MINUTES
OF THE MONETARY COUNCIL MEETING
27 AUGUST 2024

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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.

European economic activity had been subdued in 2024 Q2 as well. Confidence indicators had remained below long-term averages. In the US, economic growth had picked up in the second quarter; however, labour market data for the last month had been below expectations, indicating a slowdown in economic activity. The ongoing Russia-Ukraine war, the generally tense geopolitical situation and the weak outlook for European industrial production posed significant risks in terms of global economic growth.

Annual inflation had increased slightly in the euro area and had fallen moderately in the US in July. Market services inflation had been generally higher, which continued to restrain disinflation. Geopolitical conflicts had led to increased volatility in the energy market. However, looking ahead, slowing global economic demand pointed to moderate inflation rates. Since the latest interest rate decision, oil prices had fallen slightly, while gas prices had risen.

At the beginning of August, risk indicators had suggested a strong deterioration in global investor sentiment, followed by a reversal from the middle of the month. The global risk environment had primarily been shaped by fears of recession in the US economy, financial market developments in Japan and geopolitical tensions in the Middle East. At its July policy meeting, the Federal Reserve had left interest rates unchanged, but market expectations for starting interest rate cuts in September had strengthened in response to incoming macroeconomic data. The European Central Bank had continued to highlight the importance of incoming data in its decisions. Based on market pricing, the ECB’s interest rate path had also shifted downwards. In the CEE region, the Czech and the Romanian central banks had lowered their policy rates by 25 basis points in August.

In 2024 Q2, economic recovery had stalled in Hungary. Compared to 2024 Q1, domestic economic performance had fallen by 0.2 percent, while GDP had risen by 1.5 percent in annual terms. The performances of construction and real estate transactions had been the most significant contributing factors to annual growth, while economic expansion had been restrained by a decline in value added by industry, which constituted a large share in the national economy. The volume of retail trade had continued to grow in annual terms. Strong real wage growth had persisted in recent months; however, the consumer confidence index had remained stagnant, overall, in the first half of 2024. The unemployment rate had stood at 4.2 percent in July.

With the gradual easing of the precautionary motive, household consumption would support the expansion in Hungary's GDP in the remainder of 2024. As a result of stalling government investment and the wait-and-see approach to investment by the corporate sector, investment might still slow economic growth in 2024. Exports would be affected by opposing trends. Subdued European economic activity was holding back domestic exports, but ongoing and newly announced, significant capacity-enhancing foreign direct investment projects would continue to stimulate exports in the coming years. With the pick-up in the production of new industrial capacities built recently, balanced economic growth was expected from 2025, and Hungary's export market share was likely to increase.

In July, consumer prices had risen at a faster pace than in June, by 4.1 percent in annual terms. Core inflation and core inflation excluding indirect tax effects had also risen on the previous month, with both measures standing at 4.7 percent. Price increases relative to the previous month had been above historical averages in both inflation and core inflation. The rise in inflation had primarily reflected an increase in food and fuel prices. The increase in core inflation had been mainly driven by the higher price dynamics of processed food. Disinflation of market services continued to be slow, therefore the Council paid special attention to pricing decisions in the sector. Household inflation expectations had fallen moderately relative to the previous month but remained at high levels.

The inflation rate was expected to fluctuate close to the upper bound of the tolerance band in the coming months. Core inflation capturing underlying developments would rise close to 5.0 percent temporarily by the end of the year. Anchoring inflation expectations, preserving financial market stability and a disciplined monetary policy were crucial for the consumer price index to return to the central bank target in a sustained manner from next year onwards.

The balance of payments position had improved significantly in the first half of 2024: the current account had registered a surplus of nearly EUR 3.7 billion in the first six months of the year. The current account balance had fallen temporarily in June; however, looking ahead, it was expected to increase throughout 2024 as a whole. This primarily reflected a further improvement in the terms of trade and a sharp decline in investment activity, characterised by a high import share and inventory accumulation. Over the longer term, with earlier manufacturing investment projects turning productive, the country's increasing export market share would support the improvement in the external balance. The current account surplus would continue to rise over the forecast horizon.

Deficit reduction measures announced at the beginning of July, would support the attainability of fiscal deficit targets for 2024 and 2025, which also required keeping fiscal expenditure under control. The primary government balance was expected to reach near equilibrium levels this year. In 2025, the significant decrease in interest expenses would also contribute to the narrowing of the deficit. In order to further reduce the government debt-to-GDP ratio, it was necessary to achieve the set deficit targets in a disciplined manner.

In the Monetary Council's assessment, reducing inflation expectations further and preserving financial market stability remained key to achieving price stability again and restoring the sustainable growth path of the domestic economy. Historically high foreign exchange reserves, the persistent current account surplus, the Government's deficit reduction measures and a cautious approach to monetary policy acted in the direction of an improvement in the country's risk perception. However, the temporary sharp rise in the volatility in the financial market environment had also affected domestic financial markets over the past month. The volatile financial market developments, the renewed increase in geopolitical tensions and the risks to the outlook for inflation continued to warrant a careful and patient approach.

Following the review of macroeconomic and financial market developments, the Monetary Council discussed the details of its monetary policy decision. Members were of the view that confidence indicators in Europe had shown an unfavourable picture; therefore, external demand might remain subdued for a more prolonged period. Regarding the outlook for global inflation, members noted that although price growth in the services sector remained high, slowing global economic demand pointed to declining inflation rates. Several members highlighted that the geopolitical conflicts led to an indirect increase in the uncertainty surrounding the international outlook for inflation.

