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BACKGROUND DISCUSSION FOLLOWING THE MONETARY COUNCIL'S 21 MAY DECISION

Analyst background discussion

21 May 2024



MAIN MESSAGES: MONETARY POLICY

- Global **risk appetite has increased** since the April policy decision.
- **Accelerating economic growth, historically high foreign exchange reserves, a persistent improvement in the current account balance and a cautious approach to monetary policy** have contributed to an improvement in the country's risk perception.
- We can't sit back: the **volatile financial market environment** and **the risks to the outlook for inflation** continue to warrant a **careful and patient approach**.
- At its meeting today, the Council **cut the base rate by 50 basis points to 7.25 percent**.
- **Preserving financial market stability remains a priority**.
- The Council is constantly assessing incoming macroeconomic data, the outlook for inflation and developments in the risk environment and will take **decisions on any further reductions in the base rate in a cautious and data-driven manner**.



MAIN MESSAGES: MACROECONOMIC OUTLOOK

- **Global inflation has decreased to a low level;** however, high **services** inflation restrains disinflation.
- **Based on market pricing, the Federal Reserve may start cutting interest rates later than the European Central Bank. The divergence arising from the persistently higher US interest rate environment may lead to increased volatility in emerging markets.**
- **In 2024 Q1, Hungarian economic growth picked up.** Economic growth is likely to accelerate further in the second quarter of the year.
- **The significant rise in real wages seen since September 2023 is expected to continue this year. Precautionary motives have started to ease.**
- **In March, the current account surplus rose to another historically high level.** The current account surplus as a share of GDP was higher than expected.
- **We need to keep our focus on disinflation and achieving price stability in a sustainable manner.** The Council monitors closely the pricing dynamics in the services sector.

