HAVE INCREASED INSTEAD OF DECREASING AS USUAL DURING THE SEASON

However, this may have been influenced by the discontinuation of mandatory discounts and consumer prices linked to the purchase price of certain basic food items on 1 July.



### DEVELOPMENTS IN MONTHLY PRICE CHANGES IN FOOD PRICES

Note | Tax-adjusted, not seasonally adjusted monthly change.

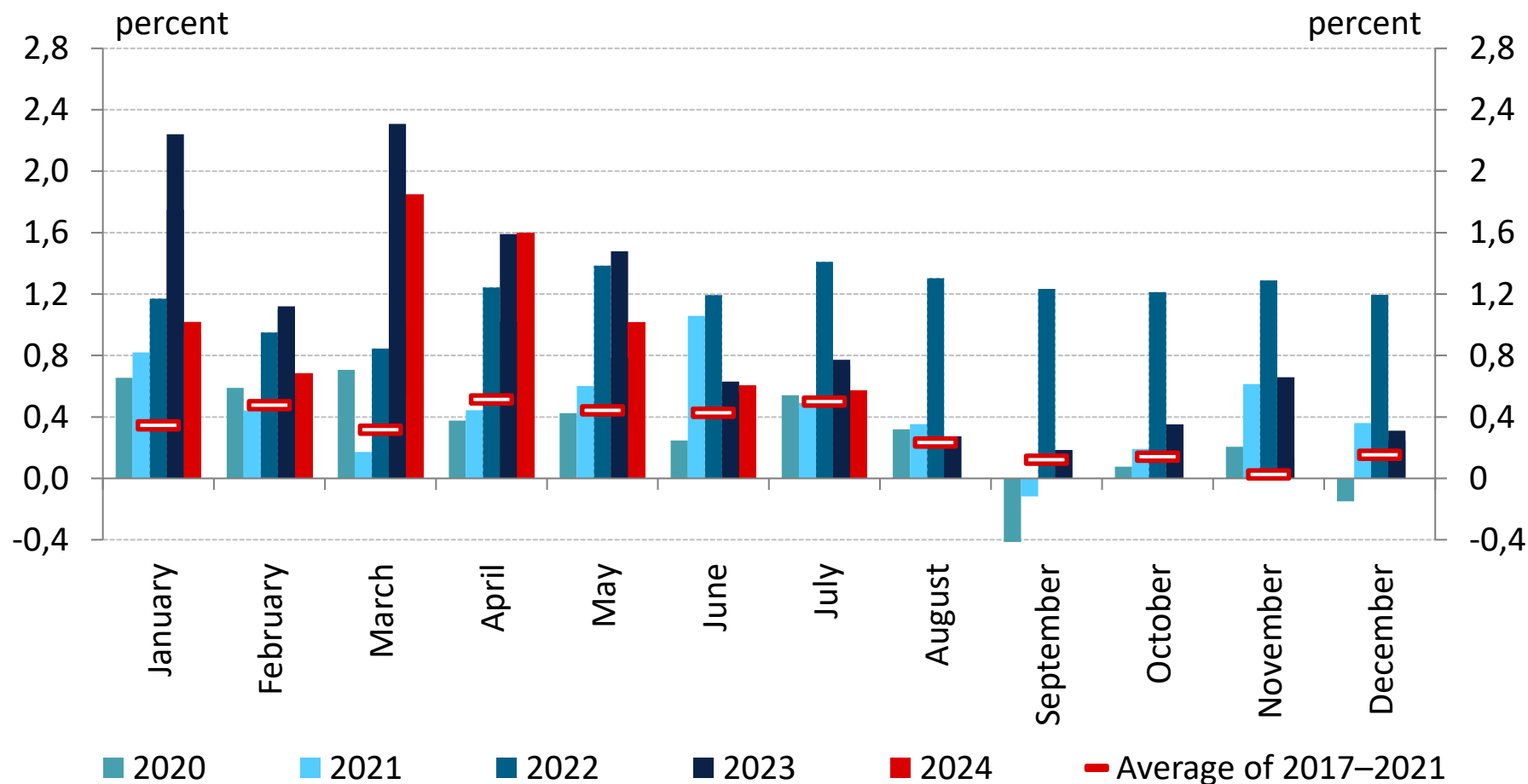
Source | HCSO, MNB





## MONTHLY REPRICING OF MARKET SERVICES HAS MATCHED HISTORICAL LEVELS...

...however, the processes still need to be monitored closely.



### MONTHLY PRICE CHANGES IN MARKET SERVICES

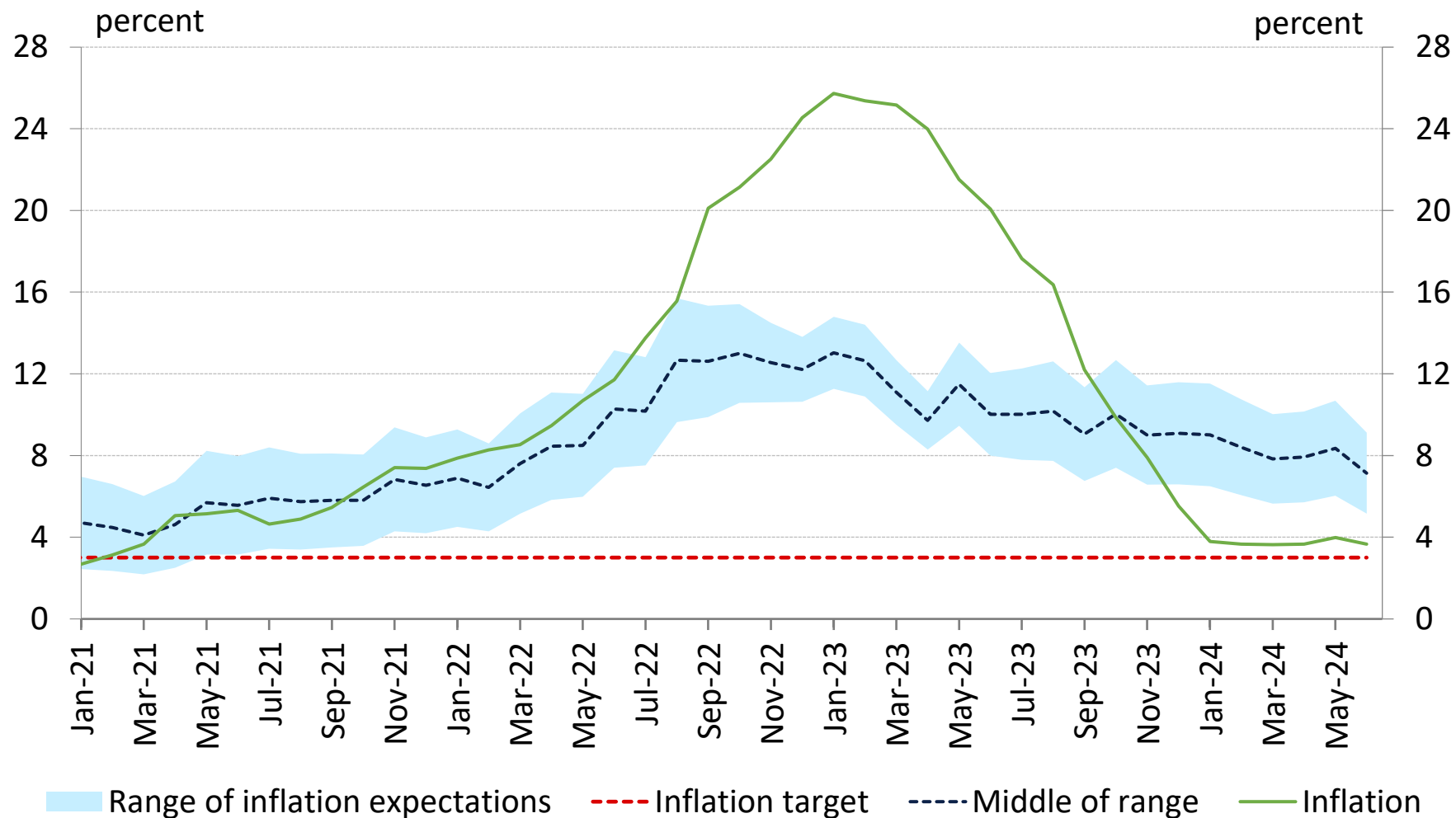
Note | Tax-adjusted, not seasonally adjusted monthly change.

