MINUTES
OF THE MONETARY COUNCIL MEETING
23 JULY 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. Confidence indicators had remained below long-term averages. In the US, growth might have continued at a moderate pace, while growth in China had been slower than expected in the second quarter. The ongoing Russia-Ukraine war, the generally tense geopolitical situation and the weak outlook for European industrial production posed risks in terms of external economic activity.

Annual inflation had fallen slightly in the euro area and had declined markedly in the US relative to the previous month. Services inflation had been generally higher compared to the levels seen before Covid-19, which continued to restrain disinflation. Geopolitical conflicts had led to increased volatility in the energy market and might cause disruptions in global value chains. However, looking ahead, subdued global economic demand pointed to moderate inflation rates. Oil and gas prices had fallen slightly since the latest interest rate decision.

Indicators of risk had continued to be volatile; however, spreads on European financial assets had fallen in the wake of election results in France and the UK. At its policy meeting in July, the European Central Bank had left interest rates unchanged. According to the ECB's communication, the pace and timing of interest rate cuts would continue to be determined by incoming data. Economic data released in the US in recent weeks had increased the probability of an interest rate reduction by the Fed at its September meeting and the degree of policy easing expected by the end of the year. In the CEE region, the Czech central bank had lowered its policy rate by 50 basis points to 4.75 percent at its rate-setting meeting in June. The Polish central bank had left monetary conditions unchanged in July, and the Romanian central had reduced interest rates by 25 basis points.

Hungarian economic growth had started in 2024 Q1; however, weak economic activity in Europe was having an increasingly lasting impact. The significant increase in real wages, the gradual easing of the precautionary motive, as well as the improvement in consumer confidence had all been reflected in growing household consumption in the first quarter. The general decline in investments had curbed the pace of economic growth. Net exports had made a positive contribution to growth with a generally subdued import demand. In May, industrial production had fallen year-on-year, continuing the weak performance of the sector since the beginning of 2023. Construction output had risen compared to the same period of 2023, while the volume of retail trade had continued to grow in annual terms. The unemployment rate had fallen slightly, standing at 4.3 percent in May.

In the remainder of 2024, the revival of household consumption would increasingly support the gradual expansion in Hungary's GDP. Investments might still slow down 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. Hungary's GDP was expected to grow by 2.0–3.0 percent this year. 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 June, consumer prices had risen by 3.7 percent in annual terms, and as a result the inflation rate had remained within the central bank tolerance band. The inflation data had been consistent with the projection in the June Inflation Report, while it had been lower than market expectations. The decline in inflation had been mainly caused by falling fuel prices. Core inflation and core inflation excluding indirect tax effects had risen slightly to 4.1 percent. Disinflation of market services continued to be slow, and therefore the Council paid special attention to pricing decisions in the sector. Household inflation expectations had fallen in June relative to the previous month but had remained at high levels.

The inflation rate was expected to fluctuate within the tolerance band, close to its upper bound in the coming months, too. However, the decline in core inflation capturing underlying developments had stopped in the second quarter and the indicator would rise close to 5.0 percent temporarily by the end of the year. According to the MNB's projection, annual inflation was expected to be between 3.0 and 4.5 percent this year on average. Anchoring inflation expectations, preserving financial market stability and disciplined monetary policy were crucial for the consumer price index to permanently return to the central bank target from next year.

In May, the current account had registered another substantial surplus. The expected increase in the balance in 2024 as a whole primarily reflected a further improvement in the terms of trade, declining 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, which was expected to reach 1.5–2.7 percent of GDP in 2024, before rising to 3–4 percent in 2025 and 2026.

The deficit reduction measures, announced in July, would support the achievement of the fiscal deficit targets of 4.5 percent and 3.7 percent in 2024 and 2025, respectively. 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, the inflation outlook continued to be consistent with the projection in the June Inflation Report. FX swap market processes at the end of the quarter had been stable, which had also been supported by the use of central bank instruments. In addition, the incipient recovery in Hungarian economic growth, 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 volatile financial market environment, significant 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. In the Council's assessment, economic activity remained subdued in Europe and confidence indicators painted an unfavourable picture. Several members pointed out that the Russia-Ukraine war, the generally tense geopolitical situation and the negative outlook for European industry posed significant risks in terms of Hungary's export partners' demand. Some members noted that high services inflation was a general phenomenon, which slowed down global disinflation.