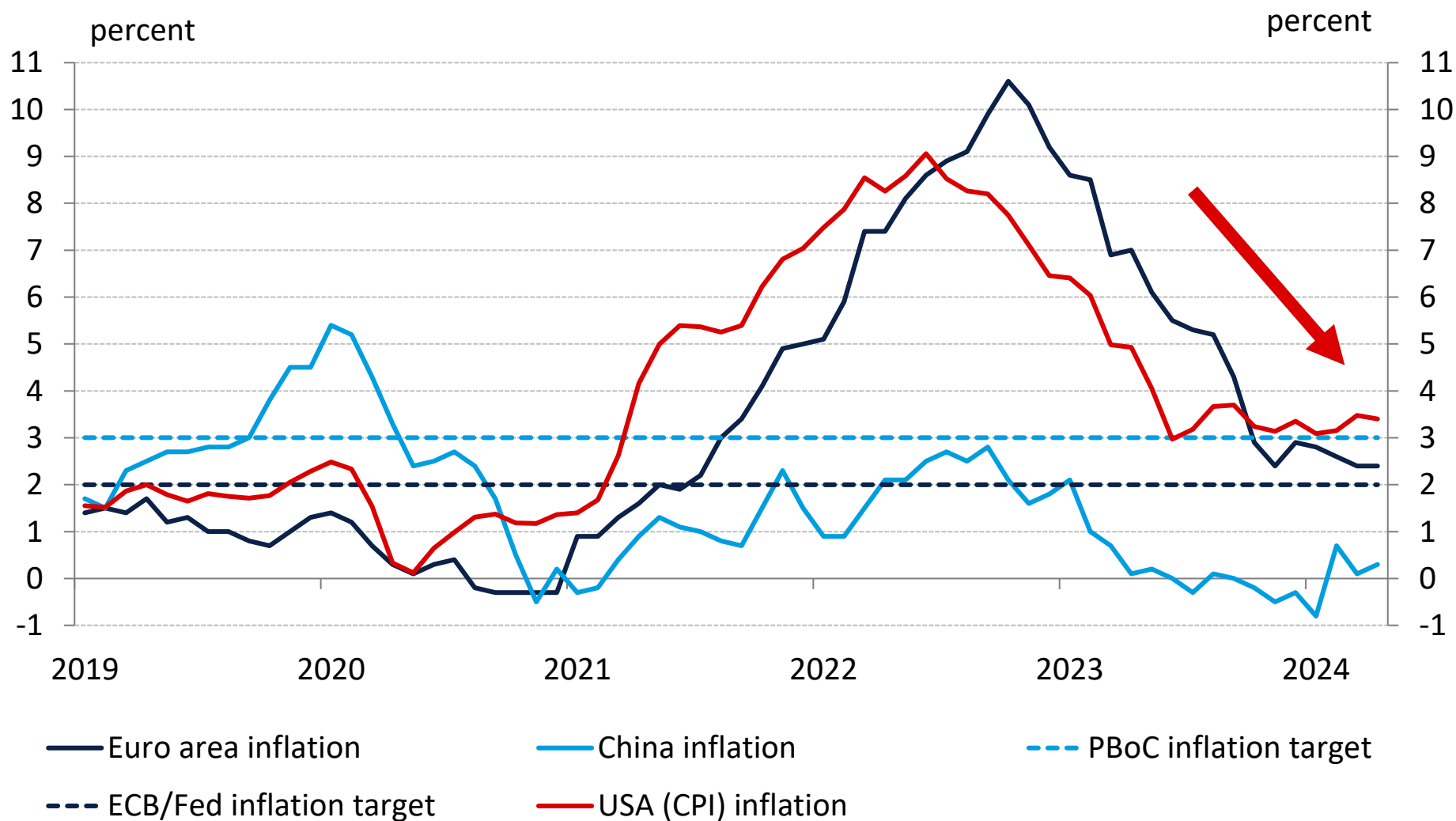


MACROECONOMIC ASSESSMENT AND OUTLOOK





GLOBAL INFLATION HAS DECREASED TO A LOW LEVEL; HOWEVER, HIGH SERVICES INFLATION RESTRAINS DISINFLATION

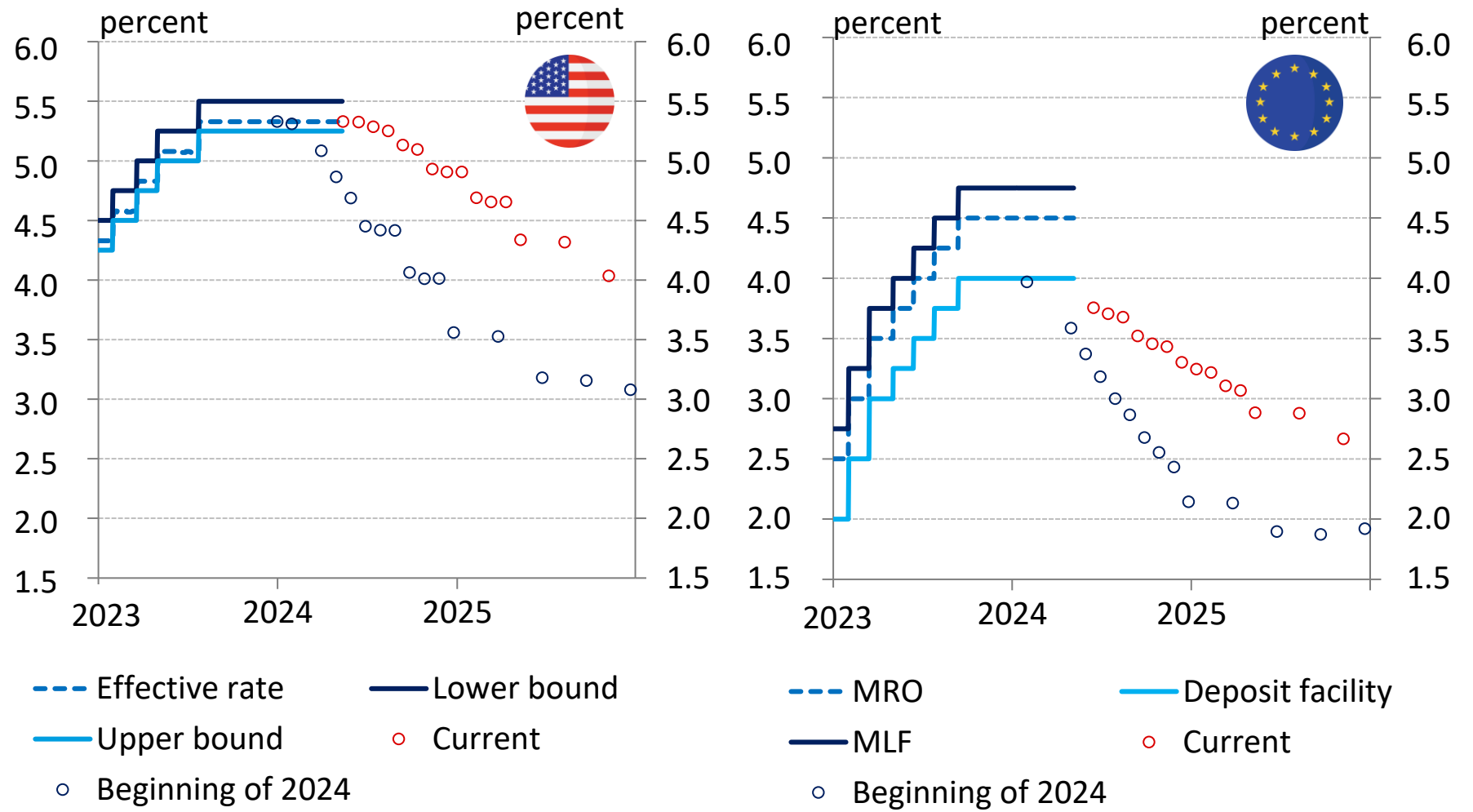


INFLATION IN THE UNITED STATES, CHINA AND THE EURO AREA

Source | Eurostat, OECD