Source | HCSO, MNB





## INFLATION CASTS A LONG SHADOW: EXPECTATIONS MUST BE ANCHORED AT THE INFLATION TARGET AGAIN

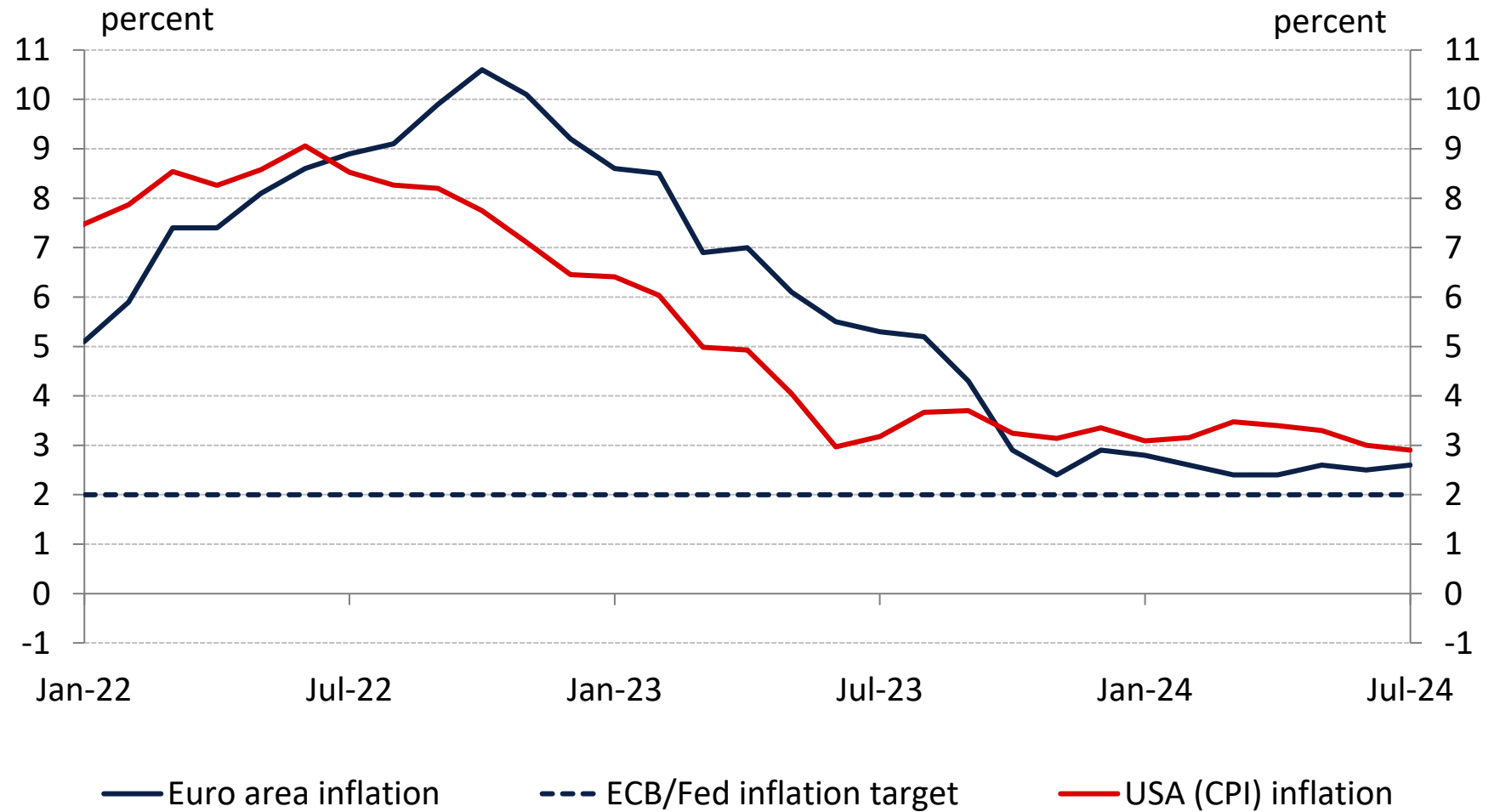


### DOMESTIC INFLATION EXPECTATIONS IN HUNGARY

Source | MNB calculation based on European Commission data



## THE DISINFLATION PROCESS HAS SLOWED DOWN IN DEVELOPED ECONOMIES

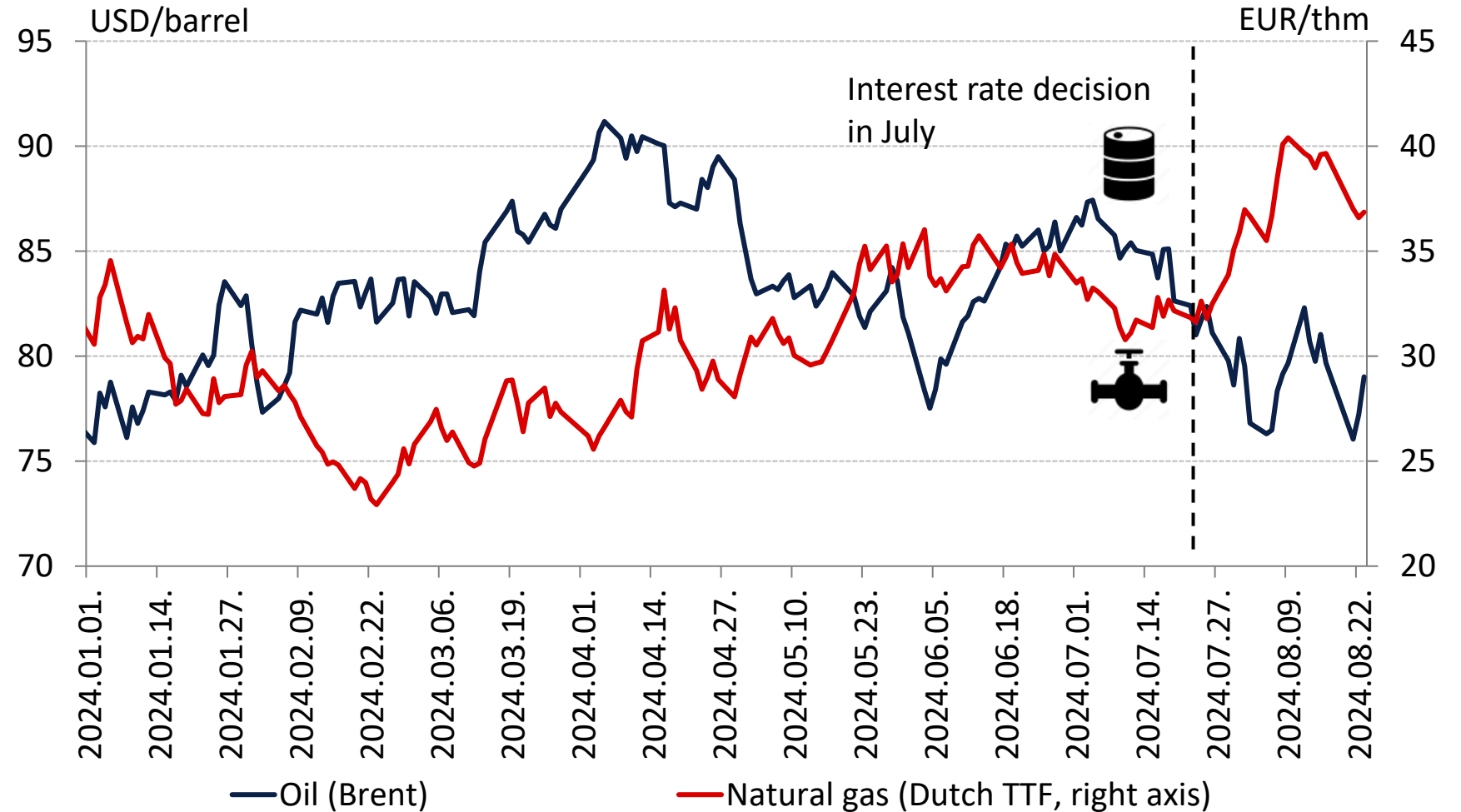


### INFLATION IN THE UNITED STATES AND THE EURO AREA

Source | Eurostat, OECD



## SINCE THE LATEST INTEREST RATE DECISION, OIL PRICES HAVE FALLEN SLIGHTLY, WHILE GAS PRICES HAVE RISEN



### DEVELOPMENTS IN OIL AND GAS PRICES

Source | Bloomberg, MNB



## A CAUTIOUS ASSESSMENT OF INFLATION OUTLOOK IS NECESSARY



**In July, inflation exceeded expectations and left the tolerance band, while core inflation, which captures underlying developments, continued to rise.**



**The inflation rate is expected to return to the tolerance band in the coming months. The August inflation data will be of great importance in terms of evaluating the inflation outlook.**



**The decline in inflation expectations turned out to be a protracted process, expectations must be anchored again on the inflation target.**

**Anchoring inflation expectations, preserving financial market stability and a disciplined monetary policy are crucial for the consumer price index to return to the central bank target in a sustained manner from next year onwards.**