In the Monetary Council's assessment, the volatility in the risk environment continued to call for caution; however, spreads on European financial markets had fallen following the elections in France and the UK. Some members drew attention to the fact that the probability that the Fed would lower interest rates in September had increased recently, while according to the ECB's communication, the pace and timing of interest rate cuts would continue to be determined by incoming data.

There was a consensus view among members that although Hungary's GDP growth had been positive in the first quarter, weak economic activity in Europe was having an increasingly lasting negative effect on domestic developments. The Council was in agreement that rising household consumption would play a key role in supporting domestic economic activity throughout the rest of the year. In terms of the country's external balance, several members saw the substantial January-May current account surplus as a positive development. Besides, several decision-makers assessed that the deficit reduction measures supporting the achievement of the budget deficit targets pointed in the direction of improving the country's risk assessment.

Regarding inflation developments, the Council was of the view that the incoming June data had been consistent with the projection in the latest Inflation Report; however, it was more favourable than market expectations. Some members pointed out that disinflation of market services continued to be slow, and therefore particular attention should be given to pricing decisions in the sector. In the Council's assessment, the easing of inflation expectations was a protracted process and expectations should again be anchored at the inflation target.

In the Council's view, the outlook for inflation remained consistent with the projection in the June Inflation Report. The temporary rise in core inflation was expected to continue in the coming months, while the consumer price index would remain close to the upper bound of the tolerance band in the second half of the year. Looking ahead, all these warranted a disciplined and tight monetary policy. Members agreed that the country's risk perception had improved due to the incipient recovery in Hungarian economic growth, historically high foreign exchange reserves, the persistent current account surplus, the Government's deficit reduction measures and a cautious monetary policy. However, several members drew attention to the fact that the volatile financial market environment, geopolitical tensions and the risks to the outlook for inflation continued to warrant a careful and patient approach.

At its July policy meeting, the Monetary Council discussed two options: reducing interest rates by 25 basis points and leaving interest rate conditions unchanged, which were primarily considered along the outlook for inflation and changes in the risk environment. Council members in general argued for maintaining tight monetary conditions and preserving financial market stability. In the members' view, reducing interest rates was warranted by an improvement in the country's risk assessment, the higher degree of policy easing expected from the Fed by the end of the year and more favourable domestic inflation data compared to analysts' expectations. As another argument in favour of reducing interest rates, several Council members highlighted that such a decision was consistent with the Bank's communication concerning a cautious approach, while the monetary policy stance remained tight. Some Council members cited the volatility in global risk appetite as an argument in favour of holding rates, stressing that in this environment, changes in the inflation outlook, as well as the evolution of interest rate paths expected from the world's leading central banks, can only be identified with certainty based on several months of data.

At the end of the discussion, the Council voted unanimously to cut the base rate by 25 basis points, and to simultaneously decrease the interest rate corridor by 25 basis points. Looking ahead, several members highlighted 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, members would continue to closely monitor all factors that would affect the outlook for domestic inflation, the country's risk perception, its relative position within the region and developments in the global risk and monetary policy environment.

In the members' unanimous view, a cautious and patient approach to monetary policy was still necessary. Tight monetary policy continued to be key to maintaining financial market stability and to achieving the inflation target in a sustainable manner. Members agreed that while keeping its forward guidance unchanged, the Council would assess incoming macroeconomic data, the outlook for inflation and developments in the risk environment from month to month, based on which it would take decisions on the level of the base rate in a cautious and data-driven manner.

At its July meeting, the Monetary Council lowered the base rate by 25 basis points to 6.75 percent. Accordingly, the lower bound of the interest rate corridor, i.e. the O/N deposit rate, was reduced to 5.75 percent, while the upper bound, i.e. the O/N lending rate, was decreased to 7.75 percent. 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 global and domestic disinflation, volatility in international investor sentiment and expected interest rate policies of the world's leading central banks warranted a careful and patient approach to monetary policy. 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 reducing the base rate to 6.75 percent, reducing the overnight collateralised lending rate to 7.75 percent and and lowering the interest rate on the overnight central bank deposit to 5.75 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 27 August 2024. The abridged minutes of that meeting will be published at 2 p.m. on 11 September 2024.