BASED ON MARKET PRICING, THE FED MAY START CUTTING INTEREST RATES LATER THAN THE ECB

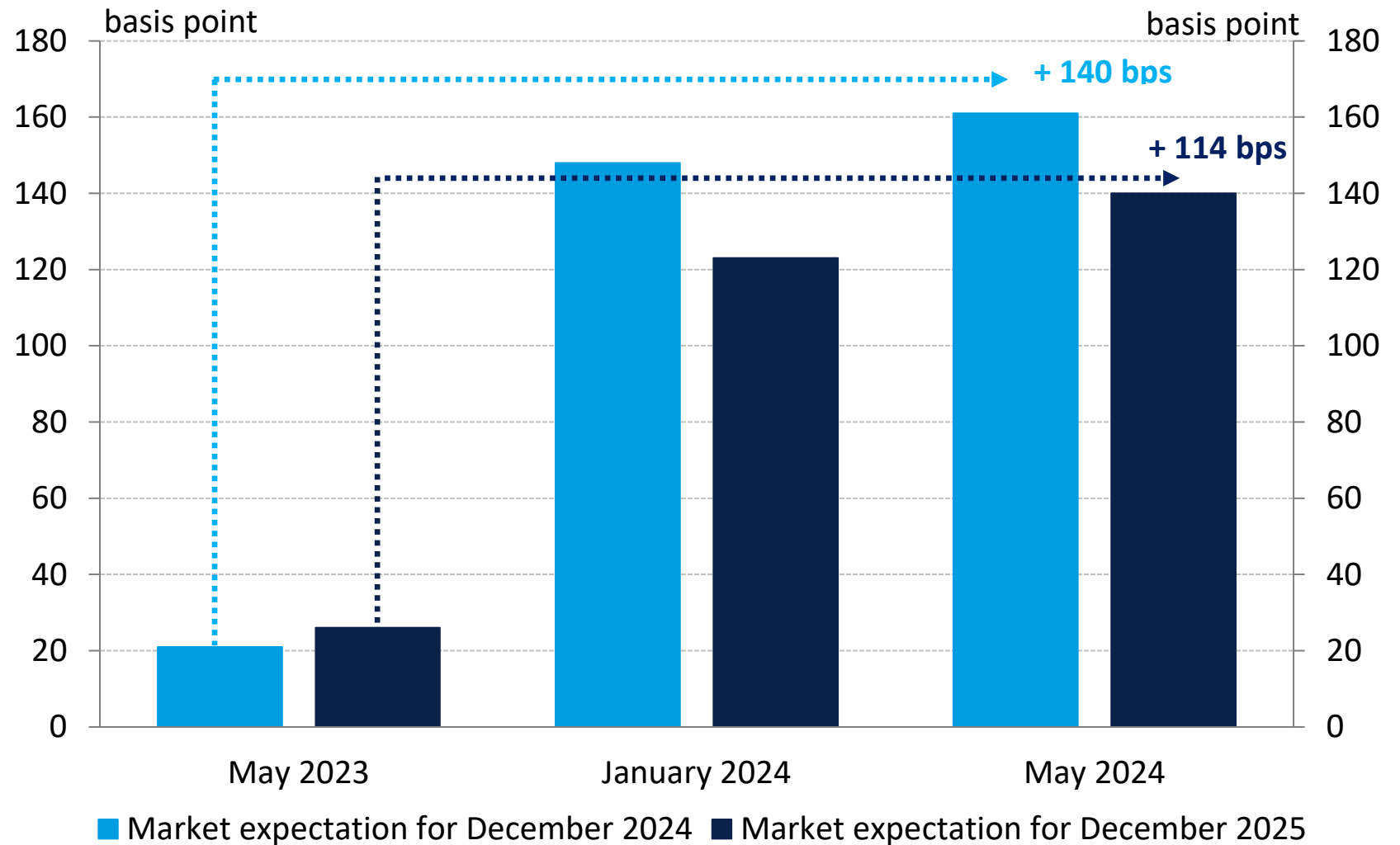


THE EXPECTED INTEREST RATE PATH OF THE ECB AND THE FED BASED ON MARKET PRICING

Source | Bloomberg



THE DIVERGENCE BETWEEN THE FED AND THE ECB WARRANTS A CAUTIOUS APPROACH TO MONETARY POLICY IN EMERGING ECONOMIES

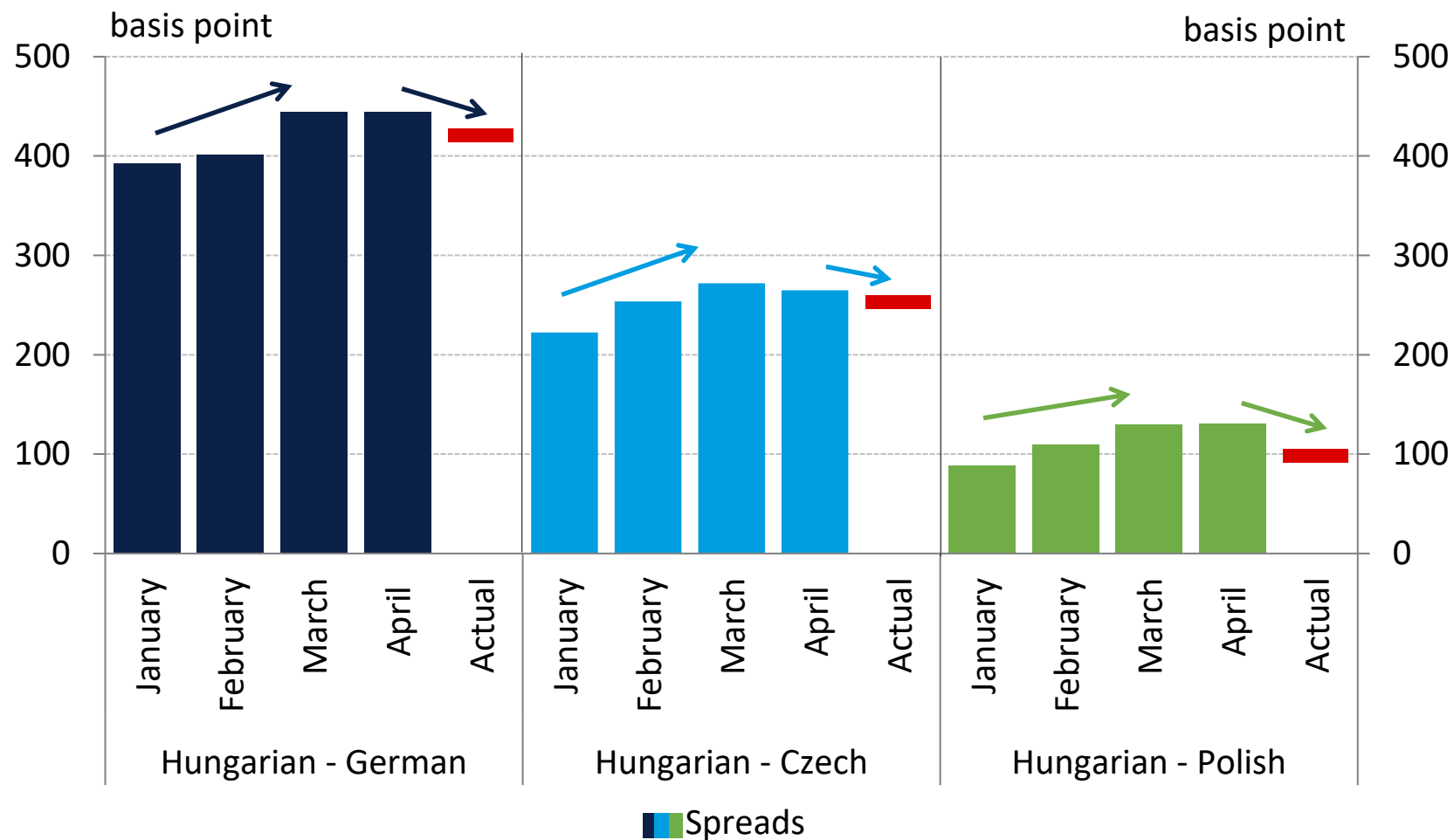