# REAL ECONOMIC ASSESSMENT





## ECONOMIC ACTIVITY IN EUROPE HAS BEEN WEAK OVERALL IN Q2

**Euro area**  
0.6

↓ **Below expectations**

↔ **Matching expectations**

↑ **Above expectations**

**United States**  
3.1

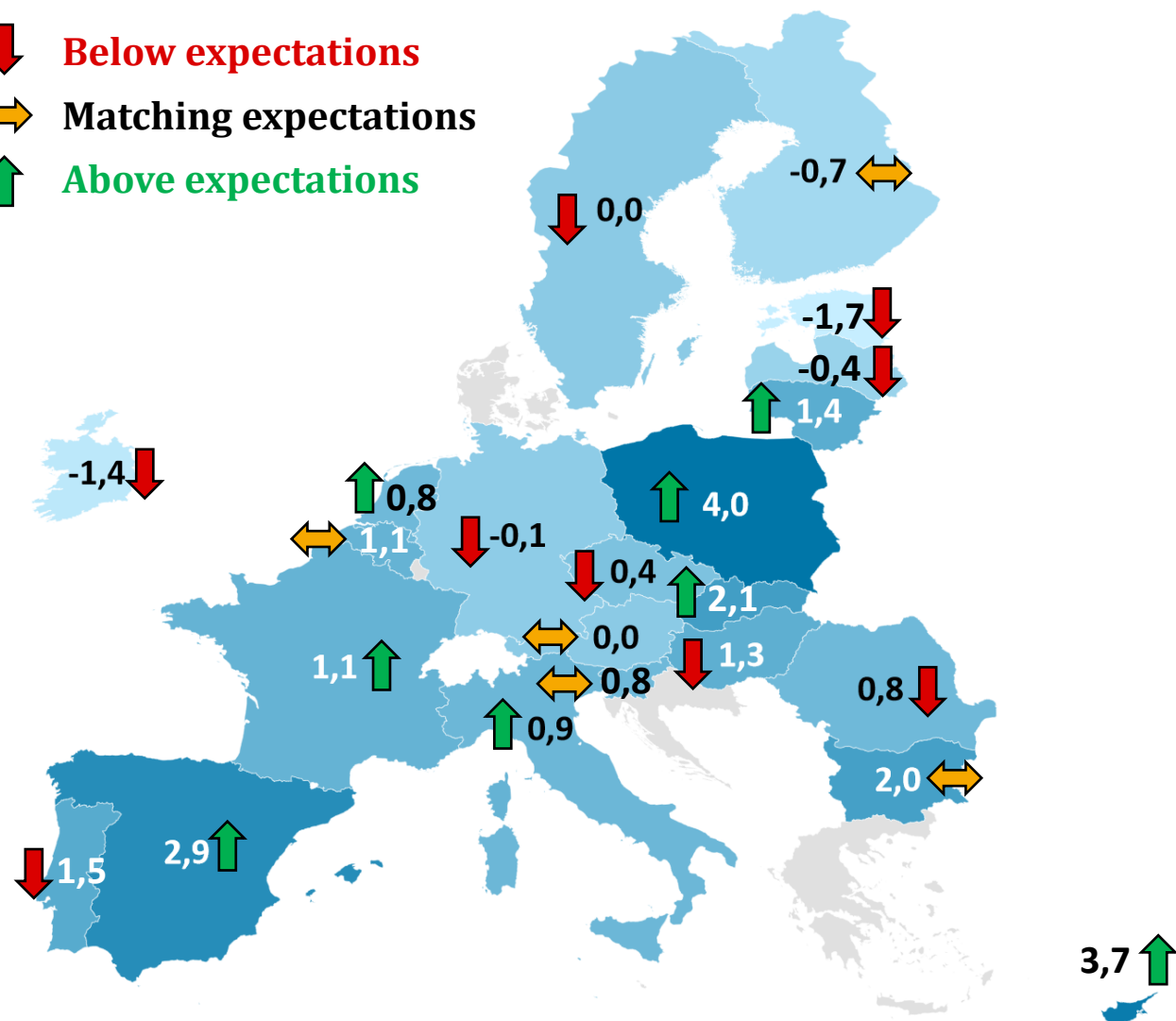
**China**  
4.7

**Core countries**  
0.3

**Northern countries**  
-0.4

**Mediterranean region**  
2.3

**Regional countries**  
1.8



### ANNUAL CHANGE IN GDP IN 2024 Q2

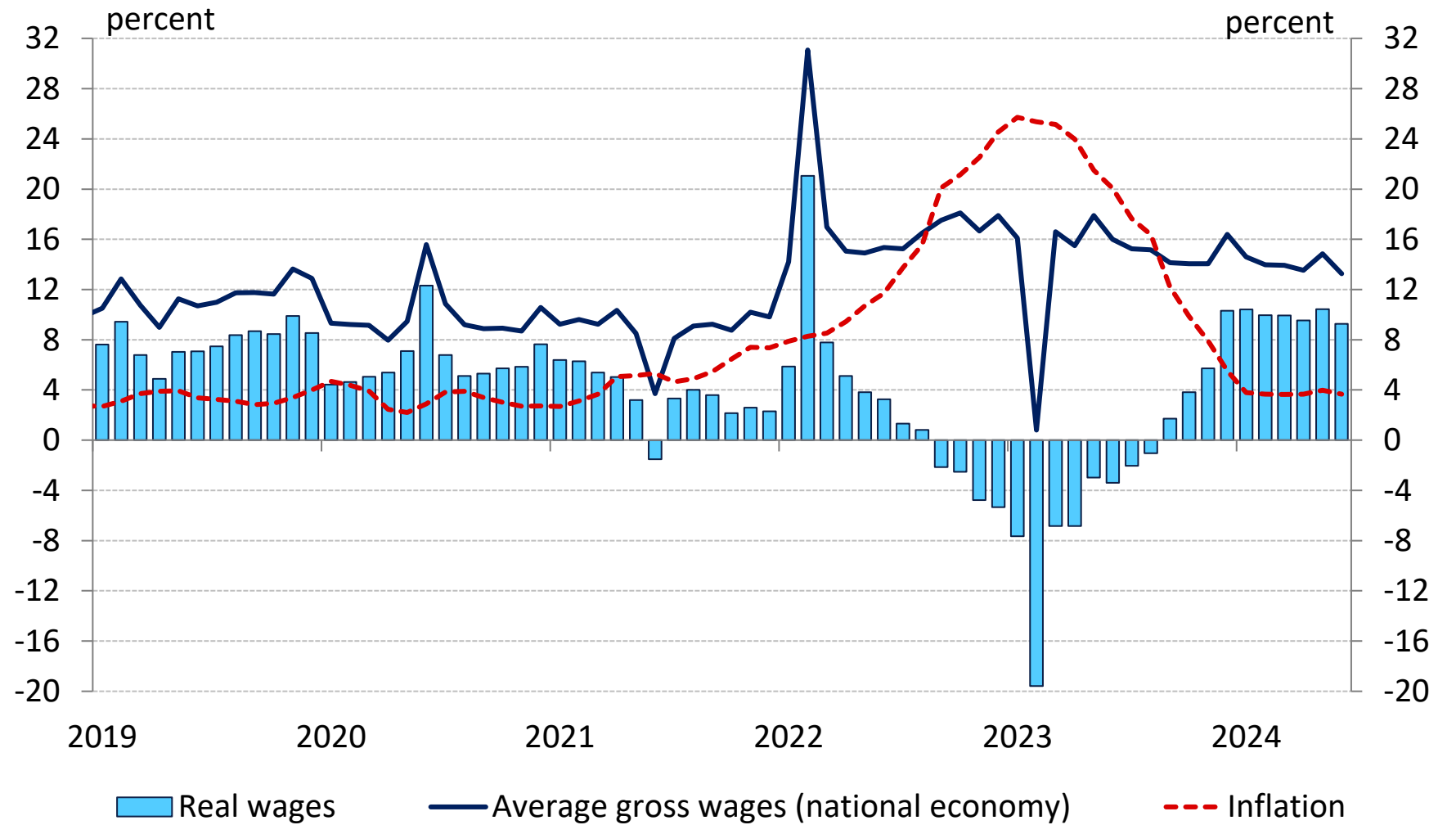
Note | Based on seasonally and calendar adjusted data. „Regional countries” consists of Poland, Slovakia, Czechia and Romania.