In the Monetary Council's assessment, the volatility in the risk environment continued to call for caution, which was also supported by a significant deterioration in financial market sentiment at the beginning of August. However, some members underlined that a reversal had taken place in risk indicators from the middle of August. Several members pointed out that the severe turbulence in financial markets had shed some light on the substantial risk exposure of emerging markets. Members concluded that based on market expectations, both the Federal Reserve's and the European Central Bank's interest rate paths had shifted downwards over the past month. Several members emphasised that interest rate cuts by the world's leading central banks might create scope in emerging markets for easing monetary conditions in the coming period.

Regarding the preliminary second-quarter data on economic growth, the Council stated that the economic recovery had stalled in Hungary. Slower-than-expected recovery of Hungary's export markets in Europe, especially in Germany, generally held back the uplift in domestic economic growth. Decision makers agreed that in the remainder of 2024, the easing of the precaution and the increase in household consumption and investment activity would be key in terms of domestic growth. In this context, several members pointed out that given the high wage dynamics, it was possible that a portion of the excess income had appeared outside of domestic consumption. Some members highlighted that weak investment activity in the corporate sector was mainly underpinned by factors related to inflation and to uncertainty. They affirmed that investment was expected to hold back economic growth in 2024.

In terms of the country's external balance, several members saw the substantial current account surplus for the first half of the year as a positive development. In addition, several decision makers assessed that as a result of the Government's measures announced in July, the attainability of the fiscal deficit target set for 2024 had improved.

Regarding inflation developments, the Council concluded that inflation had been at the upper bound of the forecast range in July, and had temporarily left the tolerance band. Some members pointed out that the higher-than-expected price growth was mainly driven by food prices. Council members assessed that this was due in part to the phasing out of the mandatory discounts and of linking the prices of some basic foodstuffs to purchase prices in July, and as a result, the outlook for inflation had not changed over the longer term. However, members underlined that the incoming data for August might significantly reduce uncertainty around the inflation path for this year. Several members emphasised that the easing of inflation expectations was a protracted process; therefore, the improvement in consumer and investor sentiment was also slow.

Members agreed that in the current macroeconomic environment, achieving price stability and maintaining financial market stability were necessary for increased precaution to ease and economic growth to restart. Decision makers reaffirmed their commitment to the achievement of the inflation target in a sustainable manner. The Council stressed that several factors indicated an improvement in Hungary's risk perceptions. However, several members highlighted that the turbulent international financial market environment had also affected domestic financial markets over the past month, while geopolitical tensions had increased, and the outlook for inflation had been exposed to risks. Council members agreed that a careful and patient approach was still warranted.

At its August policy meeting, the Monetary Council discussed two options: leaving interest rate conditions unchanged and reducing interest rates by 25 basis points. The Council considered these options primarily based on the outlook for inflation, economic agents' precaution and changes in the risk environment. Decision makers established that there were several strong arguments in favour of both options; however, leaving the base rate unchanged was a better fit to a stability-oriented approach to monetary policy in the current economic environment. Council members in general argued for maintaining tight monetary conditions and preserving financial market stability.

The Monetary Council was unanimous in its decision to discontinue interest rate cuts temporarily and to leave interest rate conditions unchanged. Looking ahead, several members confirmed the importance of a data-driven approach. The Council was in agreement that there had been no change in the most important cornerstones of tight monetary policy. Accordingly, in the coming period, Council members would continue to closely monitor all factors that would affect the outlook for domestic inflation, they would constantly assess Hungary's risk perception, the international risk and monetary policy environment and changes in household and corporate confidence, relevant to Hungary's economic growth.

In the members' unanimous view, a cautious and patient approach to monetary policy was still necessary. Decision makers underlined that tight monetary policy continued to be key to maintaining financial market stability and to achieving the inflation target in a sustainable manner. However, several members indicated that after the temporary discontinuation of interest rate cuts, there might be scope for cautiously lowering interest rates further in the coming period.

The Monetary Council was committed to continuing disinflation and the achievement of the inflation target in a sustainable manner. In the current macroeconomic environment, the Bank could 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 line with its stability-oriented approach to monetary policy, the Council left the base rate unchanged at 6.75 percent at its August meeting. Accordingly, the O/N deposit rate and the O/N collateralised borrowing rate were also left unchanged, at 5.75 percent and 7.75 percent, respectively. Restrictive monetary policy contributed to the maintenance of financial market stability and the achievement of the inflation target in a sustainable manner by ensuring positive real interest rates.

Looking ahead, risks surrounding international and domestic disinflation, as well as the volatility in investor sentiment warranted a careful and patient approach to monetary policy. In the Monetary Council's assessment, there might 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 was constantly assessing incoming macroeconomic data, the outlook for inflation and developments in the risk environment, based on which it would take decisions on the level of the base rate in a cautious and data-driven manner.

Votes cast by individual members of the Council:

In favour of maintaining the base rate at 6.75 percent, the overnight collateralised lending rate at 7.75 percent and maintaining the interest rate on the overnight central bank deposit at 5.75 percent:	7	Éva Búza, Péter Gottfried, Kolos Kardkovács, Zoltán Kovács, György Matolcsy, Gyula Pleschinger, Barnabás Virág
Vote against:	0	

<u>The following members of the Council were present at the meeting:</u>

Éva Búza

Péter Gottfried

Kolos Kardkovács

Zoltán Kovács

György Matolcsy

Gyula Pleschinger

Barnabás Virág

The Council will hold its next policy meeting on 24 September 2024. The minutes of that meeting will be published at 2 p.m. on 9 October 2024.