EXPECTED DIFFERENCE BETWEEN THE FED'S AND THE ECB'S KEY POLICY RATES BASED ON MARKET PRICING

Source | Bloomberg



DOMESTIC 10-YEAR YIELD SPREADS DECREASED OVER THE PAST MONTH



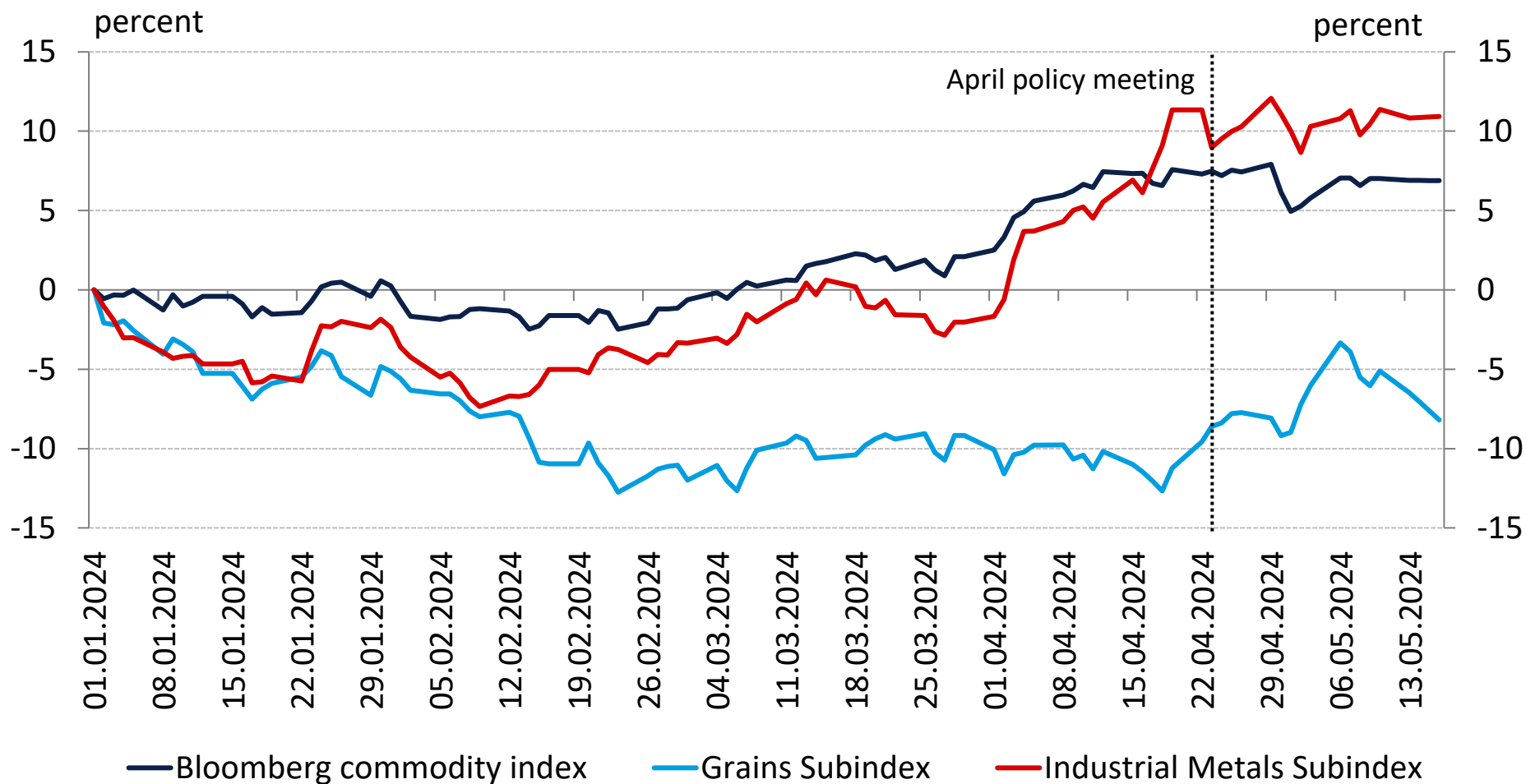
10-YEAR HUNGARIAN GOVERNMENT BOND SPREADS COMPARED TO GERMAN AND REGIONAL SOVEREIGN YIELDS IN 2024