Source | Eurostat, Trading Economics, Bloomberg





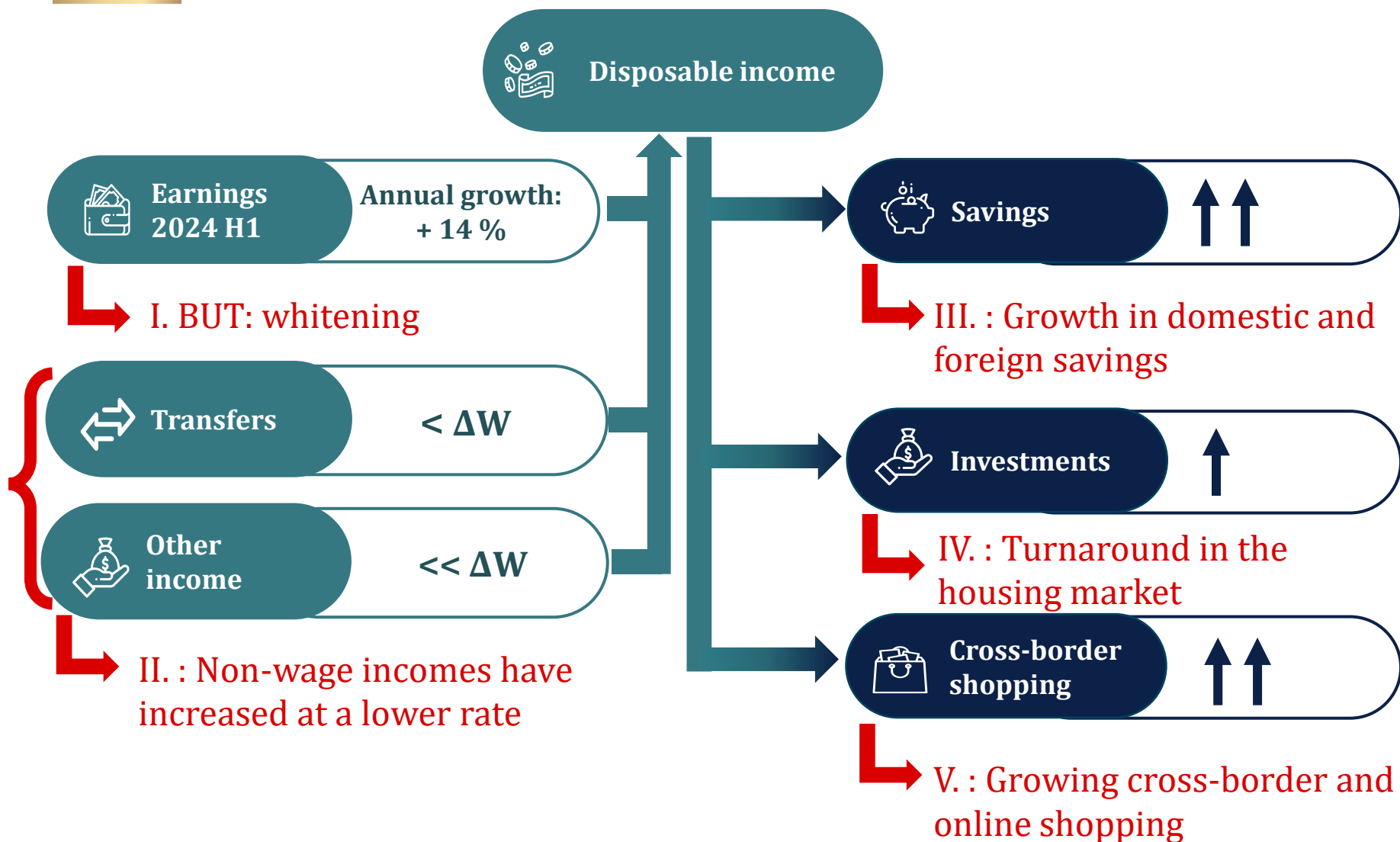
## THE LABOUR MARKET IS STRONG, WE CAN STILL SEE A DYNAMIC GROWTH IN REAL WAGES



### DEVELOPMENTS IN REAL WAGES IN THE NATIONAL ECONOMY

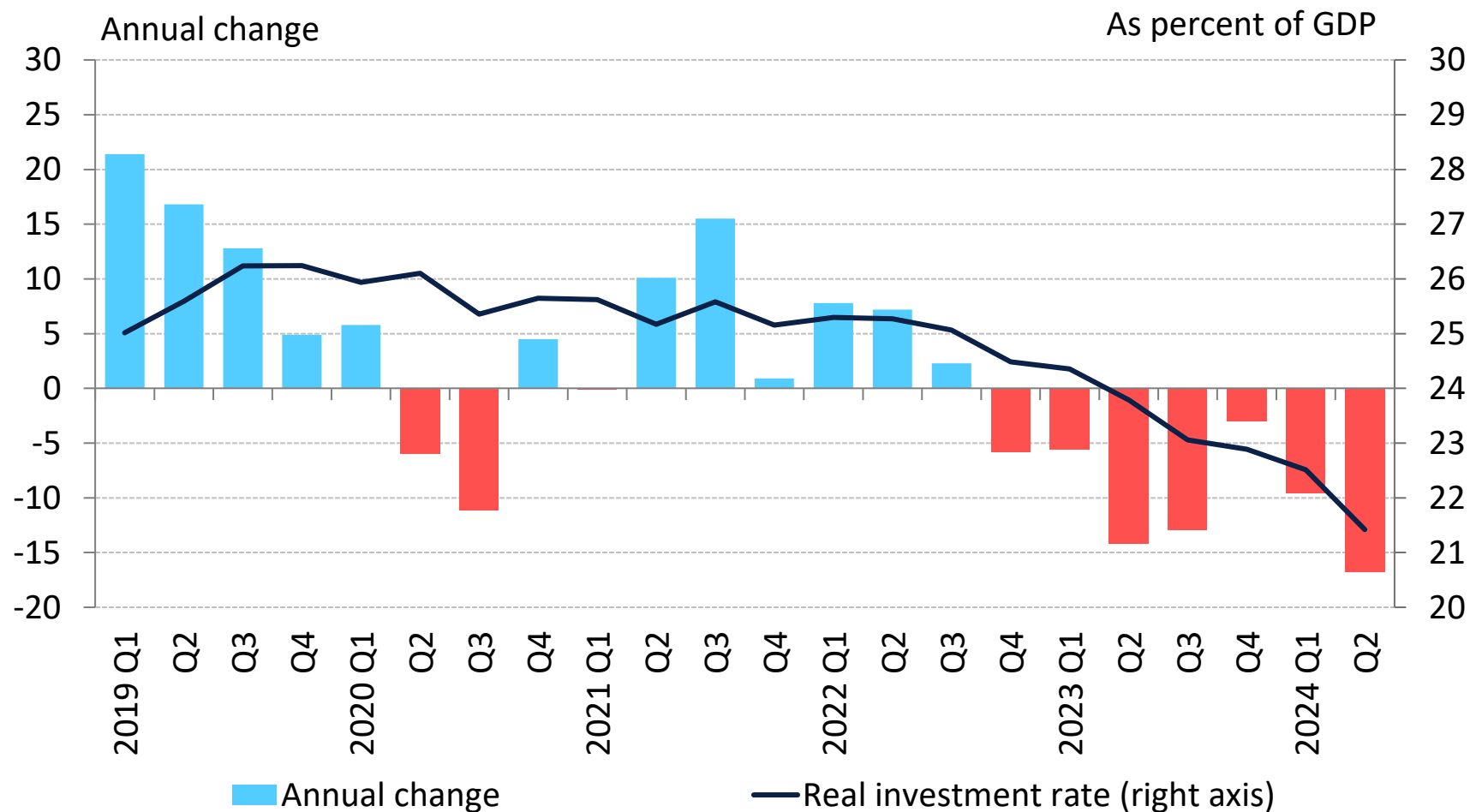
Source | HCSO

# INCOME GROWTH IS SLOWER THAN WAGE GROWTH, PART OF EXCESS INCOME IS NOT REALISED IN EITHER DOMESTIC CONSUMPTION OR SAVINGS





## INVESTMENTS ARE CHARACTERISED BY A WAIT-AND-SEE APPROACH



### THE LEVEL OF INVESTMENTS IN THE NATIONAL ECONOMY AND ITS ANNUAL VOLUME CHANGE

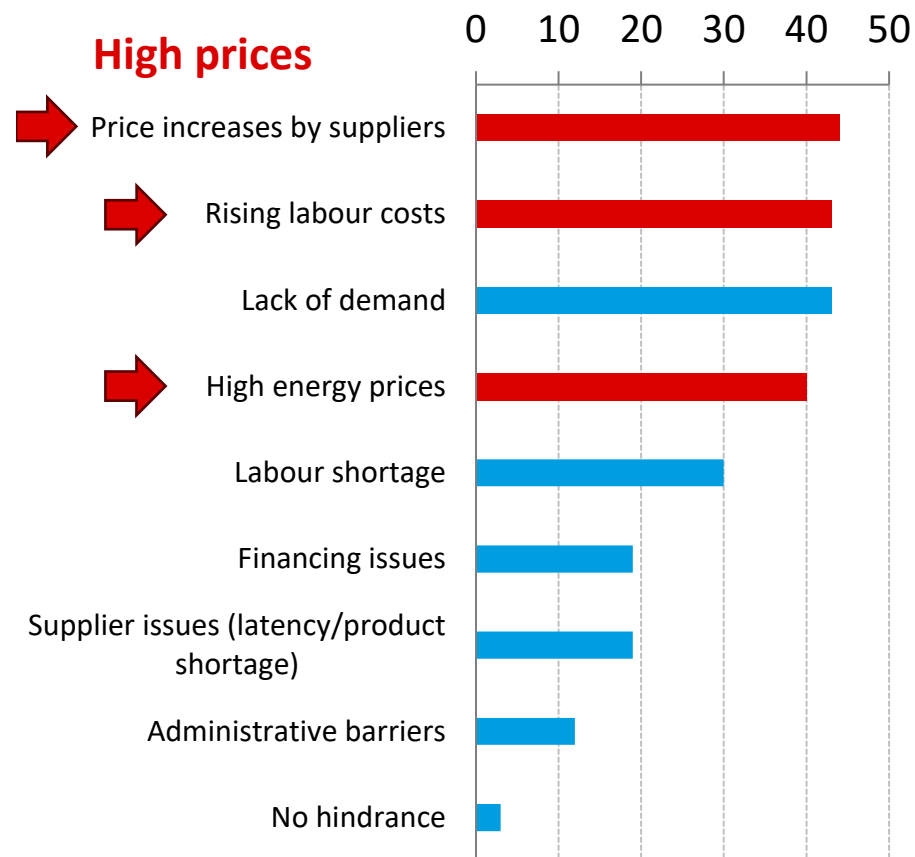
Note | Average of all quarters in 2021=100. Levels based on seasonally and calendar adjusted data.