Note | Month-end data.

Source | Bloomberg



COMMODITY PRICES HAVE STAGNATED SINCE THE PREVIOUS POLICY MEETING...

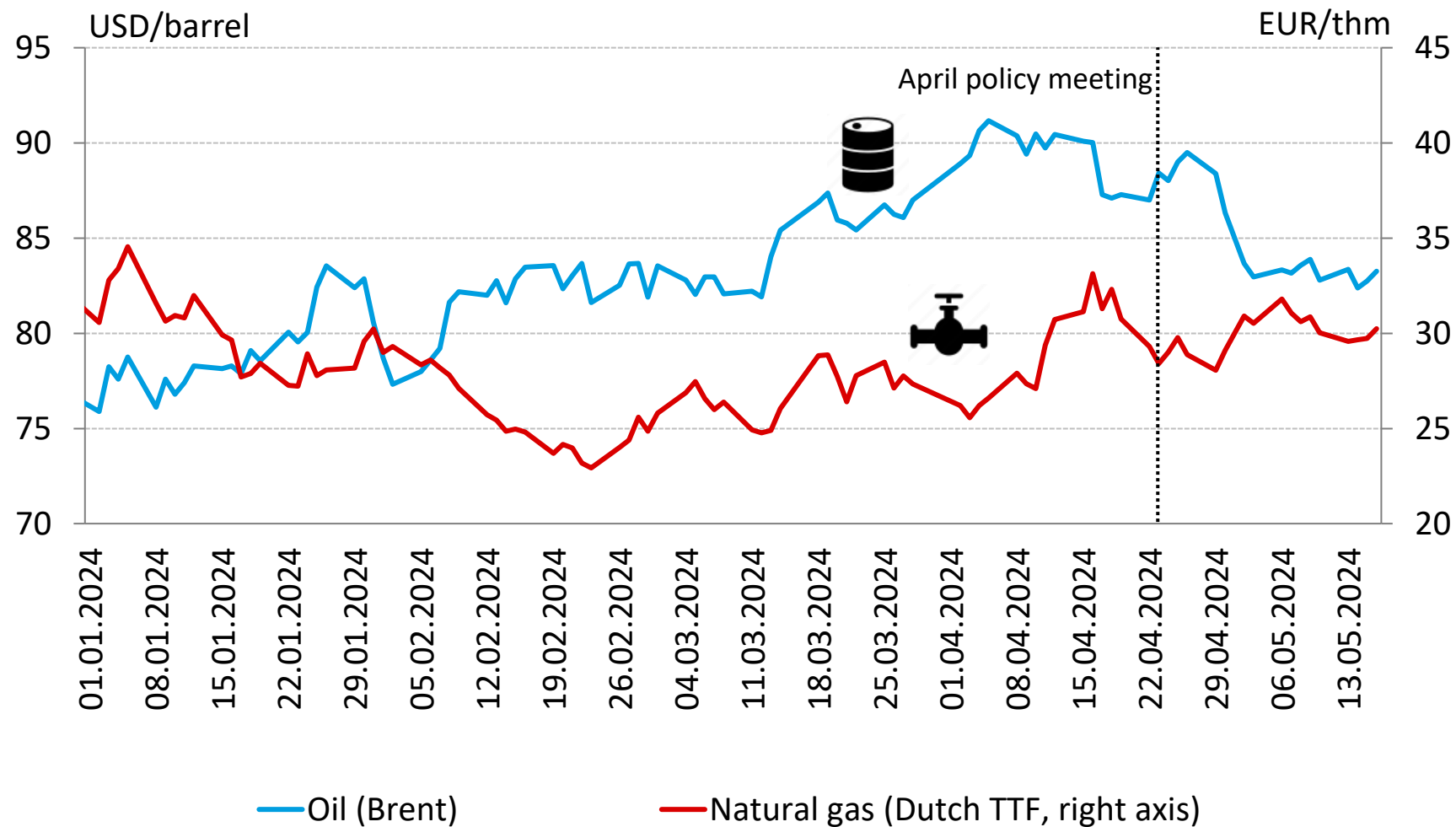


DEVELOPMENTS IN THE BLOOMBERG COMMODITY INDEX AND SOME OF ITS SUB-INDICES

Source | Bloomberg



... WHILE OIL PRICES FELL DURING THE PERIOD

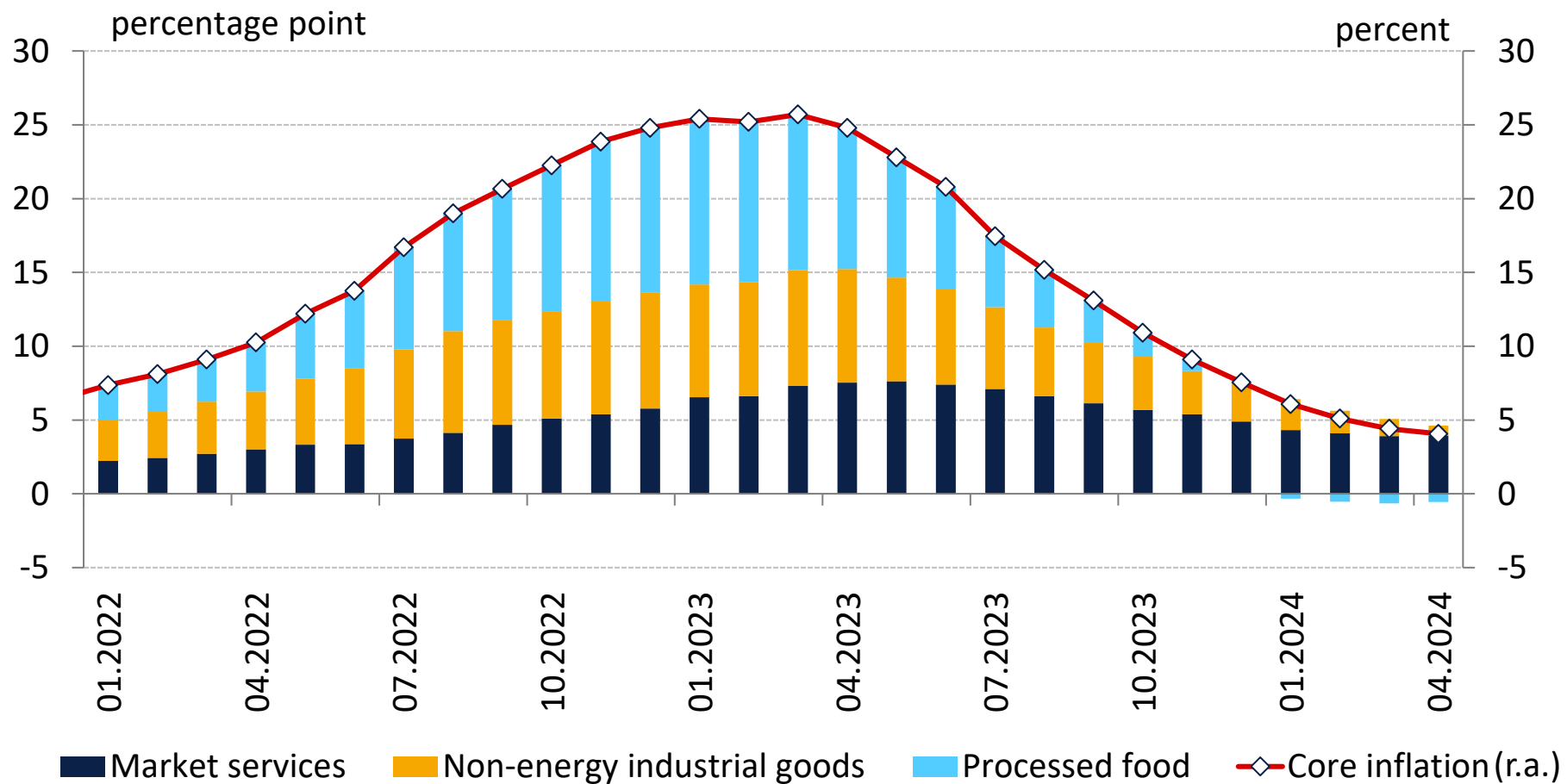


DEVELOPMENTS IN OIL AND GAS PRICES

Source | Bloomberg, MNB



THE DECLINE IN CORE INFLATION HAS CONTINUED

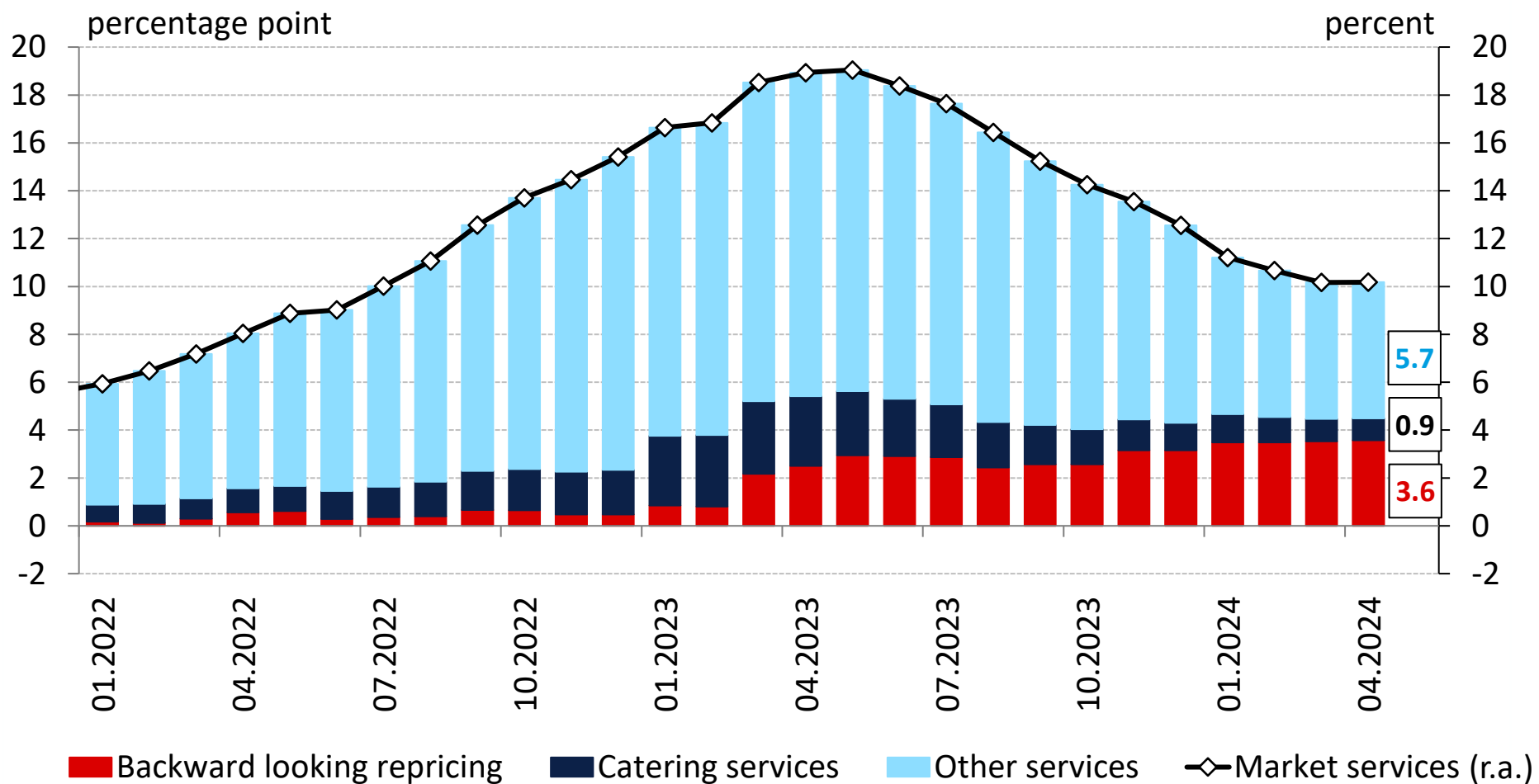


DECOMPOSITION OF CORE INFLATION