Source | HCSO, MNB



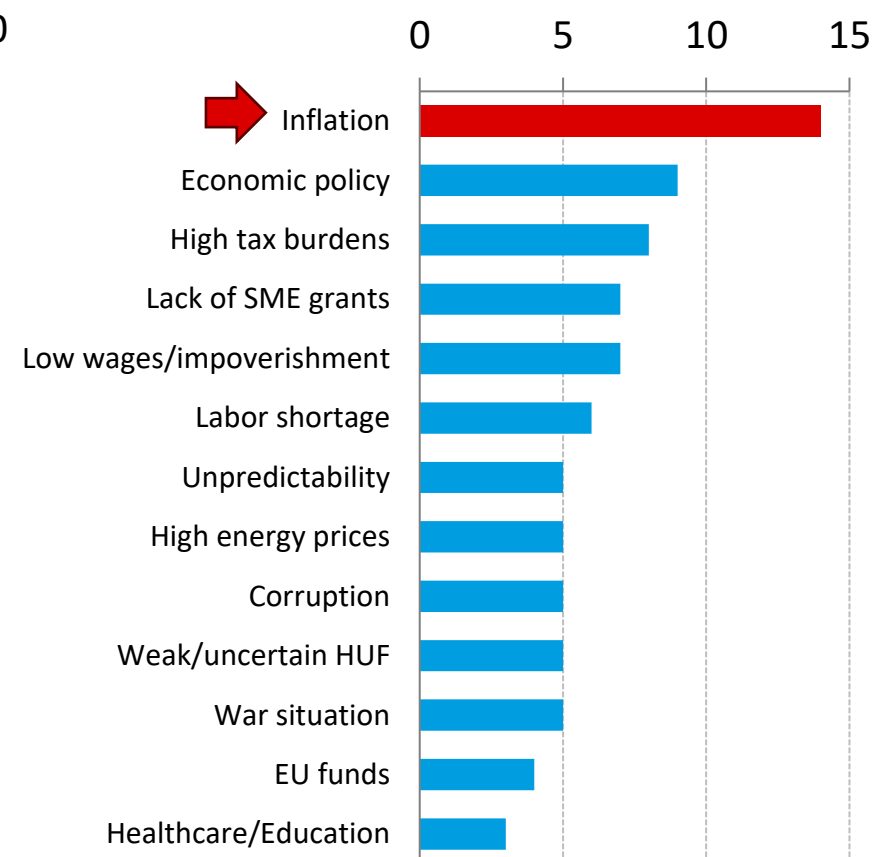


# THE BUSINESS ACTIVITY OF COMPANIES CONTINUES TO BE HINDERED BY THE LONG SHADOW OF INFLATION AND BY UNCERTAINTY



FACTORS LIMITING BUSINESS ACTIVITY OF COMPANIES

Source | MNB



MAIN ISSUES OF THE ECONOMIC SITUATION IN THE COUNTRY IN 2024 Q2

Source | National Association of Entrepreneurs and Employers (VOSZ)

## STRENGTHENING OF CONFIDENCE IS NECESSARY FOR GROWTH TO RESTART



**In recent months, the strong real wage growth has been maintained, and consumption has also started to recover.**



**At the same time, caution is still strong among both the households and companies, which is also reflected in the developments of savings and investments.**



**European economic activity was subdued in the second quarter as well. The moderate European economy poses risks for domestic growth as well.**

**In the current macroeconomic environment, the Bank can make the most effective contribution to the easing of economic agents' increased precaution and to the restart of economic growth by achieving price stability and maintaining financial market stability.**



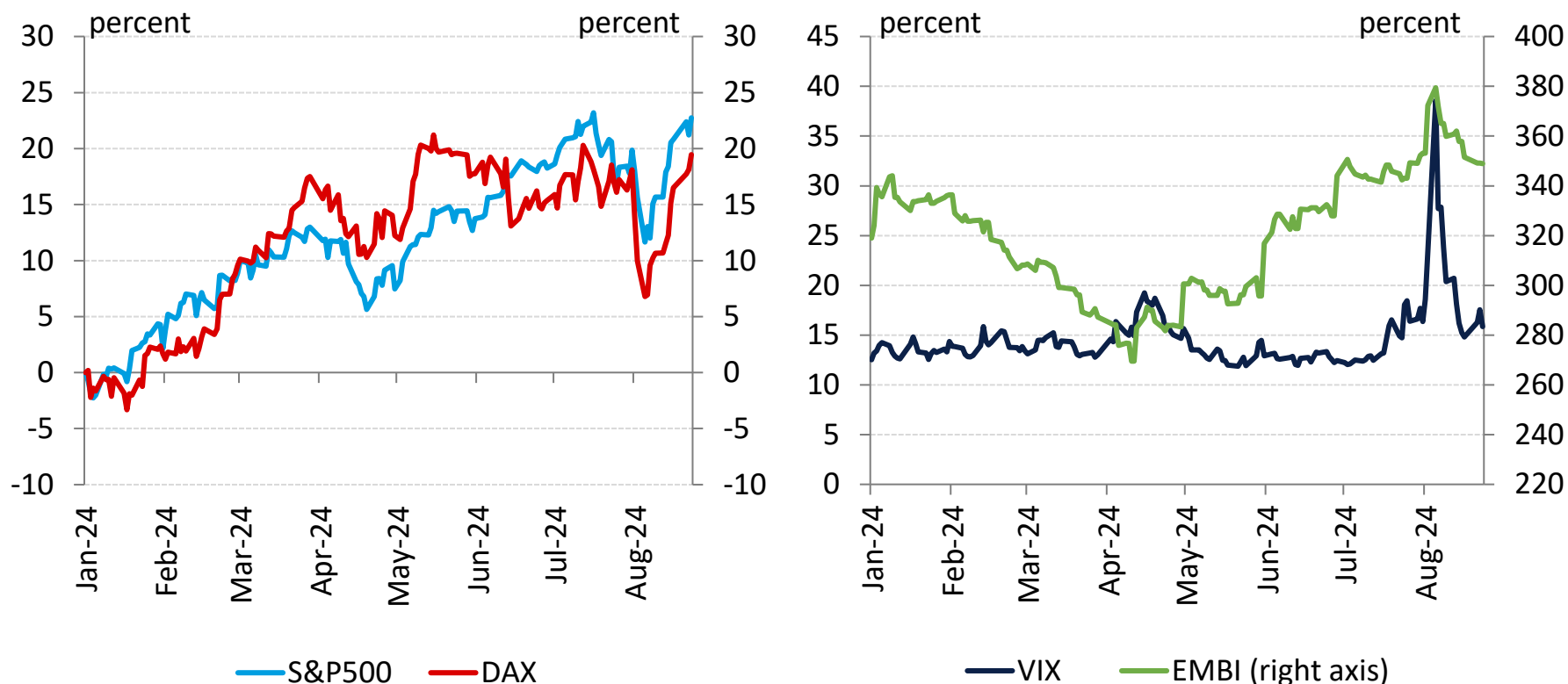
# DEVELOPMENTS IN THE RISK ENVIRONMENT





## AT THE BEGINNING OF AUGUST, VOLATILITY IN INTERNATIONAL FINANCIAL MARKETS HAS INCREASED DUE TO UNCERTAINTY RELATED TO THE ECONOMIC OUTLOOK IN THE UNITED STATES

As a result of a concentrated liquidation of yen positions, the tightening by the Bank of Japan has also resulted in strong spillover effects. However, since mid-August, a correction in risk indicators has taken place.



### DEVELOPMENTS IN AMERICAN AND GERMAN STOCK INDICES, CAPITAL MARKET VOLATILITY (VIX) AND THE EMERGING MARKET BOND INDEX (EMBI GLOBAL)

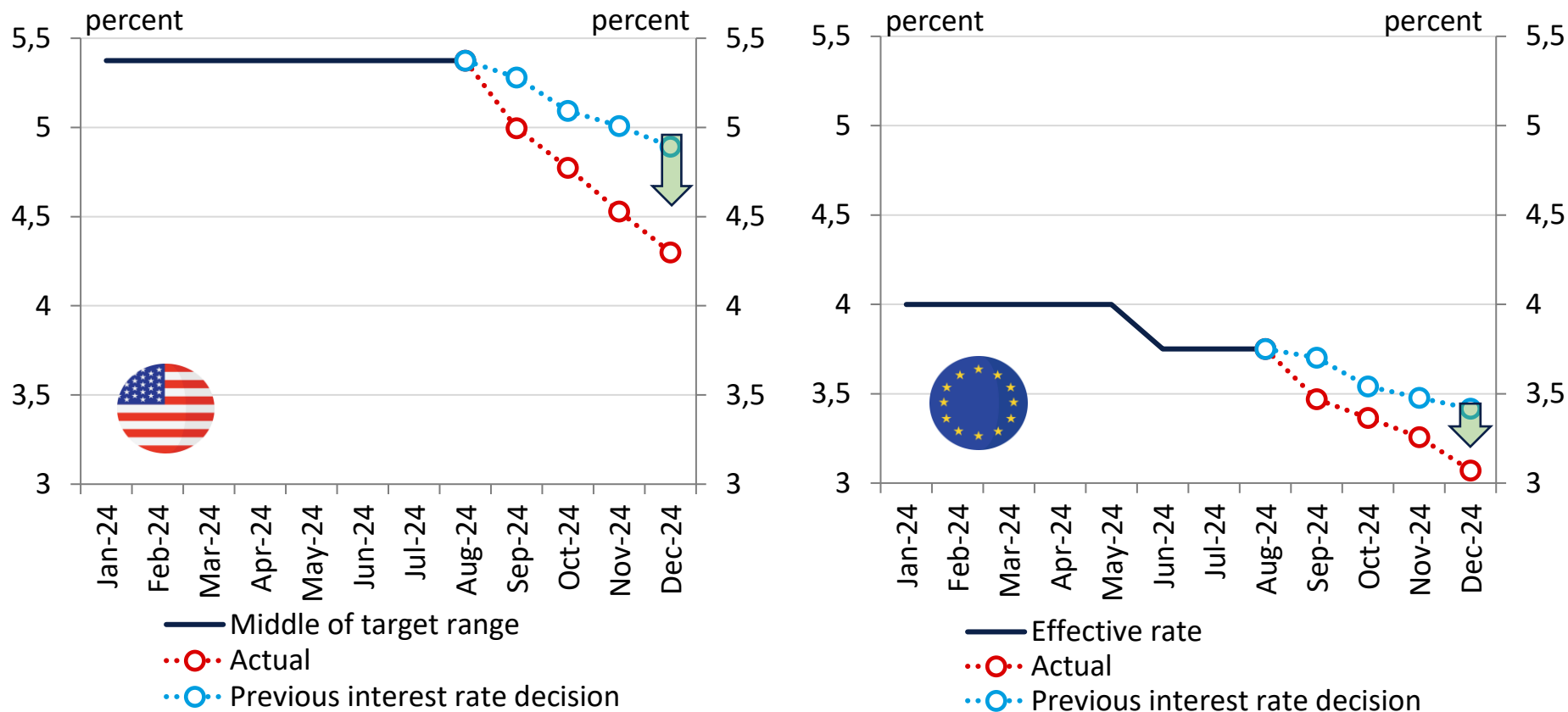
Note | S&P500 and DAX normed to 2 January 2024.

Source | Bloomberg



## THE EXPECTED INTEREST RATE PATHS OF THE FED AND THE ECB HAVE SHIFTED DOWNWARD

Based on market pricing, the ECB may lower interest rates further by 25 basis points three times and the Fed may lower interest rates by a total of 100 basis points until the end of the year.



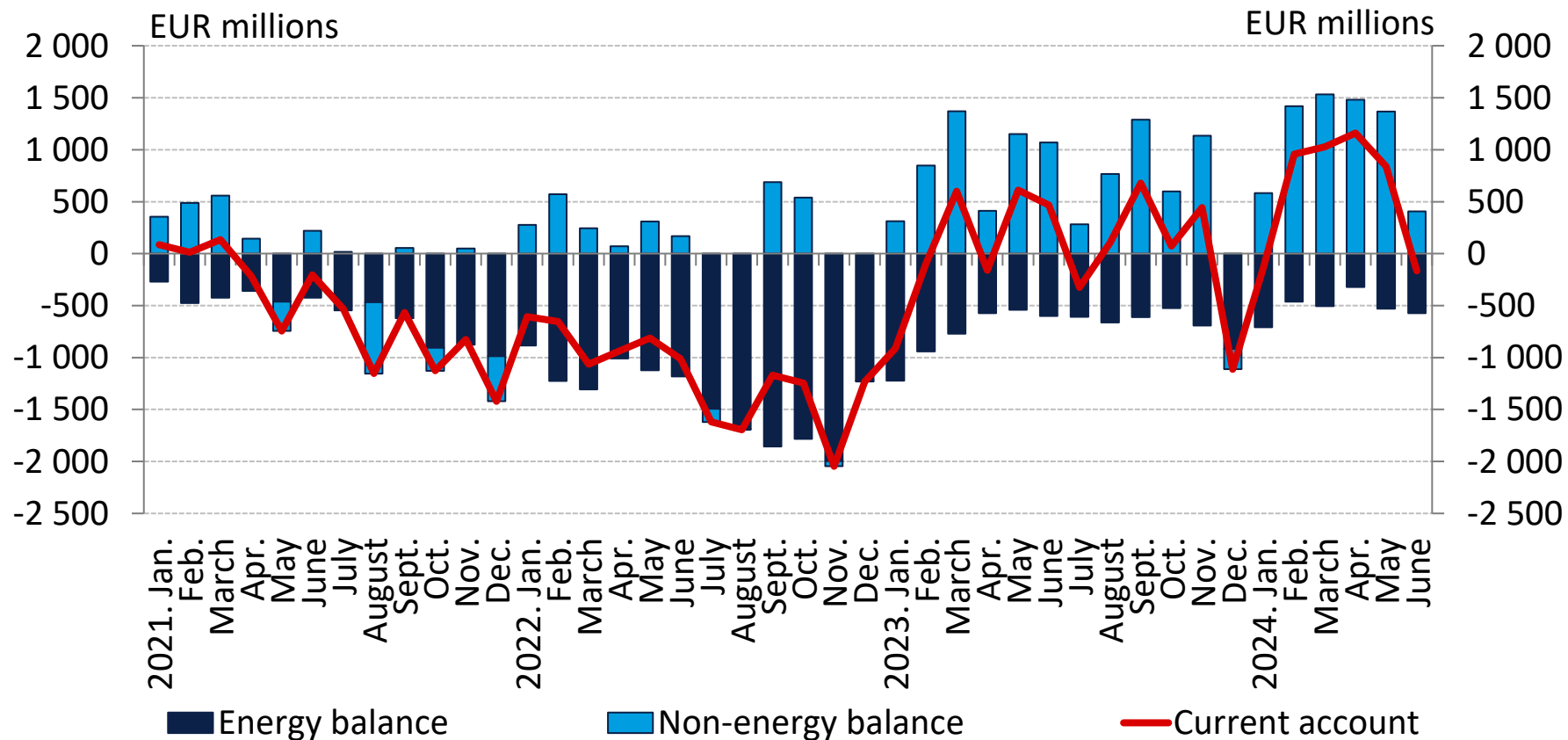
### THE EXPECTED INTEREST RATE PATH OF THE FED AND THE ECB BASED ON MARKET PRICING

Source | Bloomberg, MNB



## OVERALL, THE EXTERNAL BALANCE POSITION IMPROVED SIGNIFICANTLY IN THE FIRST HALF OF 2024

The current account registered a surplus of nearly EUR 3.7 billion in the first six months of the year. However, the balance decreased in June.