Source | HCSO, MNB calculation



THE COUNCIL MONITORS CLOSELY THE DEVELOPMENTS IN THE INFLATION OF MARKET SERVICES

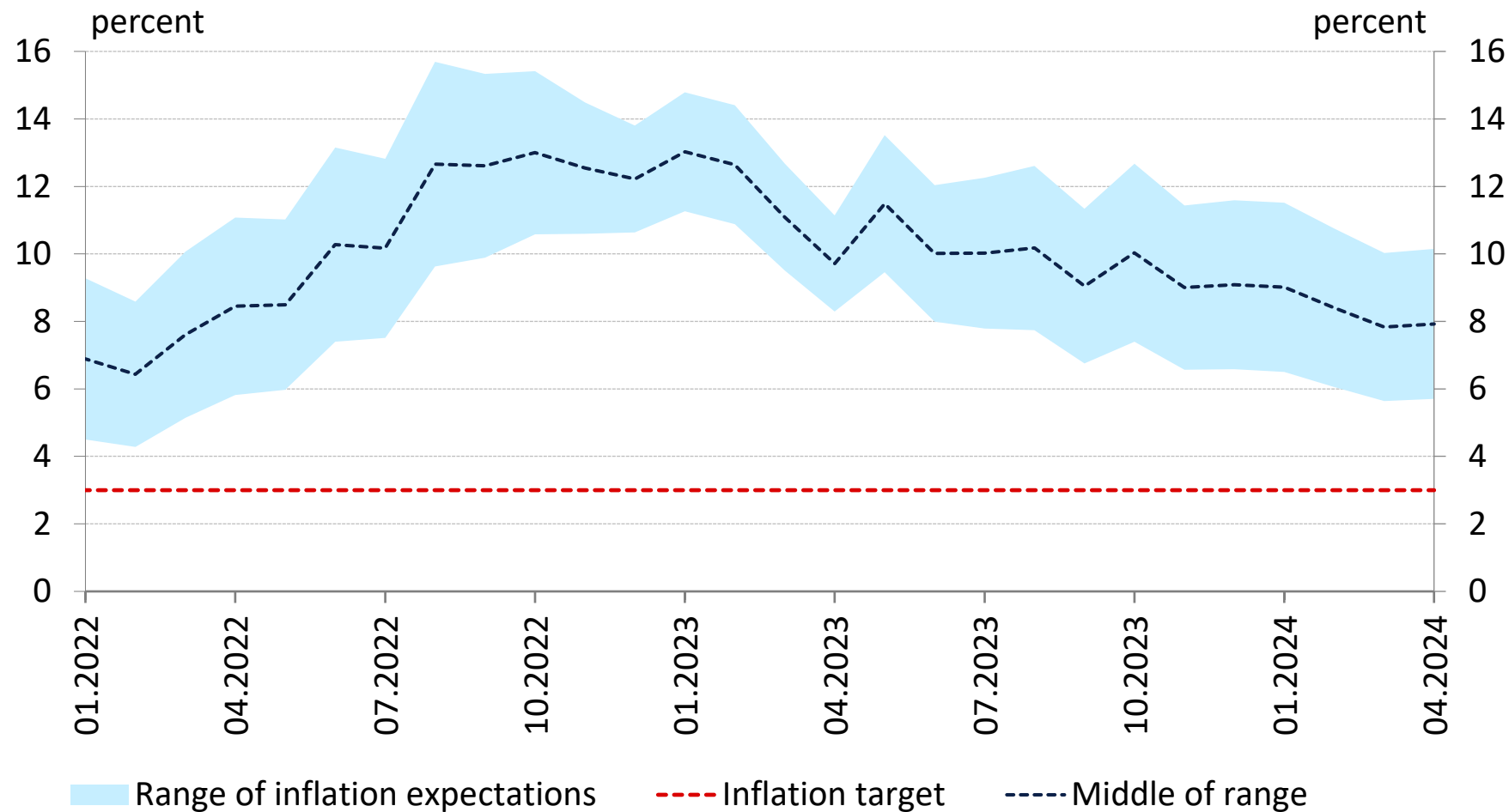


DECOMPOSITION OF MARKET SERVICE INFLATION

Source | HCSO, MNB calculation



DECLINE IN INFLATION EXPECTATIONS REQUIRES TIME; EXPECTATIONS NEED TO BE REANCHORED AT THE INFLATION TARGET



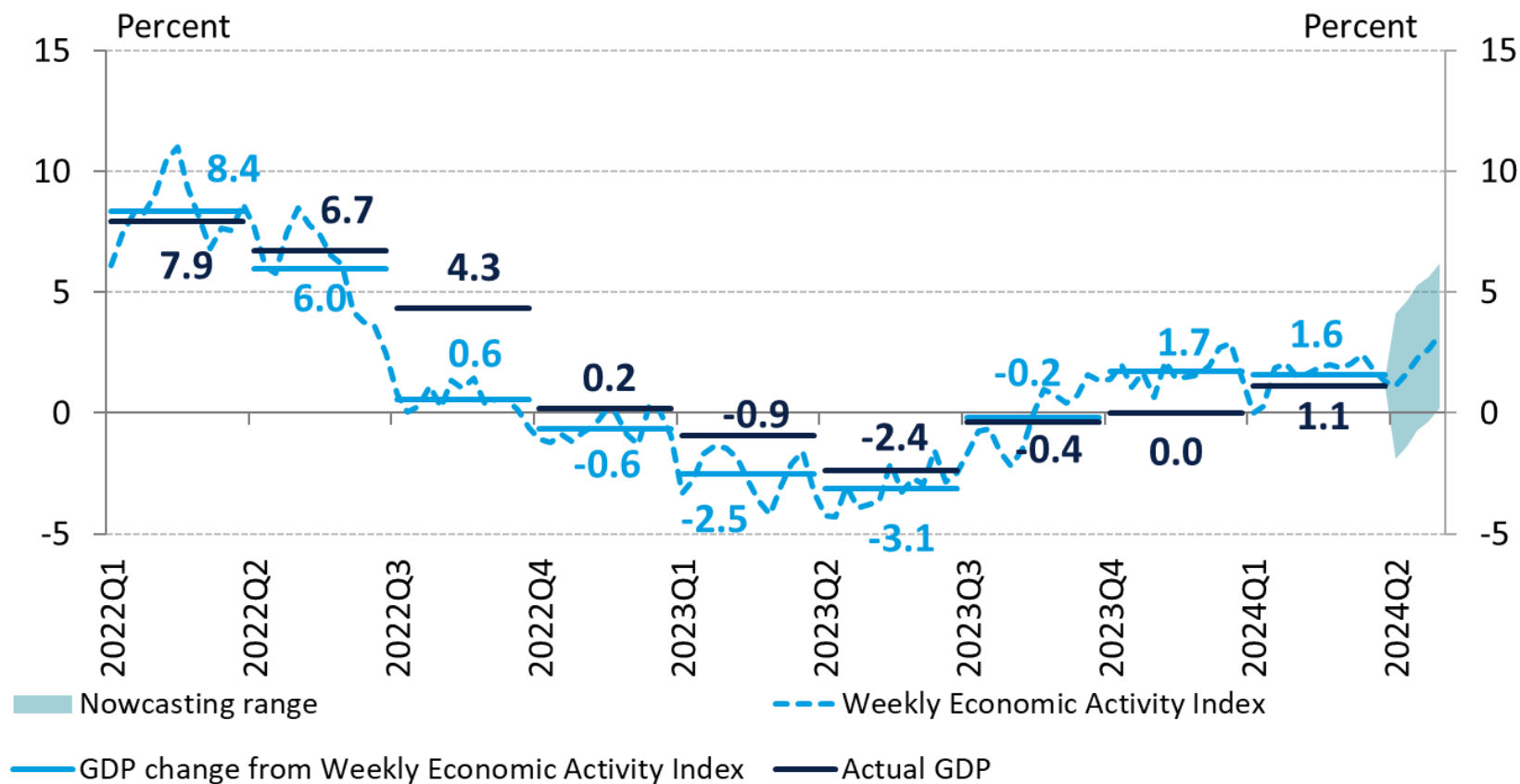
DEVELOPMENTS IN HOUSEHOLD INFLATION EXPECTATIONS IN HUNGARY

Source | MNB calculation based on European Commission data