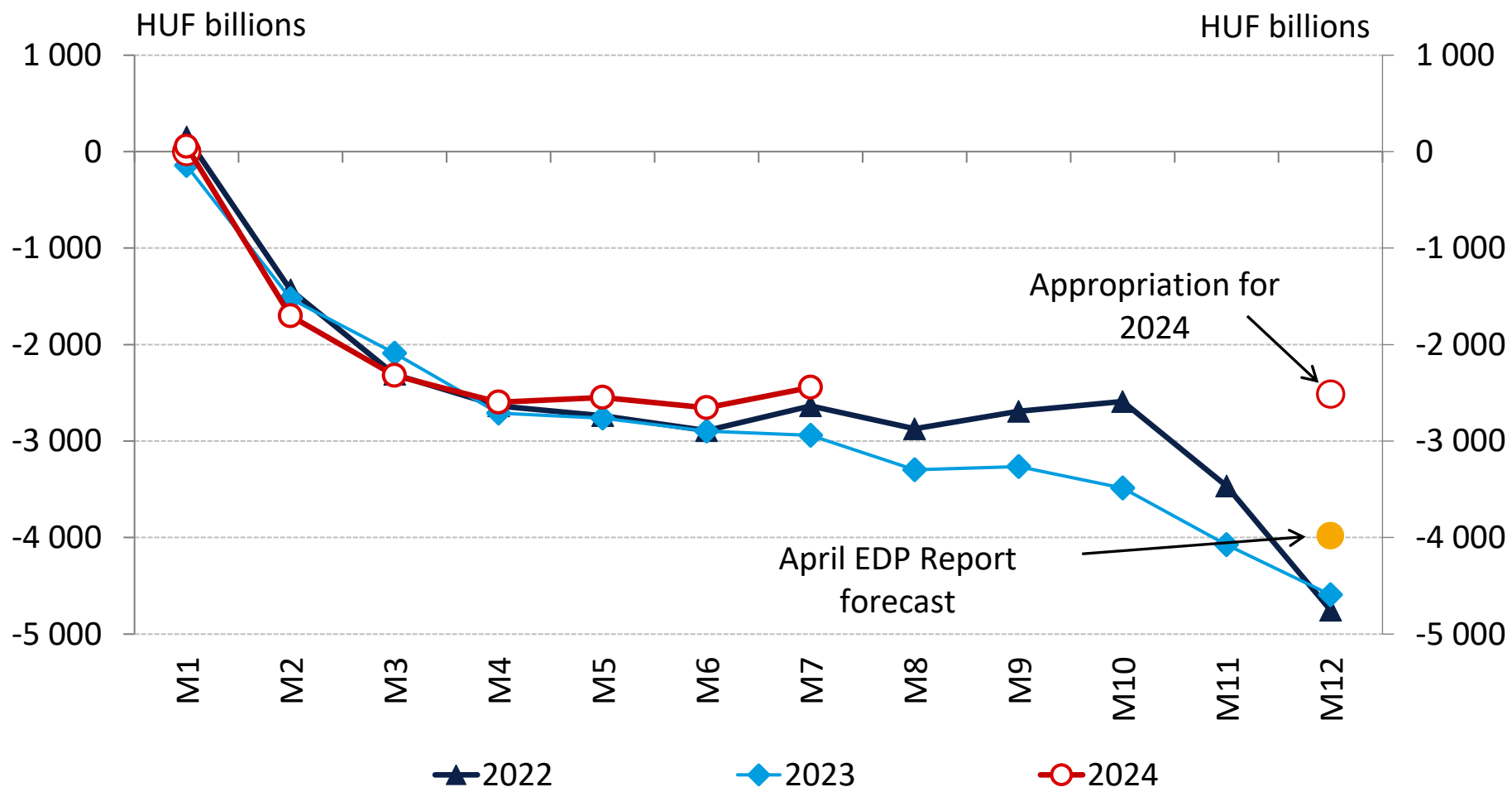


### DEVELOPMENTS IN THE CURRENT ACCOUNT AND THE ENERGY BALANCE

Note | Energy trade balance for the latest month is an estimate.  
Source | HCSO, MNB



## IN THE COUNCIL'S ASSESSMENT, THE ATTAINABILITY OF THE FISCAL DEFICIT TARGET FOR THIS YEAR HAS IMPROVED



THE CUMULATIVE CASH BALANCE OF THE CENTRAL GOVERNMENT BUDGET FROM THE BEGINNING OF THE YEAR

Source | 2024 Budget Act, Hungarian State Treasury, MNB



## THE DOMESTIC FINANCIAL MARKETS ARE STILL EXPOSED TO THE VOLATILITY OF THE RISK ENVIRONMENT



At the beginning of August, the uncertain US outlook increased international financial market volatility. At the same time, there was a correction in risk indicators from mid-August.



Expectations regarding the interest rate policies of the world's leading central banks shifted downwards, while the dollar weakened significantly over the past month.



Historically high foreign exchange reserves, the persistent current account surplus, the Government's deficit reduction measures and a cautious approach to monetary policy act in the direction of an improvement in the country's risk perception.

The global financial market turbulence at the beginning of August calls for caution. In the volatile international financial market environment, monitoring the country's risk perception remains crucial.



# MONETARY POLICY



## A CAUTIOUS AND DATA-DRIVEN APPROACH REMAINS WARRANTED

### GLOBAL RISK FACTORS

Investor sentiment deteriorated significantly in early August, however, this was followed by a correction in risk indicators from mid-month. Financial market developments remain volatile, with emerging markets being highly exposed.



The probability of the Fed cutting rates in September has increased over the past weeks. Markets are expecting larger rate cuts until the end of the year than they did previously.

Geopolitical tensions continue to contribute to the persistence of an uncertain external environment.



### PRECAUTION

Due to experiences with high inflation, households remain cautious. Inflation expectations are decreasing slowly and the improvement in the consumer confidence indicator is also taking longer.



Hungary's economic recovery has stalled. Price stability and the maintenance of financial market stability are the most effective ways to contribute to the relaunch of economic growth.

### DOMESTIC INFLATION

Inflation has left the central bank's tolerance band in July. Price increases from the previous month exceeded their historical average.







## THE MONETARY COUNCIL'S DECISION IN AUGUST

Central bank instrument	Interest rate	Previous interest rate (percent)	New interest rate (percent)
Central bank base rate		6.75	6.75
O/N deposit rate	Central bank base rate minus 1.00 percentage point	5.75	5.75
O/N collateralised lending rate	Central bank base rate plus 1.00 percentage point	7.75	7.75





## THE MONETARY COUNCIL IS COMMITTED TO CONTINUING DISINFLATION AND THE ACHIEVEMENT OF THE INFLATION TARGET IN A SUSTAINABLE MANNER

Based on incoming data, the Council takes month-by-month decisions on the level of the base rate. Decisions are made between leaving interest rates unchanged, and moderate rate cuts.

### We are closely following:



#### The inflation outlook

- The sustainable achievement of the inflation target must be ensured.
- Pricing behaviour in the market services sector has to be monitored closely.



#### Financial market stability

- Persistent maintenance of positive real interest rate environment is necessary.
- Shifts in global investor sentiment must be taken into account.



#### Hungary's risk perception

- Developments in the external balance position must be followed closely.
- Reaching fiscal targets in a disciplined manner is also necessary for an improvement in risk perception.



## A CAUTIOUS AND PREDICTABLE MONETARY POLICY IS STILL NEEDED



We cannot sit back: looking ahead, **a careful, patient, and stability-oriented** monetary policy remains warranted.

In the current macroeconomic environment, the Bank **can make the most effective contribution** to the easing of economic agents' increased precaution and to the restart of economic growth **by achieving price stability and maintaining financial market stability.**



In the Monetary Council's assessment, **there may be scope for cautiously lowering interest rates further** in the coming period, depending on the **expected interest rate policies of the world's leading central banks**, as well as **developments in the domestic inflation outlook and changes in Hungary's risk perception.**

## INCOMING DATA IN THE NEXT PERIOD COULD SIGNIFICANTLY REDUCE UNCERTAINTIES SURROUNDING THE OUTLOOK

### Main questions of the September decision:



In which direction will inflation and core inflation move following the data in July?



Are the Fed and the ECB beginning and continuing their rate cuts, respectively?



How are the factors affecting Hungary's risk perception developing?



How are consumer and business confidence, relevant to growth, evolving?



## THE MONETARY COUNCIL'S FORWARD GUIDANCE

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*„Looking ahead, risks surrounding international and domestic disinflation, as well as the volatility in investor sentiment warrant a careful and patient approach to monetary policy. **In the Monetary Council’s assessment, there may be scope for cautiously lowering interest rates further in the coming period, depending on the expected interest rate policies of the world’s leading central banks, as well as developments in the domestic inflation outlook and changes in Hungary’s risk perception.** The Council is constantly assessing incoming macroeconomic data, the outlook for inflation and developments in the risk environment, based on which it will take decisions on the level of the base rate in a cautious and data-driven manner.”*



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ATTENTION!**

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