THE GRADUAL RECOVERY IN THE DOMESTIC ECONOMY CONTINUED

In 2024 Q1, GDP grew by 1.1 percent. Economic growth is likely to accelerate further in the second half of the year.



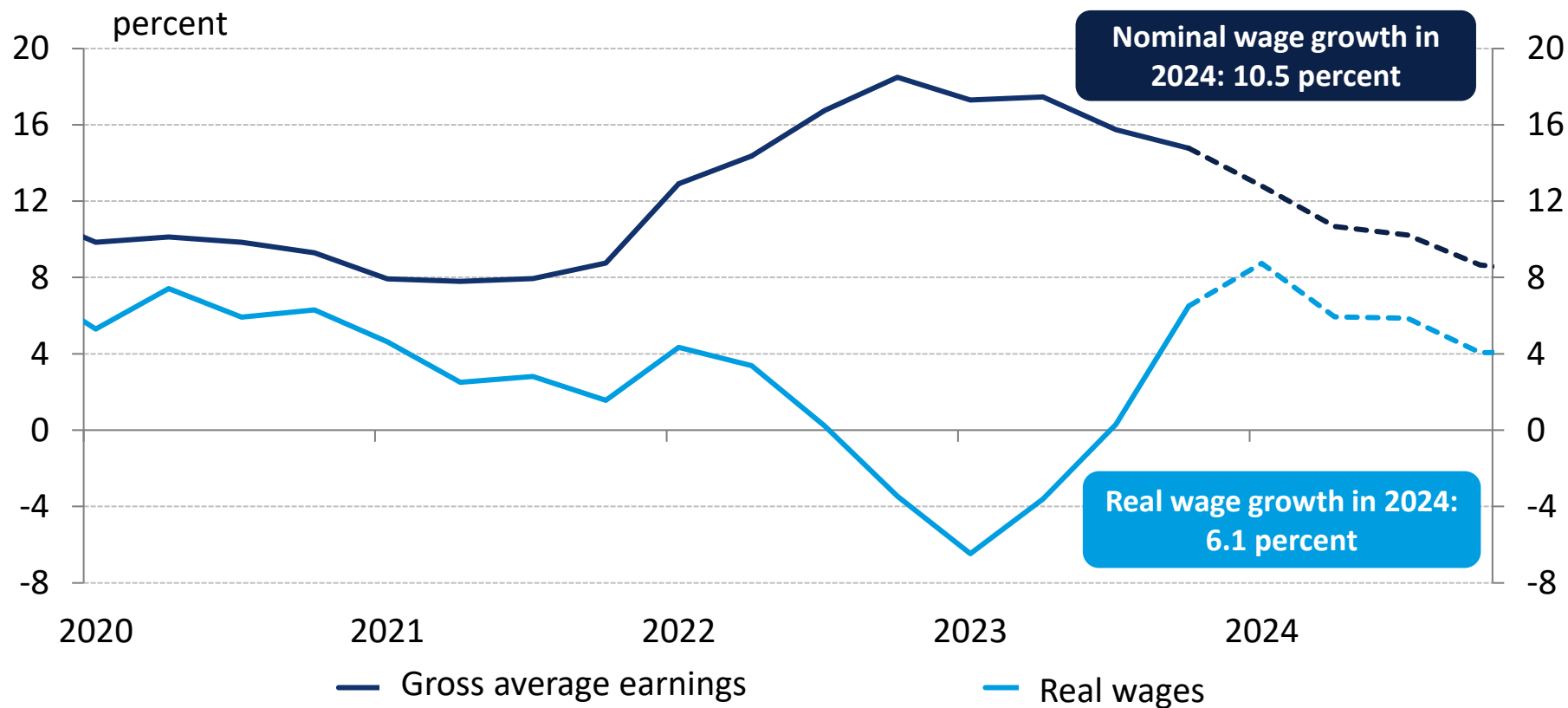
WEEKLY ECONOMIC ACTIVITY INDEX

Source | Calculation by MNB, HCSO



NOMINAL WAGE DYNAMICS MAY BE LOWER THAN LAST YEAR, BUT REAL WAGES WILL STILL RISE SIGNIFICANTLY

The gross average earnings of the national economy rose by 14.0 percent, while those of the private sector rose by 12.8 percent in February.



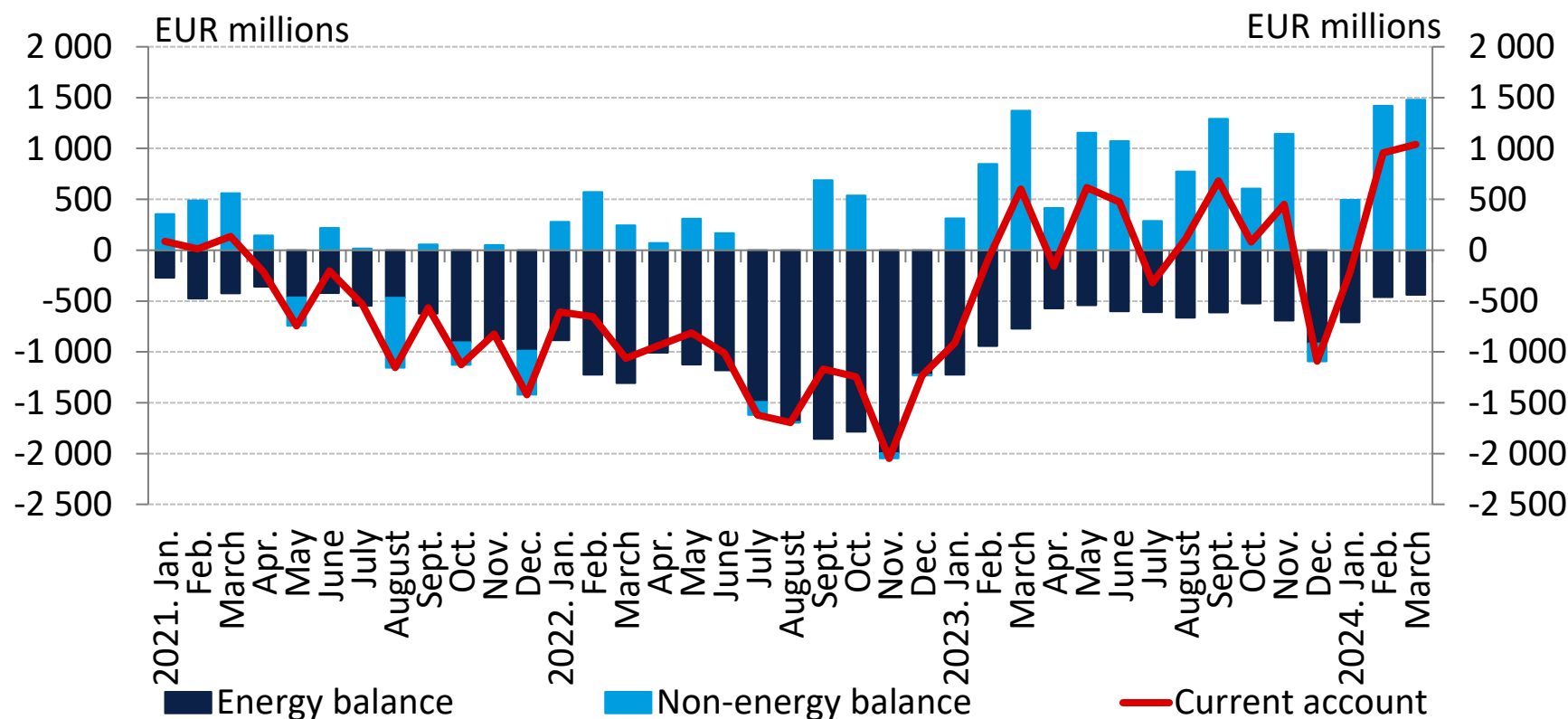
EVOLUTION AND PROJECTION OF YOY CHANGES IN GROSS AVERAGE EARNINGS IN THE PRIVATE SECTOR

Source | HCSO, MNB



THE MONTHLY BALANCE OF THE CURRENT ACCOUNT REACHED A RECORD HIGH LEVEL AGAIN AFTER THE PREVIOUS MONTH

In March 2024, the current account surplus was 1041 million euros, which was mainly due to the high surplus of trade balance of goods and the current transfer.



DEVELOPMENTS IN THE CURRENT ACCOUNT AND THE ENERGY BALANCE

Note | Energy trade balance for the latest month is an estimate.

Source | HCSO, MNB



MONETARY POLICY

A CAREFUL AND PATIENT APPROACH IS STILL WARRANTED

INTERNATIONAL FACTORS



In the global economy, disinflation has been strong ...

..., at the same time, services inflation, which has been higher compared to the levels seen before the pandemic, restrains it.



Geopolitical conflicts may increase volatility in the energy market and may cause disruptions in global value chains, leading to a renewed rise in freight costs.



International risk appetite has increased ...



..., however, the expected divergence between monetary policies of the Fed and the ECB may lead to increased volatility in emerging markets through the global interest rate environment.

DOMESTIC DEVELOPMENTS



Inflation has been within the tolerance band since the beginning of the year ...

..., at the same time, the pace of price increases will rise temporarily in the middle of this year. Services inflation is higher compared to the pre-pandemic levels.



Several factors contributed to an improvement in the country's risk perception.



In the first quarter, Hungarian economic growth picked up and is likely to accelerate further in the second half of the year.



In March, the current account surplus rose to another historically high level.



The level of foreign exchange reserves remains close to its historical peak.



THE MONETARY COUNCIL'S MAY INTEREST RATE DECISION

Central bank instrument	Interest rate	Previous interest rate (percent)	New interest rate (percent)
Central bank base rate		7.75	7.25
O/N deposit rate	Central bank base rate minus 1.00 percentage point	6.75	6.25
O/N collateralised lending rate	Central bank base rate plus 1.00 percentage point	8.75	8.25



THE MNB PAYS SPECIAL ATTENTION TO A NUMBER OF FACTORS WHEN SHAPING THE INTEREST RATE POLICY

INFLATION

Inflation **will temporarily increase in the middle of this year** due to backward-looking pricing of market services, and base effects.

Maintaining tight monetary conditions is necessary to **achieve the inflation target in a sustainable manner in 2025.**

RISK PERCEPTION

In terms of the country's risk assessment, **the credible achievement of the set deficit targets and the external balance developments in 2024** are of particular importance.

INTERNATIONAL MONETARY POLICY ENVIRONMENT

The expected divergence between monetary policies of two of the world's leading central banks may lead to **increased volatility in emerging markets** through the global interest rate environment.

FINANCIAL MARKET STABILITY

In a volatile international sentiment, a key question is **whether risks will appear that could threaten the evolution of the forint exchange rate or domestic yields.**

Looking ahead, risks surrounding global and domestic disinflation and volatility in international investor sentiment warrant a careful and patient approach to monetary policy.





THE MONETARY COUNCIL'S FORWARD GUIDANCE

*„Looking ahead, risks surrounding global and domestic disinflation and volatility in international investor sentiment warrant a careful and patient approach to monetary policy. The Council is constantly assessing incoming macroeconomic data, the outlook for inflation and developments in the risk environment and will take **decisions on any further reductions in the base rate in a cautious and data-driven manner.**”*

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YOUR KIND
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gyarapodásáért*